

#42

9/3/67

Memorandum 67-62

Subject: Study 42 - Good Faith Improvers

The attached recommendation is ready to print. It includes revisions suggested by various Commissioners who reviewed it before it was sent to the printer to be set in type. We plan to check all citations and to proofread this material before it is printed. However, we are sending it to you now so that you will have the maximum amount of time to review it before the meeting.

We believe that one change should be made in the recommended legislation. We suggest that the following sentence be added after the first sentence of proposed subdivision (4) of Code of Civil Procedure Section 339:

This subdivision does not apply if relief is sought by cross-complaint or counterclaim in another action.

Absent this change, the court--despite the language in the Comment--probably would apply the statute of limitations to bar relief sought by cross-complaint or counterclaim. See 1 WITKIN, CALIFORNIA PROCEDURE 599 (1954).

We request Commission approval to print this recommendation as an appendix to our Annual Report for 1967.

Respectfully submitted,

John H. DeMouilly
Executive Secretary

STATE OF CALIFORNIA

CALIFORNIA LAW REVISION COMMISSION

RECOMMENDATION

relating to

Improvements Made in Good Faith Upon
Land Owned by Another

September 1967

CALIFORNIA LAW REVISION COMMISSION
School of Law
Stanford University
Stanford, California 94305

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NOTE

This recommendation includes an explanatory Comment to each section of the recommended legislation. The Comments are written as if the legislation were enacted. They are cast in this form because their primary purpose is to undertake to explain the law as it would exist (if enacted) to those who will have occasion to use it after it is in effect.

To be printed on Commission letterhead as of September 22, 1967

September 22, 1967

To His EXCELLENCY, RONALD REAGAN
Governor of California and
THE LEGISLATURE OF CALIFORNIA

The California Law Revision Commission was authorized by Resolution Chapter 202 of the Statutes of 1957 to make a study relating to whether the law relating to the rights of a good faith improver of property belonging to another should be revised.

The Commission published a recommendation and study on this subject in October 1966. See *Recommendation and Study Relating to the Good Faith Improver of Land Owned by Another*, 8 CAL. LAW REVISION COMM'N. REP., REC. & STUDIES 301 (1967). Senate Bill No. 254 was introduced at the 1967 session of the Legislature to effectuate this recommendation. The bill passed the Senate but died in the Assembly.

The Commission submits herewith a new recommendation on this subject. In preparing the new recommendation, the Commission has taken into account the objections that were made to the recommendation submitted to the 1967 Legislature.

Respectfully submitted,
RICHARD H. KRATONOS
Chairman

RECOMMENDATION OF THE CALIFORNIA LAW REVISION COMMISSION

relating to

IMPROVEMENTS MADE IN GOOD FAITH ON LAND OWNED BY ANOTHER

BACKGROUND

At common law, structures and other improvements placed by one person on land owned by another became the property of the owner of the land. Continuation of this rule obviously is justified as applied to one who, in bad faith, simply appropriates another's land as a building site. However, the rule may be harsh and unjust when applied to an improver who is the victim of a mistake made in good faith. In the latter case, the landowner receives an undeserved windfall, and there would be no justification for application of the rule if his interests were fully protected in an equitable adjustment of the unfortunate situation that would ameliorate the loss to the good faith improver.

For this reason, most states have modified the common law rule. The rule has been changed by judicial decision in several states. In most jurisdictions—at least 35 states and the District of Columbia—statutes have been enacted, known as "occupying claimants acts" or "betterment acts," to modify the common law rule to provide at least a measure of relief to the good faith improver. Such statutes also have been enacted throughout Canada. Uniformly, the objective has been to provide relief to a person who makes improvements believing, in good faith, that he owns the land.

The betterment acts are based on the principle that the landowner's just claims against the innocent improver should be limited to recovery of the land itself, damages for its injury, and compensation for its use and occupation. Generally, these acts undertake to effectuate this principle by requiring the owner to choose whether to pay for the improvements or to sell the land to the good faith improver.

The California law is less considerate of the innocent improver than the law in most other states. California enacted a betterment act in 1856, but it was declared unconstitutional by a divided court in *Billings v. Hall*, 7 Cal. 1 (1857).¹ Under the existing law, in the absence of circumstances giving rise to an estoppel against the landowner, the good faith improver has no rights beyond those accorded him by Section 741 of the Code of Civil Procedure and Section 1013.5 of the Civil Code. Section 741 permits the improver to set off the value of permanent improvements if the landowner sues him for damages for use and occupation of the land. Section 1013.5 permits the improver to remove improvements if he compensates the landowner for all damages resulting from their being affixed and removed.

The existing California law is inadequate and unfair in those cases in which the value of the improvement greatly exceeds the value of the interim use and occupation of the land and the improvement either

¹ The Commission has concluded that the *Billings* case would not preclude the enactment of legislation to improve the lot of the good faith improver. Unlike the legislation recommended by the Commission, the 1856 betterment act made no distinction between good faith improvers and bad faith improvers, and this aspect of the statute was stressed by the court in holding the statute unconstitutional.

cannot be removed or is of little value if removed.² The right of removal

²Taliaferro v. Colasso, 139 Cal. App.2d 908, 294 P.2d 774 (1956), illustrates the unjust result which may obtain under present California law. A house was built by mistake on lot 20 instead of lot 21. The owner of lot 20 brought an action to quiet title and to recover possession. The defendant was a successor in interest to the person who built the house. The trial court gave judgment quieting title and for possession on the condition that \$3,000 be paid to the defendant. The district court of appeal affirmed that portion of the judgment awarding possession of the lot and house to the landowner, but reversed that portion requiring any payment to the defendant as a condition for obtaining possession. The court held that the "right of removal" (Civil Code Section 1013.5) and the "right of setoff" (Code of Civil Procedure Section 741) are the exclusive forms of relief available to a good faith improver and that, for this reason, the general equity powers of the court cannot be brought into play even though the landowner seeks equitable relief (quiet title). As a result, the landowner obtained possession of the lot and house without any compensation to the defendant for the value of the house.

in such a case is useless and the right of setoff provides only limited protection against an inequitable forfeiture by the good faith improver and an unjustified windfall for the landowner.

RECOMMENDATIONS

The Law Revision Commission recommends that California join the great majority of the states that now provide more adequate relief for the improver who is the innocent victim of a bona fide mistake.³ Ac-

³The need for corrective legislation is not alleviated by the prevalence of title insurance, nor would such legislation have any impact upon title insurance protection. With respect to the good faith improver, title policies do not cover matters of survey or location; with respect to the landowner, policies do not cover matters or events subsequent to his acquisition of the property. See CALIFORNIA LAND SECURITY AND DEVELOPMENT, Mallette, *Title Insurance*, §§ 7-1-7-21 Cal. Cont. Ed. Bar 1960.)

cordingly, the Commission recommends:

1. The relief provided should be available only to a good faith improver. The legislation should define a good faith improver as a person who acts in good faith and erroneously believes, because of a mistake either of law or fact, that he is the owner of the land. This definition would be based on language contained in Civil Code Section 1013.5 but would be more limited than that section which appears to include tenants, licensees, and conditional vendors of chattels.

Some of the betterment acts limit relief to good faith improvers who hold under "color of title." Such a limitation is undesirable. It makes relief unavailable in other situations where it is needed—where the improver owns one lot but builds on another by mistake. Moreover, the term "color of title" is of uncertain meaning. While the limitation imposed by its use may have been justified in an era when property interests were evidenced by the title documents themselves, the limitation is not suited to present conditions since virtually universal reliance is now placed upon title insurance for land transactions.

2. The good faith improver should be permitted to bring an action (or to file a cross-complaint or counterclaim) to have the court determine the rights of the parties and grant appropriate relief. This will permit the improver to obtain some measure of relief whether or not he is in possession of the property. It also will permit him to take the initiative in resolving the unsatisfactory state of affairs.

A two-year statute of limitations should apply to an action brought by a good faith improver. The period should run from the date that the improver discovers that he is not the owner of the land upon which the improvements have been made.

3. The court should not be authorized to grant any other form of relief where the right of setoff (Code of Civil Procedure Section 741) or the right to remove the improvements (Civil Code Section 1013.5) would result in substantial justice to the parties under the circumstances of the case.

4. Where neither of the existing statutory remedies would suffice, the court should be empowered to adjust the rights, equities, and interests of the improver, landowner, and other interested parties to achieve substantial justice to the parties under the circumstances of the particular case, subject to the limitation that the relief granted shall protect the landowner against any pecuniary loss while avoiding, insofar as possible, enriching him unjustly at the expense of the good faith improver. Where a choice must be made between protecting one party or the other, the landowner should prevail.

5. The legislation should not apply to an encroachment case—one where a building or other improvements constructed by a person on his own land encroaches upon adjoining land—because the power of the California courts to reach a fair result in such cases through the exercise of their equitable powers is already well established. *E.g., Brown Derby Hollywood Corp. v. Hutton*, 61 Cal.2d 855, 40 Cal. Rptr. 848, 395 P.2d 896 (1964); *Christensen v. Tucker*, 114 Cal. App.2d 554, 250 P.2d 660 (1952).

6. The legislation should not apply where the improvement is made by a governmental entity or is made on land owned or possessed by a governmental entity. Otherwise, unintended and undesirable changes might be made in the law relating to eminent domain, inverse condemnation, and encroachments on public lands.

7. Section 741 of the Code of Civil Procedure should be amended to eliminate the "color of title" requirement and to make applicable the recommended definition of a "good faith improver." This would extend the right of setoff to the situation, among others, where the improver constructs the improvement on the wrong lot because of a mistake in the identity or location of the land.

8. The recommended legislation should apply to any action commenced after its effective date, whether or not the improvement was constructed prior to such date. Decisions in other states are about equally divided as to whether a betterment statute can constitutionally be applied where the improvements were constructed prior to its effective date. *SCURLOCK, RETROACTIVE LEGISLATION AFFECTING INTERESTS IN LAND* 58 (1953). *Cf. Billings v. Hall*, 7 Cal. 1 (1857). The California Supreme Court has recently taken a liberal view permitting retroactive application of legislation affecting property rights. *Addison v. Addison*, 62 Cal.2d 558, 43 Cal. Rptr. 97, 399 P.2d 897 (1965). See 18 STAN. L. REV. 514 (1966). The Commission believes that the statute can constitutionally be applied to improvements constructed prior to its effective date. Nevertheless, a severability clause should be included in case the courts should hold that the act cannot be so applied.

PROPOSED LEGISLATION

The Commission's recommendations would be effectuated by the enactment of the following measure:

An act to amend Sections 339 and 741 of, and add Chapter 10 (commencing with Section 871.1) to Title 10 of Part 2 of, the Code of Civil Procedure, relating to real property.

The people of the State of California do enact as follows:

SECTION 1. Section 339 of the Code of Civil Procedure is amended to read:

339. Within two years:

1. An action upon a contract, obligation or liability not founded upon an instrument of writing, other than that mentioned in subdivision 2 of Section 337 of this code; or an action founded upon a contract, obligation or liability, evidenced by a certificate, or abstract or guaranty of title of real property, or by a policy of title insurance; provided, that the cause of action upon a contract, obligation or liability evidenced by a certificate, or abstract or guaranty of title of real property or policy of title insurance shall not be deemed to have accrued until the discovery of the loss or damage suffered by the aggrieved party thereunder.

2. An action against a sheriff, coroner, or constable upon a liability incurred by the doing of an act in his official capacity and in virtue of his office, or by the omission of an official duty including the nonpayment of money collected upon an execution. But this subdivision does not apply to an action for an escape.

3. An action based upon the rescission of a contract not in writing. The time begins to run from the date upon which the facts that entitle the aggrieved party to rescind occurred. Where the ground for rescission is fraud or mistake, the time

does not begin to run until the discovery by the aggrieved party of the facts constituting the fraud or mistake.

4. *An action by a good faith improver for relief under Chapter 10 (commencing with Section 871.1) of Title 10 of Part 2 of the Code of Civil Procedure. The time begins to run from the date upon which the good faith improver discovers that he is not the owner of the land upon which the improvements have been made.*

Comment. The statute of limitations established by subdivision 4 applies in any action brought by a good faith improver for relief under Sections 871.1 to 871.7. The limitation does not apply if relief under those sections is sought by cross-complaint or counterclaim in another action. The equitable doctrine of laches may be a defense to relief under Sections 871.1 to 871.7, whether the relief is sought in an action brought by the good faith improver or by cross-complaint or counterclaim in a pending action.

SEC. 2. Section 741 of the Code of Civil Procedure is amended to read:

741. (a) *As used in this section, "good faith improver" has the meaning given that term by Section 871.1.*

(b) *When damages are claimed for withholding the property recovered, upon which permanent and improvements have been made on the property by a defendant; or his predecessor in interest as a good faith improver those under whom he claims, holding under color of title adversely to the claim of the plaintiff, in good faith, the value of amount by which such improvements enhance the value of the land must be allowed as a setoff against such damages.*

Comment. Section 741 has been amended to eliminate the condition that the defendant claim the property under "color of title." The amended section requires a setoff if the defendant is a good faith improver as defined in Section 871.1. This amendment makes Section 741 consistent with later enacted Civil Code Section 1013.5. See the Comment to Section 871.1. Thus, the limited protection afforded by Section 741 is extended to include the situation, for example, where the defendant owns one lot but builds on the plaintiff's lot by mistake.

The amendment also substitutes "the amount by which such improvements enhance the value of the land" for "the value of such improvements." The new language clarifies the former wording and assures that the value of the improvement, for purposes of setoff, will be measured by the extent to which the improvement has increased the market value of the land.

SEC. 3. Chapter 10 (commencing with Section 871.1) is added to Title 10 of Part 2 of the Code of Civil Procedure, to read:

CHAPTER 10. GOOD FAITH IMPROVER OF PROPERTY OWNED BY ANOTHER

871.1. As used in this chapter, "good faith improver" means:

(a) A person who makes an improvement to land in good faith and under the erroneous belief, because of a mistake of law or fact, that he is the owner of the land.

(b) A successor in interest of a person described in subdivision (a).

Comment. The definition of "good faith improver" in Section 871.1 is based in part on the language used in Civil Code Section 1013.5 to describe a person who has a right to remove improvements affixed to the land of another. The definition in Section 871.1 is limited, however, to a person who believes he is the owner of the land; unlike Section 1013.5, the definition does not include licensees, tenants, and conditional vendors of chattels. See Comment, 27 So. CAL. L. REVIEW 89 (1953).

Under this section, a person is not a "good faith improver" as to any improvement made after he becomes aware of facts that preclude him from acting in good faith. For example, a person who builds a

house on a lot owned by another may obtain relief under this chapter if he acted in good faith under the erroneous belief, because of a mistake of law or fact, that he was the owner of the land. However, if the same person makes an additional improvement after he has discovered that he is not the owner of the land, he would not be entitled to relief under this chapter with respect to the additional improvement.

As to what constitutes "good faith," see *Brown Derby Hollywood Corp. v. Hatton*, 61 Cal.2d 855, 858-860, 40 Cal. Rptr. 848, 850-851, 395 P. 2d 896, 898-899 (1964) (encroachment case).

871.2. As used in this section, "person" includes an unincorporated association.

Comment. The definition of "person" in Code of Civil Procedure Section 17 does not clearly include an unincorporated association. Section 871.2 is included to make it clear that an unincorporated association may be a good faith improver.

871.3. A good faith improver may bring an action in the superior court or, subject to Section 396, may file a cross-complaint or counterclaim in a pending action in the superior or municipal court for relief under this chapter.

Comment. Section 871.3 requires that an action for relief under this chapter be brought in the superior court. Where relief under this chapter is sought by cross-complaint or counterclaim in a pending action in municipal court and determination of the cross-complaint or counterclaim will necessarily involve the determination of questions not within the jurisdiction of the municipal court, the action must be transferred to the superior court. See Code of Civil Procedure Section 396.

The statute of limitations for an action by a good faith improver for relief under this chapter is fixed by subdivision 4 of Section 339 of the Code of Civil Procedure.

871.4. The court shall not grant relief under this chapter if the court determines that exercise of the good faith improver's right of setoff under Section 741 of the Code of Civil Procedure or right to remove the improvement under Section 1013.5 of the Civil Code would result in substantial justice to the parties under the circumstances of the particular case.

Comment. Section 871.4 establishes a legislative ordering of priorities in determining how to deal judicially with the situation created by a good faith improver.

871.5. When an action, cross-complaint, or counterclaim is brought pursuant to Section 871.3, the court may, subject to Section 871.4, effect such an adjustment of the rights, equities, and interests of the good faith improver, the owner of the land, and other interested parties (including, but not limited to, lessees, lienholders, and encumbrancers) as is consistent with substantial justice to the parties under the circumstances of the particular case. The relief granted shall protect the owner of the land upon which the improvement was constructed against any pecuniary loss but shall avoid, insofar as possible, enriching him unjustly at the expense of the good faith improver.

Comment. Section 871.5 authorizes the court to exercise any of its legal or equitable powers to adjust the rights, equities, and interests of the parties, but this authority is subject to the limitation that the court must utilize the right of setoff or the right of removal in any case where the exercise of one of these rights would result in substantial justice to the parties under the circumstances of the particular case.

871.6. Nothing in this chapter affects the rules of law which determine the relief, if any, to be granted when a person constructs on his own land an improvement which encroaches on adjoining land.

Comment. This chapter has no effect on the law applicable in encroachment cases. There is no necessity for relief under this chapter in such cases since existing law empowers the courts to deal appropriately with such a situation. See *Brown Derby Hollywood Corp v. Hatton*, 61 Cal.2d 855, 40 Cal. Rptr. 848, 395 P.2d 896 (1964); *Christensen v. Tucker*, 114 Cal. App.2d 554, 250 P.2d 660 (1962). See also *Recommendation and Study Relating to the Good Faith Improver of Land Owned by Another*, 8 CAL. LAW REVISION COMM'N, REP., REC. & STUDIES 801, 845 n.101 (1967).

871.7. This chapter does not apply where the improver is a public entity or where the improvement is made to land owned or possessed by a public entity. As used in this section, "public entity" includes the United States, a state, county, city and county, city, district, public authority, public agency, or any other political subdivision or public corporation.

Comment. Section 871.7 is included so that this chapter will have no effect on the law relating to eminent domain, inverse condemnation, and encroachments on public lands (e.g., Streets and Highways Code Sections 660-759.3).

Sec. 4. This act applies in any action commenced after its effective date, whether or not the improvement was constructed prior to its effective date. If any provision of this act or application thereof to any person or circumstance is held invalid, such invalidity shall not affect any other provision or application of this act which can be given effect without the invalid provision or application, and to this end the provisions of this act are declared to be severable.

Comment. This act is made retroactive in the sense that it applies to improvements constructed before, as well as after, its effective date. Decisions in other states are about equally divided as to whether a betterment statute constitutionally can be applied to improvements constructed prior to its effective date. SCURLOCK, RETROACTIVE LEGISLATION AFFECTING INTERESTS IN LAND 58 (1953). Cf. *Billings v. Hall*, 7 Cal. 1 (1857). The California Supreme Court generally has taken the liberal view that permits retroactive application of legislation affecting property rights. E.g., *Addison v. Addison*, 62 Cal.2d 558, 43 Cal. Rptr. 97, 399 P.2d 897 (1965). See 18 STAN. L. REV. 514 (1966). Although it would thus appear that the act constitutionally can be applied to improvements constructed prior to its effective date, a severability clause is included in case such an application of the act is held unconstitutional. (a)