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CONTRACT-DEFYING POLICY OF EQUITABLE GRACE PERIOD REQUIRES PERMANENT IMPROVEMENT TO PROPERTY

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Normally, contracts are strictly construed, and courts are generally reluctant to veer away from the written terms. However, as with every rule, there is an exception, and with regard to long term lease agreements, there is the quiet but powerful Equitable Grace Period: quiet in that potential beneficiaries are not often aware of its existence, and powerful in that it defies the general policy of strict adherence to contract terms.

The Equitable Grace Period is Washington State's standing policy of allowing tardy lessees, who fail to comply with an "option to exercise" deadline of a lease agreement, additional time beyond the written deadline within a contract to accept an option to purchase, under a five-factor test: (1) the failure to give notice was inadvertent, (2) an inequitable forfeiture would have resulted had equity not intervened, (3) the lessor did not change its position and did not suffer prejudice, (4) the lease was for a long term, not a short term, and (5) there was no undue delay in exercising the option. *Wharf Rest., Inc. v. Port of Seattle*, 24 Wn. App. 601, 612-14, 605 P.2d 334 (1979).

ABOUT THE AUTHOR

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The Equitable Grace Period was recently tested, clarified, and reinforced in a case before the Supreme Court, *Borton & Sons, Inc. v. Burbank Properties, LLC*, 471 P.3d 871 (Wash. 2020). This case regards a lawsuit by a property owner Borton & Sons, Inc. ("Borton") who leased land to Burbank Properties, LLC ("Burbank") for a period of three years. In brief, Burbank was late to exercise the option to purchase, and sought exception from the contractual deadline, as Burbank was only approximately one week late.

The trial court ruled in favor of Burbank, permitting relief under the Equitable Grace Period, finding that Burbank's property loss in equity of crops grown on the land constituted inequitable forfeiture, in satisfaction of the second factor of the five-factor test. The Court of Appeal disagreed and reversed, on the ground that an equitable grace period required the showing that substantial improvements were made to the property, which would have resulted in inequitable forfeiture if a grace period were not granted. The Court of Appeal concluded that Burbank made no such improvements, and therefore was not entitled to an equitable grace period as a matter of law. Burbank thereafter sought and received review by the Supreme Court. The Supreme Court agreed with and affirmed the Court of Appeal.

At issue before the Supreme Court, among others not discussed here, is the significant question or whether **permanent valuable improvements** to property are required to warrant the benefit of an Equitable Grace Period.

After review and analysis of multiple cases involving the Equitable Grace Period, and the Court's application of the relevant factors, the Supreme Court clarified that the Equitable Grace Period indeed requires a showing of inequitable forfeiture of **permanent valuable improvements** to property, if a grace period were not granted. The Supreme Court rejected the argument that Burbank's loss of crops was sufficient "inequitable forfeiture" to warrant the Equitable Grace Period, noting that "planting crops as part of routine farming operations does not constitute a valuable permanent improvement to property … here, the crops had already been in rotation prior to the execution of the lease. Therefore, Burbank's inability to reap its hay crop, while unfortunate, does not amount to an inequitable forfeiture." *Borton, supra,* 471 P.3d at p. 878.

The subject land was originally owned by Burbank Properties, LLC since 2012, and it was used to harvest potatoes and grow timothy hay, which is a two to three year crop. In 2016, Burbank sold the land to Borton & Sons, Inc. following financial troubles, for a below-market price of $1,550,000 subject to a three year "Lease and Option Agreement" in consideration of the below-market price. This agreement included a "time is of the essence" clause, and the lease option required Burbank to exercise the purchase option by December 31, 2017 via certified or registered mail.

Burbank planned to exercise the option to purchase, but did not meet the explicit deadline of December 31, 2017, and did not send notice via certified or registered mail. Instead, Burbank attempted to exercise the option to purchase by mailing notice of the same on January 4, 2018 via *regular* mail; Borton did not receive the notice until January 8, 2018 – approximately one week after the deadline. Borton thereafter refused to accept Burbank's untimely notice exercising Burbank's' option to purchase, and it demanded Burbank acknowledge the notice was untimely and the option was terminated. Burbank refused.

Borton sued Burbank for declaratory judgment that Burbank's option was terminated, to which Burbank counterclaimed, on the ground that the option remained open based on entitlement to an equitable grace period. The trial court ruled in favor of Burbank, allowing Burbank to purchase the land despite the untimely exercise of the option to purchase, with the Equitable Grace Period as Burbank's saving grace.

Borton appealed, arguing, among other grounds, that Burbank was not entitled to an equitable grace period, as an equitable grace period requires substantial improvements to property such that a lessee would suffer an inequitable forfeiture without a grace period. Division Three of the Court of Appeals reversed the trial court, in agreement with Borton, ruling that an equitable grace period requires permanent valuable improvements to property such that a lessee would suffer an inequitable forfeiture without a grace period granted, and Burbank did not make such a showing. The Washington Supreme Court affirmed the Court of Appeals, ultimately ruling in favor of landowner Borton and disallowing Burbank from exercising the option to purchase after being late to do so.

Holding

Specifically, the Supreme Court ruled that **entitlement to an equitable grace period may only be permitted upon a showing of inequitable forfeiture, including valuable permanent improvements made to property.** Burbank failed to demonstrate valuable improvements to property; therefore, it could not show inequitable forfeiture and thus was not entitled to an equitable grace period.

Takeaway

Only lessees who have made valuable permanent improvement to the land of another may benefit from the quiet but powerful Equitable Grace Period. Merely planting crops was not sufficient to be considered a permanent improvement.