

UM School of Law 2009 January CLE Series

Recent Developments Affecting Business and Estate Planning

by

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**I. Effective October 1, 2008: Model Registered Agents Act**

**A. Background.** Partnerships, limited partnerships, limited liability companies and corporations (including nonprofit corporations) are entities that all have provisions for registering agents under the statutes governing that particular type of entity. Foreign entities are also required to appoint a registered agent in order to qualify to do business in Montana. The registration of an agent serves several purposes.

1. Most importantly, **service of process** may be made upon the registered agent.
2. In certain situations, the location of the registered agent establishes **venue** for a legal action (such as MCA § 25-2-122, which provides that venue for a tort action against a foreign corporation may lie in the county in which the corporation's resident agent is located).

**B. Uniform Act.** In 2006 the National Conference of Commissioners on Uniform State Laws adopted the Model Registered Agents Act to provide the efficiency of one statute governing registration of an agent, no matter the kind of entity. The purposes of the Act are as follows:

1. To apply the same rules governing registered agents for all types of entities, including partnerships, limited partnerships, limited liability companies and corporations, rather than having separate statutes for each kind of entity;
2. To disregard the location of the office of the registered agent in determining where venue is to be laid in certain actions;
3. To standardize the form of annual reports to be filed by all types of entities.

The Montana legislature adopted the Model Registered Agents Act in 2007, **effective October 1, 2008**. It is codified at MCA §§ 35-7-101 et seq.

**C. Commercial Registered Agent.** Many entities use the services of commercial registered agents, i.e., a company whose business is to serve as the registered agent of corporations, limited

liability companies and other types of business entities. These commercial registered agents are especially used by larger corporations with activities in numerous states. Law firms also often provide the service of serving as the registered agent of their organizational clients.

1. The Act provides an **option** for persons or entities that serve as registered agents to register as a “commercial registered agent.” MCA § 35-7-106. Although registration as a commercial registered agent is optional and not mandatory, **there are many benefits to registering as a commercial registered agent** for those individuals or entities who do regularly provide registration services.

2. If an individual or entity registers as a commercial registered agent, it must file with the Montana Secretary of State a “listing statement” which provides the following information:

- a. For individuals, his or her name;
- b. For entities, the name, type and state of organization of the entity;
- c. The street or physical address of a place of business at which service of process and other notices and documents may be mailed or delivered. If the firm uses another addresses for a mailing address, the mailing address must also be provided.

The form provided by the Montana Secretary of State is attached as **Appendix A**. The filing fee is **\$150.00**. A list of commercial registered agents is maintained by the Secretary of State’s office at:

**[http://sos.mt.gov/business/Reg\\_Agents.asp](http://sos.mt.gov/business/Reg_Agents.asp)**.

3. If a business entity elects to use a “commercial registered agent,” it is simply required to provide the name of its registered agent in its organizational documents and any other documents in which it is required to designate a registered agent. **It is not required to provide the address of the commercial registered agent** (because the address is determined by referring to the commercial registered agent’s listing statement). MCA § 35-7-105.

- a. If the commercial registered agent subsequently changes its address, MCA § 35-7-110 requires the commercial registered agent update its address in its “listing statement” filed with the Secretary of State. The entities that use this particular commercial registered agent are not required to file a notice of the change of the registered agent’s address; the statement of change filed by the commercial registered agent is effective for each entity for which it serves as a registered agent. A person attempting to serve a business that uses a commercial registered agent ascertains the appropriate address for service by checking the directory of commercial registered agents maintained by the Secretary of State.

4. For commercial registered agents who have more than one physical location in Montana must select one of those locations as the address of record. All service of process and other notices will be delivered or mailed to the designated address, and no other. If a commercial registered agent wishes to maintain more than one office in a state where service of process will be received by it, it can accomplish that result by organizing separate entities to conduct its business in the state and filing separate statements for each entity.

5. A commercial registered agent may stop providing registration services by filing a termination statement. MCA § 35-7-107. The termination takes effect on the 31<sup>st</sup> day after the filing of the termination statement. The agent must promptly provide notice of the termination of its services to all entities represented by it.

a. MCA § 35-7-107 is intended to apply to “wholesale” termination of services by a commercial registered agent. MCA § 35-7-111 governs the resignation of service for a single client.

**D. Consent of Registered Agent.** Under MCA § 35-7-105, **it will no longer be necessary for the entity to obtain the signature of the registered agent consenting to act as such.**

Prior to October 1, 2008, the signature of a registered agent consenting to the appointment was required. See, for example, MCA § 35-1-313 (2007) (“unless the registered agent signed the document making the appointment, the appointment of a registered agent ... on whom process may be served is not effective until the agent delivers a statement in writing to the secretary of state accepting the appointment.”)

1. MCA § 35-7-105(2) provides that “the appointment of a registered agent ... is an affirmation by the represented entity that the agent has consented to serve as such.”

2. The statute, as adopted by Montana, requires the Secretary of State to notify any person who has been designated as a registered agent as soon as practicable of filings that contain the name of the registered agent. MCA § 35-7-105(3).

**E. Change of Registered Agent.** Under MCA § 35-7-108, an **entity** may change its registered agent by filing a “statement of change” signed on behalf of the entity with the Secretary of State. The notice must contain the name of the entity and the name and address of the new registered agent, if a non-commercial registered agent, and the name only of a commercial registered agent. In the alternative, the entity may file amended organizational documents naming a new registered agent.

1. The new registered agent does not have to sign the statement or amended organizational documents. The appointment is “an affirmation by the represented entity that the agent has consented to serve as such.”

2. The Act specifically states that the change does not need to be approved, for example, by shareholders or the board of directors of a corporation (or “governors” of any other type of entity).
3. The change in registered agent is effective upon filing of the statement of change with the Montana Secretary of State.

**F. Change in Name or Address of Registered Agent.** If a **registered agent** changes its name or its address, the procedures to be followed differ, depending upon whether the registered agent is a noncommercial or commercial registered agent.

1. Under MCA § 35-7-109, a noncommercial registered agent must file, for each entity the agent represents, a statement with the Secretary of State noting the name of the represented entity and, as applicable, the old and new name of the agent and the old and new address of the registered agent. In addition, the noncommercial registered agent must also promptly notify any entities that it represents.
2. For commercial registered agents, MCA § 35-7-110 permits a commercial registered agent to make a **single filing** that has the effect of changing the name or address of the agent for all of the entities represented by it.
3. MCA § 35-7-104 requires that the address of a registered agent must always be a geographic location (either a street address or a rural route with a box number). If the entity uses a different mailing address (such as a post office box), the mailing address must also be provided.

**G. Resignation of Registered Agent.** MCA § 35-7-111 allows a registered agent to resign **without the consent** of the represented entity. The agent must file a statement of registration that includes the name of the agent, the entity, a statement that the agent is resigning, and the name the person at the entity (and the entity’s address) to which the agent will provide notice of its resignation. The resignation is effective on the earlier of (1) the 31<sup>st</sup> day after filing, or (2) the appointment by the entity of a new registered agent. Notice of resignation must be promptly provided to the represented entity.

**H. Service of Process.** MCA § 35-7-113 confirms that a registered agent is an agent of the represented entity authorized to receive service of process or any notice or demand required or permitted by law to be served on the entity.

1. If an entity no longer has a registered agent OR if its registered agent cannot with reasonable diligence be served, the entity may be served in accordance “with any applicable judicial rules and procedures.”
  - a. Montana **did not adopt** the Model Act provision specifically allowing service by certified mail addressed to the governing body of the entity at its principal

place of business and if that fails, by delivering a copy to “the manager, clerk, or other person in charge of any regular place of business or activity of the entity if the person served is not a plaintiff in the action.”

b. Montana Rule 4D of Civil Procedure provides various methods of service upon domestic and foreign business entities, including but not limited to service upon a registered agent. Those procedures have not been amended by Montana’s adoption of the Model Registered Agent’s Act.

**I. Duties of Registered Agent.** Under MCA § 35-7-114, the only duties prescribed by the Act for registered agents are:

1. to forward to the represented entity at the address most recently supplied to the agent by the entity any process, notice, or demand that is served on the agent;
2. to provide the notices required by the Act to the entity at the address most recently supplied to the agent by the entity;
3. to keep current its name and address as required by the Act.

The registered agent may undertake additional duties by contract, but in that event those duties are determined outside of the Act.

**J. Jurisdiction and Venue.** MCA § 35-7-115 provides that “the appointment or maintenance in this state of a registered agent does not by itself create the basis for personal jurisdiction over the represented entity in this state.”

1. The Montana legislation adopting the Model Registered Agents Act amends several venue provisions under the existing business entity organic statutes to change venue for many types of organizational proceedings in a manner which disregards the address of the registered agent. For example, prior to October 1, 2008, MCA § 35-1-425 provided that a judicial proceeding to remove directors may be commenced either in the county where the corporation’s principal office is located, or, IF such office is not located within Montana, such proceeding may be commenced in the county where its registered office is located. As amended by the Model Registered Agent’s Act, if the corporation’s principal office is not located in Montana, the judicial proceeding to remove directors must be commenced in **Lewis & Clark County** (rather than the county where the registered agent is located).

**K. Effective Date.** The Model Registered Agent’s Act as adopted by Montana becomes effective **October 1, 2008**.

## II Low-Profit Limited Liability Companies (L3Cs)

**A. Background.** Federal tax law creates significant limitations on the activities of those 501(c)(3) organizations that are classified as “private foundations.” In an oversimplification of a very complicated statute, a private foundation is a 501(c)(3) charitable organization that receives most of its support from a single person, family, entity or other small group. IRC § 509(a). An example would be the Bill and Melinda Gates Foundation. Because of a requirement that private foundations distribute at least 5% of their net assets annually, many private foundations provide grants to other 501(c)(3) organizations.

1. IRC § 4943 provides for the imposition of tax on the “excess business holdings” of any private foundation.

2. IRC § 4944 imposes an excise tax each if a private foundation invests any amount in such a manner as to “jeopardize the carrying out of any of its exempt purposes.” The Code does not specify what kinds of investments those might be, but the legislative history suggests that what Congress primarily meant was simply investments that were unduly risky.

**B. Program-Related Investments.** Congress created an exception to the limitations on “excess business holdings” and “risky investments” by allowing private foundations to make “program-related investments” (PRIs). IRC §4944(c); Treas. Reg. § 53.4943-10(b); PLR 2007 09065. Treas. Reg. § 53.4944-3(a) defines a “program-related investment” as an investment which possesses the following characteristics:

1. The primary purpose of the investment is to accomplish one or more of the purposes described in section 170(c)(2)(B) of the Code;

2. No significant purpose of the investment is the production of income or the appreciation of property; and,

3. No purpose of the investment is to accomplish the purpose of attempting to influence legislation or to attempt to participate in, or intervene in, any political campaign on behalf of any candidate for public office.

Treas. Reg. § 53.4944-3(b) provides many examples of investments that would qualify as a PRI, including the following:

Example (6). X is a business enterprise which is owned by a nonprofit community development corporation. When fully operational, X will market agricultural products, thereby providing a marketing outlet for low-income farmers in a depressed rural area. Y, a private foundation, makes a loan to X bearing interest at a rate less than the rate charged by financial institutions which have agreed to lend funds to X if Y makes the loan. The loan is made pursuant to a program run by Y to encourage economic redevelopment of depressed areas, and no significant purpose involves the production of income or the appreciation of property. The loan significantly furthers the

accomplishment of Y's exempt activities and would not have been made but for such relationship between the loan and Y's exempt activities. Accordingly, the loan is a program-related investment.

**C. Low-Profit Limited Liability Companies.** In an attempt to provide a vehicle that would qualify as a “program related investment” for purposes of the tax code, greater minds than mine came up with a new hybrid entity that is quasi-business, quasi-nonprofit. The purpose of creating such entities is to provide a safe harbor from the “risky investment” excise tax and to provide an entity that would qualify in determining whether a private foundation has satisfied the requirement to distribute 5% of its net assets for charitable purposes.

1. Vermont adopted the first LC3C statute in 2008.
2. According to the January 15, 2009 edition of the Great Falls Tribune, the Crow Tribe in Montana has adopted an LC3C statute.
3. Rep. Deb Kottel from Great Falls has introduced HB 235 to provide for a Montana LC3C. It is scheduled for hearing before the Judiciary Committee this week.

**D. Requirements.** HB 235 requires a low-profit limited liability company to set forth in its Articles of Organizations a business purpose that satisfies the three requirements of a PRI as set forth above. Notably (and somewhat incongruously), the L3C must state that its primary “business” purpose is charitable as defined at IRC § 170(c)(c)(2)(B), and that it does not have as a “significant” purpose the production of income or the appreciation of property. Furthermore, it may not attempt to influence legislation).

1. The legislation clarifies that if a low-profit limited liability company in fact turns out to be profitable, and produces significant income or capital appreciation, such happy fact may not be treated, in the absence of other factors, as conclusive evidence of a significant intent to make produce income or appreciate property.

**E. Potential Uses of L3C.** Examples I’ve gleaned (from perusing the Internet) of potential uses of L3Cs include:

1. Nonprofits with some commercial activity could establish separate L3Cs for these commercial activities. For example, the Charlie Russell Museum in Great Falls could establish a separate L3C for the operation of its gift shop. This would allow the gift shop to either seek private investors, or a grant or loan from the a private foundation. This could draw increased business to the gift shop, which, in turn, would increase interest in the nonprofit museum, helping it educate a wider audience than it otherwise could reach.
2. A nonprofit with an environmental or health-related mission may be able to achieve its mission better with the development of a new technology (e.g. a new energy

conversion machine or a new medical device). A nonprofit could develop a L3C that would house the technology development part of its operations. This could attract investments in the development project, since a new technology could be commercially valuable. At the same time, the resulting technological developments could be used to help the nonprofit save more lives, improve more lives, or make the environment healthier in a way that would have been otherwise impossible.

### III. Recent Estate Related Cases

**A. In re Estate of Snyder, 337 Mont. 449 (2007).** Mrs. Snyder, the owner of Snyder Drug in Great Falls (which serves some of the best milkshakes you'll ever find) prepared a will devising the residue of her estate in equal shares to her two children, Lois and Neil, provided, however, "[f]ifty-one percent (51%) of my stock in [Snyder's, Inc.] . . . shall be first apportioned and set aside to make up the share of my total estate which shall go to my son, NEIL E. SNYDER." The will explained that "it is my will and desire that [Neil] have said business, or control of the corporate business as the case may be, but without ultimately diminishing the equal distribution of my estate to my two children, whom I hold in equal regard."

1. Daughter Lois first won an argument that what mom really meant was for Neil to receive ALL of the shares of Snyder's, Inc.; Lois did not want to be a 49% owner of a closely held corporation that paid her no salaries or dividends. 299 Mont. 421 (2000).
2. One of the other major assets of the estate was 40 acres in Flathead County, valued at \$160,000 when Mrs. Snyder died in 1992 (compared to the date of death value of \$190,000 for Snyder's Inc.) In preparing to distribute the assets, Neil, the personal representative, proposed to use current market values. He believed that the value of the Flathead land had increased to over \$1,000,000, and the stock in Snyder's Inc. had remained the same or even decreased in value since mom's death in 1992. Judge Neil agreed with the personal representative's proposed method of using current, rather than date of death, values for purposes of distribution. Relying on MCA § 72-3-902, which requires date of distribution values to be used in satisfying the homestead allowance and family allowance, and further provides that the residuary estate may be distributed in "any equitable manner," Judge Neil thought it most appropriate to use date of distribution values, or else Lois would end up with far more than 50% of the estate.
3. The Supreme Court disagreed with Judge Neil, and determined that the property should be distributed based upon date of death, rather than current, market values. The Supreme Court relied upon a provision of the will that would have governed in the event that Snyder's drug was not incorporated. In that event, Neil was to receive the unincorporated assets of the business, "subject to a charge in favor of my daughter, LOIS K. SNYDER, the amount necessary to give her a full one-half (1/2) of my total estate based upon the value thereof as finally determined for Federal Estate Tax purposes. . . ."

**Lesson learned:** Consider whether it is appropriate to include language in a will providing for the use of date of distribution values in making distributions.

**B. In re the Charles M. Bair Family Trust, 343 Mont. 138 (2008).** Prior to her death, Alberta Bair established a charitable trust. US Bank served as trustee, but a Board of Advisors was granted the power and authority to make charitable distributions from trust income. Upon Mrs. Bair's death in 1993, the trust was valued at \$23,500,000. After setting forth general charitable purposes, Section 6.2(3) of the trust, entitled CREATION OF THE CHARLES M. BAIR FAMILY MUSEUM, stated "the cherished aim and foremost desire" of the Bair sisters "to establish a museum which would perpetuate the historic and artistic significance of the Charles M. Bair Ranch and the people associated with it." This provision further directed the Board of Advisors to "devote Grantor's entire residence, together with all personal property of lasting historical and artistic value located therein, and together with surrounding grounds and outbuildings necessary for such purpose, to the establishment of a museum to be named the Charles M. Bair Family Museum which shall be open for the educational benefit of the general public."

1. After opening the museum in 1996, the Board of Advisors decided to close the museum in 2003 due to their concerns over the conditions of the home, including lack of appropriate security systems, air control systems, fire protection systems, and handicapped access facilities.
2. The trustee filed a petition seeking a determination of whether the Board of Advisors had the authority to terminate operation of the museum. The district court interpreted the foregoing language as **precatory**, and did not require the establishment of the museum.
3. The Supreme Court disagreed, stating that the "Trust Agreement provides a clear directive to the Board to create the Museum and provides the Board with direction and guidance on how to proceed." The Court also ruled that the Trust Agreement clearly established a priority for the museum over general philanthropy.
4. The Supreme Court further ruled that "The Board breached its duty to administer the Trust according to the trust instrument and breached its duty to administer the trust with the 'care, skill, prudence, and diligence' of a prudent person when it failed to install a fire-prevention system, failed to install a proper air-handling system, failed to maintain an appropriate security system, and when it failed to build additional structures for the Museum." As a remedy, the Board was directed to recognize the museum as the priority of the trust, and make the necessary expenditures to improve, maintain and operate the museum. No compensatory damages were assessed against the Board.

**C. Wells Fargo Bank, N.A. v. Kaml (In re Will of Dunham), 343 Mont. 240 (2008).** Mr. DeWitt established a trust under his will, with income payable primarily to his daughter Mary Ann during her lifetime, and remainder to his grandchildren. Upon the "stern instruction" of Mary Ann, Wells Fargo invested almost exclusively in bonds to maximize income. On two

separate occasions, the remaindermen consented to the investment of 100% of the trust assets into bonds, but the trustee did not explain the disadvantages of this investment strategy to them. In 1995, the trustee presented its Fourth Accounting of the trust to the District Court for approval, encompassing a lengthy period of managing the trust assets from 1978 to 1995. Prior to the hearing, the trustee's attorney provided notice to the grandchildren of the hearing, advising that they could attend the hearing, but that their presence was not required. The notice contained no explanation about the nature of this proceeding or the implications of failing to attend.

1. The court approved the trustee's accounting for the period 1978 to 1995, which clearly set forth the investments, income and expenses of the trust.
2. In February 2006, more than 10 years after the order approving the trustee's accounting for the period 1978 through 1995, two of the grandchildren filed a motion, pursuant to M. R. Civ. P. 59, seeking a new trial on the District Court's approval of the accounting. The District Court granted the motion.
3. The Supreme Court affirmed the motion allowing a new trial, based upon the MCA § 25-11-102(4):

The former verdict or other decision may be vacated and a new trial granted on the application of the party aggrieved for any of the following causes materially affecting the substantial rights of such party:

(4) newly discovered evidence material for the party making the application which he could not, with reasonable diligence, have discovered and produced at the trial....

The Court found that it was "apparent that the Bank engaged in misrepresentations and/or inadequate advisements to [the remaindermen] about their rights and interests under the trust."

4. With regard to the trustee's argument that the remaindermen's motion for a new trial, made eleven years after the District Court's order, was untimely, **the Court ruled that all trust beneficiaries must receive notice of entry of judgment approving an accounting as "indispensable parties," even if they fail to appear.** Because the remaindermen had not received notice of entry of judgment, their motion was timely.
5. The trustee also argued that the claim was barred under MCA § 72-34-511(1)(a), which provides:

If a beneficiary has received an interim or final account in writing, or other written report, that adequately discloses the existence of a claim against the trustee for breach of trust, the claim is barred as to that beneficiary unless a proceeding to assert the claim is commenced within 3 years after receipt of the

account or report. An account or report adequately discloses existence of a claim if it provides sufficient information so that the beneficiary knows of the claim or reasonably should have inquired into the existence of the claim.

The Court remanded this issue to the District Court. The Court stated that if the trustee engaged in fraud, the District Court should refuse to apply the statute of limitations or the doctrine of laches.

6. The trustee also relied upon the proof of notice provisions of MCA § 72-35-206, which provides:

If it appears to the satisfaction of the court that notice has been regularly given or that the party entitled to notice has waived, the court shall so find in its order. When the order becomes final, it is conclusive on all persons, whether or not in being.

The Court rejected this argument on the basis that the order had not become “final” or “conclusive,” because the time for appeal had not expired due to the failure to provide notice of entry of judgment to the remaindermen.

**Lesson Learned:** In addition to sending notice of a hearing approving a trustee’s accounting to all trust beneficiaries, you also need to send **a notice of entry of judgment to all** trust beneficiaries upon the court’s approval of the accounting (including any trust beneficiaries who failed to appear).

**D. In re Estate of Strange, 343 Mont. 296 (2008).** The decedent was a resident of Arizona at the time of his death and had never resided in Montana, but visited his son on occasion and stored fishing gear and tools at the son’s home in Billings. The son, under a power of attorney, also managed a investment account for the decedent with a national investment firm, apparently using the son’s address as the address of record for the account. The son, who was named as personal representative of the decedent’s will, filed an application for informal probate in Yellowstone County. The decedent’s widow objected, arguing that the Montana district court lacked jurisdiction, and that venue was improper.

1. Judge Gustafson determined that venue was not proper in Montana because the decedent’s Montana assets did not establish a "significant connection" to Montana. She also observed that Montana would be an inappropriate forum since Arizona's elective share laws would apply to Rose's share of John's estate. Accordingly, the District Court granted Rose's motion to dismiss on the basis of venue.

2. On appeal, the Supreme Court overruled the District Court’s opinion that venue was not proper. The Court relied upon MCA § 72-3-112, which provides

(1) Venue for the first informal or formal testacy or appointment proceedings after a decedent's death is:

(b) if the decedent was not domiciled in this state, in any county where property of the decedent was located at the time of his death.

3. The Court ruled that the property located in Montana does not have to have a "significant connection." The Court noted that "contrary to the rule in civil actions, there is no 'single forum' requirement under the Uniform Probate Code," and that the personal representative could open an ancillary probate proceeding in other jurisdictions as necessary (which will be necessary since a Montana court does not have jurisdiction over the decedent's real property located in other states).

**E. In re Estates of Swanson, 2008 MT 224.** In a criminal proceeding, Jeanette Swanson, who lived near Augusta, pled guilty to deliberate homicide in the shooting deaths of her two children. The investigative report revealed that Jeanette suffered from a severe mental disorder; she stated that she had to kill the children in order to protect them from someone who wanted to harm them. The children's father subsequently sought a ruling that Jeannette would not be able to inherit from the children's estates, under MCA § 72-2-813(2), which provides:

An individual who feloniously and intentionally kills the decedent forfeits all benefits under this chapter with respect to the decedent's estate, including an intestate share, an elective share, and omitted spouse's or child's share, a homestead allowance, exempt property, and a family allowance. If the decedent died intestate, the decedent's intestate estate passes as if the killer disclaimed the killer's intestate share.

1. The District Court's order summarily denied Jeanette the right to inherit by treating her guilty plea as **conclusive evidence** that she "feloniously and intentionally" killed her children.

2. The Supreme Court ruled that a guilty plea (as distinguished from a verdict of guilty at the conclusion of a bench or jury trial) is not **conclusive** evidence of the "felonious and intentional" elements. The Supreme Court based its ruling on the following rationale:

When a criminal defendant enters a plea of guilty to the charge of deliberate homicide, the issues of whether a killer acted with intent and whether the killing was felonious are not "established" through litigation. By contrast, when a defendant undergoes a bench or jury trial, these elements are proven beyond a reasonable doubt. A guilty verdict establishes these elements, but a guilty plea does not. Thus, a guilty verdict has a conclusive effect for the purposes of the slayer statute that a guilty plea does not.

3. The personal representative also argued that a conclusive presumption of Jeanette's intent existed under MCA 72-2-813(7), which provides:

After all right to appeal has been exhausted, a judgment of conviction establishing criminal accountability for the felonious and intentional killing of the decedent conclusively establishes the convicted individual as the decedent's killer for purposes of this section.

The Court disagreed, noting that this section's purpose is to establish that a killer may be barred civilly from inheriting under this statute even if he or she was **acquitted** in a criminal proceeding. Its application was limited to "those cases where, as a result of litigation, a conviction has established a killer's criminal responsibility for the felonious and intentional killing of another."

4. The court noted that on remand, the personal representative has the burden of proof that Jeanette acted "intentionally" and "feloniously." In giving guidance, the Supreme Court stated that "feloniously" "refers to a killing that is wrongful, that is without legal excuse or justification;" the term "is not limited to the definition of 'felony' set forth in § 45-2-101(23), MCA, but includes all killings 'done with a mind bent on doing wrong.'" The Court further noted that "if a killer is 'insane' at the time he killed, the killing is not felonious in the contemplation of the slayer's rule."

**F. In Re Estate of Haugen, 346 Mont. 1 (2008).** Mr. Haugen died in 1998. His wife, Audrey, was appointed as his personal representative, and informal probate proceedings were opened in Fergus County in 1998. Mr. Haugen's estate was subsequently closed in 2000, and Audrey was appointed as trustee of the Haugen Trusts established under Mr. Haugen's will. Mr. Haugen's two daughters were also named as beneficiaries of the trust. In 2007, they brought a new proceeding in Fergus County against Audrey for mis-management of the trust, whose value had decreased by approximately \$1,000,000. They sought to remove her as trustee, and have themselves named as successor trustees in accordance with the terms of the trust. Audrey filed a petition in the closed probate proceeding, seeking appointment of a corporate trustee.

1. The daughters filed a motion to dismiss Audrey's petition in the 1998 probate proceeding for lack of subject matter jurisdiction, and a motion for substitution of Judge Phillips. Judge Phillips concluded that Audrey's verified petition was properly filed under the original probate because it dealt "with issues pertaining to both the probate of the estate and the administration of the trusts. The District Court has concurrent jurisdiction over matters pertaining to both the probate and the administration of the trusts pursuant to § 72-35-101(2)(c), MCA." Judge Phillips also denied the motion for substitution, since it was not filed in 1998.

2. The Montana Supreme Court ruled that the district court sitting in probate lacked subject matter jurisdiction. Audrey was not attempting to re-open the probate proceedings or re-litigate any probate matter; she was seeking relief under the Trust

Code. Therefore, the district court sitting in probate lacked subject matter jurisdiction to preside over her petition to have herself removed as trustee.

**Lesson Learned:** Don't use an old probate case to fight a new battle, unless the battle clearly and directly relates to a probate matter, such as fraud of the personal representative.

#### IV. Recent Cases on Covenants Not to Compete

**A. MCA § 28-2-703.** Montana has adopted statutes strictly prohibiting “any contract by which anyone is restrained from exercising a lawful profession, trade, or business of any kind,” MCA § 28-2-703. A copy of the Montana statute is attached as Appendix B.

1. An exception is provided for covenants not to compete negotiated in the context of the sale of the goodwill of the business, and in the context of a dissolution of a partnership. MCA § 28-2-704, 705.
2. Even then, covenants not to compete are restricted to the city or county where the principal office of the business is located, and any adjacent counties (or cities located therein), and only for so long as the purchaser continues the business.

**B. Early Enforcement of Statute.** In many early cases, the Montana Supreme Court strictly enforced the statutory prohibition against covenants not to compete. For example, in 1978, the Court refused to enforce a covenant not to compete that prohibited an insurance salesman from directly or indirectly selling insurance for a period of five years after termination of his employment, or from soliciting any customers of the employer. J.T. Miller Co. V. Madel, 575 P.2d 1321 (Mont. 1978).

**C. Soliciting Former Clients.** The strict prohibition against covenants not to compete in the context of employment agreements was softened in Dobbins v. Rutherford, 708 P.2d 577 (Mont. 1985). In that case, employee accountants could were allowed to compete with their employer after termination of their employment, but if they provided any accounting services to the clients they had met through their prior employer, the departed accountants were required to pay a fee equal to 100% of the fees which the employer had billed to that client in the 12 months prior to termination of employment. The Montana Supreme Court ruled that this was not a restraint on the plaintiffs' exercise of a profession; the departed accountants could still practice as accountants. They just had to pay a fee for any of the employer's clients to whom they had previously provided services. However, the court ruled that an “indirect” restraint such as this must be reasonable by meeting the following criteria: (1) limited in operation as to time or place; (2) based on some consideration; (3) reasonable protection for the employer; and (4) not unreasonable burden upon employee or public. The Court upheld the restraints as reasonable.

**D. Non-Disclosure Agreements.** The prohibition against covenants in an employment context further crumbled in 1989. In State Medical Oxygen Supply, Inc. v. American Medical Oxygen Co., 782 P.2d 1272 (Mt. 1989), the employees agreed in their employment agreement

“not to divulge, disclose or communicate to any person . . . any information concerning . . . business of State Medical Supply or its trade secrets and/or customer lists.” The court ruled that a **non-disclosure agreement** is not a restraint on trade, and will be enforceable if reasonable under the Dobbins criteria.

**E. Further Departures.** Ms. Curl worked for a company named Montana Cincha, Inc., located in Absarokee, Montana. Montana Cincha's business almost exclusively involved finishing products for another company, Montana Silversmiths. When Montana Cincha was acquired by Montana Mountain Products (MMP), Ms. Curl signed a new employment agreement that contained the following clause:

Curl acknowledges a duty of loyalty to MMP and agrees to refrain from competing with MMP during the term of her employment with MMP. Curl further agrees to refrain from competing with MMP following the termination of her employment with MMP for a period of 3 years within a 250 mile radius of any MMP location. Competition means providing subcontract labor for Montana Silversmiths or any other customer of MMP and/or reproducing MMP's designs or products placed in development or production during Curl's employment with MMP for wholesale and/or retail distribution.

When Ms. Curl started working for a competing company in 2002, which supplied products to Montana Silversmiths, MMP sought to enforce her covenant not to compete. The district court, relying on MCA §28-2-703, granted Ms. Curl's motion for summary judgment. MMP then appealed to the Montana Supreme Court. Montana Mountain Products v. Curl, 327 Mont. 7 (2005).

1. Rather than confirming the district court's reliance on the clear prohibition of restraints against trade as set forth in MCA §28-2-703, the Montana Supreme Court broadly stated that the District Court should have applied the reasonableness test to covenants not to compete entered into outside of the context of a sale of goodwill or dissolution of a partnership.
2. The Court then reviewed Curl's covenant and refused to enforce it not because of the absolute prohibition set forth in MCA §28-2-703, but because the covenant was unreasonable.

**G. January 2008 Case.** Our most recent guidance on the issue of the enforceability of covenants not to compete in an employment context is found in Access Organics v. Hernandez, 341 Mont. 73 (2008). An employer hired Andy Hernandez to sell organic produce. Four months after employment started, the employer insisted that Andy sign an agreement “not to directly or indirectly compete with the business of the Company and its successors and assigns during the period of employment and for a period of two years following termination of employment.” The agreement also contained a non-disclosure agreement, preventing the employee from disclosing the employer's trade secrets or other confidential information. The employer subsequently terminated Hernandez's employment due to financial difficulties, and

Hernandez started a competing business with another ex-employee. Access Organics brought suit to enforce the non-compete and non-disclosure agreements signed by Hernandez.

1. After noting the statutory language of MCA §28-2-703 which appears to be an absolute prohibition of covenants not to compete outside of the sale of a business or dissolution of a partnership, the Court went on to say “we have upheld agreements which impose reasonable restrictions on trade.” The court enunciated the following test:

“To be upheld as reasonable, a covenant not to compete must meet three requirements:

(1) [I]t must be partial or restricted in its operation in respect either to time or place;

(2) it must be on some good consideration; and

(3) it must be reasonable, that is, it should afford only a fair protection to the interests of the party in whose favor it is made, and must not be so large in its operation as to interfere with the interests of the public.”

2. The court added that because MCA §28-2-703 strongly disfavors restraints on trade, such agreements are strictly construed, and the employer has the burden of proof to establish their reasonableness. Because the agreement was signed after employment had commenced, the Court found that there was inadequate consideration, and refused to enforce the agreement on that basis.

## V. Recent Cases on Easements

A. **Easements in General.** Montana recognizes four types of appurtenant easements. An **appurtenant easement** is an easement that burdens one piece of land (the **servient estate**) for the benefit of another adjacent or near-by parcel (the **dominant estate**). In contrast, an **easement in gross** burdens a servient estate, but does not benefit a dominant estate. For example, a conservation easement burdens a particular piece of land, but benefits the public in general or a specific conservation group, and not any specific adjacent property. The four types of appurtenant easements recognized in Montana are:

1. **Express easements:** an easement created by **grant** or **reservation** in a deed or other written document of conveyance. Express easements may also be created, in appropriate circumstances, by **references** in deeds or other written documents of conveyance to recorded certificates of survey or plats that clearly depict the easement.

2. **Easement by necessity:** an easement that arises by **operation of law** when a single tract of land in **common ownership** is **severed** into two or more parcels with separate ownership, and the severance creates a **strict necessity** for an easement for access.

3. **Implied easement:** an easement that arises by **operation of law** when a single tract of land in **common ownership** is **severed** into two or more parcels, and prior to the severance there is an **existing use** (such as a roadway or irrigation ditch) that was **apparent** or reasonably discoverable. In addition, the parties must have **intended for the use to continue**, and continuation of the use is **reasonably necessary** in order for the transferee to use the acquired land.

4. **Prescriptive easement:** an easement that arises by **operation of law** under the principles of **adverse possession**. The claimant must establish a use that is open, notorious, continuous, and adverse (not permissive) for a period of five years.

**B. Blazer v. Wall, 2008 MT 145 (2008).** This case arising out of Flathead County is a “**must-read**” for all lawyers who draft express easements. In 1979, two co-owners of a tract of land subdivided the land into seven tracts as described on Certificate of Survey No. 4446 (“COS 4446”). The Certificate of Survey depicted an easement across two of the tracts, as follows:

Mr. Davis acquired Tracts 1 and 4, and used the 30-foot-wide easement for accessing (a) the western part of Tract 4 and (b) other property he owned to the south and west of Tract 4 (as denoted by the dotted lines that continue to run off Tract 4).

1. In 1987, Mr. Davis conveyed Tract 1 to Mr. and Mrs. Lockman. The deed did not specifically include language “**reserving**” an easement. Instead, the deed described the land being conveyed as “Tract 1 of Certificate of Survey No. 4446, SUBJECT TO 30 foot road easement as shown on Certificate of Survey No. 4446, records of Flathead County, Montana.”

a. The first issue addressed by the court was whether an express easement had been reserved by this 1987 conveyance from Mr. Davis to the Lockmans, in view

of the **lack of specific language of reservation**. The court confirmed that although the verbage “**subject to**” is **insufficient** in and of itself to create an easement, because the deed **referred** to a **recorded certificate of survey** on which an easement was “**adequately described**,” the easement could not be defeated on the grounds that words of “grant” or “reservation” were not used. ¶ 51. This is referred to as the “easement by reference” doctrine.

b. The court did not indicate that the filing of certificate of survey alone is sufficient to create an easement, even though the survey may depict the easement. The certificate of survey must be incorporated by reference into a deed or other document of conveyance.

**Lesson Learned:** In creating easements by grant or reservation, always use either the word “grant” or “reserve” as appropriate.

2. Through a series of subsequent transfers, the Wahlders acquired Tract 1; appellant Wall is a trustee of a trust to which the Wahlders conveyed the land. The appellee, Mr. Blazer, ultimately acquired the western portion of Tract 4, as well as lands south and west of Tract 4 that had been owned by Mr. Davis at the time the Certificate of Survey was filed. Mr. Blazer determined that the Wahlders had **built improvements** encroaching onto the 30' easement across Tract 1. He filed an action seeking a declaration that he had an express easement for ingress and egress purposes along the northern and western boundaries of Tract 1, and an injunction requiring the Wahlders to remove the structures built upon the easement.

a. Although the easement depicted on Tracts 1 and 4 had not been used by Mr. Wall or his predecessors for several yeras, mere non-use of an express easement is not sufficient evidence of an intent to abandon. There must be evidence of an intentional relinquishment of an express easement. Although an express easement may be extinguished by adverse possession (including acts of constructing improvements across an easement), the requisite 5-year period had not been established in this case.

3. Mr. Wall wanted to use the easement to access lands he had acquired that were adjacent to Tract 4.

a. As a general rule, **appurtenant** easements may be used for the benefit of the dominant estate only. For example, if Ann benefits from an easement across Lot 1 for access to Lot 2, she can only use the easement for access to Lot 2, and not for additional land she may acquire that is adjacent to Lot 2.

b. The district court allowed evidence from Mr. Davis explaining the parties' intent to create an easement that benefitted not only Tract 4, but his adjacent lands.

- c. The Supreme Court unanimously agreed that the “grantor’s intent to reserve an easement for the benefit of particular land must be clearly and unmistakably communicated and not left to inference, implication, or extrinsic evidence.” Because the property adjacent to Tract 4 was not clearly identified as a dominant estate that was intended to benefit from the easement, the reference in the Davis-Lockman deed to COS 4446 did not create or reserve easement rights to the lands adjacent to Tract 4. ¶ 54.
- d. This requirement serves a **notice** purpose. The grantee of the servient estate must have **notice** not only of the existence of the easement, but of the easement’s scope and purpose.
- e. The court further ruled that it was inappropriate for the district court to have allowed testimony from Mr. Davis clarifying the parties’ intent as to the property benefitted by the easement. ¶ 48.

**Lesson Learned:** The instrument by which an easement by express grant is created should describe with reasonable certainty the dominant and servient estates. A reservation of an easement is not operative in favor of land not described in the conveyance.

4. The most controversial aspect of the opinion is whether the easement depicted on COS 4446 was enforceable by Mr. Wall to establish access to Tract 4. In a 4-3 split, the majority (Nelson, Gray, Cotter and Rice) determined that the easement depicted on COS 4446 was insufficient to create an easement for the benefit of Tract 4, because it was not sufficiently clear from the certificate of survey whether the easement was intended to burden Tract 1 for the benefit of Tract 4, or burden Tract 4 for the benefit of Tract 1 (and the other tracts depicted on the certificate survey).

- a. Had the deed from Mr. Davis to the Lockmans clearly stated that Mr. Davis was “reserving an easement” rather than “subject to an easement,” the court could have found an intent that the dominant estate was Tract 4 retained by Mr. Davis. The court found that the “subject to” language was insufficient to determine whether the easement was reserved to benefit Tract 4, or granted by Mr. Davis for the benefit of Tract 1 or other tracts reflected on the survey.
- b. The majority refused to allow extrinsic evidence to clarify the parties’ intent.
- c. The dissenting justices (Morris, Leaphart and Warner) noted that it was sufficiently evident from the certificate of survey, combined with the “subject to” language in the deed, that the easement was for the purpose of providing access across Tract 1 to Tract 4.

***Lesson Learned:*** Make sure that you clearly identify the estate intended to be benefitted (dominant estate) and the estate intended to be burdened (servient estate) in every express easement that you draft.

**C. *Our Lady of the Rockies v. Peterson*, 342 Mont. 393 (2008).** In another 4-3 decision involving an express easement, the Montana Supreme Court ruled that the non-profit organization, Our Lady of the Rockies (OLR), did not have the right to develop a road to a proposed tramway to its 90-foot-high statue overlooking Butte. The case involved three parcels, ownership of which was originally acquired through the issuance of patents from the federal government for placer claims under the General Mining Act. OLR was required to cross one of the parcels (now subdivided and owned by the defendants/appellants) to reach its parcels, on which it intended to build the tramway station and other improvements. In its current condition, the road is paved at its entrance to the appellants' lots, then becomes a 12-foot wide dirt road as it traverses across the four private lots, finally reaching a metal gate at the fourth landowner's property. Thereafter, it is an unmaintained, single-track lane across the two parcels owned by OLR. OLR filed suit in Silver Bow County, seeking a declaratory judgment that the road depicted on surveys referenced in the patents is a public road (rather than a private access easement), 60 feet in width, and available for public use.

1. The district court granted summary judgment to the plaintiffs, holding that a public road was created by express reservation in the mineral survey completed for defendants' placer claim. The district court noted that various surveys and maps over the last century identified the road, and at times referred to it as "public."

2. In reversing the district court's opinion, Justice Nelson wrote:

"Past, present and future generations of Montana landowners have the right to be secure in the knowledge that they will not wake up one morning to find that a community or organization has decided to build a 60-foot-wide public highway through their back yards, based on nothing more than a surveyor's notation of a 6-foot-wide dirt road on a 115-year-old mineral survey."

3. Although there was debate as to whether state or federal law should apply, the Court concluded that the result would be the same under both. Beginning with federal law, the Court acknowledged that the Cobban Placer patent (conveying the land currently owned by the defendants) identified the land being granted as "that certain PLACER mining claim and premises, designated by the Surveyor General as Lot No. 4200," and that U.S. Mineral Survey No. 4200, with all its notes, lines, descriptions, and landmarks, is a part of the Cobban Placer patent as if such descriptive features were written out upon the face of the patent itself, including the road depicted across the Cobban Placer claim. However, the court ruled that the reference in the Cobban Placer patent to Mineral Survey 4200 did not reserve a **public road** over the Cobban Placer under federal law.

4. Alternatively, the plaintiffs asserted that under current state law, the public road easement across defendants' placer was created by express reservation through reference to a plat or certificate of survey describing the easement. After a lengthy discussion of the state law development of the "easement by reference" doctrine, the court made two rulings:

a. "First, we have only recognized the creation of *privately*-held easements under our easement-by-reference cases. We have never applied the doctrine to create a public road, and we decline to do so under the circumstances presented here." ¶ 61.

b. "Second, as explained above, the intent to create the subject easement must be clearly and unmistakably communicated on the referenced plat or certificate of survey using express language. Here, however, there is no label or other express language on MS 4200 communicating an intent to reserve the depicted road as a "public" road. Nor is there any evidence in the field notes or in the Cobban Placer patent itself of an intent on the part of the federal government to reserve a public road across the Cobban Placer. The label "ROAD" on MS 4200 is not sufficient under any of our cases to create an easement in favor of the public." ¶ 62.

**D. Nelson v. Barlow, 342 Mont. 93 (2008).** In 1990, Nelson purchased Tract 1 of a subdivision located on Flathead Lake. Nelson's deed includes the language: "TOGETHER WITH roadway easement as shown on Certificate of Survey No. 4377 *for access to Lot 8* of Cedar Hills Subdivision." In 1996, Barlow purchased Lot 8, which was unimproved at the time. Barlow's deed contained no reference to any easements. In 2004, Barlow began the process of building a cabin on Lot 8. Nelson and several other property owners in the subdivision filed suit against Barlow, seeking to enjoin him from building on the lot. Nelson alleged that the easement language in his deed provides access across Lot 8 to Flathead Lake. The other plaintiffs alleged that Barlow had orally agreed that they could cross Lot 8 to access the Lake.

1. The district court granted Barlow's motion for summary judgment to dismiss the claims. With regard to Nelson's claim, the district court ruled that the deed was not ambiguous and that "access to Lot 8" provided access to Lot 8, but not across, over or through the lot to access the lake. Only Nelson appealed to the Supreme Court.
2. The Montana Supreme Court disagreed with the district court, finding "access to Lot 8" was ambiguous, especially in view of the fact that Nelson already had access to Lot 8 via the road, so there was no reason to include a specific provision in his deed granting him such.
3. However, the Supreme Court upheld the district court's dismissal of Nelson's complaint on other grounds. Barlow had no notice of the easement. He was not a party to Nelson's deed, and the easement was not recorded in Barlow's in Lot 8's chain of title. "It is not enough for an encumbrance to be recorded in the chain of title of an easement's dominant estate. In order for the landowner of the servient estate to be bound, the encumbrance must also be found in the servient estate's chain of title." Furthermore, the recorded subdivision plat contained no reference to an easement across Lot 8 for lake access, nor was there other evidence that Barlow had knowledge of such an easement. At least one of these would have to be established in order to put the defendant on sufficient notice that his property was burdened by an easement.

***Lesson Learned:*** Always record an easement against the servient estate.

**E. *Waters v. Blagg*, 2008 MT 451.** This case involved an implied easement. The parties all own land in the east half of Section 17, as indicated below:

To access their parcels, the parties use a U.S. Forest Service Road until it reaches a private road on the Waters land, and then they cross the Waters land to reach their own parcels. All of the parties' parcels were originally owned by a single landowner, WH Field & Company. Field Co. conveyed each of the parcels at issue between 1964 and 1976, but failed to effectively reserve or grant easements for the benefit of any of the properties it conveyed. At the time Field Co. purchased its interest in Section 17, the network of roads on the property had been utilized exclusively for logging purposes. In 1996, Blagg began to harvest rocks from his property. Waters objected on several grounds to the use of the road for commercial operations. Waters argued that there was no implied easement, and that if there were, the use of the road for commercial rock harvesting exceeded the scope of the easement.

1. The court confirmed the district court's ruling that an implied easement existed, noting that the three requirements of an implied easement had been met:
  - a. the tracts at issue must have been severed from common ownership;
  - b. the use that exists on the servient tract must be apparent, continuous, and reasonably necessary for the beneficial use and enjoyment of the dominant tract at the time of severance; and
  - c. the parties must have intended the use to continue after division of the property.
2. The scope of an implied easement is controlled by the apparent intent of the landowner who effected a severance of the dominant and servient estates. At the time the parcels were severed, the road was being used for commercial logging operations. The Court considered "not only the actual uses being made at the time of the severance, but also to such uses as the facts and circumstances show were within the reasonable contemplation of the parties at the time of the conveyance." ¶ 22. The scope of an easement by implication is not permanently frozen at the time of severance, but rather it is measured "by such uses as the parties might reasonably have expected from future uses of the dominant tenement." *Ibid.* The Court concluded that exploitation of natural resources was contemplated at the time the easement was created, including rock harvesting. The Court also noted that the burden imposed by the rock harvesting traffic (16,000 pounds loaded weight per truck) was less than the burden imposed by commercial logging (80,000 pounds loaded weight per truck).
3. The Supreme Court remanded to the district court for a determination of whether the rock harvesting activities constituted a nuisance.

**VI. Stream Access.** Montana cherishes and protects the rights of its residents to recreate, especially on water. Montana also cherishes and protects the property rights of landowners. Unsurprisingly, these two values often clash. As noted by the Montana Supreme Court, "[t]he real property interests of private landowners are important as are the public's property interest in

water. Both are constitutionally protected. These competing interests, when in conflict, must be reconciled to the extent possible.” *Galt v. Montana*, 225 Mont. 142, 148 (1987).

**A. Laws Regarding Ownership of Waters and Submerged and Adjacent Lands.** Several statutes govern **ownership** surface waters and the lands lying underneath them. Ownership depends in part upon whether a body of water is navigable or non-navigable.

1. The state owns all **surface waters** for the benefit of the people. These waters are subject to appropriation for lawful uses. Mont. Const., Art. IX, §3.
2. The state owns all **lands below the low-water mark** of a **navigable lake or stream**. The adjacent land-owner owns property down to the low-water mark of the navigable lake or stream. MCA § 70-1-202; MCA § 70-16-201.
  - a. Although a landowner on a navigable stream owns down to the low-water mark, since 1933 Montana’s “angler statute” has allowed fishermen to go along the banks up to the high-water mark for purposes of fishing. MCA § 87-2-305. This is the first statute to address the conflict between “recreational rights” of water users and the property rights of adjacent landowners.
3. The landowner owns the land underlying a non-navigable lake or stream, to the center of the lake or stream.
  - a. Based upon this statute, in the early case of *Herrin v. Sutherland*, 74 Mont. 587 (1925), the Montana Supreme Court had upheld the right of the owner of the streambed of a non-navigable stream to exclude recreational users.
4. For purposes of title (versus use), whether a body of water is navigable or not is determined as of the date of Montana’s statehood (1889). Federal law applies to determine navigability for purposes of title. *Montana Coalition for Stream Access v. Curran*, 210 Mont. 38 (1984). Waters are navigable if they are “navigable in fact,” meaning those waters “used or *susceptible of use*, in their ordinary condition, as highways for commerce, over which trade and travel are or may be conducted in the customary modes of trade and travel on water.” *Id.*, citing the U.S. Supreme Court’s decisions in *The Daniel Ball*, 77 U.S. 557 (1870) and *The Montello*, 87 U.S. 430 (1874). The Montana Supreme Court adopted the “log-floating test” to determine navigability for title purposes. *Curran*, 210 Mont. at 44.

**B. Development of Recreational Use Doctrine.** The seminal case addressing the tension between landowners and surface water users is *Montana Coalition for Stream Access v. Curran*, 210 Mont. 38 (1984).<sup>1</sup> Mr. Curran, who owned both sides of land alongside the Dearborn

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<sup>1</sup>See also the companion case involving a non-navigable stream, the Beaverhead River, Mont. Coalition for Stream Access, Inc. v. Hildreth, 211 Mont. 29 (1984).

River, stretched several fences across the Dearborn's streambed that impeded recreational use by fishermen and floaters. Neither Mr. Curran nor his employees were very kind to floaters who scrambled on-shore to portage around the fences.

1. Mr. Curran contended that the Dearborn is a non-navigable river, and as the landowner of the streambed, Mr. Curran had the right to exclude others from using the streambed, in accordance with Herrin v. Sutherland, 74 Mont. 587 (1925).
2. The court determined that the section of the Dearborn crossing Mr. Curran's land was navigable, because it had been used to float logs on up to five occasions in 1887-89. As a result, Mr. Curran did not own the streambed of the Dearborn.
3. More importantly, relying upon the Montana Constitution (Art. IX, §3 -- all surface waters are the property of the State for the use of its people) and the **public trust doctrine**, the Court ruled that "any waters that are capable of recreational use may be so used by the public *without regard to streambed ownership or navigability for nonrecreational purposes.*"
  - a. If a water is capable of recreational use, the public has right to recreate on them, including *the right to use the streambed* as necessary to exercise the recreational use. The public's right to use the waters and underlying streambeds applies *up to the high water mark*. Thus, this ruling effectively imposes an easement in favor of the public upon a riparian landowner's property rights. Even though a landowner owns to the middle of a non-navigable lake or stream, the public can use the streambed as necessary to recreate. Even though the landowner owns to the low-water mark of a navigable lake or stream, the public can use the land up to the high-water mark as necessary to recreate.
4. The Court also ruled that where there is an obstruction, such as a fence, the public has the right to portage across private property **above the high water mark** "in the least intrusive manner possible."
5. The Court cautioned that its opinion should **not** be construed "as granting the public the right to enter upon or cross over private property to reach the State-owned waters hereby held available for recreational purposes."

**C. Legislative Response.** In its 1985 session, the Montana legislature enacted the Montana Recreational Stream Use Act, MCA §§ 23-2-301 et seq, which provides that all surface waters capable of recreational use may be used by the public without regard to the ownership of the land underlying the waters. **Lakes** are specifically excluded from the application of the Act. Public use of surface waters, lake beds and lake banks will be determined by further judicial interpretation of the public trust doctrine.

1. “Recreational use” includes fishing, hunting, swimming, floating, other pleasure activities and “related unavoidable or incidental uses.”
2. “Surface water” is defined to include **natural water bodies** (other than lakes), their beds and banks up to the ordinary **high water mark**.
3. The legislation grants a right of portage above the high water mark around artificial barriers in the “least intrusive manner.” MCA § 23-2-311 establishes a procedure that requires landowners to bear the expense of constructing portage routes around artificial barriers.
4. The legislation specifically allows several types of activities on “Class I” (navigable) waters, including overnight camping and construction of duck blinds, moorages and other seasonal objects between high water marks so long as not within sight of or 500 yards of an occupied dwelling. Certain types of big game hunting are also allowed on Class I waters. However, these uses are not allowed without landowner permission on non-navigable (“Class II”) waters.

**D. Galt v. Montana, 225 Mont. 142 (1987).** Jack Galt and other riparian landowners challenged the constitutionality of several portions of the Montana Recreational Stream Use Act. The Supreme Court clarified parts of the Curran decision:

1. “The public has a right of use up to the high water mark, *but only such use as is necessary to utilization of the water itself.*” The public doesn’t have the right for its recreational use to be as convenient, productive and comfortable as possible.
2. The rights of the public must be narrowly confined so that the impact to beds and banks owned by private individuals is minimal.
3. The Court struck down as unconstitutional the provisions allowing overnight camping and duck blinds between the high water marks of Class I (navigable) waters, as well as the provisions allowing big game hunting.
4. The Court struck down as unconstitutional the provisions requiring landowners to bear the cost of constructing portage routes.
5. The statute **has never been amended** to remove those portions ruled to be unconstitutional. The unconstitutional provisions remain on the books.

**E. Bitterroot River Protective Ass'n v. Bitterroot Conservation Dist., 346 Mont. 507 (2008).** The Montana Recreational Stream Use Act provides access for recreational use to both navigable and non-navigable streams and rivers capable of recreation. However, only those streams and rivers that constitute “a **natural water body**” (including its bed and its banks up to the ordinary high-water mark). MCA § 23-2-301(12). MCA 23-2-302(2)(c) further prohibits

“the recreational use of waters while diverted away from a natural water body for beneficial use pursuant to Title 85 [governing water rights], except for impoundments or diverted waters to which the owner has provided public access. For example, you can’t go fishing or water-skiing on the Greenfield Irrigation Districts’ irrigation canals.

1. The Mitchell Slough is located in Ravalli County, Montana, east of the Bitterroot River between Hamilton and Stevensville. Tucker Headgate diverts a large volume of water from the East Fork of the Bitterroot River into the Mitchell Slough. The Slough flows across private property for approximately 16 miles, through a series of diversions, weirs, and excavations at a higher elevation than the Bitterroot, before rejoining the Bitterroot River. Approximately 4,300 acres are irrigated from the Mitchell’s flow every season.

2. The District Court concluded that without man-made diversions of water into the East Fork of the Bitterroot River and then into the Mitchell Slough by Tucker Headgate, and without the water contributions from irrigation wastewater and return flows along the pathway of Mitchell Slough, the Mitchell Slough would not sustain a natural, perennial flow, and thus was not a “natural water body” for purposes of the Montana Recreational Stream Use Act.<sup>2</sup>

a. The District Court applied a Webster’s Dictionary definition of “natural” as “arising from; in accordance with what is found in nature; not artificial or manufactured.” The court concluded that the Mitchell does not fall within this definition. The court noted that the Mitchell may have been a natural water body at some point in the past, but that it is “no longer a natural water body” because the Bitterroot River has, by natural processes, migrated away from and below the elevation of the Mitchell, and the Mitchell itself has been extensively manipulated to ensure a continued, substantial flow. The court reasoned that yearly maintenance at Tucker Headgate and “massive amounts of channel work” have changed the Mitchell enough that it “can no longer be considered a natural channel even though some portions of the channel are still in identifiable historic locations.”

3. The District Court required the parties to meet “the burden of persuasion as to each fact the existence or nonexistence of which is essential to the claim for relief or defense he is asserting,” MCA § 26-1-402, by imposing the burden of preponderance of the evidence on each side. The Supreme Court found no error in the District Court’s

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<sup>2</sup>Another issue in the case is whether the Mitchell Slough was a natural, perennial-flowing stream under the 310 Law, which requires stream “projects”—physical alterations or modifications—to be pre-authorized by a conservation district. MCA §§ 75-7-101 et seq.

requirement that appellants prove their claim that the Mitchell Slough was a natural water body by a “preponderance of the evidence.”

4. The Supreme Court ruled that “whether the Mitchell is a natural water body for purposes of the SAL is ultimately a conclusion of law.” ¶ 70. In interpreting the statute, the Court recognized the additional duty of interpreting the “to implement the objectives that the Legislature sought to achieve.” ¶ 71.

5. The Court noted that almost all Montana rivers have been altered by man to some degree, and thus rejected the District Court’s dictionary-based definition, “which essentially requires a pristine river unaffected by humans in order to be deemed natural.” ¶ 72.

6. The Court stated that whether a stream is “natural” is a fact intensive inquiry. An important fact was that the Mitchell flows perennially, whether in or out of irrigation season, and that the Mitchell’s flow increases during its course. The Court determined that the District Court erred in determining that it could not consider as “natural” the increase in the Slough’s flow added by irrigation return flows. The Court also noted that the presence of fish, although not determinative, is a fact to be considered in the determination of a stream’s naturalness. The Court concluded that although the Slough was “man-improved,” it was not “man-made,” and was a natural body of water. “[W]hile the Mitchell has been improved primarily by irrigators, it is much more than an irrigation ditch.” ¶ 82.

**F. Access to Streams Via Bridges.** The Supreme Court has repeatedly emphasized that the public’s right to use surface waters for recreational use is not the equivalent of a right to access the streams across private property. A user must access a stream through a public access site or with permission of a landowner. In many locations, counties have constructed bridges across rivers on county roads. Although county roads typically include a 60' right of way, counties often allow landowners to fence up to or underneath the county bridges to control livestock. Depending upon the steepness of the slope and other factors, the fences may impede or obstruct the public’s ability to use the right-of-way to access the river.

1. A Montana Attorney General's Opinion in 2000 (48 A.G. Op. 13) held that the use of a county road right-of-way to gain access to streams and rivers is consistent with and reasonably incidental to the public's right to travel on county roads and that the public may gain access to streams and rivers by using the bridge, its right-of-way, and its abutments/

2. A recent district court case involved the public’s right to access the Ruby River from three county roads. Fences built, with the permission of the County, by adjacent landowners (including apparently unpopular James Cox Kennedy, an heir to the Cox Communications empire) extended along each county road to the ends of each bridge.

The public has crossed the fences (all wooden) to reach the Ruby River from the county roads.

3. The Public Lands Access Association, Inc. contended that the fences are "encroachments" into the 60-foot public right of way, and must be removed. The Association contended that the use of electric fences and high wooden fences at the three bridges was done in a manner that went beyond controlling or keeping cattle in but to keep the public out. The landowners contended that the public has sufficient access to the Ruby River at designated state fishing access sites, and that the public is not entitled to use county road rights-of-way to access streams. Landowners also argued that the 60-foot right-of-way narrowed at the bridge to the width of the bridge.

4. Citing the county's authority to "maintain, control, and manage county roads and bridges within the county," MCA § 7-14-2101 (1)(a)(i), the district court found that the county had authority to allow landowners to construct fences to the ends of bridges for appropriate reasons, including livestock control. Thus, the bridges were not an encroachment and did not have to be removed.

5. The district court rejected the landowner's theories that the 60' right-of-way narrowed to the width of the bridges as they crossed the river. Thus, the public right of way maintains at a width of 60' across the river. Although the district court's decision did not explicitly state as much, the result is that the public has the right to cross the fences to reach the river.

a. Because one of the public roads was acquired through a prescriptive easement, the issue of the width of the easement as to that particular bridge was to be determined at trial.

6. Representative VanDyk has introduced H.B. 190 to provide a legislative response to the issue of stream access from county bridges.

a. The legislation clarifies that fences that abut bridges are not encroachments and are not required to be removed.

b. The legislation confirms that a person may gain access to surface waters for recreational use by using a public bridge, its right-of-way, and its abutments; or a county road right-of-way. The person using the right-of-way must stay within the width of the right-of-way.

c. Perhaps the most controversial provision: each fence attached to or abutting a county road bridge edge, guardrail, or abutment for must provide for public passage to surface waters for recreational use. Suggested forms include a gate, stile or walk-over. An administrative procedures is provided if a dispute arises as to the appropriate method to allow public passage. The Department of

Transportation must provide the materials, installation, and maintenance of any fence modifications necessary to provide public passage.

## VII. Nuisance Cases

**A. Tarlton v. Kaufman**, 2008 MT 462. Nuisance claims developed at common law to protect the right of a property owner to the use and enjoyment of her land (versus the right to exclude that is protected by a trespass action). Nuisance law places certain limits on how a property owner can use her property. Under the maxim *sic utere tuo ut alienum non loedas*, no one may make an unreasonable use of her property to the material injury of the interests of an adjacent property owner.

1. In recognition that there are certain annoyances we all must put up in society, the majority of courts have ruled that a nuisance must be **unreasonable** and give rise to a **significant harm** in order to give rise to liability or injunctive relief. The majority of courts engage in a balancing test, weighing the utility of the conduct against the gravity of the harm.
2. The majority of jurisdictions have refused to allow a nuisance action to lie against a neighbor whose buildings or other improvements interfere with his light, air or view. For example, in *Fontainebleau Hotel Corp. v. Forty-five Twenty-five, Inc.*, 114 So. 2d 357 (Fla. App. 1959), the court refused to enjoin a hotel from building a new 14-story edition that would block the sun from hitting the neighboring hotel's beach for a substantial part of the afternoon. American courts have long expressed concern that recognition of prescriptive rights to light, air, and view would retard development of vacant land.
3. Similarly, a vast majority of jurisdictions have refused to allow a nuisance action to lie against visually offensive uses of land. For example, in *Wernke v. Halas*, 600 N.E.2d 117 (Ind. App. 1992), the defendant constructed a "privacy fence" that included vinyl strips, orange plastic construction fencing, and license plates. The defendant also mounted a toilet seat atop a post overlooking the plaintiff's land. The court denied plaintiff's request for relief, holding that "it is well-settled throughout this country that, standing alone, unsightliness, or lack of aesthetic virtue, does not constitute a private nuisance." *Id.* at 122.
  - a. The court expressed its concern that aesthetic values are "inherently subjective." A yard full of plastic pink flamingos may be art to one person and junk to another, and courts shouldn't get involved in making those determinations.
  - b. Visually offensive uses are better regulated through ordinances and restrictive covenants.

4. Although few courts grant relief for visually offensive uses of property, where a property owner erects a “spite fence” or other structure for the sole, or at least primary, purpose of annoying a neighbor, a court will grant relief.

5. The Tarltons and Kaufmans owned neighboring parcels of land near Lolo. Neighborly relations began to deteriorate when the Tarltons constructed large lights in their yard, which interfered with the Kaufman’s hobby of viewing stars and caused Mrs. Kaufman to move out of her bedroom to get some sleep. Tarltons also maintained a pond that spanned their two properties, further angering Mr. Kaufman. In 2006, the Kaufmans built a 20' high chain link fence on top of a 6' berm for a length of 270' between their property and the Tarltons, and covered the fence with dark material. The Tarltons brought a law suit.

a. In Count I, the Tarltons claimed that the fence was a nuisance. The Tarltons alleged that the fence destroyed the aesthetic value of their property, that it reduced the value of their property, that it destroyed their view, and that it was an eyesore.

b. Count II of the complaint sought a declaratory judgment that the Kaufmans’ fence was a spite fence.

c. The Kaufmans counterclaimed that the Tarltons’ yard lights constituted a nuisance, stating that the lights “unreasonably interfere[d] with the Kaufmans’ pursuit of their hobbies, disturb[ed] wildlife in the area and interfere[d] with the Kaufmans’ general use and enjoyment of their property.”

d. The jury returned a verdict that the Kaufman’s fence did not constitute a nuisance and was not a spite fence. The jury also concluded that the Tarltons’ mercury vapor lighting did not constitute a nuisance.

6. On appeal, the Montana Supreme Court (in a 5-2 decision) determined that the jury had not been properly instructed as to what constitutes a nuisance under Montana law. The jury instruction included the following statement:

“Generally, a structure or condition cannot constitute a nuisance merely because it is unsightly or because it obstructs a party’s view.”

The Court agreed with the Tarltons that the Montana statutory definition of nuisance contains no such limitation, and that they had been prejudiced by the limitation contained in the jury instruction. MCA § 27-30-101(1) broadly defines nuisance to include “[a]nything which is injurious to health, indecent or offensive to the senses, or an obstruction to the free use of property, so as to interfere with the comfortable enjoyment of life or property.... ”

7. The Court affirmed the district court's decisions to exclude evidence that the fence violated local building codes and to deny a jury view of the property in this case.

## VIII. Homeowner Associations

**A. Eastgate Village Water and Sewer District Assoc. v. Davis, 2008 MT 141.** In 1978, the Lewis and Clark County Commission created a rural special improvement district to construct and install parks, streets, and a water and sewer system for the Eastgate Village subdivision. The non-profit Eastgate Village Water and Sewer District Association was formed and agreed to undertake the responsibility for the maintenance, repair and operation of the water and sewage systems within the district, which provided water to over 600 homes. The Articles of the Association provided that “[e]very person or entity who is a record owner of a fee or undivided fee interest in any Lot within the subdivision, including contract sellers, shall be a member of the Association.”

1. In the summer of 2003, in response to drought conditions, the Association's governing board instituted temporary water restrictions limiting the days that Eastgate residents could water their lawns in order to preserve sufficient water pressure for drinking, household uses, and fire suppression. The Association's governing board also voted to ban the drilling of private wells within the subdivision to avoid the possibility of cross-contamination of the drinking water supply.

2. In 2004, Mr. and Mrs. Davis, who owned a home in the district and who were members of the Association, arranged for a contractor to drill a well on their property for lawn and garden irrigation purposes. They filed a well completion report with the DNRC, which subsequently issued a Certificate of Water Right allowing usage of up to 35 gpm, not to exceed 10-acre feet per year. The well was drilled into the same aquifer used by the Association. The Association filed suit to declare the well ban valid and enforceable after Mr. and Mrs. Davis refused to abide by an Association demand to cease using the well.

3. The Davises argued that an association's power over the property of residents within a subdivision must come from the restrictive covenants for that subdivision. The Davises noted that the restrictive covenants for the Eastgate subdivision do not prohibit private wells or specify that the sole source of water for residents of Eastgate is the Association's system, nor do the covenants even contemplate the existence of the Association.

4. The district court granted summary judgment in favor of the Association, finding the well ban rule valid and enforceable and ordering the defendants to permanently abandon their well. The Montana Supreme Court affirmed. Every member of the subdivision is a member of the Association, and each landowner is in a contractual relationship with the Association and bound by the Association's rules. As members, the Davises are entitled to all the benefits of membership but also subject to the obligations of membership. The

rule banning private wells was directly related to the Association's responsibility to protect Eastgate's water system. The private well posed a threat of contamination of the subdivision's water supply, and of depletion of the aquifer used by the Association for Eastgate's watering needs. Therefore, the ban was reasonable in light of the Association's duty to preserve Eastgate's water supply.

## **IX. Takings**

**A. Seven Up Pete Venture v. Schweitzer, 523 F.3d 948 (9<sup>th</sup> Cir. 2008), cert. denied 2008 U.S. LEXIS 5613.** Plaintiffs purchased six leasehold interests in state-owned mineral estates in 1991, planning to extract gold and silver through open-pit and cyanide leaching mining operations. Although the plaintiffs engaged in discussions with the State regarding their pending permits and began environmental review, no permit was issued for the projects. In 1998, the citizens of Montana passed ballot initiative I-137, which banned cyanide leach mining, with a grandfather clause for any mining operating as of the date the initiative was passed. Plaintiffs thereafter filed suit against the governor of the State of Montana and the director of the Montana Department of Environmental Quality in both federal and state court, claiming I-137 and the state's refusal to issue a permit after its passage effectuated a taking of their property, as no other mining processes would "allow economically viable production of the gold and silver" in the project.

1. The federal district court stayed the plaintiffs' Fifth Amendment takings claims, finding those claims not ripe for review until plaintiffs exhausted their state court claims. In 2005, the Montana Supreme Court granted summary judgment for the state on the Fifth Amendment claims, holding that the plaintiffs were not entitled to a mining permit as a matter of law with or without I-137, and therefore could not demonstrate the loss of a vested property right. The federal district court thereafter reopened the case and dismissed the claims on grounds of 11<sup>th</sup> Amendment immunity; and alternatively, that the claims were barred by issue preclusion in light of the state court's decision.
2. The appellate court upheld the district court, confirming that the claims against the Montana state officials were barred by 11th Amendment sovereign immunity. "[The State] enjoys sovereign immunity in the federal courts from [a] federal takings claim..." Because it confirmed the district court's judgment on this ground, the appellate court did not reach the question of issue preclusion.

**B. Kafka v. Mont. Dep't of Fish, 2008 MT 460 (decided December 31, 2008).** Appellants, owners and operators of elk farms, brought takings claims against the State of Montana and the Department of Fish, Wildlife & Parks under the Fifth Amendment to the U.S. Constitution and Article II, Section 29 of the Montana Constitution. These claims alleged that the enactment and enforcement of initiative I-143 (approved by the citizens of Montana on November 7, 2000), constituted a taking of their private property and that they were entitled to just compensation for this taking. In a 4-3 decision, the Montana Supreme Court affirmed the Twelfth Judicial District Court's denial of their takings claims.

1. As explained by the Court: I-143 “did not revoke appellants’ Licenses, nor did it result in the confiscation of their alternative livestock. Instead, I-143 prohibited game farm operators from charging a fee to shoot alternative livestock. This was a significant departure from the previous scheme because some individuals were willing to expend significant amounts of money to shoot alternative livestock within the confines of a Game Farm. By prohibiting fee-shooting, I-143 eliminated the most profitable use of the alternative livestock, and thus the profitability of Game Farms in Montana.” ¶ 7.

2. The majority affirmed the district court’s conclusion that the Licenses were privileges and not compensable property interests under the Fifth Amendment of the U.S. Constitution, or Article II, Section 29 of the Montana Constitution. ¶ 54.

3. Appellants also argued that I-143 constituted a “taking” of their intangible business interests, including goodwill and going-concern value, alleged a taking of their intangible business assets because I-143 eliminated the in-state market for fee-shooting, prohibiting them from operating their business to allow fee-shooting, a significant source of their income. The Court ruled that the District Court had “correctly recognized that takings claims for goodwill and going-concern value have never been recognized in the regulatory taking context. The unique circumstances required to assert a taking of these intangible assets, namely a physical condemnation of some sort by the State, are not present in this case.” ¶ 63.

4. The Court then turned to appellants’ claim that I-143 constituted a taking of their alternative livestock and real property interests. The Court first concluded that there had been no “categorical” taking; there had been no physical condemnation or occupation of appellants’ real or personal property. Although the value of their livestock had diminished significantly, it nonetheless retained economic value. Thus, *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003 (1992) (which found a taking when the plaintiff’s coastal lot was rendered entirely valueless as a result of restrictive regulations) was not the appropriate standard.

a. Prior to I-143, the Kafkas received approximately \$5,000 to \$6,000 per head of alternative livestock; after I-143 that figure was reduced to \$1,700 to \$1,800. ¶ 84.

5. The Court then applied the “Penn Central” standard to determine if the “regulatory” taking was compensable. *Penn Central Transportation Co. v. New York City*, 438 U.S. 104, (1978) sets forth three factors to consider in determining whether a regulation goes so far as to constitute a taking, including (a) the character of the governmental action; (b) the extent to which the regulation has interfered with distinct investment-backed expectations; and (c) the economic impact of the regulation on the claimant. ¶ 69.

6. In discussing the game-farm owners' reasonable expectations, the court noted that none of the appellants had reported taxable profit on their tax returns for the years their game farms were in operation, and thus their economic loss was not significant. The Court cited with approval the district court's acknowledgment that appellants' had expectations of profit, but noted "their subjective expectation of profit must be legally tempered by the objective reality that they were engaged in a highly regulated and speculative new industry." ¶ 74.

7. Regarding the character of the government's action, the Court noted that I-143 "prohibited only one use of the alternative livestock—i.e., charging a fee to shoot them—and that otherwise appellants maintained all their rights and property interests in the alternative livestock." As a result, I-143 left appellants "free to make other economically viable use of their property, removing only one potential use that has been validly deemed to be injurious to public health, safety, and welfare." ¶ 75.

a. The Court also noted that I-143 served a legitimate state interest, insofar as it promoted Montana's hunting heritage, protected wild game populations from the spread of disease and hybridization, and thus generally protected the sport of hunting in Montana. ¶ 18.

8. The Court upheld the district court's ruling that appellants were not entitled to compensation under the Penn Central test.

9. The Court came to the same conclusion in a companion case out of the First Judicial District, *Buhmann v. State*, 2008 MT 465. The court further ruled in *Buhmann* that the district court did not err in reserving to itself, rather than a jury, the question of whether the State was liable for an uncompensated. The Court also concluded that the district court had not erred in applying federal law, because plaintiffs had failed to establish that the Montana constitution's protection was greater than that afforded by the federal constitution.

**Appendix A**  
**Listing Statement**

**Appendix B**  
**Montana Statutes on Covenants Not to Compete**

**28-2-703. Contracts in restraint of trade generally void.** Any contract by which anyone is restrained from exercising a lawful profession, trade, or business of any kind, otherwise than is provided for by 28-2-704 or 28-2-705, is to that extent void.

**28-2-704. Exception -- sale of goodwill of business**

(1) One who sells the goodwill of a business may agree with the buyer to refrain from carrying on a similar business within the areas provided in subsection (2) so long as the buyer or any person deriving title to the goodwill from him carries on a like business therein.

(2) The agreement authorized in subsection (1) may apply in:

- (a) the city where the principal office of the business is located;
- (b) the county where the principal office of the business is located;
- (c) a city in any county adjacent to the county in which the principal office of the business is located;
- (d) any county adjacent to the county in which the principal office of the business is located; or
- (e) any combination of the foregoing.

**28-2-705. Exception -- dissolution of partnership.** Partners may, upon dissolution of the partnership, agree that one or more of them may not carry on a similar business within the areas provided in 28-2-704(2).