

Unrecorded Leases Not Automatically Voided by Indiana's Recording Statute

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Indiana statute provides that leases for a period exceeding three years must be recorded within 45 days of execution, lest they be deemed void as against any subsequent purchaser, lessee, or mortgagee "who acquires the real estate in good faith and for valuable consideration." See Ind. Code § 32-31-2-2. Given a recent decision from the Indiana Court of Appeals, however, new or prospective real estate owners should be cautioned against concluding that such unrecorded leases can automatically be voided as a matter of law.

Commercial Coin Laundry v. Park P, LLC, 934 N.E. 2d 142 (Ind. Ct. App. 2010) involved a dispute between the new owner of an apartment complex and the pre-existing lessee operator of on-site laundry facilities. As you might suspect, the lessee's ten-year lease was unrecorded. After negotiations for an amended lease agreement stalled, the new owner filed a lawsuit in which it requested that the unrecorded lease be declared void as a matter of law. The trial court concluded that the plain language of the statute justified the owner's request, and the lease was declared void in an order of summary judgment.

The lessee appealed and argued that the statute only operated to protect *bona fide* purchasers or, in other words, purchasers without notice of the rights of pre-existing lessees. The Court of Appeals agreed with the lessee's suggested proposition that the statute does not automatically void unrecorded leases, and continued its analysis by discussing how it is that a purchaser of property might be charged with knowledge of a pre-existing lease. The Court discussed that such knowledge obviously arises constructively where a properly recorded lease appears in the chain of title. Because the lease was not recorded, the Court focused on whether the new owner actually knew, or should have known, of the lease when it purchased the property.

The Court essentially concluded that a new owner of real estate will be charged with actual knowledge of a pre-existing lease if the owner has any knowledge to justify an inquiry that would reveal the lease. If the new owner should inquire but does not, the owner is charged with all facts that would have been revealed through reasonable inquiry. Perhaps most importantly, the Court referenced a statement from the Indiana Supreme Court that "one who fails to examine land which he is about to purchase, and to inquire as to the rights of one in possession, is not acting in good faith and will not be treated as a bona fide purchaser." See *Mishawaka, St. Joseph Loan & Trust Co. v. Neu*, 209 Ind. 433 (1935).

In the *Commercial Coin Laundry* case, the lessee/coin laundry operator had placed large signs on the walls of the laundry room and labels on each of the laundry machines stating that they were owned and operated pursuant to a written lease. Because that equipment was

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present when the property was purchased, the Court ruled that the lease could not be automatically voided as a matter of law.

In our experience, parties commonly fail to record leases exceeding three years. The moral of *Commercial Coin Laundry*, however, should be that prospective or new purchasers of real estate should not deem such failure as automatic license to void unfavorable leases. And they certainly should not purchase real property based upon the assumption that the existing tenant can easily be dispossessed. For example, it seems that adequate signage and/or operations will arguably justify the sort of inquiry and, consequently, notice of an existing lease that will spare it from being voided by the statute.

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