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Restrictive Covenants As a Land-Use Tool

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Restrictive covenants and other limitations on the use of real property can play an important role in development—and can have significant implications for the value of the land subject to these kinds of restrictions.

One of the key issues to consider when contemplating the purchase or development of a parcel of property is whether a restrictive covenant "runs with the land" and therefore is binding on subsequent owners. The rules relating to that issue were discussed recently by the Court of Appeals in *328 Owners Corp. v. 330 W. 86 Oaks Corp.*[1]

The case involved a five-story townhouse in Manhattan, constructed around 1900, that served as an eight-unit multiple dwelling. The property came into municipal ownership through an in rem tax foreclosure proceeding; at the time, it had many municipal code violations and was in a deteriorated condition and in need of rehabilitation.

New York City, through the Asset Sales Program of the Department of Housing Preservation and Development (HPD), decided to sell the building as an Urban Development Action Area Project. It offered the occupant tenants the right of first refusal to purchase the property at an appraised value of $340,000 based on the capitalization of its income, contingent on the tenants agreeing to remove all city code violations and hazardous conditions, and maintaining the existing tenants' rent at its then-current amount for two years.

The tenants submitted a letter to HPD offering to purchase the premises and formed a corporation, 330 West 86 Oaks Corp. for the purpose of taking title to the property. After a public hearing, the City Council directed that the property be sold.

The deed conveying the property to Oaks Corp. recited that the project consisted "solely of the rehabilitation or conservation of existing private or multiple dwellings or the construction of one to four unit dwellings without any change in land use permitted by existing zoning." The habendum clause referenced Oak Corp.'s duty to remedy all building violations of record within six months and to maintain existing tenants' rents at a fixed rate for two years. It also declared that the agreements and covenants set forth in the deed "shall run with the land and shall be binding to the fullest extent permitted by law and equity."

Oaks Corp. apparently never corrected the code violations but instead sold the building to another company, 330 West 86th Street, LLC, for at least $1 million.[2] This new owner allegedly planned to demolish the building and develop a high-rise "sliver" apartment building in its place. The owners of an adjacent building, which shared a party wall with the building, brought suit seeking a declaratory judgment that the deed restricted the use of the land and that the new owner and any successors or assigns had to act within those constraints. The parties moved for summary judgment.

Manhattan Supreme Court ruled in favor of the plaintiff and declared that the building "may not be used other than for (a) rehabilitation or conservation of the existing building thereon, or (b) construction of one to four unit dwellings without any change in land use."

The Appellate Division, First Department, in a divided opinion, reversed and held that there was no intent by the original parties to the deed that the covenant run with the land nor did it touch and concern the land. The case reached the Court of Appeals, which reversed and reinstated the Supreme Court's order and judgment.

The Court of Appeals explained that when a deed declares that a restrictive covenant will run with the land, it must comply with three conditions to be enforceable against successors-in-interest:

(1) it must appear that grantor and grantee intended that the covenant should run with the land;

(2) it must appear that the covenant was one "touching" or "concerning" the land; and

(3) it must appear that there was "privity of estate" between the promisee or party claiming the benefit of the covenant and the right to enforce it, and the promisor or party who rested under the burden of the covenant.

In examining these conditions, the Court found that the parties' intent to restrict the use of the property was clear from the deed's "multiple references" to the Urban Development Action Area Project's requirements and from the inclusion, within the habendum clause, of an explicit provision stating that "agreements and covenants…shall run with the land."

It added that the low appraisal value and exemption from both competitive bidding and a time-consuming land-use review were directly related to the city's intent to restrict the use of the land for the purposes of the completion of the project. The purchase price alone was indicative of the parties' intent, the Court found, noting that HPD had appraised the property's value based on its current

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income in its current state and did not calculate the potential income stream for a possible use of the land with a high-rise building, which HPD could have realized had it sold the building on the open market without restriction.[3]

The Court also found the second condition, that the covenant touched and concerned the land, to be met. Although the requirements of offering renewal leases and correcting code violations were finite in nature, they also were relevant to the economic development of the property, the Court observed.

It added that the requirement that the project be completed within a reasonable time appeared to be "merely a reflection of prudent business practices" and was not meant to restrain the ongoing duty to conserve, rehabilitate or reconstruct within the constraints of the deed and the Urban Development Action Area Project.[4]

Finally, the Court ruled that the privity of estate factor had been met as there existed a "direct chain of title" running from the city to Oaks Corp. to 330 West. Accordingly, the Court held that the building's land use ran with the land.[5]

Time Constraints

The plaintiff in *328 Owners Corp.* was able to bring a successful action, but parties need to keep in mind that there may be time limits within which actions must be brought or be barred.

For example, *Bailey v. Chernoff*[6] involved a planned unit development located in the City of Saratoga Springs that had been sponsored by Homeland Development Corporation, which sold parcels subject to a filed "Covenants and Declarations of Restrictions," as well as the bylaws of the Regatta View Homeowners Association.

During a July 2004 open meeting of the association's board of directors, the owners of a waterfront parcel applied for permission to build a boathouse on their property. While the development's original covenants and restrictions did not specifically identify boathouses as being prohibited, the board was unsure whether the application could be granted and indicated that Homeland Development would be contacted about an amendment that would unambiguously permit boathouse structures within the subdivision, subject to architectural review by the board.

Although several homeowners were present at the meeting, no objections were recorded. Thereafter, on Oct. 8, 2004, Homeland Development amended the covenants and restrictions to permit boathouses.

In April 2005, the City of Saratoga Springs approved the homeowners' request to construct a boathouse and issued a building permit. Construction began in May 2005. Neighboring homeowners whose property adjoined that property first noticed work being done on the project in June 2005. They consulted legal counsel in late August 2005, who inspected the boathouse with one of the plaintiffs on Aug. 30, at which point it "looked to be complete from all outward appearances."[7]

The neighbors brought an action in November 2005, claiming the boathouse was erected in violation of the covenants and restrictions because Homeland Development allegedly lacked the authority to, among other things, issue the October 2004 amendment. The trial court concluded that the defendants' affirmative defense of laches was meritorious, and the plaintiffs appealed.

The Third Department declared that even assuming that the plaintiffs were correct in contending that the amendment to the development's covenants and restrictions to permit boathouses was improper, restrictive covenants "will not be enforced in inequitable circumstances, such as…where the party seeking enforcement is guilty of laches." It agreed with the trial court that laches applied, noting that during the July 2004 open meeting of the board, all homeowners in the development were given notice of the defendants' intention to build a boathouse on their property and that, in addition, the plaintiffs were on notice after construction of the boathouse began yet did not seek a preliminary injunction and, instead, waited until after construction was completed to commence their action.[8]

The appellate court also found that the record supported the defendants' assertion that they were unaware that the plaintiffs intended to commence a suit against them because they had never received any objection or complaint from them prior to, during or upon completion of construction of the boathouse, and that the defendants would be severely prejudiced if forced to tear down the boathouse after allegedly expending approximately $125,000 for its construction.[9]

Draft Carefully

Restrictive covenants should be carefully drafted to ensure that they cover what is intended—no more, no less.

Earlier this year, the Supreme Court, Suffolk County, issued a decision in *Censi v. Cove Landings Inc.*[10] that illustrates how carefully (and narrowly) courts interpret restrictions in deeds.

The case was a proceeding pursuant to RPAPL Article 15 to determine the right, title and interest to a parcel of real property comprising a portion of Fish Cove Road in the Town of Southampton.

Three different sets of parties asserted that they owned and, therefore, had the sole right to determine whether utilities could be laid thereunder. The dispute arose over the interpretation of a provision in a deed that stated that it was "RESERVING to and subject to the right of the grantor and others to pass and repass over and upon Fish Cove Road." The nonmunicipal defendants argued that that language granted them the right to lay utilities under their right of way. Specifically, they claimed that the conveyance gave them the right to unobstructed passage and also such rights "incidental or necessary to the enjoyment of such right of passage."

The court found that the right of ingress and egress did "not entitle defendants to lay utilities" but merely granted the holders of that right "unobstructed passage over the roadway." Interestingly, the court also ruled that although Fish Cove Road had become a public highway pursuant to Highway Law §189 because it had been maintained by the Town of Southampton for a period in excess of 10 years, including the installation of traffic control signs and plowing, used by the public, and listed in the town's inventory of roads, that declaration did not entitle the non-municipal defendants to lay utilities under the road without the express permission of the plaintiffs as fee owners of the roadbed.

Conclusion

When they are enforceable, restrictive covenants certainly can affect the value of property[11] as well as the potential uses of property. Owners and purchasers should pay careful attention to the terms of deeds to make sure they are aware of any restrictions that might affect their property in the event it is transferred or they seek to develop it.

1. 8 N.Y.3d 372 (2007).
2. According to a footnote in the Court of Appeals' decision, Oaks Corp. may have sold the property to 330 West for $2.25 million. 8 N.Y.3d at 379, fn. 4.
3. 8 N.Y.3d at 383.
4. 8 N.Y.3d at 384.
5. 8 N.Y.3d at 384. The Court further noted that current or future owners could seek to extinguish the land use restrictions under RPAPL 1951 to the extent such owner desired to make different use of the property. 8 N.Y.3d at 384-385. Interestingly, the Fourth Department, relying on the *328 Owners Corp.* decision, has determined that a provision in a deed obligating the purchaser to pay the balance of the purchase price in 50 annual installments, which provision was binding on the purchaser's successors and assigns, was not a covenant that ran with the land because it did not touch and concern the land. *Village of Philadelphia v. Fortisus Energy Corp.*, 48 A.D.3d 1193 (4th Dep't 2008).
6. 45 AD3d 1113 (3rd Dept. 2007).
7. 45 A.D.3d at 1114.
8 45 A.D.3d at 1115.
9. 45 A.D.3d at 1115.
10. 18 Misc. 3d 1142(A) (Sup. Ct. Suffolk Co. 2008).
11. Earlier this year, the Court of Appeals, in *McCurdy v. State of New York*, 10 N.Y.3d 234 (2008), explained the proper "measure of damages" when a condemnor takes a temporary easement that encumbers a vacant parcel's entire highway frontage.