50 Clarkson Partners LLC v Old Republic Natl. Tit. Ins. Co.
2019 NY Slip Op 31553(U)
May 30, 2019
Supreme Court, Kings County
Docket Number: 516966/18
Judge: Leon Ruchelsman
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF KINGS : CIVIL TERM: COMMERCIAL PART 8

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50 CLARKSON PARTNERS LLC,

Plaintiff, Decision and order

- against - Index No. 516966/18

MS #1

OLD REPUBLIC NATIONAL TITLE INSURANCE COMPANY,

Defendant, May 30, 2019

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PRESENT: HON. LEON RUCHELSMAN

The defendant has moved pursuant to CPLR §3211 seeking to dismiss the complaint. The plaintiff has opposed the motion. Papers were submitted by the parties and arguments held. After reviewing all the arguments this court now makes the following determination.

On April 10, 2017 the owner of property located at 50-54 Clarkson Avenue in Kings County sold the property to Bluejay Capital LLC for $13,500,000 pursuant to a Purchase and Sale Agreement. On June 2, 2017 Bluejay Capital assigned all its rights in the contract to the plaintiff. The property had a covenant dated June 13, 1945 restricting development of any structure more than two stories high. On July 13, 2017 the restrictive covenant was modified.

In connection with the purchase of the property the plaintiff secured title insurance from the defendant. The policy provided that it covered various risks including "any defect in or lien or encumbrance on the Title" (see, Owner's Policy of Title Insurance, §2). The policy also included exceptions from coverage contained

in Schedule B, however, Schedule B did not contain the restrictive covenant. The policy also contains numerous exclusions. These exclusions state that the following are "expressly excluded from coverage" and include "any law, ordnance, permit, or governmental regulation...restricting, regulating, prohibiting, or relating to the occupancy, use or enjoyment of the land" and "defects, liens, encumbrances, adverse claims, or other matters created, suffered, assumed, or agreed to by the Insured Claimant" (see, Owner's Policy of Title Insurance, Exclusions From Coverage, 1(a)(i), 3(a)).

Following the closing the plaintiff realized the building plans contemplated violated the restrictive covenants. On June 18, 2018 the plaintiff sought $5,000,000 in damages based upon losses incurred as a result of the changes to the development plans. The defendant denied the claim arguing the inability to develop the property pursuant to any desired plan or specific manner was excluded based upon the exclusions noted above. Moreover, the defendant asserted the plaintiff was fully aware of the restrictive covenant as well as the modification consequently the plaintiff was further excluded from pursuing any claims. That denial prompted this lawsuit. The complaint alleges four causes of action including a declaratory judgement, breach of contract, breach of good faith and fair dealing and the bad faith denial of an insurance claim. The defendant has now moved seeking to dismiss the complaint arguing it has no merit and that they cannot be

liable for the damages suffered by the plaintiff.

Conclusions of Law

"[A] motion to dismiss made pursuant to CPLR §3211[a][7] will fail if, taking all facts alleged as true and according them every possible inference favorable to the plaintiff, the complaint states in some recognizable form any cause of action known to our law" (see, e.g. AG Capital Funding Partners, LP v. State St. Bank and Trust Co., 5 NY3d 582, 808 NYS2d 573 [2005], Leon v. Martinez, 84 NY2d 83, 614 NYS2d 972, [1994], Hayes v. Wilson, 25 AD3d 586, 807 NYS2d 567 [2d Dept., 2006], Marchionni v. Drexler, 22 AD3d 814, 803 NYS2d 196 [2d Dept., 2005]. Whether the complaint will later survive a motion for summary judgment, or whether the plaintiff will ultimately be able to prove its claims, of course, plays no part in the determination of a pre-discovery CPLR §3211 motion to dismiss (see, EBC I, Inc. v. Goldman Sachs & Co., 5 NY3d 11, 799 NYS2d 170 [2005]).

There is no merit to the argument the plaintiff's lawsuit must be dismissed because the restrictive covenant is an encumbrance regarding the use of the property and is not a defect affecting ownership of the property. The defendant asserts that "the weight of authority in New York and numerous other jurisdictions recognizes that title insurance provides coverage for defects affecting the ownership of the Property, not defects

affecting the physical condition, use, or economic marketability of the Property" (see, Memorandum of Law in Support of Motion to Dismiss, page 9). However, the cases cited by defendant all concern regulatory notices of non-compliance which do not affect marketability (Logan v. Barretto, 251 AD2d 552, 675 NYS2d 102 [2d Dept., 1998]). Indeed, there are no New York cases discussing whether a restrictive covenant is a defect for which title insurance must provide coverage. However, there are other sources upon which the court may draw. Thus, there is no statutory definition of the term 'encumbrance' (In re Smith's Estate, 188 Misc 814, 65 NYS2d 457 [Surrogate's Court New York County 1946]). However, early cases explained that "if it affects the land either in itself or in its value or the way in which it can be enjoyed, it is an encumbrance" (Bull v. Burton, 227 NY 101, 124 NE 111 [1919]). The court in Bull further observed that "any right existing in another to use the land, or whereby the use by the owner is restricted, it is an incumbrance within the legal meaning of the term" (id). Thus, in Glyn v. Title Guarantee & Trust Co., 132 AD 859, 117 NYS 424 [1st Dept., 1909] the court held a title insurer liable for breaching the contract where the title insurer failed to disclose a nine inch encroachment. Of course, the encroachment did not affect title to the land and only affected its use, the court nevertheless held a breach had occurred. The court reasoned that the

"encroachment constituted an incumbrance upon the property referred to in the policy, for they were matters which might interfere with or prevent the free use and improvement of the property by the owner, and which the owner could not at will remove" (id).

Modern trends are in accord. Thus, in an article entitled 'Title Insurance in New York Today' (New York State Bar Journal, February 1996 by James Pedowitz) the author notes that "the term Encumbrances broadly covers any burden or charges on property, or some right or interest in a third party that interferes with the use or transfer of the property, or otherwise lessens the value of the estate. Some examples of encumbrances in addition to liens include survey encroachments, easements, party wall agreement, restrictive covenants, leases and various agreements affecting the property" (id). Thus, restrictive covenants are surely encumbrances within the meaning of the title insurance policy as well as New York law.

The defendant further argues the restrictive covenant did not render title unmarketable because the mere economic unmarketability of a property does not mean there is no marketability of title. While that may be true depending on the specific facts of each case that does not in any way mean the restrictive covenant in this case was not an encumbrance. The defendant elides the distinction that must be drawn between the

marketability of property and an encumbrance on property. The defendant argues that "as numerous courts have held, restrictions and limitations on the use of the Property, including the ability to develop it, do not constitute defects or encumbrances that trigger title policy coverage" (see, Memorandum of Law in Support of Motion to Dismiss, page 11). The title insurance policy provides distinct covered risks for encumbrances (Section 2) and Unmarketable Title (Section 3), highlighting that a defect can be an encumbrance even though the property is marketable or title can be unmarketable even though no encumbrance exists. Even if the restrictive covenant in this case did not render the property unmarketable as defined by the title insurance policy, there has been no evidence presented that as a matter of law the restrictive covenant was not an encumbrance. The defendant cites to Pavillion Park LLC v. First American Title Insurance Company, [2011 WL 43222, W.D. Kentucky 2011] for the proposition that restrictive covenants are not encumbrances. However, that case does not stand for that proposition and is in any event readily distinguishable. In Pavillion Park, the restrictive covenant demanded that any future owner "shall be solely responsible for any further acts which may be required by the Department for Natural Resources and Environmental Protection as a result of any future problem or situation which may arise from the disposal of said waste on said property" (supra). The court observed the

covenant did "not state any fact, obligation or ownership interest that would constitute a legal impediment to the interest passing of title to the Property. Thus, for our purposes, the restrictive covenant here is conceptually similar to a future assessment. Neither the assessment nor the covenant constitutes an encumbrance that affects the insured's title to the property" (id). The court did not conclude that all restrictive covenants are not encumbrances but rather that the particular encumbrance in that case, which was only potential and not actual, could not be deemed an encumbrance. The court cited to Somerset Savings Bank v. Chicago Title Insurance Company, 420 Mass. 422, 649 NE2d 1123 [Supreme Judicial Court of Massachusetts, Suffolk 1995] to support that contention. Somerset Savings Bank dealt with the fact that zoning regulations are not encumbrances since they do not affect title. It is difficult to discern how Somerset Savings Bank supports the conclusion the covenant in Pavillion Park was not an encumbrance because it was deemed a "future assessment" except for the fact in both cases the courts held the encumbrances did not really affect title. It is further curious that Pavillion Park would base its support upon such a factually distinguishable case (Somerset Savings Bank, supra). As one commentator has observed "unlike private restrictive covenants in recorded deeds and plats, zoning ordinances are in personam rather than in rem. They are but part of a considerable volume of

legislation regulating and restricting the use of property, both real and personal" (see, Patton and Palomar on Land Titles, §609: Restrictive Covenants, Statutes and Ordinances, 3rd Edition 2018).

In any event Pavillion Park is squarely based on the fact the encumbrance in that case was only of a potential nature and did not involve any actual harm.

Thus, as a matter of law, at this stage of the litigation, the title insurance policy covered the restrictive covenant in question.

The title insurance policy further excludes any claims "created, suffered, assumed or agreed to by the Insured Claimant" (Owner's Policy of title Insurance, Exclusion 3(a)) and that since the plaintiff was aware of the restrictive covenant the exclusion applies and the complaint must be dismissed.

Section 3.01(o) of the Purchase and Sale Agreement states that the seller shall accept title to the property free of any liens except those enumerated in Exhibit B-1. Exhibit B-1 entitled 'Additional Permitted Exceptions' contains three items, the first of which is the restrictive covenant. However, Exhibit B-1 contains an additional provision that states that the above item "is subject to the terms and conditions of Section 9.01(f) of the Purchase and Sale Agreement" (id). Section 9.01 of the Purchase and Sale Agreement contain conditions precedent to

closing. Subsection (f) states that "seller shall have obtained licensing, easements and other agreements, including an agreement to modify the existing restrictive covenants, with the Owners of the properties adjacent to the Land necessary for the underpinning and shoring and which shall be reasonably required to perform the Construction pursuant to the Plans" (id).

Thus, the plaintiff agreed to purchase the property subject to the restrictive covenant only if the seller satisfied certain conditions prior to closing pursuant to Section 9.01(f). The plaintiff argues that since those conditions were not satisfied prior to closing they "never agreed to either the Original RC or the RC Modification because, subsequent to closing, the Approved Plans were determined to be in violation thereof" (Plaintiff's Memorandum in Opposition, §57). However, the failure on the part of the seller to comply with any conditions precedent does not undo or eliminate imputed knowledge of the covenants on the part of the plaintiff. Indeed, the Purchase and Sale Agreement specifically states in the same Section 9.01(f) that "in the event that all conditions precedent for Closing as specified in the Agreement are not fulfilled on the Closing Date or waived by Purchaser in writing, then, upon notice from Purchaser, the Seller shall return the Deposit...to Purchaser and this Agreement shall be deemed terminated and of no further force or effect" (id). Therefore, there can be no question the plaintiff was

aware of the covenants and contracted remedies in the event the covenants were not modified in preparation of the anticipated work being performed. Furthermore, the condition requiring a modification of the covenant was in fact satisfied prior to closing and e-mails from plaintiff's counsel acknowledging the modification have been submitted. The plaintiff argues that, nevertheless, the plaintiff "affirmatively disagreed to taking title subject to the Original RC and RC Modification" (see, Plaintiff's Memorandum in Opposition, §62). However, even if that argument is plausible it does not alter the fact the closing in fact took place and it took place with full knowledge of the restrictive covenants.

Lastly, there is no merit to the argument the defendant is liable pursuant to Coverage 10 which protects against any defect "created or attached or has been filed or recorded in the Public Records subsequent to Date of Policy and prior to the recording of the deed" (Owner's Policy of title Insurance, §10). First, this coverage by its very nature only involves new liens filed during the gap period between the date of the policy and the date the deed is recorded. Moreover, since the plaintiff had full knowledge of the restrictions this covered risk is inapplicable.

Thus, there can be no claim against the defendant title insurance company.

Therefore, based on the foregoing the motion seeking to

dismiss the complaint is granted.

So ordered.

ENTER:

DATED: May 30, 2019
Brooklyn N.Y.

Hon. Leon Ruchelsman
JSC