

RESTRICTIVE COVENANTS: (1) "UNIFORM SCHEME OF DEVELOPMENT"; (2) "EQUITABLE SERVITUDE"; (3) REAL PROPERTY MARKETABLE TITLE ACT; (4) "AUTOMATIC RENEWAL" CLAUSES; (5) HOW MANY OWNERS MUST SIGN AMENDMENT?

## A NEW CASE HEADED TO THE COURT OF APPEALS – A LESSON IN ENFORCEMENT

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### 1. General comments

The case of *Rice v. Coholan*, 06-CVS-22261, should be noted. This case, won by the Plaintiffs seeking to enforce the covenants against the defendants, is apparently on its way to the Court of Appeals on some *very* interesting issues. While not decided by the Court of Appeals yet, it is in our opinion validly decided and at the appellate level, will be an important case. The Plaintiffs prevailed on all of their points discussed below. The Plaintiffs contended, and the lower court held, that (1) there was a uniform scheme of development even though only 14 of 18 lots were restricted, so 14 lots were subject to the covenants; (2) an equitable servitude also existed; (3) The Real Property Marketable Title Act did not extinguish the covenants; (4) the Defendants, even *if* they had the sufficient number of signatures, could amend the covenants on 9-20-2006 during a renewal period *but* only to go into effect on 1-1-2015, before the 1-1-2015 renewal period begins with the covenants unamended; and (5) the covenants required the amendment to be executed by a majority of the owners, rather than the owners of the majority of the lots, and the defendants did not have enough signatures. We'll keep you informed.

### 2. Plaintiff's summary of facts

Jefferson Park is a subdivision located off of Providence Road adjacent to Temple Israel. Jefferson Park is divided into two plats, designated Phase I and Phase II.

The real property at issue consists of approximately eighteen (18) lots in Phase I of Jefferson Park ("Phase I"), which consists of 16 actual defined lots, and a portion of two additional lots. Neither Lot 9 in Block 1 nor Lot 9 in Block 2 is fully identified on the filed map that delineates Phase 1 of Jefferson Park. Therefore, there is doubt regarding whether these two portions of lots constitute "lots" for purposes of determining the number of lots contained in Phase I of Jefferson Park. Nevertheless, for ease of reference and because the outcome is inevitably the same, the Plaintiffs acknowledge the existence of 18 lots in Phase I of Jefferson Park.

Phase I consists of Blocks 1 and 2. Each contains 9 lots. The plat recorded in Map Book 1166, page 131 of the Mecklenburg County Registry shows Lots 1 through 9 for each block in Phase I, and is entitled, "A Subdivision Plan of a Part of Jefferson Park." There are 9 owners of the real property located on the Phase I Map. They are: (1) Bryant Marks – record owner of Block 1, Lots 1 and 2; (2) Nachum and Mary Eshet-record owners of Block 1, Lot 3; (3) Gayle Smith-record owner of Block 1, Lots 4 and 5; (4) Ernest and Debbie Castellano – record owners of Block 1, Lot 6; (5) J. Fredrick Rice – record owner of Block 1, Lot 7; (6) The Coholans – record owners of Block 1, Lots 8 and 9; (7) Temple Israel – record owner of Block 2, Lots 1 through 6; (8) Madison Geer – record owner of Block 2, Lot 7; and (9) The Crouches – record owners of Block 2, Lots 8 and 9.

The real property encompassing Phase I and Phase II of Jefferson Park was initially owned by a common grantor, the Blankenships. The Blankenships subdivided Phase I into approximately 18 lots. Each lot in Phase I (and II) contains 1 acre, generally. Of the 18 lots in Phase I, 14 are expressly subject to deed restrictions found in individual deeds in the recorded chain of title (the "deed restrictions"). Deed restrictions were not found in the recorded chain of title for Lots 2 and 9 of Block 1, or for Lots 4 and 5 of Block 2.

The deed restrictions prohibit the lots from being subdivided or altered in size or dimension. The deed restrictions also contain front and side set-back requirements. All of the deed restrictions expressly state that they are deemed to run with the land and bind all parties claiming under them until January 1, 1975, at which time they are automatically extended for successive 10-year periods unless a majority of owners agrees to change them. The Plaintiffs noted that the restrictions are substantially similar, but not identical. For instance, the deed restrictions for Lot 8, Block 1 (the lot at issue in this litigation) state that "a majority of the owners of Jefferson Park" is necessary to change the covenants, while the deed restrictions for Lots 2 and 3 of Block 2 state that "a majority of the then owners of said lots in Jefferson Park" is necessary. The deed restrictions for Lots 6 and 8 of Block 2 state that "a majority of the then owners of said lots as shown on said map" is necessary to alter the deed restrictions. The Plaintiffs argued that these

minor differences in the language were unremarkable and had no effect. The deed restrictions were not altered or amended (or attempted to be altered or amended) on January 1, 1975, January 1, 1985, January 1, 1995, or January 1, 2005.

On September 6, 2006 (some 20 months after the January 1, 2005 anniversary date), the Coholans and/or Madison filed in the Mecklenburg County Public Registry a document entitled, "Termination of Restrictions Termination Agreement," (hereinafter, the "Termination Agreement"), which on its face, states (with this author's parenthetical remarks): "This Termination of Restrictions Termination Agreement is made this 5<sup>th</sup> day of September, 2006, by and among the undersigned owners, Temple, Israel, Inc., a North Carolina corporation (one owner), Jeffery H. Millick (unmarried) (one owner), George S. Crouch, Jr. and wife Mary Ann C. Crouch (the Crouches counted as one owner)....", as well as the Coholans (counted as one owner), bringing the total to four owners.

Around July to August 2006, Lots 8 and 9 of Block 1 were each subdivided into three separate lots, thus creating six lots in an area previously comprising only two. The Coholans owned these six subdivided lots, and engaged Madison and JSCH to construct six residential homes, one on one each of the subdivided lots.

(The Plaintiffs noted that on June 8, 2007, the parties agreed to settle all claims related to Lot 9 and signed a Consent Order dismissing the claims associated with that lot. Plaintiffs' claims now relate only to Lot 8.)

If constructed, the three residential homes would violate the front and/or side setback requirements contained in the deed restrictions governing Lot 8 and the one-residence-per-lot restriction. Plaintiffs were seeking a judgment declaring the Termination Agreement ineffective to alter or amend the deed restrictions and a permanent injunction order, precluding the construction of more than one residence on Lot 8 in Block 1 of Phase I of Jefferson Park.

### **3. Each of the Phase I Lots is bound by the deed restrictions – uniform scheme of development**

Where a common grantor subdivides a tract of real property and conveys the subdivided lots subject to restrictions on its use pursuant to a common scheme of development, the restrictions may be enforced by and against all lot owners within the development. *Myers Park Homes Co. v. Falls*, 184 N.C. 426, 430, 115 S.E. 184, 186 (1922). The test for determining whether a subdivision constitutes a common scheme of development is "whether substantially common restrictions apply to all similarly situated lots." *Medearis v. Trustees of Myers Park Baptist Church*, 148 N.C. App. 1, 5-6, 558 S.E.2d 199, 203 (2001). This is true even where, as in the case we are discussing, the restrictions are not incorporated into each and every deed as discussed in *Franklin v. Elizabeth Realty Co*, 202 N.C. 212, 162 S.E. 199 (1932) ("[T]he omission of a restriction from a single deed goes not destroy the general plan.").

Also, see *Bailey v. Jackson*, 191 N.C. 61, 131 S.E. 567 (1926). In *Davis v. Robinson*, 189 N.C. 589, 127 S.E. 697 (1925), a uniform scheme of development did not exist where 164 lots were conveyed with restrictive covenants, but 142 lots were conveyed without covenants. In *Sedberry v. Parsons*, 232 N.C. 707, 62 S.E.2d 88 (1950), a tract of land was subdivided into twenty-one residential lots of various shapes and sizes. The developer conveyed eleven lots to purchasers by deeds containing restrictions prohibiting sale of the land conveyed by the deed into parcels less than one-half acre. The developer conveyed ten other lots to purchasers with deeds which did not contain any restrictive covenants. The court stated that the "substantial uniformity in restrictions essential to the existence of the general plan" did not exist. Thus, the restrictions did not run with the land. The covenants in deeds need not be absolutely identical in order to have a common or uniform scheme of development. Minor variations are not determinative. *Higdon v. Jaffa*, 231 N.C. 242, 56 S.E.2d 661 (1949).

The Plaintiffs noted that 14 of the 18 lots have nearly identical restrictions. The only lots without restrictions were those retained by the grantor-the Blankenships. The fact that the deeds to four lots in Phase I did not contain deed restrictions did not defeat the general plan and scheme of development intended by the Blankenships, the Plaintiffs contended. See, *Franklin*, supra, ("[T]here may be departure in a few instances in the sale of lots without restrictions without defeating what is otherwise an apparent general scheme of development"); *Higdon v. Jaffa*, 231, N.C. 242, 56 S.E.2d 661 (1949) ("[Absolute] uniformity in details is not required to establish a general plan for the development of a tract subdivided into a number of building lots").

The original deed for Lot 8 of Block 1 in our case discussed expressly states:

1. That said lot of land is to be used for residential purposes only, and no structure shall be erected, altered, placed or permitted on said lot other than *one detached, single-family dwelling* not to exceed 2 ½ stories in height ... Said lot *shall not be subdivided or altered in size or dimensions* (emphasis added).

2. No building shall be erected on said lot nearer than 100 feet to the center-line of Jefferson Drive; and no building shall be erected nearer than 25 feet of the side lot lines.

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10. These covenants are to run with the land and shall be binding on all of said parties claiming under them until January 1<sup>st</sup>, 1975, at which time said covenants *shall be automatically extended for successive periods of 10 years unless by a vote of the majority of the owners of Jefferson Park it is agreed thereby to change said covenants in whole or in part* (emphasis added).

14 of the 18 lots contain similar, but not identical language. The Plaintiffs contended that the Coholans' attempt to sign the Termination Agreement was the best indication that the Coholans acknowledged that Lot 8 of block 1 was subject to the deed restrictions.

#### **4. The deed restrictions are enforceable as equitable servitudes, by and against all Phase I owners – equitable servitude**

The Plaintiffs contended that the deed restrictions are enforceable in equity by and against all lot owners in Phase I. "In order to enforce a restrictive covenant on the theory of equitable servitude it must be shown (1) that the covenant touches and concerns the land, and (2) that the original covenanting parties intended the covenant to bind the person against whom enforcement is sought and to benefit the person seeking to enforce the covenant." *Runyon v. Paley*, 331 N.C. 293, 310, 416 S.E.2d 177, 189 (1992). Phased differently, "[t]o enforce a restrictive covenant as an equitable servitude, it is only necessary to show that the covenant is of such a nature as to bind the party sued and to be enforceable by the party suing." *Id.* A restrictive covenant touches and concerns land where it has "some economic impact on the parties' ownership rights by, for example, enhancing the value of the dominant estate and decreasing the value of the servient estate." *Id.* The deed restrictions are intended to benefit Plaintiffs as lot owners by enhancing the value of their property and maintaining the general and uniform nature of Jefferson Park. *Runyon v. Paley*, supra. "[A] restriction limiting the use of land clearly touches and concerns the estate burdened with the covenant because it restricts the owner's use and enjoyment of the property and thus affects the value of the property." *Id.* The deed restrictions benefit (and burden) owners of lots in Phase I, and therefore touch and concern the Phase I property.

See *Terres Bend Homeowners Ass'n v. Overcash*, \_\_ N.C. App. \_\_, 647 S.E.2d 465 (2007), holding that where a declaration of restrictions stated that the restrictions were to "run with the land and shall be binding on all parties and all persons claiming under them" for a period of thirty years, the restrictions were enforceable by the grantor, his heirs, successors and assigns.

#### **5. The North Carolina Real Property Marketable Title Act does not operate to extinguish the deed restrictions**

North Carolina's Real Property Marketable Title Act (the "act"), codified at N.C. Gen Stat. § 47B-1, et seq. (2008), was developed to "expedite the alienation and marketability of real property." N.C. Gen. Stat. § 47B-1(2). The General Assembly's stated purpose is as follows:

It is the purpose of the General Assembly of the State of North Carolina to provide that if a person claims title to real property under a chain of record title for 30 years, and no other person has filed a notice of any claim of interest in the real property during the 30- year period, then *all conflicting claims based upon any transaction prior to the 30-year period shall be extinguished.*

G.S. 47B-1 (emphasis added).

Defendants contended that the act extinguished the restrictions, citing the lone case of *King Associates, LLP v. Bechtler Dev. Corp.*, 179 N.C. App. 88, 632 S.E.2d 243 (2006), as an example of a case in which the North Carolina Court of Appeals "extinguished a recorded real property right pursuant to the Marketable Title Act."

The act contains a number of exceptions, which prevent the extinguishment of certain property rights. One such exception is the residential exception, found at G.S 47B-3(13). That exception states that the act shall not affect or extinguish the following rights:

(13) Covenants applicable to the general or uniform scheme of development which restrict the property to residential use only, provided said covenants are otherwise enforceable. The excepted covenant may restrict the property to multi-

family or single-family residential use or simply to residential use. Restrictive covenants other than those mentioned herein which limit the property to residential use only are not excepted from the provisions of Chapter 47B.

The Plaintiffs argued that the residential exception applies in this case because the deed restrictions encumber lots in a general or uniform scheme of development. With respect to restrictive covenants applicable to a general or uniform scheme of development, the residential exception protects all of the covenants in the document. The exception does not permit redlining certain covenant restrictions to the exclusion of others. This idea is supported by the last sentence of the exception, which makes clear that a residential-use restriction that does not burden a general or uniform scheme of development is not covered by the exception.

Consequently, the Plaintiffs contended that the deed restrictions have not been extinguished by the Marketable Title Act.

#### **6. The Deed Restrictions Cannot be Terminated by Less than Unanimity Prior to January 1, 2015**

The Termination Agreement was held to be not effective to terminate the deed restrictions because it was not executed on or before January 1, 2005, the ten-year anniversary date. Rather, certain of the Defendants executed the Termination Agreement on September 5, 2006, long after the ten-year anniversary date, and well within the automatic, 10-year extension period. In this case, the deed restrictions expressly state that they run with the land and bind all parties claiming under them until January 1, 1975, at which time they are automatically extended for successive 10-year periods unless a majority of the owners agrees to change them.

The only North Carolina case that has interpreted similar restrictive covenant language is *Zumkehr v. Hidden Lakes Property Owners Ass'n, Inc.*, 158 N.C. App. 747, 2003 WL 21496467 (2003) (unpublished). In that case, the pertinent amendment language stated:

The covenants and restrictions herein are to run with the land and shall be binding on all parties acquiring title to lots in Hidden Lakes up to and including the 14<sup>th</sup> day of August, 2000, *at which time said covenants shall be automatically extended for successive periods of ten years unless by vote of a majority of then owners of the residential building sites covered by these or substantially identical covenants, it is agreed to change said covenants in whole or in part.*

(Emphasis added) In *Zumkehr*, the defendant property owners' association attempted to amend the restrictive covenants at its annual meeting on November 16, 1999, almost 9 months before the August 14, 2000 anniversary date. *Id.* The plaintiff argued that the vote for the attempted amendment was invalid because it could only occur on the anniversary date itself. Therefore, the plaintiff argued, the attempted amendment was null and void.

The trial court rejected this argument and granted summary judgment in favor of the defendant on the plaintiff's declaratory judgment claim. In affirming the lower court's ruling, the North Carolina Court of Appeals recognized that, "[a]lthough the property owners voted to amend the covenants on 16 November 1999, *such amendments were not effective until 14 August 2000,*" after the end of the automatic term. *Id.* (Emphasis added.)

The *Zumkehr* case makes clear that where restrictive covenants are automatically extended for a set period of time, any attempt to amend or terminate them by majority vote is not effective until the end of the current automatic term. The amendment language in *Zumkehr* is practically identical to the amendment language contained in the deed restrictions for Lot 8 in Block 1 – the lot at issue in this case:

These covenants are to run with the land and shall be binding on all of said parties claiming under them until January 1<sup>st</sup>, 1975, *at which time said covenants shall be automatically extended for successive periods of 10 years unless by a vote of the majority of the owners of Jefferson Park it is agreed thereby to change said covenant in whole or in part.* (Emphasis added.)

On January 1, 2005, the deed restrictions (by their terms) were automatically extended for a new 10-year period. Accordingly, any amendment or termination of the deed restrictions by majority vote is not effective, if at all, until the end of that period (January 1, 2015).

Courts in other jurisdictions agree with the North Carolina Court of Appeals' approach in *Zumkehr*. Each of these cases dealt with substantially similar or identical restrictive covenant language. In each case, the court held that when restrictive covenants on their face dictate that they are to be "automatically extended for successive periods of 10 years unless [changed] by a vote of the majority of the owners" as in the case at bar, then those restrictions cannot be terminated outside the anniversary date. 874 p.2d 818 (Okla.1994). See *In re Wallace's Fourth Southmoor Addition to the City of Enid. Propps, Inc. v. Rogers*, 874 P. 2d 818 (OKLA. 1994).

Other state courts agree with this approach. See *Johnson v. Howells*, 682 P.2d 504 (Colo.App. 1984) (holding that, where provision stated that restrictive covenants were binding for 20-year periods unless an instrument signed by sixty percent of the owners had been recorded agreeing to change them, restrictive covenants could not be amended prior to expiration of the initial 20-year period); *Scholten v. Blackhawk Partners*, 909 P.2d 393 (Ariz. Ct. App. 1995), *as supplemented on reconsideration* (Oct. 3, 1995), *review denied* (Jan. 17, 1996) (holding that attempted amendment of restrictive covenants during restrictions' automatic renewal term was ineffective because it would render meaningless the language providing for the automatic extension).

The law is clear that any attempt to terminate the deed restrictions in 2006 is ineffective. As such, while the deed restrictions can be amended by unanimous vote of the Phase I owners at any time, the express language thereof reveals that a majority vote is insufficient to amend or terminate them prior to January 1, 2015. Thus, even if the Termination Agreement is otherwise valid and Defendants obtained the requisite majority vote (which Plaintiffs denied), the termination cannot be effective until January 1, 2015.

The lesson seems clear. And, you must obtain a termination under such a provision as that in controversy during the term, to be effective for the next term, in order for the next term to not "kick in," pursuant to the extension or rollover provision, unamended.

#### **7. How many owners must sign termination? – The Termination Agreement is invalid for lack of consent by a majority of owners in Phase I of Jefferson Park**

At the time of the purported execution of the Termination Agreement, there were 10 owners in Phase I. The Termination Agreement was executed by only 4 owners: Jeffery H. Millick, Temple Israel, Inc., the Crouches and the Coholans. Obviously, 4 is not a majority of 10. Therefore, the Termination Agreement was not executed by a majority of owners in Jefferson Park.

Defendants take the position that the deed restrictions can be amended by a vote of the owners of a majority of lots in Phase 1. There is no support for this in the documents. The deed restrictions expressly state that they require agreement by "a majority of the owners of Jefferson Park," or "a majority of the then owners of said lots in Jefferson Park," or "a majority of the then owners of said lots as shown on said map." Thus, the plain language of the deed restrictions makes clear that amendment requires the agreement of a majority of the owners in Jefferson Park, rather than the owners of a majority of lots.

Although North Carolina courts have not addressed the issue, other jurisdictions have recognized this distinction in the face of almost identical language, and uniformly agreed with above analysis. See, *Cieri v. Gorton*, 587 P.2d 14(Mont. 1978) (holding that, a restrictive covenant requiring agreement by " a majority of then owners of lots affected thereby" to change the restrictive covenants, meant a majority of property owners, rather than a majority of lots); *Duffy v. Sunburst Farms East Mut. Water and Agr. Co. Inc.*, 604 P.2d 1124 (Ariz. 1979) (holding that a provision allowing restrictive covenants to be amended or revoked "by vote of a majority of the then owners of lots" required vote of a majority of owners, rather than a vote of the owners of a majority of lots); *French v. Diamond Hill-Jarvis Civic League*, 724 S.W.2d 921 (Tex. App. 1987) (holding that a provision allowing for the release of deed restrictions "by a vote of a majority of the then owners of the lots," required a vote of the majority of owners, rather than votes from the owners of a majority of lots).