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## *AXYS, LLC v. Ng:* A Close Encounter of the Marketable Title Kind

By Marvin N. Bagwell

It is not often that a title person is given the opportunity to participate in history-making litigation. On one extremely busy Thursday afternoon, a late phone call from Rachel Warren,<sup>1</sup> one of defendant's counsel in the matter, *AXYS, LLC v. Ng*,<sup>2</sup> gave me that very opportunity. The litigation involved a quintessential title issue—what exactly is marketable title? As is often the case when legal history is being made, the pending litigation was little known even to the real estate bar. However, this case had the potential of roiling the real property marketplace for years to come. If the court chose to follow legal precedence, the titles to hundreds of townhouses in Manhattan would immediately have become unmarketable. Because of the standing and deference accorded to decisions coming out of the First Department, the case could have had the effect of bringing into question the titles to townhouses in Brooklyn, Queens and similar properties throughout the state. Would the court find that the law has ossified or would it find that it—(“it” in this case refers to both the law and the court) had evolved? This is my firsthand (admittedly biased and possibly immodest) account of *AXYS, LLC v. Ng*. And to think, I almost did not take Ms. Warren's call.

The defendants own a townhouse located on East 10th Street in New York City within the Greenwich Village Landmark Preservation District. On December 22, 2003, they entered into a contract to sell the premises to *AXYS, LLC* for \$11.5 million. To seal their deal, the parties executed the standard New York City real estate sales contract and *AXYS* deposited \$1.5 million with the seller's attorney as escrow agent. After several fits and starts to schedule a closing, on April 2, 2004, counsel for the defendants set a time of the essence closing for May 3, 2004. In response, *AXYS* accepted a June 3, 2004 closing date. However, on April 20, 2004, *AXYS* notified the defendants that it declined to close because title was unmarketable. *AXYS* demanded that the defendant return the deposit. The basis of *AXYS*'s unmarketability claim was that the title report disclosed that several parts of the premises either projected into or encroached upon

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the public right-of-way, i.e., East 10th Street. Specifically, the survey revealed that vent pipes, window trim, capstone, roof cornices, leader, and a stoop, among other items attached to the main structure, encroached into East 10th Street by distances ranging from 1-1/4 inches to 6 feet 10 inches. As is wont to happen when that much money is involved, litigation ensued. AXYS brought suit essentially to re-claim its \$1.5 million down payment. Early in the litigation, after the normal procedural maneuvering, the parties agreed to close title on a date certain if the court found that title was marketable. Hence, the parties placed the ancient concept of marketability squarely before the court.<sup>3</sup>

The sales contract contained the standard language for "permitted exceptions" for stoops, cornices and other normal encroachments that one would encounter in Manhattan. However, AXYS argued first, that the rider to the contract contained language which supersedes the permitted exceptions clause and second, that the property contained encroachments in addition to the permitted exceptions. Comparing the property survey to the permitted encroachments as set forth in the sales contract, the court found that only the vent pipes, leader and window guards (which were not specifically identified in the contract's permitted exceptions clause) encroached or projected into the street and hence could lead to the title's being rendered unmarketable. Justice Ramos, however, quickly accepted the defendant's arguments that these items were de minimis and did not impact upon marketability. Given that the sales price of the premises was over \$11 million and that the buyer did not submit adequate evidence as to the cost of the removal of the encroachments, "none of the remaining items were difficult to move or remove and as such could not rise to the level of encroachments that would render title unmarketable . . ." <sup>4</sup> But that did

not end the discussion. The court still had to dispose of additional encroachments which were not eliminated as issues by the terms of the contract.

As is illustrated by the legion of cases appearing under the topic "Marketability of Title" in *Warren's Weed*, under traditional or classical title theory, any encroachment or projection onto the property of another would have rendered title unmarketable. Recognizing that this position was inherently impractical, Justice Cardozo had long ago written that unmarketability of title could not be construed so broadly. He wrote in *Norwegian Evangelical Free Church v. Millhauser* that:

[T]he law assures to a buyer a title free from reasonable doubt, but not from every doubt. There must be some fairly debatable ground on which the doubt can be justified: something more than a mere speculation or a bare possibility. The test is not the hazard of possible litigation, for, as has been pointed out, it seems to be the inalienable right of any person to start a lawsuit. The test is rather a chance of successful attack.<sup>5</sup>

More recently, but still over a half century ago, the First Department, following Justice Cardozo's reasoning, held in *Whittier Estates v. Manhattan Savings Bank* that, "[T]he test of [marketability] is not the hazard of possible litigation, for as has been pointed out, 'it seems to be the inalienable right of any person to start a lawsuit.' The test is rather the chance of successful attack."<sup>6</sup> These statements provided the analytical framework into which Justice Ramos had to fit *AXYS v. Ng*. Since parts of the property which encroached upon East 10th Street, i.e., the public right-of-way, the litigants agreed that only the City of New York had the right to sue for removal of the encroachments. The parties also agreed that if

the City did so, it would prevail. The question thus became whether the City would exercise its inalienable right to start a lawsuit to remove the encroachments, thereby instantly rendering title unmarketable.

As is often in the law, there is a counterweight to the court's general statements as to the meaning of marketability of title. That counterweight was the leading, and seemingly directly on point, decision rendered in 1915 by the Court of Appeals in *Acme Realty Co. v. Schinasi*.<sup>7</sup> The case involved a seven-story apartment building located on 116th Street in Manhattan whose front stoop and windows encroached into the public right-of-way by over four feet. The Court of Appeals ruled that the encroachments rendered title to the building unmarketable as a matter of law even if the City of New York had explicitly authorized the encroachments. AXYS's counsel, relying upon *Schinasi*, argued that title was, in effect, per se unmarketable because of the uncontested mere existence of the encroachments into the public's right-of-way. However, *Schinasi* contained the roots of its own limitation if not outright destruction. As counsel for the defendants and their experts pointed out, the *Schinasi* Court had recognized that the City at that time was removing encroachments so as to widen and develop streets in accordance with its then-policy of promoting the free flow of traffic and commerce. Since 1915, the City's orientation toward its neighborhoods had changed. Instead of destroying neighborhoods to promote unencumbered traffic and commerce, the City, certainly since the vastly unpopular and deeply regretted destruction of the original Penn Station, has pursued a policy of preserving its historical structures and neighborhoods.

Also, counsel for the defendants referred the court to section 26-226 of the City's Administrative Code, adopted in 1938, which explicitly provided that, "[S]uch parts of buildings

as project beyond the street line on January first, nineteen thirty-eight, may be maintained as constructed, unless their removal, rearrangement or relocation is directed by the city council or board of estimate." Witnesses for both AXYS and the defendants confirmed that the subject townhouse was constructed in 1840, almost a full century before the City adopted Code provision 26-226. The same witnesses, ranging from Charles Smith, the City's former Department of Buildings Commissioner, and William Higgins, an expert in historical preservation, all testified that in light of the Code provisions and under subsequent Landmark Preservation legislation, absent an emergency, it was extremely unlikely that the City would bring suit to require the removal of the projections and encroachments. This author testified that although *Schinasi* had not been overruled by the Court of Appeals, the lower courts had over time, vastly eroded the *Schinasi* strict unmarketability standard.<sup>8</sup> The insurability of title as represented by the coverage provided by a title insurance policy had largely supplanted marketability. Although title underwriters still insure that title is "not unmarketable,"<sup>9</sup> the considerations of practicality as eliminating the risk that someone might bring suit now govern their risk assessment.<sup>10</sup> In this case, it was and remains the author's opinion that the City through Code Section 26-226 and Landmark legislation had virtually estopped itself from requiring the removal of the offending encroachments and projections. Therefore it was reasonable to insure, as one title insurance company had done, that the defendant's title was marketable.

However, it was not the experts nor even this author who would have the last word. The court wanted more, perhaps even some law. Counsel for the defendants directed the court's attention to the case, *English Speaking Union (New York) Inc. v. Payson*,<sup>11</sup> the fact situation of which was remarkably similar to the case

before Justice Ramos. In *English Speaking Union*, Payson contracted to purchase 19-21 East 59th Street, New York City, from English Speaking Union. After several adjournments, the parties finally stipulated to close on August 1, 1957. Payson then sought another adjournment past the August 1 date partly on the basis that title was unmarketable because the property's entrance columns, steps and other attachments encroached into the public street. The court took note of the fact that Payson, a sophisticated real estate investor, must have known of the encroachments when he entered into the contract but that he only raised the objections on the eve of the court stipulated closing. The contract of sale which Payson had entered into contained exactly the same provision as the "permitted exceptions" clause in this case. The *English Speaking Union* court held "[T]his provision is a complete answer to the objection based on the foregoing street encroachments." In other words, having executed the contract of sale, Payson waived any objection to title on the basis of the encroachments which the survey later revealed. The court went on to find that the other objections were trivial and did not make title unmarketable. Further, to the court, section 26-233 of the Administrative Code (now section 26-226) meant that there was little likelihood that the encroachments would be disturbed by the City. Therefore, the court found title to be marketable.

The stage was thus set. Under classical marketability theory, and under *Schinasi*, AXYS's counsel opined that the encroachments clearly rendered title unmarketable. Counsel for the defendants argued that under *English Speaking Union* and in the real world of practicality where homeowners, investors, and risk-averse title insurers exist, classical marketability theory had long been supplanted by hard-nosed calculations as to whether the City would likely bring suit to require the removal of the stoops, fencing and other details

that gave this particular property and the neighborhood in which it was located, its desirable and expensive character. Would legal evolution or ossification carry the day?

Now, we return to Justice Ramos's opinion.

Before we digressed, the court, citing *English Speaking Union*, had ruled that most of the encroachments were covered by Paragraph 9 of the contract. Therefore, AXYS had waived any objection as to marketability of the encroachments listed in Paragraph 9. Only three other encroachments and projections, those of the leader, the vent pipes and the window guards, remained. The court held that in addition to being *de minimis*, these encroachments were open and notorious, were covered by Landmark designation and were specifically authorized by the Administrative Code. Landmark designation in particular was important to the court. The fact that the premises are located within a landmark area reduced the risk to the purchaser (AXYS) that the City would sue to remove the encroachments to a negligible one. Landmark protection, in addition, had the effect of estopping the City from taking action to remove building characteristics which are now prized and protected unless they constitute a safety hazard. In line with Justice Cardozo's admonition that marketability is determined by the probability of the risk that a third party could bring a successful suit to upset the fee owner's title, Justice Ramos held that the risk that the City would bring suit over the encroachments was so negligible that the title was marketable. Times had changed since *Schinasi*. Evolution won.

After finding that title was marketable, the court concluded that it was clear that the plaintiffs brought this suit only to avoid their obligation to purchase and to secure the return of their down payment. Their actions thereby provided support to a thesis which this author proposed in an earlier article to the effect that allega-

tions of unmarketability are most often used as a sword and not as a shield. When a purchaser wants out of a contract of sale, when all else fails, the purchaser will assert that title is unmarketable. However, in this case, since the defendants could not prove that they were prejudiced by the fact that AXYS had waited to the eve of closing to raise the unmarketability allegation, the court did take AXYS's strategy into consideration in reaching its decision. Also, in a blow to the egos of title underwriters everywhere, the court found that the fact that the defendants had obtained affirmative title insurance coverage which covered the cost of remedying the encroachments was not "dispositive." Talk about putting us in our place.

Although the author is somewhat prejudiced by participating as an expert witness for the winning defendants, the court's decision was correct and appropriate. Justice Cardozo's advisory calls essentially for a two-pronged analysis. First, the court must determine whether there will be litigation regarding the issue which is the basis of the unmarketability claim. Then, if it is likely that there will be litigation, the question becomes whether the litigation will be successful. The quandary faced by Justice Ramos, sitting 80 years after Justice Cardozo had established the analytical framework, was that the answer to the second question was a resounding "yes" from both the seller and the purchaser. If the New York City Counsel or the Mayor authorized the bringing of a suit to remove the encroachments in compliance with Code Provision 26-226, all parties agreed that the suit would be successful. Therefore, the first question became seminal. Would the City bring suit? Based upon the landmark area designation, Judge Ramos found the answer to that question to be highly unlikely. Hence, title was marketable.

The importance of the court's decision is in the court's acceptance of the evolutionary nature of the mar-

ketability doctrine. *Schinasi*, decided in 1915, established that the very encroachments at issue here made title unmarketable. However, *Schinasi* was a product of City policy at that time. The City's vision has changed. Rather than opening all streets for commerce, the City now seeks to preserve its neighborhoods. The court implicitly recognized that the doctrine of marketability is not immutable or prone to ossification but is evolutionary. This recognition is of great importance to those of us who make a living from or who live in real property located in some of Manhattan's most expensive neighborhoods. After all, had the court ruled differently, the title to virtually every townhouse in Manhattan would have been rendered unmarketable. The impact upon the City's real estate market, and upon the claims departments of those unfortunate title underwriters whose policies did not contain the appropriate exceptions, would have been frightening. Sometimes, common sense, with the help of good lawyering and a perceptive judge, will carry the day. This was one of those days.

## Endnotes

1. Larry Hatcher and Rachel L. Warren of the firm Davidoff, Malitto and Hatcher, New York City, represented the defendants. The defendants retained the author as their expert witness on title insurance matters including marketability of title. Joseph H. Lessem of Warshaw Burstein Cohen Schlessinger & Kuh, New York City, represented the plaintiff, AXYS, LLC. The plaintiff retained James Pedowitz to serve as its expert witness on title matters and marketability.
2. N.Y.L.J., June 16, 2004, p. 18, col. 1 (Sup. Ct., N.Y. Co.).
3. Justice Ira Gammerman heard this matter initially. He ruled that if the court determined that the defendant sellers were able to convey marketable title under the contract of sale, then the parties would be required to close at a date certain. Justice Gammerman subsequently transferred this case to Justice Charles E. Ramos to decide the question of marketability of title.
4. *AXYS, LLC v. Ng*, N.Y.L.J., June 26, 2004, p. 18, col. 2 (Sup. Ct., N.Y. Co.).
5. 252 N.Y. 186 at 190 (1929).

6. 181 Misc. 662, 666 (1st Dep't 1944).
7. 215 N.Y. 495 (1915).
8. See, e.g., *Morrisseau v. Judicial Title Insurance Agency*, N.Y.L.J., Sept. 8, 1999, (Mount Vernon City Court), (incorrect building permit); *Chu v. Chicago Title*, 452 N.Y.S.2d 229 (2d Dep't 1982) (certificate of occupancy violation); *Logan v. Baretto*, 251 A.D.2d 552 (2d Dep't 1998) (sanitary code violation); *Wolf v. Commonwealth Land Title Ins. Co.*, 180 Misc. 2d 307 (1st Dep't 1999) (zoning violation); *John Hancock v. 491-499 7th Avenue Associates*, 644 N.Y.S.2d 953 (Sup. Ct., N.Y. Co. 1996) (disclosed oil spill); and *Vandervoort v. Higginbotham*, 634 N.Y.S.2d 800 (3d Dep't 1995) (property's value does not render title unmarketable. Even the Court of Appeals without overturning *Schinasi* has found that certain title problems which would have rendered title unmarketable long ago, currently no longer do so.). See *Voorheesville Rod and Gun Club, Inc. v. E.W. Tompkins Company, Inc.*, 606 N.Y.S.2d 132 (1993) (failure to obtain subdivision approval).
9. See American Land Title Association's 1992 form of Owner's Title Policy, insuring paragraph 3.
10. See, e.g., *What is Marketability?*, N.Y.L.J., Mar. 13, 2002, p. 5, col. 2; *Marketability—The Legislature (and Title Insurers, of Course) Save the Day*, N.Y.L.J., May 8, 2002, p. 5; and *Marketability—Insuring That There is Something to Sell*, N.Y.L.J., July 10, 2002, p. 5, col. 2.
11. 11 Misc. 2d 669, 174 N.Y.S.2d 775 (Sup. Ct., N.Y. Co. 1958).

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