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Recording Act Takes Precedence Over CAFRA

New Jersey Supreme Court rules in favor of property owner in DEP deed restriction dispute

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You are in the market for real estate for its development potential. In a dream-like scenario, you identify a parcel and, with the assistance of a team of real estate professionals, complete your due diligence. After a thorough review, including a title search, you find nothing precluding development of the parcel and justifiably conclude your contemplated use is viable. You acquire the property and apply for necessary development permits.

But then your dream is interrupted. Your permits are denied. No, you and your top-notch team of professionals did not miss something. But, the property was subdivided from another parcel subjected to a deed restriction precluding the type of use you are proposing. Although the deed restriction is not in the chain of title for your property, the permitting agency declares it was supposed to be, and will not issue you a permit. The mistake was not yours, and

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was at least partially the agency's, but you are stuck with the consequences.

That was essentially the scenario before the Supreme Court in *Island Venture Associates v. DEP*, 179 N.J. 485 (2004). Fortunately, there was a happy ending for the involved property owner. The Court ruled the Department of Environmental Protection's (DEP) denial of an application for a Coastal Area Facility Review Act (CAFRA) permit for property located in Long Beach Township, Ocean County, was improper. The Court concluded the public's interest in the integrity of the recording system and the policies underlying the Recording Act preclude DEP from subjecting the property to a deed restriction called for by a prior permit issued by DEP, where the deed restriction was recorded against an adjacent parcel, but was not recorded in the chain of title for the subject property.

Background of the Case

The dispute in this case involved Island Venture Associates' proposal to develop a single family home on each of two adjoining lots located in Long Beach Township, designated as lots 3.03 and 3.04, block 25.12. Prior to purchasing the property, Island Venture conducted a diligent title search. No restrictions were discovered that would

preclude the proposed development. In 1999, Island Venture submitted an application to DEP for a permit pursuant to CAFRA for the proposed development. DEP denied the application, however, finding the property was restricted to water dependant use pursuant to a CAFRA permit issued to Island Venture's predecessor in interest, High Bar Harbor Development Company (High Bar).

In January 1989, High Bar owned several adjoining lots in Long Beach Township, which included the two lots that later became the Island Venture property. An existing marina was located on two of these lots. To the west and south of the marina was Lot 3, which was largely unimproved. The two residential lots owned by Island Venture were ultimately subdivided from Lot 3. To the north of the marina were four other tax lots.

High Bar applied to DEP for a CAFRA permit, which was granted, to construct eighteen single family homes on the four lots to the north of the marina. The approval was conditioned upon High Bar's imposition of a DEP-approved deed restriction on the adjacent marina site limiting those lots to water-dependent uses in perpetuity. DEP approved High Bar's form of deed restriction, which was to be included into a "Master Deed of Condominium" due to High Bar's proposed conversion of the marina into a condominium or "dockominium" type of ownership.

High Bar duly recorded the approved deed restriction with the Ocean County Clerk. The proposed deed language pro-

vided that the "condominium property" would remain a water dependent use, and defined "condominium property" by reference to the marina site. The marina site was supposed to include what ultimately became the Island Venture property. But the marina site identified and depicted in the Master Deed of Condominium was limited to the marina and did not include the property south of the marina that later became the Island Venture property.

After securing CAFRA approval, High Bar obtained subdivision approval for the lot south of the marina, establishing the two residential lots (3.03 and 3.04) subsequently purchased by Island Venture. Thereafter, in furtherance of its plans to construct a single family dwelling on each of the two new lots, High Bar sought a CAFRA jurisdictional determination from DEP. DEP issued a written determination that no CAFRA, wetlands or other coastal permits would be required for the proposed development.

High Bar did not proceed with development of Lots 3.03 and 3.04 and Island Venture acquired them in 1994. The title search conducted by Island Venture did not reveal any recorded restrictions within the chain of title of either lot that would prohibit residential development. Island Venture did discover the deed restriction contained in the Master Deed of Condominium, which, by its terms, did not affect Lots 3.03 and 3.04.

Upon seeking construction permits in 1999, Island Venture was informed it could modify the 1989 CAFRA permit issued to High Bar. DEP believed the property was part of the nonmarina, approved residential area covered by the High Bar permit. But, DEP changed its position and required Island Venture to apply for a new CAFRA permit, because the two lots were within the marina area subject to the water dependent use restriction of the 1989 High Bar CAFRA permit. Island Venture submitted an application and, although the criteria for issuance of a permit were satisfied, DEP denied the application because the proposed residential use violated the water dependent use restriction required by the 1989 CAFRA permit.

Island Venture requested an adjudicatory hearing, and in granting summary disposition to DEP the Administrative Law Judge (ALJ) found the DEP-

approved deed restriction applied to the "adjacent marina property" and was not in the chain of title for the Island Venture property. Island Venture was a good faith, innocent purchaser, and had no actual or constructive notice that the High Bar CAFRA permit was intended to restrict the Island Venture property. However, the ALJ decided the Island Venture property should be restricted to water dependent use because DEP "intended" the Master Deed of Condominium to also apply to the Island Venture property when it issued the 1989 permit, and because enforcement of the permit restriction was required pursuant to the public policies underlying CAFRA. The DEP Commissioner adopted the ALJ's initial decision as his final decision.

The Appellate Division reversed in *Island Venture Associates v. DEP*, 359 N.J. Super. 391 (2003), concluding the public policy considerations underlying CAFRA were outweighed by the public's interest in the "integrity and reliability of our recording statutes."

Supreme Court Decision

The Court adopted the Appellate Division's approach of balancing the competing public policy considerations of CAFRA and the Recording Act, finding "the policies underlying the Recording Act outweigh those reflected in CAFRA." The Court recognized the public interest in the proper development of the coastal area and the ability of DEP to impose land use restrictions by deed restriction. It also recognized CAFRA permit conditions are generally intended to run with the land. N.J.S.A. 13:19-14. However, these considerations were insufficient to overcome the strong public interest in the recording statutes that are of paramount importance.

New Jersey is a race-notice jurisdiction affording priority to persons first to record without actual knowledge of an earlier acquired interest. *Cox v. RKA Corp.*, 164 N.J. 487 (2000). The recording statutes are "designed to compel the recording of instruments affecting title, for the ultimate purpose of permitting purchasers to rely upon the record title and to purchase and hold title to lands within this state with confidence." *Palamarg Realty Co. v. Rehac*, 80 N.J. 446 (1979). "The

fundamental purpose of our recording legislation is clearly to provide stability and certainty in land ownership by permitting subsequent takers in a chain to rely on what the record shows." *Palamarg*, 159 N.J. Super. 293 (App. Div. 1978). "The integrity of the recording scheme is paramount" (*Cox*, supra) and courts "should decide a question of title . . . in the way that will best support and maintain the integrity of the recording system." *Palamarg*, 80 N.J. 446. These considerations, as noted by the Court, are clearly set forth in the New Jersey Recording Act, which provides any instrument affecting title "shall, until duly recorded . . . be void and of no effect against . . . all subsequent bona fide purchasers. . . ." N.J.S.A. 46:22-1.

Beyond the immediate impact on Island Venture, the decision has broad policy implications for property owners and real estate professionals generally and is an important affirmation of the property recording system. Property owners are faced with ever increasing regulatory burdens requiring thorough due diligence prior to purchase. The ability to rely on a search of record title is essential. In holding "the policies underlying the Recording Act outweigh those reflected in CAFRA," the decision ensures a *bona fide* land purchaser will be able to continue to rely on the certainty and protections afforded by the public land record system notwithstanding competing environmental policy concerns.

The Court cautioned future decisions should be based on consideration of "the totality of circumstances," such as the failure to record the subject instrument, the impact on the subject property owner, and the public interest concerns. Here, the equities favored Island Venture because of its unchallenged status as a good faith, innocent purchaser. Any environmental disturbance from the proposed development would be minimal and could be addressed in the permitting process, as the Court did not order DEP to issue a CAFRA permit. The Court chided DEP for failing to assure the lots were properly restricted. DEP approved the High Bar restriction that failed to include the Island Venture lots and "seemed unaware" of the restriction when it issued a CAFRA non-jurisdiction determination in 1991. The affect of that uncertainty on the integrity

of title dictated *Island Venture*, as an innocent purchaser, prevail.¹

But the Court's framing its decision in the context of the specific facts should not limit the broader scope of the decision. The policy concerns of the Recording Act should be invoked and the paramount importance of the "integrity of the recording scheme" should take precedence in any future scenario involving a *bona fide* purchaser. Moreover, the Court did not allow its concern for the policy considerations at issue to be controlled by the specific facts. It could have avoided the conflict between the goals of CAFRA and the Recording Act by leaving *Island Venture* to rely on its traditional property owner remedy, the Constitutional right to just compensation for the taking of private property. The Court noted "[b]inding *Island Venture* to the water-dependent restriction effectively would defeat the entire two-lot project . . ." But, this would have placed a cloud on public land records generally. The Court's greater concern for the policy implications of its decision is evident by its ignoring the potential individual remedy available to *Island Venture*.

The decision may also mark a trend in reluctance of the judiciary to bow to DEP in cases involving conflicts between environmental policy and other statutory policy. The Court did not disregard CAFRA, but instead found other policy considerations more compelling. Similarly, the Appellate Division recently invalidated provisions of DEP's Technical Requirements for Site Remediation regulations because they conflicted with the New Residential Construction Off-Site Conditions Disclosure Act. *New Jersey Association of Realtors v. DEP*, 367 N.J.

Super. 154 (2004). Given the proliferation of the State's so-called "smart growth" initiatives, including the Highlands Water Protection and Planning Act passed by the Legislature on June 10, 2004, and anticipated "growth-sensitive" and endangered and threatened species habitat regulatory initiatives, these rebukes of DEP in relation to counterveiling policy concerns are noteworthy.

The ramifications of this decision for property owners and practitioners in the DEP-permitting context are uncertain. DEP adopted regulations and has implemented practices requiring submission of proof of recording of deed restriction instruments. While this should help avoid future similar disputes, recent experience suggests this practice lengthens an already slow permitting process. Despite the use of mostly "form" deed restriction, permits for regulated activities are conditioned upon DEP's review and approval of deed restrictions prior to recording. DEP's review of draft restrictions has in many cases been dreadfully slow, as there is no regulatory or permit-based clock governing the review period.

Recording before DEP approves an instrument can result in a need to release and re-record the instrument, a statutory process requiring a public hearing and approval by the DEP Commissioner upon a finding of public need. Waiting for DEP approval can often mean considerable project delays. Starting construction without recording is a permit violation that could result in an enforcement action. Permittees are left with difficult choices.

The conservation restriction is a popular open space preservation tool that DEP will continue to utilize. In the wake

of this decision, it is expected DEP will attempt to adopt regulations requiring the recording of deed restrictions before permit issuance. Given the difficulty involved in releasing conservation restrictions, this would likely lengthen the permit process and complicate the development process in general with respect to timing and coordination of securing local and state approvals, modifying development plans, and transferring permitted parcels to third parties.

This case, in overturning a decision that ran the risk of eviscerating the clarity of title and rendering useless public land records, is an important affirmation of the integrity and reliability of the property recording system that should allow prospective purchasers and property owners to continue to rely on a search of record title for a property with confidence. But, an unintended practical effect of the decision may be further complication and delay of the DEP permitting process as DEP revises its procedures for assuring proper recording of deed restrictions. Ultimately, it is imperative that DEP implement a procedure for timely review and approval of deed restrictions to avoid costly delays and expenditures of resources for both property owners and the DEP staff. ■

Footnote:

¹. The Court also distinguished *Aldrich v. Schwartz*, 258 N.J. Super. 300 (App. Div. 1992) relied on by DEP. The Court's treatment of *Aldrich* is discussed in R. Hluchan and E. Ehrhardt, *Island Venture: An Abrupt Departure from Aldrich v. Schwartz*, 177 N.J.L.J. 84 (starts on p. S-4 of this supplement) (July 12, 2004).