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Applying Merger Doctrine to Contracts for Sale of Real Estate

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Under the doctrine of merger by deed, certain terms, covenants and conditions of a contract for the sale of real property are merged with and into the deed to the property upon delivery. Based on the common law doctrine of *caveat emptor*, merger by deed provides a sense of finality to the transaction process. Since a deed is a subsequent writing between the parties, there is some logic to the terms of the deed taking precedence over the terms of the prior contract of sale, at least as to the subject matter of the deed.

Taken to an extreme, the merger doctrine mandates that prior agreements made between buyer and seller are superseded by the terms of the deed, so that the deed (along with other agreements delivered at closing) stands alone as the sole source of legally enforceable obligations between buyer and seller. Most sophisticated contracts of sale contain representations, warranties and covenants that are far broader than the subject matter of a deed, though, so the doctrine of merger by deed can result in unintended consequences.

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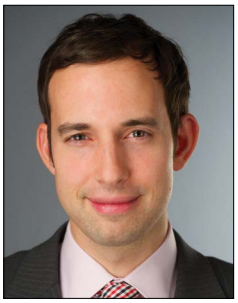

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Compared to courts in other states, New York courts are expansive in their application of merger by deed, tending to view many contract provisions as central to the conveyance and therefore subject to merger.

In *Davis v. Weg*, 104 A.D.2d 617, 619 (1984), the court articulated the general principle with respect to merger by deed under New York law

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as follows: "the obligations and provisions of a contract for the sale of land are merged in the deed and, as a result, are extinguished upon the closing of title" unless "there is a clear intent evidenced by the parties that a particular provision shall survive delivery of the deed, or where there exists a collateral undertaking." In other words, provisions which the parties did not intend to merge with the deed and provisions which are "not connected with the title, possession or quantity of land," are excluded from merger and will survive closing. *Alexey v. Salvador*, 217 A.D.2d 877, 878 (1995).

The court in *Davis* held that an obligation to the seller to pay the cost of curing violations was not merged into the deed, but the holding was based on an express survival clause in the contract of sale.

In the *Alexy* case, the court found that an easement for beach use purportedly reserved by a seller in the contract of sale, but not stated in the deed, should not be deemed a collateral obligation and should be merged into the deed. The *Alexy* holding is not surprising since matters of title are central to the subject matter of the deed.

Courts have also interpreted New York's merger doctrine to consider contract provisions entitling purchasers to prepaid rents, provisions requiring payment for change orders, and representations and warranties about hazardous substances on a property as central to the purchase and sale agreement and therefore subject to merger. See *Dourountoudakis v. Alesi*, 706 N.Y.S.2d 476 (2000) (regarding rents prepaid by tenants as of the closing that were not turned over to the purchaser at closing); *CGM Construction, Inc. v. Miller*, 693 N.Y.S.2d 763 (1999) (regarding payment owed by a purchaser to a seller for additional construction costs for work performed by the seller under the contract of sale that were not paid at closing); *Bickerstaff Real Estate v. Hanners*, 665 S.E.2d 705 (2008) (regarding an alleged breach of a representation and warranty arising from hazardous substances discovered following the closing).

Many courts outside New York take a more limited view of the merger doctrine. For example, courts have considered the provision of title insurance and the construction of a home as collateral rather than central to a purchase and sale agreement. See *Chavez v. Gomez*, 423 P.2d 31 (1967) (a New Mexico case regarding a promise to provide a title abstract or title insurance at closing, which the court held was not merged into the deed as it was intended to be delivered contemporaneously with the deed); *Urban v. Fed. Home Loan Mortg. Corp*., Civil No. 11-10915-FDS (2012) (a Massachusetts case regarding a promise to pay for title insurance at closing that was held to be a collateral obligation); *Kandalis v. Paul Pet Constr. Co*., 123 A.2d 345 (1956) (a Maryland case regarding an agreement to construct a home on the parcel sold that was also held to be a collateral obligation). Some courts have adopted additional exceptions to merger, including fraud exceptions.

Other courts outside New York have adopted other modifications to merger to bring the doctrine more closely in line with its original

purpose as well. For example, states such as Illinois and Georgia have adopted latency exceptions to merger, whereby defects that are not discoverable through a reasonably thorough inspection are actionable subsequent to the passage of title. See *Peterson v. Hubschman Construction Co.*, 389 N.E.2d 1154 (1979) (regarding the latency exception in Illinois); see *Worthey v. Holmes*, 287 S.E.2d 9 (1982) (regarding the latency exception in Georgia).

As the court noted in *TIAA Global Investments, LLC v. One Astoria Square LLC*, 127 A.D.3d 75, 88 (2015), New York courts do not recognize such an exception. Additionally, while New York courts apply merger irrespective of industry norms about the inclusion of certain contract terms in deeds, Florida courts define a collateral obligation as any promise that would not ordinarily be found in the terms of a deed, thereby significantly limiting the scope of merger. See *Burkett v. Rice*, 542 So. 2d 480 (Fla. Dist. Ct. App. 1989); *Bennett v. Behring Corp.*, 466 F. Supp. 689, 701 (S.D. Fla. 1979).

Notably, although merger is typically considered a seller-friendly doctrine, New York courts have applied merger regardless of which party benefits, even to the detriment of a seller. New York's broad interpretation of merger by deed is exemplified by two recent cases decided by the New York Supreme Court in New York County: *19 Stanton St. LLC v. 19 Stanton Realty LLC* and *Stempeck v. Townhouse W. 83rd, LLC*.

In the matter of *19 Stanton St. LLC v. 19 Stanton Realty LLC*, a buyer of real estate sued the seller for fraudulent misrepresentation arising out of the sale. The buyer's fraudulent misrepresentation claims were dismissed on the ground that the contract provisions on which they were based merged with the deed upon closing. Subsequently, the seller filed a claim for attorneys' fees it incurred in the dispute based on the attorneys' fees provision of the purchase and sale agreement. The court ruled that the attorneys' fees provision had merged with the deed because the provision did not include a survival clause (whereas other provisions did include a survival clause) and because "the court's decision in the prior action was explicitly based upon the merging of the parties' obligations into the executory contract, thus making the dispute, and the attorney's fees arising therefrom, integral to the contract." See *19 Stanton St. LLC v. 19 Stanton Realty LLC*, N.Y. Slip Op. 31766 (N.Y. Sup. Ct. 2020).

The matter of *Stempeck v. Townhouse West 83rd, LLC* originated as a suit by the buyer of a single-family home for breach of contract and related claims, which the court dismissed, ruling that the contract provision in question had merged with the deed. Subsequently, the sellers filed a motion for attorneys' fees pursuant to the attorneys' fees clause in the purchase and sale agreement.

Relying on *19 Stanton*, the court held that the attorneys' fees clause had also merged with the deed, rendering it unenforceable. Notably, the court rejected arguments that the clause was intended to survive closing and that the clause represented a collateral undertaking. The court rejected the former argument on account of the parties' failure to include a survival clause. The court rejected the latter argument because "any

attorneys' fees awarded in the action would have arisen during disputes related to the agreement, and attorneys' fees expended in enforcing a contract do not reflect an independent obligation." See *Stempeck v. Townhouse W. 83rd, LLC*, 2023 N.Y. Slip Op. 32419 (N.Y. Sup. Ct. 2023).

19 Stanton and *Stempeck* are significant because they highlight the broad reach of merger by deed in New York, affecting the enforceability of matters that are not ordinarily included in deeds and which parties might, therefore, not expect to merge. Given the purpose of the attorneys' fees clause—to create a disincentive to bringing frivolous claims—there is a compelling argument (in addition to the policy argument) that the parties intended the clause to apply to post-closing actions. Regarding attorneys' fees in particular, courts in Florida and Connecticut have held that attorneys' fees obligations do not merge upon the passage of title. See *Burkett v. Rice*, 542 So. 2d 480 (Fla. Dist. Ct. App. 1989) (holding that attorneys' fees did not merge with the deed because they constitute a collateral agreement); *Feinstein v. Keenan*, 2013 Conn. Super. LEXIS 2365 at 14 (2013) (holding that the application of the merger doctrine to the attorneys' fees clause would "make that provision nugatory from its inception" and would not reflect "the intent of the contract provision, nor the intent of the contracting parties").

As noted in the *Davis* case, parties often include express survival clauses for certain provisions, such as representations and warranties, in a contract for the sale of real property to establish clear intent that a particular provision should not be merged into the deed.

In the absence of a survival clause explicitly stating the parties' intentions regarding particular provisions in purchase and sale agreements, New York courts are likely to rule in favor of merger. Even when there is a strong basis to argue the intent of the parties for survival or that a contested provision is a collateral obligation, without an express survival clause there is a substantial risk that New York courts will apply the merger doctrine.

Notably, *19 Stanton* suggests that the inclusion of survival clauses pertaining to certain terms of a purchase and sale agreement may be used to read into the contract an intention to merge provisions not covered by a survival clause. The lesson for New York practitioners (buyers' and sellers' counsel alike) is that nothing should be left to chance. In order to overcome a defense of merger by deed, any intention by the parties to have a provision survive closing should be clearly expressed in the contract.