CITY OF MILWAUKEE

Form CA-43

GRANT F. LANGLEY
City Attorney

RUDOLPH M. KONRAD
PATRICK B. McDONNELL
LINDA ULISS BURKE
Deputy City Attorneys

OFFICE OF CITY ATTORNEY
800 CITY HALL
200 EAST WELLS STREET
MILWAUKEE, WISCONSIN 53202-3551
TELEPHONE (414) 286-2601
TDD 286-2025
FAX (414) 286-8550

THOMAS O. GARTNER
BRUCE D. SCHRIMPF
ROXANE L. CRAWFORD
SUSAN D. BICKERT
HAZEL MOSLEY
STUART S. MUKAMAL
THOMAS J. BEAMISH
MAURITA F. HOUREN
JOHN J. HEINEN
MICHAEL G. TOBIN
DAVID J. STANOSZ
SUSAN E. LAPPEN
JAN A. SMOKOWICZ
PATRICIA A. FRICKER
HEIDI WICK SPOERL
KURT A. BEHLING
GREGG C. HAGOPIAN
ELLEN H. TANGEN
MELANIE R. SWANK
JAY A. UNORA
DONALD L. SCHRIEFER
EDWARD M. EHRLICH
LEONARD A. TOKUS
VINCENT J. BOBOT
MIRIAM R. HORWITZ
MARYNELL REGAN
G. O'SULLIVAN-CROWLEY
DAWN M. BOLAND
KATHRYN M. ZALEWSKI
MEGAN T. CRUMP
ELOISA DE LEÓN
ADAM STEPHENS

Assistant City Attorneys

May 25, 2005

Dr. Teodoros Medhin, Chair
Zoning Code Technical Committee
Room B-11, City Hall

Re: Proposed § 295-122, Milwaukee Code of Ordinances
(Banning "Negative Use" Restrictive Covenants)

Dear Dr. Medhin:

This letter will respond to your request of May 23, 2005 for the opinion of this office as to the legality and enforceability of a proposed ordinance (new § 295-122, Milwaukee Code of Ordinances, hereafter "MCO"), which would amend the City of Milwaukee Zoning Code (ch. 295, Milwaukee Code of Ordinances, hereafter the "Code"). This proposed ordinance has been introduced by Alderman T. Anthony Zielinski, and would ban, as against public policy, so-called "negative use" restrictive covenants within the City of Milwaukee (the "City").

A "negative use" covenant as referred to in proposed new § 295-122, MCO, is a measure sometimes employed by retailers that are vacating a site and selling the underlying real estate, and refers to a restriction imposed by the seller banning its sale to a potential competitor (*i.e.*, to a buyer engaged in the same or a similar line of retail trade). The ostensible motivation for proposed § 295-122, MCO is to preclude situations whereby the use of "negative use" restrictive covenants renders segments of the commercial real estate market and thus whole City neighborhoods essentially unavailable for location of retail establishments that are useful and necessary for City residents. The emphasis in this respect is apparently upon grocery stores and pharmacies, although neither the text of

proposed new § 295-122, MCO nor its philosophical underpinnings are necessarily limited to those or any other branch of retail trade.

On October 18, 2004, this office transmitted an opinion (copy attached) to Alderman Zielinski and to Commissioner Richard Marcoux of the Department of City Development concluding that an ordinance of this type "would expose the City to litigation and liability," and that its legality and enforceability was thus problematic. Subsequently, Alderman Zielinski informed our office of an effort by the City of Chicago to adopt a similar ordinance banning "negative use" restrictive covenants in that city. We agreed to reconsider our earlier opinion in light of that information. Following reconsideration and the conduct of further research, we conclude that our earlier opinion of October 18, 2004 was correct in its conclusions, and we therefore reaffirm those conclusions. While we are certainly mindful of the concerns underlying proposed § 295-122, MCO, we do not believe that its particular approach (*i.e.*, a declaration that all "negative use" restrictive covenants are void as against public policy) is consistent with Wisconsin law, or that a reviewing court would find that proposed ordinance to be either legal or enforceable.

Our analysis begins with the text of proposed § 295-122, MCO, which states as follows:

> **295-122. Private Negative Use Restrictions Prohibited.** A private agreement that purports to imposed negative use restrictions upon real property in the city so as to prohibit or materially limit the use of such property for a particular type of general retail establishment after an operator of the same type of general retail establishment has terminated operations at the site, when such establishment would otherwise be a permitted use, limited use or special use under this chapter, shall be against public policy, shall be void and unenforceable and shall be subject to the penalty provisions of s. 295-309-6.[1]

[1] The counterpart ordinance currently under consideration in Chicago is similar, but not identical to proposed § 295-122, MCO, and is specifically directed at grocery stores and drug stores. It reads as follows:

> 17-1-1004. Negative Use Restrictions Prohibited As Against Public Policy. Notwithstanding Section 17-1-1003, a private agreement that purports to impose negative use restrictions upon real property in the City so as to prohibit or materially limit the use of such real property for grocery store or drug store purposes after a grocery store or drug store operator has terminated operations at the site, when such uses would otherwise be permitted under the Zoning Ordinance, shall be against public policy, shall be void and unenforceable, and shall be subject to the City's remedial and enforcement powers under Section 17-16-0508, Section 17-16-0509, Section 17-16-0511 (with each day such negative use covenant remains of record or otherwise effective constituting a separate and distinct offense) and Section 17-16-0512.

At the outset, we do not believe that the purposes and objectives of proposed § 295-122, MCO, quoted above, pertain to the exercise of the City's zoning power. Thus, it would not be suitable to include such a provision within the text of the Code. Proposed § 295-122, MCO is a trade-regulation measure aimed at forestalling a particular type of anticompetitive restrictive covenant that has become increasingly common in the retail sector. In contrast, zoning is concerned with regulation of land use, and with preclusion of incompatible uses that would be detrimental to the health, safety, and general welfare of a community. These objectives are set forth in the State's enabling act conferring the zoning power upon municipalities, Wis. Stat. § 62.23(7)(a), which states as follows:

> (7) ZONING. (a) *Grant of power.* For the purpose of promoting health, safety, morals or the general welfare of the community, the council may regulate and restrict by ordinance, subject to par. (hm), the height, number of stories and size of buildings and other structures, the percentage of lot that may be occupied, the size of yards, courts and other open spaces, the density of population, and the location and use of buildings, structures and land for trade, industry, mining, residence or other purposes if there is no discrimination against temporary structures. This subsection and any ordinance, resolution or regulation enacted or adopted under this section, shall be liberally construed in favor of the city and as minimum requirements adopted for the purposes stated. This subsection may not be deemed a limitation of any power granted elsewhere.

In *Euclid v. Ambler Realty Company*, 272 U.S. 365, 47 S.Ct. 114, 71 L.Ed. 303 (1926), the seminal decision of the United States Supreme Court upholding the constitutionality of the municipal exercise of the zoning power, the Court confirmed that the focus of the zoning power is upon preclusion of incompatible land uses that impair the public welfare, stating as follows:

> The matter of zoning has received much attention at the hands of commissions and experts, and the results of their investigations have been set forth in comprehensive reports. These reports which bear every evidence of painstaking consideration, concur in the view that the segregation of residential, business and industrial buildings will make it

> easier to provide fire apparatus suitable for the character and intensity of the development in each section; that it will increase the safety and security of home life, greatly tend to prevent street accidents, especially to children, by reducing the traffic and resulting confusion in residential sections, decrease noise and other conditions which produce or intensify nervous disorders, preserve a more favorable environment in which to rear children, etc. . . .

272 U.S. at 394, 47 S.Ct. at 120.

Similarly, in *Town of Hobart v. Collier*, 3 Wis. 2d 182, 87 N.W.2d 868 (1958), the Wisconsin Supreme Court characterized the purpose of zoning as follows:

> The purpose of zoning is to set aside areas for specific uses and to protect them from encroachments in the form of other uses inconsistent with the uses to which they are dedicated. *Tingly v. Gerda* [209 Wis. 63, 243 N.W. 317 (1932)], *supra*. In making the classifications necessary to facilitate that purpose, the municipality must recognize the natural reasons and differences suggested by necessity and circumstances existing in the area with which the ordinance deals.

3 Wis. 2d at 189, 87 N.W.2d at 872.

See also, 1 Rathkopf's The Law of Zoning and Planning (2004 ed.) § 1:3, stating that: "Zoning is the regulation by the municipality of the use of land within the community, and of the buildings and structures which may be located thereon, in accordance with a general plan and for the purposes set forth in the enabling statute."

In Wisconsin, municipalities exercise their zoning powers through the provisions of a comprehensive plan and/or a comprehensive zoning ordinance, which involves the division of the municipality into various zoning districts "of such number, shape and area as may be deemed best suited to carry out the purposes . . ." of the plan and/or ordinance, and within which the municipality "may regulate and restrict the erection, construction, reconstruction, alteration or use of buildings, structures or land." Wis. Stat. §§ 62.23(7)(b) and (c); *see also Step Now Citizens Group v. Town of Utica Planning and Zoning Committee*, 2003 WI App. 109 ¶¶ 25, 39-45, 264 Wis. 2d 662, 678, 683-686, 663

N.W.2d 833, 841, 843-845. Milwaukee's Code is of this type. It classifies the City into residential, commercial, downtown, industrial, "special," and "overlay" districts, subdivides each of these district classifications into a number of specific "zoning districts," and then assigns one of four use classifications (*i.e.*, permitted, limited-use, special-use, and prohibited) to each category of land uses within each of these zoning districts in accordance with the various "Use Tables" incorporated into the Code. The Code thus expresses the essence of land-use based comprehensive zoning, as envisioned by the model originally upheld in *Euclid v. Ambler Realty Company, supra*, and its extensive progeny.

Significantly absent from the concept of zoning and from the Code is any suggestion of any objective of restraining otherwise-valid private contracts and covenants affecting the use of land for the purpose of promoting specific types of uses (in this instance, retail uses). Proposed § 295-122, MCO, which purports to ban "negative use" restrictive covenants as against public policy in the interests of promoting the continuation or reestablishment of specific types of retail uses engaged in by the former owners of those parcels is a measure of this type. It has little or nothing to do with zoning–a fact confirmed by its literal text, which limits its applicability to property that has already been deemed suitable (or at least conditionally suitable) in the zoning context, for the location of the type of retail establishment(s) within the scope of the proposed ban. Indeed, such a ban runs counter to the second sentence of § 295-111, MCO, entitled "Interpretation," which states that: "It is not the intent of this chapter [referring to ch. 295, MCO, the Code] to interfere with, abrogate, or annul any easements, covenants, or other agreements between parties, or to impair or interfere with any provision of law or ordinance or any rules, regulations or permits previously adopted or issued or which shall be adopted or issued pursuant to law relating to the use of structures or premises." This provision expresses the well-established proposition that the zoning power and restrictions imposed by private covenants respecting the use of land operate independently. In this respect, Rathkopf's, *supra*, § 82:2, states as follows:

> . . . As an exercise of the state police power to promote the general welfare, zoning is entirely divorced in concept, creation, enforcement, and administration from restrictions arising out of agreements between private parties who, in the exercise of their constitutional right of freedom of contract, can impose whatever lawful restrictions upon the use of their lands that they deem advantageous or desirable. . . .

> Both types of land use restrictions are held by courts to legally operate independently of one another. Whether either type of restriction is valid and enforceable presents two separate and distinct legal issues. As a local governmental exercise of the police power, zoning restrictions are subject to the usual constitutional and statutory limitations imposed on the exercise of the zoning power. Private covenant restrictions are subject to limitations imposed by the sometimes technical common law real property rules in each state which govern the creation, operation, termination, and enforcement of covenant restrictions that "run with the land." . . .
>
> An important implication of the "independent operation rule" is the uniformly held view of state courts that a zoning ordinance does not terminate, supersede, or in any way affect a valid private restriction on the use of real property. The fact that a use may be permitted by a zoning ordinance does not relieve an owner of the obligation to comply with a more restrictive private covenant. When a zoning restriction and a private covenant are in conflict, the more restrictive of the two prevails. . . .

[Footnotes omitted.]

Wisconsin courts are in accord. *See Sills v. Walworth County Land Management Committee*, 2002 WI App. 111, ¶¶ 27-28, 254 Wis. 2d 538, 557-558, 648 N.W.2d 878, 887. Decisions in other states have reaffirmed the principle that otherwise-valid restrictive covenants are matters of private contract while zoning regulations are a method of governmental exercise of the police power, and thus the latter cannot destroy, impair, or abrogate the former. *See, McDonald v. Emporia-Lyon County Joint Board of Zoning Appeals*, 10 Kan. App. 2d 235, 237-238, 697 P.2d 69, 71-72 (1985); *Myers v. Smith*, 112 Ohio App. 169, 171-172, 171 N.E.2d 744, 746 (1960); *In re Michener's Appeal*, 382 Pa. 401, 404-405, 115 A.2d 367, 369-370 (1955). We thus conclude that the type of regulation represented by proposed § 295-122, MCO is fundamentally unrelated to the purposes and objectives of the exercise of the City's zoning powers, and thus should not be included as a provision of the Code even if it would otherwise be valid.

We now turn to consideration of the validity of proposed § 295-122, MCO, which, as already noted, seeks to ban a particular type of restrictive covenant as against "public

policy." The law is well established in Wisconsin that, while restrictive covenants are not particularly favored (due to the fact that they restrict the free transferability and use of property), they will be enforced if their intention is clear and their language is unambiguous. This conclusion has been expressed in numerous Wisconsin court decisions. *See, e.g., Pertzsch v. Upper Oconomowoc Lake Association*, 2001 WI App. 232 ¶ 8, 248 Wis. 2d 219, 225, 635 N.W.2d 829, 831; *Pietrowski v. Dufrane*, 2001 WI App. 175 ¶ 7, 247 Wis. 2d 232, 240, 634 N.W.2d 109, 113. In *Crowley v. Knapp*, 94 Wis. 2d 421, 434-435, 288 N.W.2d 815, 822 (1980), the Court stated as follows:

> This court consistently holds that public policy favors the free and unrestricted use of property. Accordingly, restrictions contained in deeds and in zoning ordinances must be strictly construed to favor unencumbered and free use of property. *McKinnon v. Benedict*, 38 Wis. 2d 607, 619, 157 N.W.2d 665 (1968); *State ex rel. Bollenbeck v. Village of Shorewood Hills*, 237 Wis. 501, 297 N.W. 568 (1941); *Cohen v. Dane County Board of Adjustment*, 74 Wis. 2d 87, 91, 246 N.W.2d 112 (1976). In *Cohen*, we cited *Rathkopf*, 1 The Law of Zoning and Planning (4th ed.), ch. 9, at p. 9.1, for the proposition that restrictions on the use of property are to be construed in favor of free use. A provision either in a zoning ordinance or in a deed restriction which purports to operate in derogation of the free use of property must be expressed in clear, unambiguous, and peremptory terms.

In *Zinda v. Krause*, 191 Wis. 2d 154, 528 N.W.2d 55 (Ct. App. 1995), the Court of Appeals confirmed that a restrictive covenant will be enforced if its purpose and intent are clearly ascertainable, even beyond any specific enumeration of prohibited activities expressed by the text of the covenant itself, stating in pertinent part as follows:

> . . . [I]f the intent of a restrictive covenant can be clearly ascertained from the covenant itself, the restrictions will be enforced. *Voyager Village Property Owners Association v. Johnson*, 97 Wis. 2d 747, 749, 295 N.W.2d 14, 15 (Ct. App. 1980). By intent we do not mean the subjective intent of the drafter, but the scope and purpose of the covenant as manifest by the language used. See *Hall v. Church of the Open Bible*, 4 Wis. 2d 246, 248, 89 N.W.2d 798, 799 (1958). . . .

> We are mindful that the Wisconsin Supreme Court has indicated that a restrictive covenant is only enforceable if it imposes the restriction by express terms [citing *Crowley v. Knapp*, 94 Wis. 2d 421, 434-436, 288 N.W.2d 815, 822-823 (1980)]. However, . . . we do not construe *Crowley* to mean that a restrictive covenant is enforceable only as to those activities specifically enumerated in the covenant itself. Rather, we conclude that where the purpose of a restrictive covenant may be clearly discerned from the terms of the covenant, the covenant is enforceable against any activity that contravenes that purpose. This conclusion is supported by cases decided both before and after *Crowley*. . . .
>
> Based upon the foregoing cases, we conclude that a restrictive covenant need not expressly prohibit the specific activity in question in order to be enforceable. See also *Joyce v. Conway*, 7 Wis. 2d 247, 96 N.W.2d 530 (1959); *Voyager Village*, 97 Wis. 2d 747, 295 N.W.2d 814.

Zinda v. Krause, supra, 191 Wis. 2d at 166, 167, 170, 528 N.W.2d at 59, 60.

Several Wisconsin decisions have adopted a "reasonableness" test for determining the enforceability of restrictive covenants. That is, a restrictive covenant will be enforced if its terms are found to be "reasonable," and will not be enforced if they are found to be "unreasonable." *McKinnon v. Benedict*, 38 Wis. 2d 607, 619, 157 N.W.2d 665, 670 (1968); *Hall v. Church of the Open Bible*, 4 Wis. 2d 246, 248-249, 89 N.W.2d 798, 799-800 (1958); *Doherty v. Rice*, 240 Wis. 389, 393, 3 N.W.2d 734, 735 (1942). In *Weiland v. Paulin*, 2002 WI App. 311, 259 Wis. 2d 139, 655 N.W.2d 204, the Court of Appeals expressed the applicable "reasonableness" standard as follows:

> In determining whether a deed restriction is reasonable, a court must inquire (1) whether it is reasonable under all the facts and circumstances of the transaction in light of the situation, business, and objects of the parties; and (2) whether it is for a just and honest purpose, for the protection of the legitimate interest of the party in whose favor it is imposed. *Dodge v. Carauna*, 127 Wis. 2d 62, 65, 377 N.W.2d 208 (Ct. App. 1985).

2002 WI App. 311 ¶ 17, 259 Wis. 2d 139, 150-151, 655 N.W.2d at 210.

In *Dodge v. Carauna*, 127 Wis. 2d 62, 377 N.W.2d 208 (Ct. App. 1985), the Court of Appeals stated the following:

> Public policy in Wisconsin favors the free and unrestricted use of property. *Crowley v. Knapp*, 94 Wis. 2d 421, 434, 288 N.W.2d 815, 822 91980). "Accordingly, restrictions contained in deeds . . . must be strictly construed to favor unencumbered and free use of property. . . . [such restrictions] must be expressed in clear, unambiguous, and peremptory terms." *Id.* at 434-35, 288 N.W.2d at 822.
>
> The fundamental inquiry regarding a deed restriction is: "Is [it] a reasonable one under all the facts and circumstances of the transactions in the light of 'the situation, business, and objects of the parties,' and [is] the restriction 'for a just and honest purpose, for the protection of the legitimate interests of the party in whose favor it is imposed . . .'" (Citations omitted). *McKinnon v. Benedict*, 38 Wis. 2d 607, 619, 157 N.W.2d 665, 670 (1968). The standard of validity for a deed restriction in Wisconsin is reasonableness. *Le Febvre v. Osterndorf*, 87 Wis. 2d 525, 533, 275 N.W.2d 154, 159 (Ct. App. 1979).

[Footnote omitted.] *Dodge v. Carauna*, 127 Wis. 2d at 65, 377 N.W.2d at 210.

The enforceability in Wisconsin of clear, unambiguous and reasonable restrictive covenants therefore cannot be questioned. Stated alternatively: "[U]nder Wisconsin law, reserving a covenant that will run to one's benefit will not void a land transaction." *Freedom from Religion Foundation, Inc. v. City of Marshfield*, 203 F.3d 487, 492 (7th Cir. 2000), citing *In re Barkhausen*, 142 Wis. 292, 125 N.W. 680 (1910). This prevailing rule of decisional law expresses the "public policy" of the State of Wisconsin. We are not persuaded that the attempt embodied in proposed § 295-122, MCO to declare "negative use" restrictive covenant as void for "public policy" reasons can validly change this result.

A restrictive covenant is a species of contract that confers promises, benefits, and obligations pertaining to the ownership or use of real property. 20 Am. Jur. 2d "Covenants, Conditions and Restrictions" §§ 1, 4, 8, 9 (2d ed. 1995). It is well established that the power to declare a contract void as being against public policy may

be exercised "only in cases free from doubt." *Continental Insurance Company v. Daily Express, Inc.*, 68 Wis. 2d 581, 589, 229 N.W.2d 617, 621 (1975); *Northern States Power Company v. Natural Gas Company, Inc.*, 232 Wis. 2d 541, 545-546, 606 N.W.2d 613, 615-616 (Ct. App. 1999); *Trumpf v. Shoudy*, 166 Wis. 353, 359, 164 N.W. 454, 456 (1917). Indeed, the Wisconsin Supreme Court has recently characterized this type of ruling as "extreme." *Whirlpool Corporation v. Ziebert*, 197 Wis. 2d 144, 149, 539 N.W.2d 883, 884 (1999). We do not view these circumstances as the type that would justify the "extreme" measure of banning an entire class of restrictive covenants.

Furthermore, there is significant doubt as to whether such an objective, even if otherwise valid, may be accomplished by way of a local ordinance, given that the "public policy" in question is that of the State of Wisconsin, and not that of a particular municipality or other subdivision of the State. "Public policy" may be expressed by statute, by administrative regulation, or "by the court's expression of the policy of the common law." *Northern States Power Company v. Natural Gas Company, Inc., supra*, 232 Wis. 2d at 545, 546, 606 N.W.2d at 615-616; see also *Baierl v. McTaggart*, 2001 WI 107 ¶ 12, 245 Wis. 2d 632, 640, 629 N.W.2d 277, 281. The "public policy" of the State respecting the enforceability of restrictive covenants cannot, in our opinion, be overturned by an inconsistent local ordinance.[2]

We have examined the case law cited by counsel for the City of Chicago in support of Chicago's parallel proposed ordinance, and conclude that that case law is neither inconsistent with the discussion contained herein, nor does it suggest a different result. The Chicago Corporation Counsel has cited the following two cases: *Davidson Brothers Inc. v. D. Katz & Sons, Inc.*, 274 N.J. Super. 159, 643 A.2d 642 (1994) and *Natural Products Company v. Dolese & Shepard Company*, 309 Ill. 230, 140 N.E. 840 (1923). Neither of these cases support the legality and enforceability of a measure such as proposed § 295-122, MCO.

In *Davidson Brothers, supra*, the seller (Davidson Brothers, Inc.), a grocery store chain, had operated a supermarket for a number of years on a parcel located in the inner city of New Brunswick, New Jersey, a poor neighborhood containing many residents that did not

[2] Nor is this a situation one in which the enforcement of the restrictive covenant in question would violate an important public policy expressed in a constitutional guarantee or a clear statutory provision. *Cf. Shelley v. Kraemer*, 334 U.S. 1, 68 S.Ct. 836, 92 L.Ed. 2d 1161 (1948) (holding that the Fourteenth Amendment to the United States Constitution precludes the enforcement of racially based restrictive covenants).

have convenient transportation to outlying supermarkets or grocery stores. Davidson Brothers, Inc. relocated its inner-city supermarket to a site approximately two miles away, and sold its former site to D. Katz & Sons, Inc., with a restrictive covenant precluding the operation of a supermarket or grocery store upon the site for a period of 40 years following the date of sale. The City of New Brunswick and the New Brunswick Housing Authority unsuccessfully attempted to attract a food retailer to the neighborhood within which the store was located. The Housing Authority thereupon purchased that former Davidson Brothers grocery site site from D. Katz & Sons, Inc. and invited proposals to lease that property for a supermarket, contrary to the terms of the restrictive covenant associated with the Davidson Brothers/D. Katz & Sons, Inc. sale. Davidson Brothers filed an action seeking an injunction against the proposed lease, which proceeded all the way to the New Jersey Supreme Court. *Davidson Brothers, Inc. v. D. Katz & Sons, Inc.*, 121 N.J. 196, 579 A.2d 288 (1990).

In that decision, the New Jersey Supreme Court announced a rule that noncompetitive covenants restraining the use of property would be subject to a "reasonableness" standard closely analogous to the "reasonableness" standard adopted by the several Wisconsin decisions pertaining to the enforceability of such restrictive covenants, discussed earlier in this letter. The New Jersey court emphasized that the applicable analysis must be undertaken on a case-by-case basis, depending upon the business conditions underlying each particular restrictive covenant for which enforcement may be sought, stating as follows:

> Courts today recognize that it is not unreasonable for parties in commercial property transactions to protect themselves from competition by executing non-competition covenants. Business persons, either as lessees or purchasers may be hesitant to invest substantial sums if they have no minimal protection from a competitor starting a business in the near vicinity. Hence, rather than limiting trade, in some instances, restrictive covenants may increase business activity.
>
> We recognize that "reasonableness" is necessarily a fact-sensitive issue involving an inquiry into present business conditions and other factors specific to the covenant at issue. . . . The pivotal inquiry, therefore, becomes what factors should a court consider in determining whether such

a covenant is "reasonable" and hence enforceable. We conclude that the following factors should be considered:

1. The intention of the parties when the covenant was executed, and whether the parties had a viable purpose which did not at the time interfere with existing commercial laws, such as anti-trust laws, or public policy.

2. Whether the covenant had an impact on the considerations exchanged when the covenant was originally executed. This may provide a measure of the value to the parties of the covenant at the time.

3. Whether the covenant clearly and expressly sets forth the restrictions.

4. Whether the covenant was in writing, recorded, and if so, whether the subsequent grantee had actual notice of the covenant.

5. Whether the covenant is reasonable concerning area, time or duration. Covenants that extend for perpetuity or beyond the terms of a lease may often be unreasonable. . . .

6. Whether the covenant imposes an unreasonable restraint on trade or secures a monopoly for the covenantor. This may be the case in areas where there is limited space available to conduct certain business activities and a covenant not to compete burdens all or most available locales to prevent them from competing in such activity. . . .

7. Whether the covenant interferes with the public interest. . . .

8. Whether, even if the covenant was reasonable at the time it was executed, "changed circumstances" now make the covenant unreasonable. . . .

121 N.W. at 210-212, 579 A.2d at 295.

The key point of *Davidson Brothers, supra,* is that the enforceability of a "negative use" restrictive covenant is to be determined on a case-specific and not on a blanket basis. In New Jersey, this is to be accomplished by application of the eight-factor test announced by the New Jersey Supreme Court in *Davidson Brothers, supra*, quoted above. The decision cited by counsel for the City of Chicago, *Davidson Brothers, Inc. v. D. Katz & Sons, Inc.*, 274 N.J. Super. 159, 643 A.2d 642 (1994), which was the subsequent decision of the Superior Court following remand from the New Jersey Supreme Court, simply applied this eight-factor test to the particular facts, circumstances and economic conditions prevailing in the inner city of New Brunswick, and on that basis invalidated the Davidson Brothers/D. Katz & Sons, Inc. restrictive covenant. This case cannot be fairly read to endorse a blanket ban on the enforceability of "negative use" restrictive covenants such as that sought by proposed § 295-122, MCO.

We believe that a Wisconsin court, confronted with a similar set of circumstances, would engage in a similar (although perhaps not identical) form of analysis, particularly in light of the prevailing "reasonableness" standard already announced by Wisconsin courts in evaluating the enforceability of restrictive covenants of this type. While the *Davidson Brothers* cases do indicate that under the proper set of facts and circumstances, the public interest in assuring the availability of a particular type of retail service to an urban population **may** provide justification for non-enforcement of a "negative use" restrictive covenant, they emphasize that that cannot be assumed in every case and that the applicability of a case-specific multi-factor test for determining the "reasonableness" of each particular restrictive covenant precludes the legality and enforceability of an across-the-board ban. Indeed, the application of New Jersey's eight-factor "reasonableness" test to a different set of facts and circumstances than that prevailing in *Davidson Brothers, supra*, produced quite a different result in another New Jersey case occurring at approximately the same time. *Acme Markets, Inc. v. Wharton Hardware and Supply Corporation*, 890 F.Supp. 1230 (D.N.J. 1995) (denying motion for summary judgment seeking invalidation of restrictive covenant against establishment of a retail food business).

The remaining case cited by counsel for the City of Chicago, *Natural Products Company v. Dolese & Shepard Company, supra*, does not indicate or suggest the legality or enforceability of proposed § 295-122, MCO. Indeed, its holding suggests the opposite result:

> Every owner of property has the legal right to dispose of his estate, either absolutely or conditionally, or to regulate the manner in which the estate shall be used and occupied, as he may deem best and proper, and if conditions and restrictions imposed are not subversive of public interests they will be enforced. . . .

309 Ill. at 233-234, 140 N.E. at 841.

This language holds that restrictive covenant, even of the "negative use" type, are enforceable if they are not "subversive of public interests." Of course, an inquiry as to whether a particular covenant is "subversive of public interests" involves a case-by-case inquiry, which may include the application of the type of "reasonableness" test endorsed by the Wisconsin and New Jersey courts, as discussed above. This runs contrary to the notion that such covenants may lawfully be subjected to an ordinance-based ban, whether on "public policy" grounds or otherwise.

We also believe that proposed § 295-122, MCO is of doubtful constitutionality, on two separate grounds. First, we believe that it may violate the constitutional ban on impairment of contract contained in Art. I § 10 of the United States Constitution and Art. I § 12 of the Wisconsin Constitution. Proposed § 295-122, MCO would deprive the seller of property of a valuable contractual right–*i.e.*, the right to preclude the sale of property, by way of a restrictive covenant, to a potential competitor. The prohibition conferred by the "impairment of contract" clauses of the United States and Wisconsin Constitutions is not absolute, and is subject to the reasonable exercise of governmental police powers. Nevertheless, those clauses "must be understood to impose *some* limits upon the power of a State to abridge existing contractual relationships, even in the exercise of its otherwise legitimate police power." [Emphasis in original] *Chappy v. Labor and Industry Review Commission*, 136 Wis. 2d 172, 187, 401 N.W.2d 568, 574-575 (1987) quoting *Allied Structural Steel Company v. Spannaus*, 438 U.S. 234, 242, 98 S.Ct. 2716, 2721, 57 L.Ed.2d 727 (1978). Wisconsin courts have articulated a multi-part test for analyzing challenges brought under the constitutional "contract clauses," as follows:

> 1. Whether an obligation of contract has been impaired, i.e. whether the legislation in question "alters the contractual expectations of the parties";

2. Whether any impairment of the obligation of contract is unconstitutional, which involves an inquiry as to the severity of the impairment;

3. Whether the legislative enactment impairing the obligation of contract has a significant and legitimate public purpose, "such as the remedying of a broad and general social or economic problem."; and

4. Whether the legislative enactment is "reasonable and of a 'character appropriate to the public purpose justifying the adoption.'"

State ex rel. Cannon v. Moran, 111 Wis. 2d 544, 554-561, 331 N.W.2d 369, 374-378 (1979). Other Wisconsin decisions have enunciated similar multi-part tests for constitutional "contract clause" analysis. See, *e.g., Wisconsin Professional Police Association, Inc. v. Lightbourn*, 2001 WI 59 ¶¶ 146-148, 243 Wis. 2d 512, 593-594, 627 N.W.2d 807, 848; *Chappy v. Labor and Industry Review Commission, supra*, 136 Wis. 2d at 187-188, 401 N.W.2d at 575; *Reserve Life Insurance Company v. LaFollette*, 108 Wis. 2d 637, 644-645, 323 N.W.2d 173, 176 (1982). Whether proposed § 295-122, MCO would survive these tests of constitutional "contract clause" scrutiny is uncertain, particularly in light of: (1) its "blanket" applicability without consideration for the particular facts and circumstances underlying each specific restrictive covenant at issue; and (2) the necessity of evaluating the public interest in access to retail services as against the proposed ordinance's undoubted impairment of a seller's contract right to insist upon a non-competitive "negative use" covenant as a condition of sale.

Second, we are concerned that proposed § 295-122, MCO may constitute a "taking" of a property right without the provision of just compensation in violation of the Fifth Amendment to the United States Constitution and of Art. I § 13 of the Wisconsin Constitution. While both of these constitutional provisions address the taking of property "for public use without just compensation," it is quite possible that this constitutional prohibition may extend to this situation, which results in impairment of a property owner's right via the mechanism of a "negative use" restrictive covenant, to exclude potential commercial competitors. It is established that the "government does not have unlimited power to redefine property rights." *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 438, 102 S.Ct. 3164, 3178, 73 L.Ed.2d 868 (1982); *Webb's*

Fabulous Pharmacies, Inc. v. Beckwith, 449 U.S. 155, 164, 101 S.Ct. 446, 452, 66 L.Ed.2d 358 (1980) (holding that "a State, by *ipse dixit*, may not transfer private property into public property without compensation"); *Noranda Exploration, Inc. v. Ostrom*, 113 Wis. 2d 612, 625-626, 335 N.W.2d 596, 603-604 (1983) (holding that the State "lacks the power to restructure rights so as to interfere with traditional attributes of property ownership, such as the right to exclude others.").

The right to preclude a future and a nearby commercial competitor is indeed a valuable property right possessed by any seller of commercial real estate, particularly when that seller intends to relocate its operation within the general vicinity of the real estate to be sold. Whether a municipality or any other unit of government may deprive that seller of that right by legislative or regulatory fiat without the provision of just compensation may very well present a substantial constitutional question, which cannot be resolved without consideration of particular facts and circumstances. Certainly, it may be argued that the government, in so doing, oversteps its authority by transferring to private property owners the burden of providing a public benefit, *i.e.*, ready access by residents of a particular neighborhood or area to grocery stores, pharmacies, or other specified retail services of the government's selection.

Accordingly, we conclude that proposed § 295-122, MCO, banning the enforceability of "negative use" restrictive covenants in the retail context, would likely be neither lawful nor enforceable. The basis for our conclusion is primarily premised upon the "blanket" nature of that proposed ordinance, voiding all such restrictive covenants as violative of "public policy" irrespective of their "reasonableness" or application to particular facts and circumstances and upon the proposed ordinance's doubtful constitutionality.

Very truly yours,

GRANT F. LANGLEY
City Attorney

Stuart S. Mukamal

STUART S. MUKAMAL
Assistant City Attorney
SSM:lmb: 1172-2005-1477:93491
attachment

CITY OF MILWAUKEE

Form CA-43

GRANT F. LANGLEY
City Attorney

RUDOLPH M. KONRAD
PATRICK B. McDONNELL
LINDA ULISS BURKE
Deputy City Attorneys

OFFICE OF CITY ATTORNEY
800 CITY HALL
200 EAST WELLS STREET
MILWAUKEE, WISCONSIN 53202-3551
TELEPHONE (414) 286-2601
TDD (414) 286-2025
FAX (414) 286-8550

BEVERLY A. TEMPLE
THOMAS O. GARTNER
BRUCE D. SCHRIMPF
ROXANE L. CRAWFORD
SUSAN D. BICKERT
HAZEL MOSLEY
HARRY A. STEIN
STUART S. MUKAMAL
THOMAS J. BEAMISH
MAURITA F. HOUREN
JOHN J. HEINEN
MICHAEL G. TOBIN
DAVID J. STANOSZ
SUSAN E. LAPPEN
JAN A. SMOKOWICZ
PATRICIA A. FRICKER
HEIDI WICK SPOERL
KURT A. BEHLING
GREGG C. HAGOPIAN
ELLEN H. TANGEN
MELANIE R. SWANK
JAY A. UNORA
DONALD L. SCHRIEFER
EDWARD M. EHRLICH
LEONARD A. TOKUS
MIRIAM R. HORWITZ
MARYNELL REGAN
G. O'SULLIVAN-CROWLEY
DAWN M. BOLAND
KATHRYN M. ZALEWSKI
Assistant City Attorneys

October 18, 2004

Alderman T. Anthony Zielinski
14th Aldermanic District
City Hall, Room 205

Richard Marcoux
DCD Commissioner
Department of City Development
809 North Broadway, 2nd Floor
Milwaukee, WI 53202

Re: Banning Imposition of Deed Restrictions on Private Property

Dear Alderman Zielinski and Commissioner Marcoux:

DCD made us aware of Alderman Zielinski's interest in the city passing an ordinance that would ban the imposition of deed restrictions on private property if the restrictions would prevent the leasing of a building for grocery stores or pharmacies. The purpose of the ordinance would be to promote (or remove impediments to) development of grocery stores and pharmacies.

A deed restriction is also sometimes referred to as a restrictive covenant, which, is defined as follows:

> "Restrictive covenant. Provision in a deed limiting the use of the property and prohibiting certain uses. In context of property law, term describes contract between grantor and grantee which restricts grantee's use and occupancy of land; generally, purpose behind restrictive convenants is to maintain or enhance value of lands adjacent to one another by controlling nature and use of surrounding lands. Cunningham v. Hiles, 182 Ind. App. 511, 395 N.E.2d 851, 854. Covenants which restrict use of property on basis of race are

> unenforceable. Barrows v. Jackson, 346 U.S. 249, 73 S.Ct. 1031, 97 L.Ed. 1586; Evans v. Newton, 382 U.S. 296, 86 S.Ct. 486, 15 L.Ed.2d 373." Black's Law Dictionary, Sixth Edition (1990).

"Public policy favors the free and unrestricted use of property, so restrictions in deeds must be strictly construed to favor the unencumbered, free use of property. *Pietrowski*, 247 Wis.2d 232, ¶7, 634 N.W.2d 109. 'It is contrary to the public policy of this state to impose a restriction upon the use of land when that restriction is not imposed by express terms.' Id . . ." *Zuelsdorf v. Hetzel*, 272 Wis.2d 856, 679 N.W.2d 927, 2004 WL 555643 (Wis. App., March 23, 2004) (unpublished). *Pertzsch v. Upper Oconomowoc Lake Association*, 248 Wis.2d 219, 635 N.W.2d 829 (Ct. App. 2001) ¶¶ 8 and 17.

Thus, while public policy favors unrestricted conveyances, generally speaking, courts will enforce clearly defined, lawful deed restrictions.

In *Diamondback Funding, LLC v. Chili's of Wisconsin, Inc.*, 2004 WL 1660347 (Ct. App. July 27, 2004), the Court of Appeals indicated that restrictive covenants will be enforced if not ambiguous or vague, and if the purpose of the covenant may be clearly ascertained (¶12). This case involved a Home Depot that sold one parcel to Diamondback (an entity that operates the restaurant, Tumbleweed Southwest Mesquite Grill and Bar) and later, another adjoining parcel to Chili's of Wisconsin (an entity that operates Chili's Grill and Bar). The court upheld the validity of restrictive covenants that Diamondback and Home Depot had negotiated with respect to the second parcel and how that second parcel could be used (i.e., second parcel may not be used for restaurant that serves primarily Mexican food, or for a Mexican restaurant, or for a restaurant that specializes in Mexican food, ¶19).

See, also *Weiland v. Paulin*, 259 Wis.2d 139, 655 N.W.2d 204, 2002 WI App. 311, ¶8:

> "If the intent of a restrictive covenant can be clearly ascertained from the covenant itself, the restrictions will be enforced . . ."; and ¶17: "[i]n determining whether a deed restriction is reasonable, a court must inquire (1) whether it is reasonable under all the facts and circumstances of the transaction in light of the situation, business, and objects of the parties; and (2) whether it is for a just and honest purpose, for the protection of the legitimate interest of the party in whose favor it is imposed."

If the City were to create an ordinance as Ald. Zielinski contemplates, we believe that would expose the City to litigation and liability. A party adversely affected could argue that such an

ordinance amounts to a taking of a real property interest requiring compensation for the interest taken.

In *Spence v. Kolodzienski*, 259 Wis.2d 483, 655 N.W.2d 547, 2003 WI App. 1, unpublished, the Court of Appeals, in upholding a trial-court decision requiring the Kolodzienskis to remove the storage shed they built on their residential property in violation of restrictive covenants, said, with respect to a restrictive covenant, that it "constitutes at least an equitable servitude upon the land, and constitutes a valuable property right that a court of equity will enforce in the absence of facts and circumstances making such enforcement unjust or inequitable." ¶14. See, also, Wis. Stat. §840.01, "interest in real property" includes "rights under covenants running with the land . . .", and Wis. Stat. Ann. §706.10 concerning covenants that run with the land versus personal covenants.

Moreover, an ordinance prohibiting private deed restrictions of the sort contemplated might also be challenged as an impairment of contract rights. See, e.g., *Sills v. Walworth County Land management Committee*, 254 Wis.2d 538, 648 N.W.2d 878, 2002 WI App. 111:

> "'[Z]oning is entirely divorced in concept, creation, enforcement and administration from restrictions arising out of agreements between private parties who, in the exercise of their constitutional right of freedom of contract, can impose whatever lawful restrictions upon the use of their lands that they deem advantageous or desirable. Zoning restrictions and restrictions imposed by private covenants are independent controls upon the use of land, the one imposed by the municipality for the public welfare, the other private imposed for private benefit.
>
> Both types of land use restrictions are held by courts to legally operate independently . . ..
>
> [I]f a property owner is otherwise entitled to a variance or special exemption, it should be granted, notwithstanding private covenants which would prohibit the proposed use.'" Id at ¶28 quoting with approval 5 Edward H. Ziegler, Jr., Rathkopf's The Law of Zoning and Planning §§82:2, 82:3 (2001).

And, per *Sills, supra*, at ¶31:

> "[a] government cannot enact a law that impairs a legal contract. Ordinances must recognize that private contractual rights and government enforcement of

> zoning laws coexist so that government may implement zoning laws without impinging on private contract rights between citizens."

Thus, while deed restrictions are not favored since free and unencumbered alienation is preferred, in general, so long as the grantor does not, for example, discriminate against protected classes or otherwise attempt to impose unlawful restrictions, wholly aside from governmental zoning restrictions, an owner has the right to convey subject to deed restrictions. In fact, when the City of Milwaukee and RACM convey, they sometimes impose deed restrictions or other restrictive covenants, along with reversionary clauses whereby the property conveyed automatically "reverts back" to the grantor in the event of breach by the grantee. See, e.g., Milwaukee Code of Ordinances §304-49-8 and Wis. Stat. §66.1333(9)(b) and (c). See, also, 38 Wis. Op. Atty. Gen. 386 (1949), County has general power to include deed restriction on use of property in conveyance of land County acquired by tax deed. Moreover, when the City acquires parcels via in rem property-tax foreclosure under Wis. Stat. §75.521, the City itself takes title subject to recorded deed restrictions. See, Wis. Stat. §75.521(8) and §75.14(4).

It is not unusual for sophisticated, private owners and tenants to negotiate restrictions. For example, a grocery-store-anchor tenant of a strip mall would be expected to negotiate a lease whereby the landlord would be prohibited from leasing other space in the strip mall to other grocery stores.

We hope this has been helpful. Please call if you have questions or comments.

Very truly yours,

GRANT E. LANGLEY
City Attorney

GREGG C. HAGOPIAN
Assistant City Attorney

GCH/mll:86038
c: Martha Brown
1033-2004-2851