The Rule Against Perpetuities Lives On

by Douglas J. Good and Adam L. Browser

The bane of law students, the centuries-old Rule Against Perpetuities is, surprisingly, alive and well in the 21st century. Despite the perception that the rule is merely an academic oddity, in New York it has continued applicability to modern real estate transactions. In fact, in the last year alone, the Rule Against Perpetuities has been the subject of two appellate court decisions, *Reynolds v. Gagen* [1] and *Dimon v. Starr*.[2]

The Rule Against Perpetuities was a creature of case law that evolved in England during the 1600s. Its purpose was to ensure the productive use and development of property by simplifying ownership, facilitating the exchange thereof and freeing property from unknown impediments to alienability.[3]

New York has codified the Rule Against Perpetuities in Section 9-1.1 of the Estates Powers and Trusts Law. The rule has two parts, §§9-1.1(a) and 9-1.1(b). Section §9-1.1(a) deals with restraints on the ability to convey real property. It provides that no interest in real property is valid if the instrument conveying the interest suspends the absolute power of alienation for longer than lives in being plus 21 years.[4]

Remote Vesting

The second part, §9-1.1(b), deals with remote vesting — circumstances where an estate or interest in real property will not arise (or vest) until some future occurrence. Section 9-1.1(b) provides that no estate in property is valid unless it vests no later than 21 years after one or more lives in being at the creation of the estate and any period of gestation involved.[5]

Section §9-1.1(b)'s proscription is non-waivable,[6] "rigid" and "invalidates any interest that may not vest within the statutory time period even if the consequences are capricious."[7] And the assessment of whether an interest may not vest within the statutory period must be based on the circumstances that existed at the time of its granting, not on whether the interest in fact vested within the permitted time.[8]

Indeed, "in determining whether a disposition violates the Rule Against Perpetuities, one must 'look at what might have happened . . . rather than to what has actually happened.' "[9]

Frequently, Rule Against Perpetuities issues show up in option agreements. An option grants to the holder the power to compel the owner of property to transfer real property, whether or not the owner is willing to part with the property.[10] The rule applies to options.[11] From a policy standpoint, the existence of the option discourages the owner from improving property, or third parties from buying the property, since the holder of the option could force a conveyance. However, purchase options that are part of a lease — so-called options appurtenant — do not deter development and do not violate EPTL 9-1.1(b) even if the option holder's interest may vest beyond the perpetuities period.[12]

Courts have consistently held that an option containing no limitation demonstrates the parties' intention that it last indefinitely.[13] The inclusion of terms such as "successors and assigns" — and particularly "heirs" — indicates that the parties intend the option to be indefinite.

Options that contain such terms violate the Rule Against Perpetuities. For example, in *Buffalo Seminary v. McCarthy*,[14] the Appellate Division, Fourth Department, held that the inclusion of language making an option binding on "successors, assigns and executors" indicated the parties' intention that the option was to "extend in duration for an indefinite period of time" and thereby created an interest that could vest beyond the permissible period contained in E.P.T.L. §9-1.1(b). This was affirmed by the Court of Appeals.

'Reynolds v. Gagen'

Recently, in *Reynolds v. Gagen*, the First Department held that an option agreement did not violate the Rule Against Perpetuities even though the parties' contract contained a clause stating the contract was "binding on the heirs and assigns of the parties."

Reynolds and Gagen entered into a contract to purchase property jointly. Due to financial problems, Reynolds could not close, and Gagen purchased

the property alone; nevertheless, they entered into an agreement whereby Gagen gave Reynolds an option to purchase a half interest in the property.

Significantly, the parties agreed that the agreement bound their "heirs and assigns." Three years later, Reynolds sought to exercise her option. Reynolds sued after Gagen refused, and Gagen defended, claiming the agreement violated the Rule Against Perpetuities.

The court agreed with Gagen and held that the "heirs and assigns" language in the agreement reflected the parties' intention that the option would last indefinitely and therefore the agreement violated the rule.

Initially, the First Department agreed, and affirmed the dismissal of the complaint (with slight modification).[15] However, five months later the First Department recalled its prior decision, re-examined the contract language and ruled that the option did not violate the Rule.[16]

The parties' "heirs and assigns" were only bound to perform in place of their predecessors, but they did not receive the benefits of the contract. Thus, by the unambiguous language of the contract, only Reynolds — not her heirs or assigns — could exercise the option. As the option was personal to Reynolds, if she died without exercising it, the option was extinguished. However, Gagen's death would not extinguish the option; Gagen's "heirs and assigns" would still have to honor Reynolds' exercise of the option. Thus, Reynolds' estate had to vest — if at all — within her lifetime and the option agreement did not violate the Rule Against Perpetuities.

'Dimon v. Starr'

More recently, in *Dimon v. Starr*, the Second Department applied the Rule Against Perpetuities to prevent the plaintiff from exercising an option contained in a contract that had been prepared by their respective counsel.

The plaintiff held a mortgage on unimproved property in Southhampton. The mortgage was delinquent and Dimon had commenced a foreclosure proceeding. By written agreement, Dimon assigned the mortgage and foreclosure action to Starr.

Significantly, the assignment specifically used defined terms for each party that included their respective "successors, heirs or assigns". Under the agreement, "Dimon" (defined to include his successors, heirs and assigns) had an option to acquire two lots if Starr (or her successors, heirs and assigns) acquired the property through the foreclosure, and if she subdivided the property.

The agreement contained no expiration date for Dimon, his successors, heirs or assigns to exercise the option; Starr (her successors, heirs or assigns) had no obligation to purchase the property in foreclosure, or — even if she did — to subdivide it. But if and when Starr, her successors, heirs or assigns, filed a subdivision map, Dimon, his successors, heirs or assigns could exercise the option.

Starr bought the property in foreclosure and years later, following several related party transfers, the property was subdivided.

Dimon commenced an action seeking specific performance of his option. Starr opposed, contending that the agreement violated the Rule Against Perpetuities. Dimon successfully moved the court for summary judgment and obtained an order directing Starr to transfer title to two lots to him.

On appeal, the Second Department reversed, holding that the agreement violated E.P.T.L. 9-1.1(b)'s prohibition against remote vesting, and dismissed the complaint. The key, according to the Second Department, was that the parties used the terms "successors, heirs or assigns," thus unambiguously indicating their collective intention that Dimon's option rights would last indefinitely. Because the occurrence of the events that might trigger his option might not occur within the Rule Against Perpetuities' permissible period (lives in being plus 21 years), the option was void.

Litigants faced with a Rule Against Perpetuities defense typically will allege that the rules of construction clause of E.P.T.L. §9-1.3 saves a transaction that might otherwise violate the rule.

The primary purpose of §9-1.3 is to avoid annulling dispositions that inadvertently violate the rule.[17] Absent a contrary intent in the instrument giving rise to an estate in real property, EPTL §9-1.3 creates a presumption

that where the vesting of an estate is contingent upon the occurrence of an event, such as probate of a will, settlement of an estate or appointment of a fiduciary, the parties intended that the contingency would occur within 21 years from the date of the instrument, thereby rescuing the transaction.

Notwithstanding this apparently broad presumption, however, courts will not rewrite an unambiguous open-ended agreement to provide that an option should vest, if at all, only within the permissible period.[18]

In *Dimon*, plaintiff attempted to invoke §9-1.3 to save his option. However, the agreement was unambiguous and the use of the terms "successors, heirs or assigns" clearly indicated the parties' intention that the agreement was to last indefinitely — thereby creating the possibility that Dimon's estate would not vest within the permissible period (if Starr did not subdivide the property during their lifetimes and her successors, heirs and assigns did not do so within 21 years of their death). Thus, §9-1.3 could not save the Dimon-Starr agreement.

Conclusion
The implications for practitioners who use the boilerplate phrase "successors, heirs and assigns" without so much as a second thought can be disastrous.

Lawyers must exercise great care every time they draft a contract to ensure that they are not creating estates that may vest beyond the permissible period.

Language such as that used in *Dimon*, where each party was defined to include their "successors, heirs and assigns," may well extend the time during which an estate may vest beyond the period measured by lives in being plus 21 years (or 21 years in the case of corporate transactions) and thus run afoul of the rule.

Not just the bane of law students, the Rule Against Perpetuities may be the bane of us all, including our successors, heirs and assigns.

FootNotes:
[1] 292 A.D.2d 310, 739 N.Y.S.2d 704 (1st Dept. 2002).

[2] 299 A.D.2d. 313, 749 N.Y.S.2d 78 (2d Dept. 2002) app. den., N.Y. Slip Op. 229 (2003).

[3] Symphony Space, Inc. v. Pergola Properties, Inc., 88 N.Y.2d 466, 475, 646 N.Y.S.2d 641, 644 (1996).

[4] Where the parties to a transaction are corporations and no measuring lives are specified, the perpetuities period is 21 years. Symphony Space, supra.

[5] See note 3, supra.

[6] Metropolitan Transportation Authority v. Bruken Realty Corp., 67 N.Y.2d 156, 161, 501 N.Y.S.2d 306, 308 (1986); Symphony Space, supra.

[7] Wildenstein & Co., Inc. v. Wallis, 79 N.Y.2d 641, 647-48, 584 N.Y.S.2d 753, 756-57 (1992); see also Symphony Space, supra.

[8] Metropolitan Transportation Authority, supra.

[9] Matter of Will of Shehan, 157 Misc.2d 904, 597 N.Y.S.2d 1017, 1020 (Surr. Ct., Erie Co. 1993); In re Shaul's Estate, 58 Misc.2d 967, 297 N.Y.S.2d 209 (Surr. Ct., Otsego Co. 1969).

[10] Metropolitan Transit Authority, supra; see also Bloomer v. Phillips, 164 A.D.2d 52, 562 N.Y.S.2d 840 (3d Dept. 1990).

[11] Buffalo Seminary v. McCarthy, 86 A.D.2d 435, 451 N.Y.S.2d 457, 463 (4th Dept. 1982), aff'd, 58 N.Y.2d 867, 460 N.Y.S.2d 528 (1983); Symphony Space, supra (holding that option containing no limitation in duration violated EPTL 9-1.1(b).)

[12] Symphony Space, supra.

[13] Symphony Space, supra.

[14] Buffalo Seminary, supra.

[15] 287 A.D.2d 417, 732 N.Y.S.2d 4 (1st Dept. 2001).

[16] 292 A.D.2d 310, 739 N.Y.S.2d 704 (1st Dept. 2002).

[17] Symphony Space, supra.

[18] Symphony Space, supra; In re Kellogg's Trust, 35 A.D.2d 145, 316 N.Y.S.2d 293 (4th Dept. 1970), app. den., 28 N.Y.2d 481, 319 N.Y.S.2d 1025 (1971).

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