University of Richmond Law Review

Volume 8 | Issue 2 Article 18

1974

Real Property- The Rule Against Perpetuities- Option Contract Held Void Due to Violation of the Common Law Rule

Real Property—THE RULE AGAINST PERPETUITIES—OPTION CONTRACT HELD VOID DUE TO VIOLATION OF THE COMMON LAW RULE—*United Virginia Bank v. Union Oil*, 214 Va. 48, 197 S.E.2d 174 (1973).

The Rule against Perpetuities as originally developed in England and crystalized over two centuries[1] is still alive and thriving in the Commonwealth of Virginia as evidenced by the recent supreme court case of *United Virginia Bank v. Union Oil.*[2] While a number of states have enacted legislation or judicially adopted[3] ways and means to avoid the harsh results often dictated by the common law rule,[4] it appears that Virginia may be defending a rearguard position which may not be functional in terms of today's commercial world.

In *United Virginia Bank v. Union Oil*, W.J. Abbitt, now deceased and represented by United Virginia Bank, entered into an agreement granting Union Oil a 120 day option to purchase a parcel of land located at the intersection of two highways which were proposed for future construction in the City of Newport News, Virginia. Union Oil subsequently assigned its rights under the contract to Sanford & Charles, Inc., the active appellee in this suit. Under the terms of the agreement,[5] the 120 day option became exercisable by the optionee only after the rights-of-way to both highways

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1. While Lord Nottingham is credited with the original statement of the Rule against Perpetuities in the Duke of Norfolk's Case, 3 Ch. Cas. 1, 22 Eng. Rep. 931 (1682), it was not until a full 150 years later that the period of perpetuities was firmly established in Cadell v. Palmer, 1 Cl. & Fin. 372, 6 Eng. Rep. 956 (1833). The rule as stated by Gray in his comprehensive treatment of the subject is as follows:

> NO INTEREST IS GOOD UNLESS IT MUST VEST, IF AT ALL, NOT LATER THAN TWENTY-ONE YEARS AFTER SOME LIFE IN BEING AT THE CREATION OF THE INTEREST. J. GRAY, THE RULE AGAINST PERPETUITIES § 201 (4th ed. R. Gray 1942).

The often criticized decision in Longon & Southwestern Ry. v. Gomm, [1882] 20 Ch. D. 562, marked the initital application of the Rule against Perpetuities to option contracts for the sale and purchase of real estate. This decision, however, dealt with a perpetual option agreement declaring it in violation of the Rule.

2. 214 Va. 48, 197 S.E.2d 174 (1973).

3. For a general outline of the trends in this area see Committee on Rules Against Perpetuities, *Further Trends in Perpetuities*, 5 REAL PROP. PROB. & TR. J. 333 (1970); Lynn, *Perpetuities Reform: An Analysis of Developments in England and the United States*, 113 U. PA. L. REV. 508 (1965); Schuyler, *The New Biology and the Rule Against Perpetuities*, 15 U.C.L.A. L. REV. 420 (1968); 13 AM. U. L. REV. 67 (1963); 28 WASH. & LEE L. REV. 184 (1971).

4. Leach, *Perpetuities In a Nutshell*, 51 HARV. L. REV. 638 (1938); Leach, *Perpetuities: What Legislatures, Courts, and Practitioners Can Do About the Follies of the Rule*, 13 KAN. L. REV. 351 (1965).

5. 214 Va. at 49, 197 S.E.2d at 175. The agreement provided as follows:

> It is expressly understood that the 120 days option period shall begin at the time the City of Newport News, Virginia acquires the right of way of Boxley Boulevard Extension and new U.S. 60.

were turned over to the City of Newport News for administration and maintenance. The Supreme Court of Virginia, in a decision by Justice Carrico, held the *option in gross*[6] (not appurtenant to a leasehold interest) provided for in the agreement invalid,[7] and in so doing, followed a strict common law approach to the problem.[8] The court pointed out that the Rule against Perpetuities would apply to a contingent equitable future interest created by an option contract for the sale of real estate.[9] It then went on to hold the option agreement void *ab initio*[10] because the option was exercisable only after the contingencies provided for in the agreement

6. Society's interests demand that land and other property not be tied up for immeasurable periods of time, but rather that they remain as freely alienable as possible so as to foster economic growth. An *option in gross*, which is a right to purchase property not incident to a lease may, however, have disastrous effects upon the alienability and improvement of the land involved. As long as the option remains exercisable the owner of the property cannot afford to make improvements which may subsequently be taken without additional compensation by an exercise of the option. *See* Barton v. Thaw, 246 Pa. 348, 92 A. 312 (1914); Leach, *Perpetuities In a Nutshell*, 51 HARV. L. REV. 638 (1938).

An *option appendant*, which is an option to purchase given to a lessee of property, creates a situation entirely opposite from the one described above as improvement of the land is not hindered. The lessee can build as he pleases and make other improvements which he may deem necessary to the property. He is assured that he will not lose the value of the work he has put into the land by virtue of his option to purchase incident to the lease. *See* W.B. LEACH & O. TUDOR, THE RULE AGAINST PERPETUITIES § 24.57 (1957); Abbot, *Leases and the Rule Against Perpetuities*, 27 YALE L. J. 878 (1918); *cf.* RESTATEMENT OF PROPERTY § 395 (1944), wherein the enforceability of *options appendant* are upheld subject to the added stipulation that they must not under any circumstances be exercisable after the lease terminates. *Contra*, J. GRAY, THE RULE AGAINST PERPETUITIES § 230.3 (4th ed. R. Gray 1942), which holds, in accordance with the English approach, that an *option appendant* which exceeds, or may possibly exceed, the limits of the perpetuities period is void. *See generally* 13 FLA. L. REV. 214 (1960), for a discussion of the different effects a fixed price option as opposed to a market price option may have upon the problem under discussion.

Note that while *options in gross* are generally held to be invalid if they "may" exceed the period of perpetuities, the *option appendant* capable of doing likewise is always held valid. One of the few cases ever to attack the validity of an *option appendant* was First Huntington Nat'l Bank v. Gideon-Broh Realty Co., 139 W. Va. 130, 79 S.E.2d 675 (1953). This situation, however, was soon rectified by statute in W. VA. CODE § 36-1-24 (1957).

7. This decision of the Virginia Supreme Court reversed the Corporation Court of Newport News, which found in favor of Sanford & Charles, Inc., when it originally decided that the agreement did not violate the Rule against Perpetuities.

8. *See* note 14 *infra*, for an outline of the common law approach to solving an option perpetuities problem.

9. *See* Skeen v. Clinchfield Coal Corp., 137 Va. 397, 119 S.E. 89 (1923); Starcher Bros. v. Duty, 61 W. Va. 373, 56 S.E. 524 (1907). These cases are based directly upon London & Southwestern Ry. v. Gomm, [1882] 20 Ch. D. 562. *See also* 1 R. MINOR, THE LAW OF REAL PROPERTY § 823 (2d ed. F. Ribble 1928).

10. *Accord*, Burruss v. Baldwin, 199 Va. 883, 887, 103 S.E.2d 249, 252 (1958), *citing* Claiborne v. Wilson, 168 Va. 469, 192 S.E. 585 (1937), *and* Skeen v. Clinchfield Coal Corp., 137 Va. 397, 119 S.E. 89 (1923).

were met,[11] and there existed the "distinct possibility"[12] that these conditions precedent would in fact not be fulfilled within the twenty-one year period set by the Rule.[13]

The application of the Rule against Perpetuities to option contracts and commercial transactions[14] has been subjected to wide attack.[15] It is argued that the period fixed by the Rule, that of a "life or lives in being plus twenty-one years and ten months,"[16] has little or no significance and meaning in the modern business world. While the period may have proven useful to control family gifts and to limit the effect the "dead hand" might exercise over property, it has been argued that today, in modern commercial transactions, it is devoid of any rationale.[17] Proponents of reform also argue that an option agreement, in and of itself, before it is exercised, creates no interest in the property at all, but is merely a contract right and therefore should not be subject to the Rule in the first place, regardless of its potential duration.[18]

Various arguments made by the appellees based on recent decisions and legislation involving the Rule against Perpetuities all proved unconvinc-

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11. *See* note 5 *supra*.

12. 214 Va. at 52, 197 S.E.2d at 177.

13. While the Rule demands that the interest vest, if at all, within the period of a life or lives in being plus twenty-one years and ten months, if the parties have not contracted with reference to lives in being then the gross period of twenty-one years becomes determinative in passing on the validity of the interest. *See* Murphy v. Johnston, 190 Ga. 23, 8 S.E.2d 23 (1940); Barton v. Thaw, 246 Pa. 348, 92 A. 312 (1914).

14. The first application of the Rule against Perpetuities to option contracts for the sale or purchase of land came in the much criticized English decision of London & Southwestern Ry. v. Gomm, [1882] 20 Ch. D. 562. The holding stated that the optionee possessed a contingent equitable future interest in the property by virtue of the fact that his rights were specifically enforceable in a court of equity. Furthermore, because there existed the possibility that the option might not be exercised within the period fixed by the Rule, it was held that such an interest would be void *ab initio*. This case overruled Birmingham Canal Co. v. Cartwright, [1879] 11 Ch. D. 421, which previously had decided that an option contract created no interest in the property before it was exercised. *See* Berg, *Long-Term Options and the Rule Against Perpetuities*, 37 CALIF. L. REV. 235 (1949).

15. *See* W.B. LEACH & O. TUDOR, THE RULE AGAINST PERPETUITIES § 24.56 (1957); Berg, *Long Term Options and the Rule Against Perpetuities*, 37 CALIF. L. REV. 235 (1949); *accord*, Leach, *Perpetuities in Real Estate: Legislative Reform*, 6 PRAC. LAW., Dec. 1960, at 36.

16. *See* note 1 *supra*, for the derivation of this period of perpetuities.

17. *See* W.B. LEACH & O. TUDOR, THE RULE AGAINST PERPETUITIES § 24.56 (1957); Leach, *Perpetuities In a Nutshell*, 51 HARV. L. REV. 638 (1938).

18. *See* Berg, *Long Term Options and the Rule Against Perpetuities*, 37 CALIF. L. REV. 235 (1949), for a well-written and thorough discussion of why the Rule should never have been applied to option contracts, using the contract theories of Williston and Corbin. *Contra*, Skeen v. Clinchfield Coal Corp., 137 Va. 397, 119 S.E. 89 (1923); Woodall v. Bruen, 76 W. Va. 193, 85 S.E. 170 (1915); RESTATEMENT OF PROPERTY §§ 393-94 (1944); J. GRAY, THE RULE AGAINST PERPETUITIES § 330 (4th ed. R. Gray 1942).

ing to the supreme court.[19] A plea that the court exercise its *cy pres* power of judiciary and imply a "reasonable time" provision into the contract, as was done in *Isen v. Giant Food, Inc.*,[20] was refused. The court held that *Isen* was "factually and legally different from the case at bar"[21] apparently because it involved an agreement to lease land after proper zoning had been obtained. In upholding the agreement, the District of Columbia court pointed to certain phrases which were included in the contract,[22] and from these was able to construe an intention of the parties that the contract be completed within a "reasonable" time, which would certainly be shorter than twenty-one years as provided by the Rule.[23] The Virginia court, however, noted that the agreement and the circumstances presented in the case at bar were absolutely devoid of any such "dominant intent" from which such a reasonable time provision could be implied.[24] In fact, an objective analysis of the case indicates a good probability that the proposed highways would not be completed as scheduled,[25] and that the option would therefore exceed the limits of the stipulated perpetuities period. The court, in refusing to apply *cy pres*, also relied upon a prior Virginia case which established a policy against the judicial utilization of this doctrine to avoid the effects of the Rule against Perpetuities.[26]

The appellee then urged the court to adopt the "wait and see" approach which has been both judicially and legislatively accepted into the law of a

19. *See* articles cited in note 3 *supra* for a survey of the trends in the perpetuities area.

20. 295 F.2d 136 (D.C. Cir. 1961), *noted in* 37 NOTRE DAME LAW. 561 (1962) *and* 19 WASH. & LEE L. REV. 91 (1962).

21. 214 Va. at 53, 197 S.E.2d at 177.

22. Language in the contract provided for Isen as landlord to "diligently pursue" the petition for commercial zoning, and for Giant Food, Inc., as tenant, to "cooperate to the end that such zoning be obtained as soon as possible." Isen v. Giant Food, Inc., 295 F.2d 136, 137 (D.C. Cir. 1961).

23. *Id.* at 138.

24. 214 Va. at 52, 197 S.E.2d at 177.

25. Facts revealed that while the city council of Newport News had requested the state highway department to begin construction of "new U.S. 60" in August of 1966 (a few months after the agreement in question was signed), official approval of the major thoroughfare plan did not come until July, 1968. "New U.S. 60," a joint city-state-federal project, was under construction at the time of the trial in 1971 and was scheduled for completion around the beginning of 1973. The status, however, of the "Boxley Boulevard Extension," to be constructed as a private project by the owners of the property through which it would pass, was entirely another matter. This highway, according to W.H. Gordon, Jr., the city's chief engineer of traffic and transportation, would be completed "hopefully" by 1985 or, at the latest, by January, 1987. Mr. Gordon also pointed out that the fixing of a target date for completion did not indicate absolutely that it would be met, because of ever-changing conditions and revisions of the plans which might be required. 214 Va. at 50, 197 S.E.2d at 176.

26. 214 Va. at 52, 197 S.E.2d at 177, *citing* Shenandoah Valley Nat'l Bank v. Taylor, 192 Va. 135,149, 63 S.E.2d 786,795 (1951).

number of states.[27] This doctrine is in effect an "actualities test", wherein only those events which take place after the agreement is completed are considered when deciding whether or not a limitation is valid or void under the Rule.[28] Only when the period fixed by the Rule is violated "in fact" is the option declared void.[29] The court, in rejecting appellee's request, noted that the established law in Virginia on this issue,[30] to which it would adhere,[31] was that a perpetuities problem is solved not on the basis of those events which occur subsequent to the contract, but solely upon the facts as they existed at the time the agreement was entered into.[32] Therefore, in the case at bar, the court could refuse to take into account any evidence of the present state of construction of the two roads.[33] It would consider only their status at the inception of the agreement when the perpetuities period actually began to run.[34] The end result, holding the option contract to be void *ab initio*, is therefore dictated by the existence of the possibility that the option might not be exercisable within the allowable perpetuities period because of the contingency attached thereto.[35]

It is submitted that the court's decision in *United Virginia Bank v. Union Oil* was correct insofar as it effectively struck down what was a potentially dangerous obstacle to the alienability and improvement of the

27. Leach, *Perpetuities: What Legislatures, Courts, and Practitioners Can Do About the Follies of the Rule*, 13 KAN. L. REV. 351 (1965); Lynn, *Perpetuities Reform: An Analysis of Developments in England and the United States*, 113 U. PA. L. REV. 508 (1965); Lynn, *Raising the Perpetutities Question: Conception, Adoption, "Wait and See," and Cy Pres*, 17 VAND. L. REV. 1391 (1964); Schuyler, *The New Biology and the Rule Against Perpetuities*, 15 U.C.L.A. L. REV. 420 (1968); 13 AM. U. L. REV. 67 (1963); 4 VILL. L. REV. 144 (1958).

28. *See* 28 WASH. & LEE L. REV. 184,191 (1971).

29. *Id.*

30. In *Claiborne v. Wilson*, the court noted:

> Nor is it material in such cases how the fact actually turns out. The possibility that the event may, in point of time, exceed the limits allowed, vitiates the limitation ab initio. 168 Va. 469,474, 192 S.E. 585,586 (1937), *quoting* 1 R. MINOR, THE LAW OF REAL PROPERTY § 820 (2d ed. F. Ribble 1928).

31. 214 Va. at 53, 197 S.E.2d at 178.

32. The common law would treat an option to purchase, which is exercisable after a stated event takes place, without regard to whether or not the contingency has in fact been fulfilled. So an agreement giving X an option to buy "when man reaches the moon" would be declared void *ab initio* if it was made before man had in fact reached the moon. Even if man did reach the moon one day after the agreement was made this would have no effect on the declaration of the interest as being void, because the Rule takes into account only those facts in existence at the time the agreement is entered into. The vesting of the contingency after the agreement has no effect whatsoever on its validity. *See* W.B LEACH & O. TUDOR, THE RULE AGAINST PERPETUITIES § 24.24 (1957).

33. *See* note 25 *supra*.

34. 214 Va. at 53, 197 S.E.2d at 178.

35. *See* note 5 *supra*.

property involved.[36] However, the court's strict adherence to common law principles when dealing with modern commercial transactions is somewhat disturbing when one takes into consideration the fact that a valid *option in gross*,[37] capable of lasting over a century, could easily be created by anyone reasonably well versed in perpetuities law.[38] Realizing that such an option would be repugnant in modern society,[39] the need develops to formulate a uniform rule that would be more meaningful in light of our present day business situation. The decision in *United Virginia Bank*, and the precedent setting cases on which it is based,[40] indicates a need for corrective legislation which will insure the salability and development of our land resources by establishing new modern standards that will also prove sensible and just in our dynamic commercial setting.

S. R. K.

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36. The parcel of land subject to the option contract is for all practical purposes tied up and removed from the market until the contingencies are met and the 120 day option period runs out. The contingencies, however, may not be fulfilled for twenty-one or more years. While subject to the option, the land cannot be sold because no one would be willing to buy it subject to the option agreement, and the vendor would be leaving himself open for a breach of contract suit if he were to sell to anyone other than the optionee. There can be no improvement of the property for fear that anything added will subsequently be taken if the option is exercised at the already predetermined price.

37. *See* note 6 *supra* for an explanation of the *option in gross*.

38. To formulate such a valid option the parties could contract with reference to an administratively acceptable number of healthy infants, one of whom would probably live to reach age eighty. This period of lives in being (80 years) would then be added to the additional twenty-one years provided by the rule thus creating a probable 100 year option, clearly within the perpetuities period.

39. *See* note 14 *supra*.

40. Shenandoah Valley Nat'l Bank v. Taylor, 192 Va. 135, 63 S.E.2d 786 (1951); Claiborne v. Wilson, 168 Va. 469, 192 S.E.2d 585 (1937).