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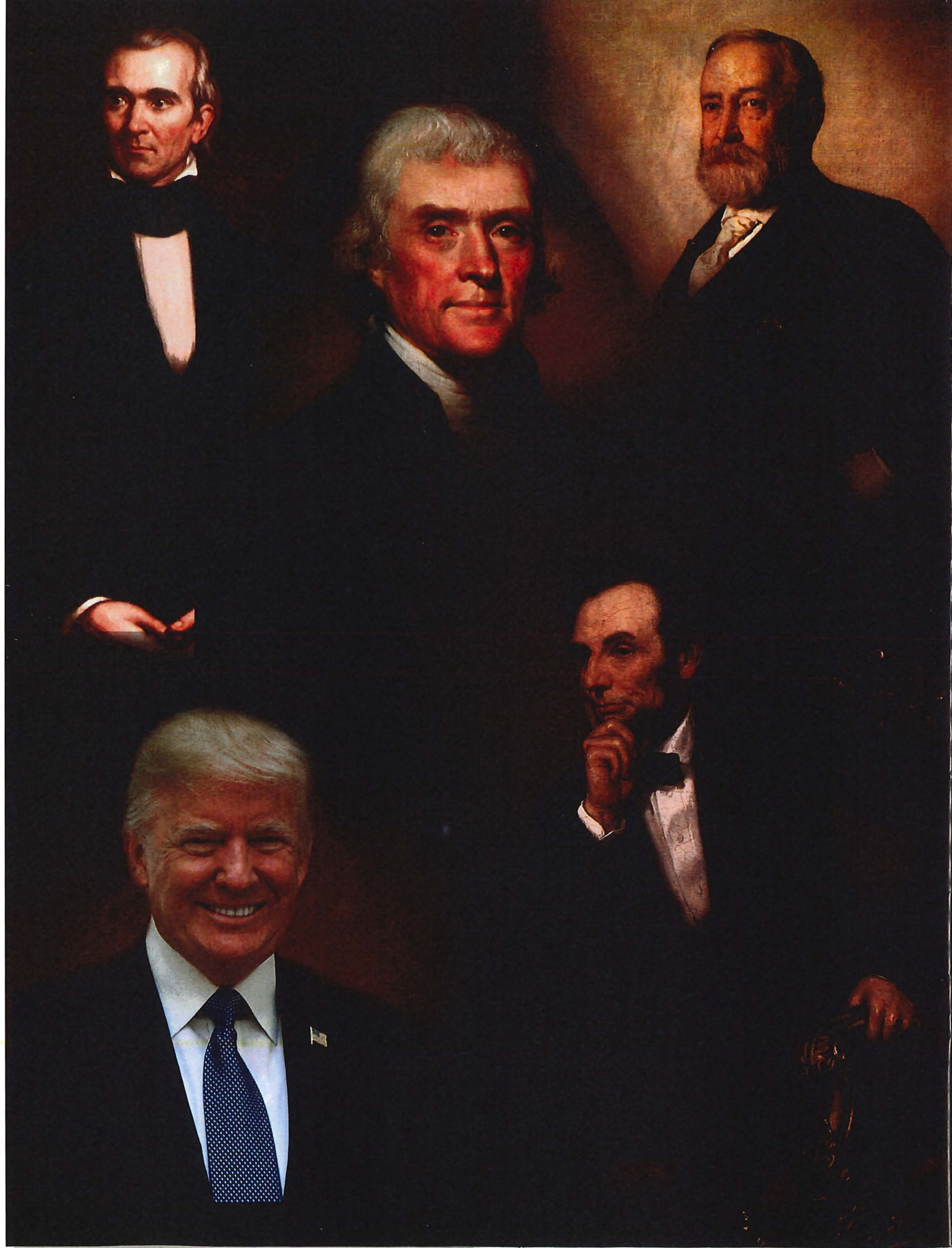
March/April 2018 Vol. 32 No. 2

PROBATE & PROPERTY

A Publication of the Real Property, Trust and Estate Law Section ABA American Bar Association

The Tax Code's Hidden Gem: Installment Sales for Wealth Management and Estate Planning



PRESIDENTS AND PROPERTY LAW

By Blake A. Watson

The current president of the United States does not hesitate to bring legal action to protect or enhance his real estate investments. From the mid-1990s through 2011, Donald Trump sued the New York City Tax Commission 55 times over property assessments, and in 2006 saved about $3 million by winning a 10% tax reduction over ten years on the Trump Tower in midtown Manhattan. Nick Penzenstadler & David McKay Wilson, *More than 100 Lawsuits, Disputes over Taxes Tied to Trump and His Companies*, USA Today (May 19, 2016), www.usatoday.com/story/news/2016/05/19/trumps-tax-troubles/84543538. More recently, while campaigning for the presidency, Trump sued neighbors of his Doral golf club in Miami for destroying trees and causing $15,000 of damage to landscaping. Jose Lambiet, *Donald Trump Sues Neighbors over Golf Course Landscape*, Miami Herald (Feb. 28, 2016), www.miamiherald.com/entertainment/ent-columns-blogs/jose-lambiet/article63062187.html.

The first president of the United States also did not hesitate to bring legal action to protect or enhance his real estate investments. In 1784, George Washington traveled on horseback as far as western Pennsylvania, where he found his lands occupied without permission. After returning to Mount Vernon, the hero of the American Revolution instructed his lawyer, Thomas Smith, to sue the squatters "for Trespasses, rents or otherwise as you shall judge best & most proper to obtain justice for me." A trial was held in October 1786—in the town of Washington—and the jury came back with a favorable verdict. General Washington evicted the squatters and kept the land until 1796, when he accepted a promissory note from a purchaser who was unable to complete his payments, causing the property to revert to the president. Joel Achenbach, *The Grand Idea: George Washington's Potomac and the Race to the West* 144–50 (2004).

It should not be surprising that American presidents have been involved with issues of property law. Many of our past presidents (such as Washington, Madison, Jackson, and the Roosevelts) were extensive landowners, and another sizeable group (including Adams, Jefferson, Pierce, and Lincoln) were lawyers with experience in real estate matters. This article matches five presidents with five topics of property law: (1) Thomas Jefferson and the fee tail, (2) James Polk and the rule against perpetuities, (3) Abraham Lincoln and deed covenants, (4) Benjamin Harrison and the Takings Clause, and (5) Donald Trump and liquidated damages. In each instance, these presidents—as legislator, lawyer, or landowner—were involved with basic principles of American property law.

Thomas Jefferson and the Fee Tail

First-year law students know (or should know) that land ownership is defined by duration (term, life, or fee estates) and the presence or absence of conditions. Most states today recognize four

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types of fee simple estate. Fee simple absolute is not subject to conditions. The other three variations (the fee simple determinable, fee simple subject to a condition subsequent, and fee simple subject to an executory limitation) are subject to conditions and differ regarding the consequence of a breach. Common law, however, recognized another fee estate: the fee tail.

A fee tail keeps land in the family by restricting the ability of future generations to alienate the property. Hence, if John conveyed Blackacre "to my son Blake and the heirs of his body," Blake received a fee tail and John retained a reversion in fee simple absolute. On Blake's death, the property would pass to Blake's lineal heir or, if none existed, John's reversion would become possessory. The holder of a fee simple absolute could frustrate the hopes of an heir apparent by selling the property, but the holder of a fee tail (the "tenant in tail") could not easily defeat the rights of lineal descendants. Jane Austen begins chapter seven of *Pride and Prejudice* by explaining that "Mr. Bennet's property consisted almost entirely in an estate of two thousand a-year, which, unfortunately for his daughters, was entailed, in default of heirs male, on a distant relation." Consequently, Mrs. Bennet was most anxious that one of her daughters marry their second cousin, William Collins, an obsequious and pompous clergyman who held the reversion in fee simple absolute.

Thomas Jefferson disliked the fee tail estate for several reasons. His wife Martha had inherited land in fee tail, which made it nearly impossible to sell (and Jefferson needed money). Consequently, in 1774 the couple petitioned the Virginia House of Burgesses to "dock the tail" and remove the restriction. Governor Dunmore, however, failed to approve the bill before dissolving the legislature in response to increasing revolutionary fervor. Aside from his personal affairs, Jefferson also viewed the fee tail as antithetical to republican government insofar as it promoted and protected the landed aristocracy. Finally, Jefferson appreciated the power of the threat of disinheritance and believed that the inability to sell entailed lands "does injury to the morals of youth by rendering them independent of, and disobedient to, their parents." 1 *The Papers of Thomas Jefferson* 560 (J. Boyd ed. 1950); and David Thomas Konig, *Legal Fictions and the Rule(s) of Law: The Jeffersonian Critique of Common-Law Adjudication*, in The Many Legalities of Early America 115 (2001).

Shortly after writing the Declaration of Independence, Jefferson introduced a bill in the Virginia House of Delegates to abolish the fee tail estate. A prominent plantation owner, Landon Carter, declared in a letter to Washington that Jefferson must be a "midday drunkard" to attack the "right to do as we please with our own property." Dumas Malone, *Jefferson the Virginian* 255 (1948). Nevertheless, the bill passed, and nearly all states have followed Virginia's example—including Connecticut, which provided in 2015 that an estate "given in fee tail shall be an absolute estate in fee simple to the named grantee." Conn. Gen. Stat. Ann. § 47-3. Thus, as Thomas Jefferson envisioned, the fee tail estate is no longer a viable form of land ownership in the United States.

JAMES K. POLK, THE 11TH PRESIDENT OF THE UNITED STATES, WAS A POSTHUMOUS VICTIM OF THE COMMON-LAW RULE AGAINST PERPETUITIES.

James Polk and the Rule Against Perpetuities

Under the common law rule against perpetuities, no interest is good unless it must vest, or fail to vest, not later than 21 years after a life or lives in being at the creation of the interest. In other words, the rule against perpetuities (RAP) is a rule against possible remote vesting. It applies to contingent remainders, executory interests, and open class gifts, and it may apply to other property interests, such as rights of first refusal, options to purchase, and oil and gas leases. Furthermore, as noted in the 2011 movie, *The Descendants*, the rule applies to trusts and can limit their duration.

In its unmodified form, the perpetuities rule is concerned with what *could* happen instead of what actually does happen. Consequently, the common law RAP invalidates property interests based on such improbable and theoretical scenarios as the "fertile octogenarian," the "unborn widow," and the inexhaustible gravel pit. W. Barton Leach, *Perpetuities in a Nutshell*, 51 Harv. L. Rev. 638, 642–43 (1938). Most states, however, have modified and constrained the common law rule. Lynn Foster, *Fifty-one Flowers: Current Perpetuities Law in the States*, Prob. & Prop., July/Aug. 2008, at 30.

James K. Polk, the 11th president of the United States, was a posthumous victim of the common-law rule against perpetuities. After honoring his promise to serve one term, Polk left the White House in 1849 and returned to Nashville. Just two months later, the childless 53-year-old lawyer-politician contracted cholera and died. Polk had drafted his own will, which left "Polk Place" to his wife Sarah for life. The remainder in fee simple was given to the state in trust, with instructions to permit occupation of the house and property by blood relatives on the condition they shall "keep the same in repair, so as to prevent them from delapidating [*sic*] or falling into decay, shall pay the public taxes thereon, and shall preserve and keep in repair the tomb which may be placed or erected over the mortal remains of

my beloved wife and myself." George H. Armistead Jr., *The Void Provisions of a President's Will*, 15 Tenn. Hist. Q. 136, 138 (June 1956), available at https://drive.google.com/file/d/0BwyFMYMZ5JV0MFFJZEpTYnBEaGs/view.

Because he was a cholera victim, James Polk was initially buried in the city cemetery; however, in 1850 he was re-interred at Polk Place, a few blocks from the state capitol. His wife remained at the residence until her death in 1891. Soon after, 47 descendants of Polk's seven siblings filed suit in chancery court to declare the testamentary trust null and void. Their chief contention was that the trust violated the rule against perpetuities "in that it provides that Polk Place shall be held . . . for such persons of the house of Polk as may be designated by the State, from time to time, forever."

The court agreed, and held that the will "must be set aside so far as concerns Polk Place, and that property turned over to his heirs-at-law." *The Tennessean*, May 25, 1892, at 3. Although acknowledging the beneficiaries of the trust "need not be in existence at the creation of the trust," the court held "they must be designated and come into existence within the time prescribed by the rule against perpetuities."

Polk Place was sold and demolished. On September 19, 1893, James Polk's body was moved yet again to the east side of the state capitol and buried alongside his wife. Their gravesite is rarely visited, overshadowed by an equestrian statue of Andrew Jackson. State legislators in 2017 considered relocating James Polk a third time to the family home in Columbia, Tennessee. The proposal was opposed by some of Polk's descendants and defeated.

According to one commentator, "[t]he frequent observation that a lawyer is incapable of making his own will has been forcibly exemplified in the will of James K. Polk." 26 Am. L. Rev. 897, 897 (1892). As chief executive, Polk annexed Texas, presided over the Mexican-American War, and achieved the major goals of his presidency (an independent treasury, reduction of tariffs, and acquisition of the Oregon Country, California, and New Mexico). As a lawyer, however, he violated the rule against perpetuities by creating a trust granting rights to a potentially endless line of "the house of Polk."

THE ISSUE IN *MOORE V. VAIL* WAS NOT WHETHER THE GRANTORS BREACHED THEIR COVENANT, BUT WHETHER THE STATUTE OF LIMITATIONS BARRED THE ACTION FOR BREACH.

Abraham Lincoln and Deed Covenants

Numerous articles and books have been written about Lincoln the lawyer. See, e.g., Roger Billings, *Lincoln and Illinois Real Estate: The Making of a Mortgage Lawyer*, in Abraham Lincoln, Esq.: The Legal Career of America's Greatest President 105 (Roger Billings & Frank J. Williams eds., 2010); Brian Dirck, *Lincoln the Lawyer* (2007); Mark E. Steiner, *An Honest Calling: The Law Practice of Abraham Lincoln* (2006); and Allen D. Spiegel, *A. Lincoln, Esquire: A Shrewd, Sophisticated Lawyer in His Time* (2003). By one estimate, Abraham Lincoln was involved in more than 5,100 cases, including one United States Supreme Court appearance and hundreds of cases before the Illinois Supreme Court. Norman Gross, *Presidential Bar Leaders: Fascinating Facts About America's Lawyer-Presidents*, 34 Bar Leader No. 3 (Jan./Feb. 2010), www.americanbar.org/groups/bar_services/publications/bar_leader/2009_10/january_february/presidential.html.

One of his cases was *Moore v. Vail*, 17 Ill. 185 (1855), which was argued and decided during the December session of the Illinois Supreme Court. Ten months earlier, on February 8, 1855, Lincoln came within five votes of being elected by the Illinois House of Representatives to the United States Senate. Without abandoning his political aspirations, Lincoln represented Joshua Moore in a suit brought by George Vail and Moses Dodd for breach of a deed covenant. As it turned out, Lincoln also was unsuccessful in this particular lawsuit. At issue in the case was the transfer of property—subject to judgment liens—in 1836 from Charles Collins, Ira Munn, and Joshua Moore to George Vail and Moses Dodd. The liens were subsequently foreclosed. Bonesteel purchased the property and took a sheriff's deed in 1839. After a series of conveyances, title vested in Catherine Lynch, who in 1842 took possession of the vacant premises. In light of her assertion of paramount title, Vail and Dodd sued for breach of the covenant, contained in their 1836 deed, that the grantors would "warrant and defend the title to the said premises."

The issue in *Moore v. Vail* was not whether the grantors breached their covenant, but whether the statute of limitations barred the action for breach. Deed covenants fall into two groups: present covenants and future covenants. Present covenants (the covenants of seisin, right to convey, and the covenant against encumbrances) are breached, if at all, upon delivery of the deed. In contrast, the future covenants (warranty, quiet enjoyment, and further assurances) are breached "only when the grantee is actually or constructively evicted by someone holding superior title or suffers other damage." John G. Sprankling, *Understanding Property Law* 432 (2d ed. 2007). The issue in *Moore* was whether the future covenant

of warranty was breached in 1836 when the deed was delivered or in 1842 when Lynch took possession. Lincoln argued for the earlier date, relying on a stipulation that Collins, Munn, and Moore "had no good title to the land when they so sold and conveyed." 17 Ill. at 189. The court, however, refused to equate lack of title with breach of the future covenant of warranty:

> There must not only be a want of title, but there must be an ouster under a paramount title. . . . There was no interference [in this case], till Mrs. Lynch entered and took possession of the property in 1842. This entry being by paramount title, although peaceable and without opposition from the covenantee, was at least a constructive ouster and a breach of the covenant.

17 Ill. at 189, 191. In other words, if Vail and Dodd had sued for breach of the *present* covenants of seisin, encumbrances, and right to convey, their action would have been time-barred. Their grantors, however, gave the *future* covenant of warranty, which was breached in 1842 by the constructive eviction caused by Lynch's assertion of possession and paramount title.

The Illinois Supreme Court cited the holding of *Moore v. Vail* with approval in *Scott v. Kirkendall*, 88 Ill. 465 (1878). The *Scott* decision, in turn, was deemed "controlling" by the same court in *Brown v. Lober*, 389 N.E.2d 1188, 1192 (Ill. 1979). Several property textbooks use *Brown v. Lober* to educate students on the differences between present and future covenants. See, e.g., Grant S. Nelson et al., *Real Estate Transfer, Finance, and Development: Cases and Materials* 215 (9th ed. 2015); and Jesse Dukeminier et al., *Property* 620 (8th ed. 2014). Law students—and lawyers—who read *Brown v. Lober* most likely are unaware its legal reasoning is based in part on a case involving Abraham Lincoln.

Benjamin Harrison and the Takings Clause

Benjamin Harrison is the only president who was the grandson of another president (William Henry Harrison). He is also the only chief executive who was preceded and succeeded by the same man (Grover Cleveland) and is one of just eight presidents to argue before the U.S. Supreme Court (the others were John Quincy Adams, James Polk, Abraham Lincoln, James Garfield, Grover Cleveland, William Howard Taft, and Richard Nixon). Harrison appeared 15 times before the Supreme Court and "remained active in law practice until his death on March 13, 1901, reportedly averaging $150,000 a year." Allen Sharp, *Benjamin Harrison: High-Priced Counsel*, *in America's Lawyer-Presidents* 203 (Norman Gross ed., 2004).

MORE THAN A CENTURY LATER, IN A HIGHLY CONTROVERSIAL OPINION, THE COURT IDENTIFIED *FALLBROOK* AS A STARTING POINT FOR ITS CURRENT "PUBLIC PURPOSE" INTERPRETATION OF THE "PUBLIC USE" REQUIREMENT.

In *Fallbrook Irrigation Dist. v. Bradley*, 164 U.S. 112 (1896), the Court adopted the position taken by Harrison's client and held condemnation of land for an irrigation project constitutes a "public use" for purposes of the Fifth and Fourteenth Amendments. The Fifth Amendment to the Constitution, made applicable to the states by the Fourteenth Amendment, provides "private property [shall not] be taken for public use, without just compensation." California in 1887 enacted a law "providing for the organization and government of irrigation districts, and to provide for the acquisition of water and other property, and for the distribution of water thereby for irrigation purposes." 164 U.S. at 114. The statute was challenged in federal court on the grounds that "the use for which the water is to be procured is not in any sense a public one, because it is limited to the landowners who may be such at the time when the water is to be apportioned, and the interest of the public is nothing more than that indirect and collateral benefit." Id. at 156. In a decision that "stagger[ed] investors and invalidat[ed] all the bonds issued under the act," the district court declared the 1887 statute unconstitutional. William P. Aiken, *The Irrigation Question in California*, 5 Yale L.J. 122, 126 (1896) (quoted in Kay Russell, *The Fallbrook Irrigation District Case*, 21 J. San Diego History No. 2 (Spring 1975), www.sandiegohistory.org/journal/1975/april/fallbrook/).

The irrigation district hired Benjamin Harrison to argue its case before the Supreme Court (which included David Brewer, Henry Billings Brown, and George Shiras Jr., appointed by the ex-president). Harrison apparently earned his fee, as the state law was upheld. In his opinion for the Court, Justice Rufus Peckham equated "public use" with "public purpose" and held "[i]t is not essential that the entire community, or even any considerable portion thereof, should directly enjoy or participate in an improvement in order to constitute a public use." 164 U.S. at 161–62.

More than a century later, in a highly controversial opinion, the Court identified *Fallbrook* as a starting point for its current "public purpose" interpretation of the "public use" requirement. *Kelo v. City of New London*, 545 U.S. 469, 480 (2005). The 1896 *Fallbrook* decision is cited, both by Justice John Paul Stevens, in his majority opinion, and by Justice Clarence Thomas, in his strongly

worded dissent. The highly publicized *Kelo* case presented the issue of whether "a city's decision to take property for the purpose of economic development satisfies the 'public use' requirement of the Fifth Amendment." Id. at 477. In a 5–4 decision, the Court held "there is no basis for exempting economic development from our traditionally broad understanding of public purpose." Id. at 485. According to Justice Stevens, the *Fallbrook* decision is the origin for the contemporary interpretation of the "public use" requirement: "[W]hen this Court began applying the Fifth Amendment to the States at the close of the 19th century, it embraced the broader and more natural interpretation of public use as 'public purpose.'" Id. at 480 (citing *Fallbrook Irrigation Dist.*).

Justice Thomas agreed with Justice Stevens that "the 'public purpose' interpretation of the Public Use Clause stems from *Fallbrook Irrigation Dist. v. Bradley* . . . ." Id. at 515. In his view, however, *Fallbrook* was wrongly decided and is the first of "a string of our cases construing the Public Use Clause to be a virtual nullity, without the slightest nod to its original meaning." Id. at 506. See also Alberto B. Lopez, *Revisiting* Kelo *and Eminent Domain's "Summer of Scrutiny,"* 59 Ala. L. Rev. 561, 581–82 (2008) ("According to Justice Thomas's public use genealogy, the Court began its misguided trek toward its modern broad interpretation of the public use limitation in *Fallbrook Irrigation District v. Bradley*"). Despite such protestations, Benjamin Harrison's *Fallbrook* case continues to influence the scope and meaning of the Fifth Amendment's Public Use Clause.

Donald Trump and Liquidated Damages

Donald Trump, through his companies, is the owner of the Trump World Tower at 845 United Nations Plaza in New York City. In 1999, two Turkish billionaires, Cem and Hakan Uzan, agreed to pay approximately $32 million for luxury apartments. But, after terrorists destroyed the World Trade Center on September 11, 2001, the Uzan brothers refused to complete the transaction and asked for their $8 million down payment. To their surprise, the deposit was not returned, and to their further dismay, the retention of the $8 million was upheld by the New York courts. The purchase agreement was terminated and the apartments were once again available for sale.

Question: how did Donald Trump do this? Answer: by including a provision in the purchase agreement that, in the event of buyer default, the seller "shall have the right to retain, as and for liquidated damages, the Down payment and any interest earned on the Down payment." *Uzan v. 845 UN Ltd. Partnership*, 778 N.Y.S.2d 171, 173 (N.Y. App. Div. 2004). A liquidated damages clause "is a contractual provision by which the parties stipulate to a fixed sum to be paid in the event of a breach." Id. at 176 n.3. A liquidated damages clause typically will only be enforced if three conditions are satisfied: "(1) the damages anticipated as a result of the breach are uncertain in amount or difficult to prove; (2) the parties intended to liquidate damages in advance; and (3) the amount agreed upon must be reasonable and not greatly disproportionate to the presumable loss or injury." *Orr v. Goodwin*, 953 A.2d 1190, 1193 (N.H. 2008). If the amount forfeited is considered excessive or punitive, the clause may be deemed an unenforceable penalty.

A LIQUIDATED DAMAGES CLAUSE "IS A CONTRACTUAL PROVISION BY WHICH THE PARTIES STIPULATE TO A FIXED SUM TO BE PAID IN THE EVENT OF A BREACH."

The Uzan brothers argued that forfeiture of their 25% down payment was an unenforceable penalty. The New York Supreme Court disagreed, holding that (1) the purchase agreements "were a product of lengthy negotiation between parties of equal bargaining power, all represented by counsel"; and (2) a 25% down payment "is common usage in the new construction luxury condominium market in New York City." 778 N.Y.S.2d at 172. The court was less concerned with whether $8 million was a reasonable up-front estimate of probable damages and more focused on whether the Uzan brothers could show "disparity of bargaining power between the parties, duress, fraud, illegality or mutual mistake." Id. at 176. According to the authors of a leading property law textbook, the *Uzan* court "ultimately held that 'reasonableness' did not matter—any deposit, even an unreasonable one, can be retained by the vendor under New York law." Nelson et al., supra, at 71. Not all courts agree, however. See *McIlvenny v. Horton*, 302 S.W.2d 70, 72 (Ark. 1957) (liquidated damages amount, which was 16% of the purchase price, was "out of all proportion to the probable damages, and . . . should be construed as a penalty and not liquidated damages").

This was not the first setback for the Uzan brothers, who in 2003 were found liable for damages in excess of $4 billion in connection with a fraudulent deal to develop a cellular telephone network in Turkey. *Motorola Credit Corp. v. Uzan*, 274 F. Supp. 2d 481 (S.D.N.Y. 2003). As for Trump, when asked to comment on the Trump Tower lawsuit, the future president and author of *The Art of the Deal* said he was "happy" with the decision. *Asbury Park (N.J.) Press* (June 16, 2004), at 11. ■