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Restraints on Alientation of Property Not Held in Trust

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COMMENTS

RESTRAINTS ON ALIENATION OF PROPERTY NOT HELD IN TRUST

Restraints on the alienation of property may roughly be divided into two categories, direct and indirect. The possible invalidity of a direct restraint is based on common-law principles, while the invalidity of an indirect restraint is covered by statutory regulations. The purpose of this article is to distinguish valid from invalid restraints which may be attached to the transfer of property. Restraints on property held in trust are not covered in this comment, but are discussed in a related article.[1]

Direct Restraints

By a direct restraint is meant a provision which, by its terms, prohibits or penalizes the exercise of the power of alienation. There are three classes of direct restraints: disabling, forfeiture and promissory.[2] The application of Wisconsin law to the three types of direct restraints will be taken up in this order.

A disabling restraint exists when property is conveyed or devised with a direction to the effect that it shall not be alienated.[3] The basic rule of common-law and of equity jurisprudence is that, except in the case of property settled or devised to the separate use of married women or on charitable uses, no property interest, real or personal, legal or equitable, can be held by any person in such a way that he or she can enjoy the income or benefits thereof but cannot alienate it or subject it to his or her debts.[4]

There is no doubt that such a restraint is void in Wisconsin if attached to the transfer of a fee simple estate. In *Zillmer v. Landguth*[5] an estate in fee simple was devised to two daughters in undivided moieties, with a condition annexed to the effect that the devisees should not convey the same until the eldest child should attain the age of twenty-five years (which would be eleven years after the death of the testator); or, in other words, that all power of alienation should be absolutely suspended for a fixed period. The court held the condition void, stating that "when a conveyance or devise is made in fee, a condition attempted to be annexed thereto to the effect that the purchaser or devisee shall not for any period of time convey or alien the estate is void for repugnancy."

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[1] Comment 36 Marq. L. Rev. 97 (1952).
[2] Simes, Handbook on the Law of Future Interests sec. 100 (1951). (hereafter cited as Simes)
[3] *Ibid.*, sec. 100.
[4] Gray, Perpetuities sec. 119 (2d ed.)
[5] 94 Wis. 607, 69 N.W. 568 (1896).

The general rule is that a condition, annexed to a conveyance in fee or by devise that the purchaser or devisee should not alien, is unlawful and void.[6] Conditions are not sustained when they are repugnant to the estate granted, or infringe upon the essential enjoyment and independent rights of property and tend manifestly to public inconvenience.[7]

The invalidity of a disabling restraint seems to apply only when such restraint is attached to a full fee. A direct restraint against the alienation of a life estate was not declared void in *Meinert v. Roeglin.*[8] In that case a will contained a restraint against alienation. The testator by said will devised land to a son to have and to hold the same to himself and his heirs forever, with the proviso that the son should not sell the land, but that the land should go to his heirs after his decease. The question was whether the restraint was valid. The court construed this to be a life estate in the son with a remainder over to his children. This was a forced construction carrying out the intent of the testator. Thus a disabling restraint attached to a life estate would appear to be valid for the *unstated* reason that the right of alienation was not apparently considered an essential feature of a life estate.

The basic reason why a disabling restraint is void only when attached to the transfer of a full fee seems to lie in the old common-law theory of an estate. At one time, when the system of feudal tenures was in force, an overlord could transfer a fee simple estate and prevent its alienation. The reason why this was allowed was that the overlord still retained an interest in the land as a result of the complicated feudal system of that day. This feudal system was galling on most people of that era and was gradually changed. The statute of *Quia Emptores* (18 Edw. I, c. 1) abolished subinfeudations in regard to all the common tenures and declared that every freeman might thereafter sell at his own pleasure his lands and tenements. This took away the reversion from the immediate lord, and thus deprived him of the power of imposing restraints on alienation. After the statutes of 18 Edw. I c. 1 and 12 Car. II c. 24 the right of alienation was treated as an incident of an estate in fee simple. The foundation of the power to restrain alienation, when recognized as existing, now rests on the fact that there remains or is vested in someone a valid remainder or reversion, whose estate in possession is contingent on some event which defeats the precedent estate, and who is entitled to take advantage of the prohibited act or use.[9]

The second class of direct restraints are those of forfeiture. These restrictions exist when, by the terms of an instrument of transfer, the

[6] Van Osdell v. Champion, 89 Wis. 661, 62 N.W. 539, 27 L.R.A. 773 (1895).
[7] *Ibid.*
[8] 169 Wis. 531, 173 N.W. 224 (1919).
[9] 21 R.C.L. 325.

estate transferred will be subject to forfeiture on alienation.[10] In general, forfeiture restraints on life estates and on a lease for years are valid.[11] However, a forfeiture restraint on a fee is valid in Wisconsin. A grant can be made which would be determinable by the transferor, or by limitation of the estate over to another upon the occurrence of a certain event such as insolvency, bankruptcy, or the occurrence of any other act or event arising out of the conduct or neglect of the grantee or devisee.[12] It should be noted that such an estate is *not* a fee absolute, but a base or conditional fee. The difference between a fee simple estate and the lesser conditional fee seems to be the point on which Wisconsin law turns. When a fee is granted, limitations inconsistent with a fee, either on the use or on the grantee's freedom of conveyance, are deemed to be void as repugnant to the main purpose of the grant *unless* by reasonably direct language, disobedience of such limitations is declared a condition subsequent upon which the title conveyed is to terminate. The law does not permit the grantor to convey full title to land, and yet to restrain the conduct of the grantee with reference thereto in respects essential to a fee, though equity does recognize such a power when, and only when, a trust is created.[13] It would thus appear that a direct restraint on alienation would be valid if it created a conditional fee rather than a fee simple absolute. It should be noted, however, that the distinction between a fee simple and a conditional fee is mainly theoretical. Because of the general trend of decisions in Wisconsin it is quite probable that the difference would be recognized when there are good reasons for the distinction. A restraint which is plainly a disabling restraint, although couched in the technical language of a forfeiture restraint creating a conditional fee, would be in great danger of being held invalid as a direct restraint on the alienation of a fee simple estate.

The third type of restrictions are promissory restraints. A promissory restraint refers to a covenant in an instrument of conveyance, or to a contract, in which the promisor agrees not to alienate the property. To the extent that a contract not to alienate is enforceable in an action for damages, its validity is a matter of contract law, rather than of the law of property. But if the contract is of a sort which would be specifically enforceable, then its enforcement is concerned with the ownership of property.[14] This definition of a promissory restraint is concerned with a direct restraint on alienation rather than an indirect restraint resulting from a restriction on the use of property.

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[10] SIMES sec. 100.
[11] SIMES sec. 103.
[12] *Supra,* note 6.
[13] Danforth v. Oshkosh, 119 Wis. 262, 97 N.W. 258 (1903).
[14] SIMES sec. 100.

The Wisconsin Supreme Court had an opportunity to decide the question in *Doherty v. Rice*,[15] but preferred to sidestep the issue. In this case a restriction against sales to a non-Caucasian was in issue. The court held that a tax sale cut off the restriction in the deed so that a decision on the possible invalidity of the promissory restraint was unnecessary. From this case it is clear that a tax sale will cut off a restriction on the *sale* of property. The court, however, cited a number of cases from other jurisdictions which had been decided on both sides of the question and seemed to place particular emphasis on a West Virginia[16] case holding such a provision void as a restraint against alienation under the common-law rule. The restriction against sale to a non-Caucasian was the cause of the indecision in the Wisconsin case. The court seemed to have little doubt that if the racial question was not present the restriction would be invalid. It stated:

> "There is a multitude of cases however not involving any racial question that hold restrictions against alienation for any period of time or to any class of persons void for such reason. [As a restraint on alienation.] The ground of these decisions in large part is that the restrictions are void because repugnant to the granting or devising clause of a deed or will purporting to convey or transfer a fee simple title."

The remainder of the problem concerning promissory restrictions on sale has been decided by the United States Supreme Court.[17] In *Shelley v. Kraemer* it was held that restrictive covenants, based on racial distinctions, are unenforceable as violative of the due process clause of the Fourteenth Amendment. This does not mean that the covenants are invalid. However, they are not enforceable by recourse to the courts. As a practical matter such covenants no longer have any binding effect since a state cannot through the exercise of any of its functions uphold the validity of these restrictions.

In Wisconsin, today, no restrictions on the sale of property will be valid. Restrictions as to use are generally enforceable in Wisconsin, with the exception of a restriction against use by a class based on racial discrimination. Reasonable restrictive covenants will be enforced in favor of landowners for whose benefit they were imposed, but the restriction must be a reasonable one and the grantee must take from a private grantor holding under a chain of title from the original grantor who imposed the restriction.[18] However, it should be noted that such covenants are not enforceable where the character of the neighborhood has so changed as to make it impossible to accomplish the purposes

[15] 240 Wis. 389, 3 N.W. 2d 734 (1942).
[16] White v. White, 108 W. Va. 128, 150 S. E. 531 (1929).
[17] Shelley v. Kraemer, 334 U. S. 1 (1948).
[18] *Supra*, note 15.

intended by such covenants. If previous violations of the restrictions in an area are so general as to indicate a purpose and intention on the part of the residents to abandon the general scheme or purpose, an equitable action to enforce the covenant will not be recognized.[19] Such covenants are strictly construed since they are not favored in the law and must be clearly drafted in order to withstand any attack.[20]

The reason why a restriction against use is held to be valid and enforceable by injunction is that it is treated as a negative easement, an equitable servitude,[21] or a covenant running with the land.[22] Whether a restriction is a covenant running with the land or merely a personal covenant binding upon the parties depends on the intention of the said parties.[23] This type of partial restraint on alienation will be held valid if care is used in its drafting. Although these covenants are in fact a detriment to free alienability, they are a restraint as to user rather than on alienability. This distinction is important in deciding whether a proposed covenant is valid or invalid since the validity of the restriction on use depends on its reasonableness.

Personal property, generally, is subject to the same rules regarding direct restraints.[24] However, there is a class of personal property in which direct restraints are allowed, if not directly encouraged. This class comprises corporation stock in which, through by-laws or by contract, a mandatory provision is inserted whereby the stockholder must offer the stock to the corporation or the other stockholders before attempting to sell on the open market. The corporation, if it wishes to increase its capital stock, must offer such issue to the then existing stockholders before offering it to the general public.

It is sometimes necessary and often desirable that a corporation protect itself against the acquisition of shares of its stock by rivals in business. Therefore, restrictions upon the transfer of shares are generally recognized and held valid where they form part of the charter or articles of organization of the corporation and are matters of contract between the shareholders.[25]

A corporate by-law which prohibits the alienation of shares of stock or which amounts to an unreasonable restraint upon the transfers is void. There is a distinction between charter provisions or by-laws absolutely or unreasonably restrictive of transfer and those placing

[19] Ward v. Prospect Manor Corporation, 188 Wis. 534, 206 N.W. 856, 46 A.L.R. 364 (1926).
[20] Mueller v. Schier, 189 Wis. 70, 205 N.W. 912 (1926); Boyden v. Roberts, 131 Wis. 659, 111 N.W. 701 (1907).
[21] *Supra*, note 15; Boyden v. Roberts, supra, note 20.
[22] Stein v. Endres Home Builders, Inc., 228 Wis. 620, 280 N.W. 316 (1938).
[23] Clark v. Guy Drews Post, 247 Wis. 48, 18 N.W. 2d 322 (1945).
[24] SIMES sec. 102.
[25] Farmers Mercantile & Supply Co. v. Laun, 146 Wis. 252, 131 N.W. 366 (1911).

reasonable conditions upon the transfer of stock.[26] Restrictions are reasonable if their purpose is to prevent purchase of stock by outsiders, rivals or other disturbers. Sale to another stockholder, without first offering the stock to the corporation, would be valid.[27] Absolute restrictions upon alienation or transfer are void, but do not forbid *contractual* provisions whereby one, in acquiring title, agrees that another, or others, shall have the refusal of such property in case the stockholder desires to sell.[28]

A corporation must allow stockholders to retain their equity in the business. In an already established and going concern, an increase of capital stock, accomplished either by formal increase of the amount originally authorized or by issue of what had originally been withheld, though within the authorized amount, without first giving opportunity to all existing stockholders to take their proportionate shares of such increase, is wholly beyond the power, not only of the directors, but of any mere majority of stockholders.[29]

INDIRECT RESTRAINTS

A second main type of restraints are those due to the creation of future estates. The restriction of free alienation of property has not been favored in the law. Two methods of meeting the problem have developed: (a) the rule against perpetuities, and (b) the statutory rule prohibiting the suspension of alienation beyond a specified period.

The rule against perpetuities is aimed at preventing the postponement of vesting of a fee. The allowable period within which the vesting of the fee could be postponed under the common-law rule was for life or lives in being plus twenty-one years and the period of gestation.[30]

The second method of preventing so-called "perpetuities" is by statute, which is aimed at the prevention of the suspension of alienation. This method is used in Wisconsin.

When Wisconsin adopted the statutory rule from New York[31] on the suspension of alienation, there was a question whether the statute abrogated the common-law rule against perpetuities or was merely an addition to it. In a series of opinions, the Wisconsin Supreme Court held that the common-law rule was superseded and that it no longer had any effect in this state as to personalty.

In *Dodge v. Williams*[32] the court states that the statute limiting the rule against perpetuities to realty manifestly abrogates the English

[26] *Ibid.*
[27] Rychwalski v. Baranowski, 205 Wis. 193, 236 N.W. 131 (1931).
[28] *Supra*, note 25.
[29] Luther v. C. J. Luther Co., 118 Wis. 112, 122, 94 N.W. 69 (1903); Dunn v. Acme A. & G. Co., 168 Wis. 128, 169 N.W. 297 (1918); Hammer v. Cash, 172 Wis. 185, 178 N.W. 465 (1920).
[30] 41 AM. JUR. PERPETUITIES sec. 4.
[31] Danforth v. Oshkosh, *supra*, note 13.
[32] 46 Wis. 70, 1N.W. 92, 50 N.W. 1103 (1879).

doctrine as applicable to personalty. For a considerable period the state of the law on this point was uncertain. The court seemed to be undecided as to whether the statute abrogated the common-law rule or not.[33] Finally, in 1902,[34] the rule laid down in the Dodge case was definitely affirmed that the statute was effective to abolish the common-law rule against perpetuities as to *personalty.*

It does not appear that the court has ever directly decided that the common-law rule against perpetuities has been abolished in regard to realty. By reason of the manner in which personalty was handled in the above cases it is logically impossible that the common-law rule against perpetuities is still in effect in Wisconsin as applied to realty.

Section 230.14, Wisconsin Statutes, provides in part:

> "Every future estate shall be void in its creation which shall suspend the absolute power of alienation for a longer period than is prescribed in this chapter; such power of alienation is suspended when there are no persons in being by whom an absolute fee in possession can be conveyed."

If it be held that the statute is merely declarative of the common-law, then the holding that the common-law rule does not apply to personalty necessarily also abrogates any portion of the rule which is not covered by the express terms of the statute. It is now essential to note closely the difference between the common-law and the statute. At common-law, the evil aimed at was the undue prevention of the *vesting* of a fee.[35] The Wisconsin statute, however, is aimed at the prevention of the *suspension of alienation.*[36] The effect of both rules would be the same in many cases since an estate which is vested is not subject to either rule. Still the vesting of the estate is not the thing aimed at by the statute since a future estate is void only when it is limited to unascertained persons.[37] The failure to see the fundamental purpose of each rule seems to have been the main cause of confusion which has led to uncertainty as to whether or not the common-law rule is in effect in Wisconsin.

It is clear that the statute is not merely declarative of the common-law, but is an entirely new concept in the struggle to keep property from becoming tied down and out of the stream of commerce. A simple example of this is contained in a contingent remainder to ascertained persons. If A conveys land to B for life, then to the heirs of B when they reach thirty-five years of age, the remainder is invalid under the

[33] De Wolf v. Lawson, 61 Wis. 469, 21 N.W. 615 (1884); Webster v. Morris, 66 Wis. 366, 28 N.W. 353 (1886).
[34] Becker v. Chester, 115 Wis. 90, 91 N.W. 87 (1902); Miller v. Douglass, 192 Wis. 486, 213 N.W. 320 (1927).
[35] *Supra,* note 31.
[36] Miller v. Douglass, *supra,* note 35.
[37] Ford v. Ford, 70 Wis. 19, 33 N.W. 188 (1887).

common-law rule but valid under the Wisconsin Statutes. The contingent remaindermen are ascertained and can join in a conveyance.

The Wisconsin rule is contained in Sections 230.14 and 230.15 of the Wisconsin Statutes. Section 230.14 is quoted above; Section 230.15 reads as follows:

> "Limit of suspension. The absolute power of alienation shall not be suspended by any limitation or condition whatever for a longer period than during the continuance of a life or lives in being at the creation of the estate and thirty years thereafter, except when real estate is given, granted or devised to a charitable use or to literary or charitable corporations which shall have been organized under the laws of this state, for their sole use and benefit, or to any cemetery corporation, society or association, nor shall this section apply to gifts, grants, devises or bequests absolute, limited or in trust, for the advancement of medical science, to a state society of physicians and surgeons incorporated under the laws of this state."

The purpose of Section 230.14 is to prevent the creation of future estates which shall suspend the absolute power of alienation for a longer period than that prescribed by Section 230.15. The effect of the statute is to allow a restraint on property but to limit the period for which the restraint may run.

The main question which has to be decided is when is the power of alienation suspended. When there are no persons in being by whom an absolute fee *in possession* can be conveyed, within the meaning of the statutes, a suspension of the power of alienation is absolutely void.[38] The absolute power of alienation is not suspended within the meaning of the statute so long as absolute power is located somewhere to alienate, regardless of the condition in which the equivalent of the property alienated may be left; that undue suspension of the absolute ownership of an estate is one thing, and unlawful suspension of the power of alienation of real estate is another.[39] The purpose of Section 230.14, Wisconsin Statutes, is not to keep full ownership of land in one person, but only to allow a full fee to be transferred, even though a number of persons may have to join in order to accomplish this. Neither was it the intention of the legislature to force persons to convey within a specified period. It is enough that the fee may be conveyed within this specified period.

If the future legal estate is vested, then the power of alienation is not suspended within the force of those words in our statutes.[40] Therefore, the statute restricting the power of alienation cannot come into effect unless a future contingent estate is created. The legislature has

[38] *Ibid.;* Wis. Stats. (1951), sec. 230.14.
[39] Becker v. Chester, *supra,* note 35.
[40] *Supra,* note 13.

laid down the test by which future estates, both vested and contingent, are to be measured. Section 230.13, Wisconsin Statutes, provides:

> "Vested and contingent estates. Future estates are either vested or contingent. They are vested when there is a person in being who would have an immediate right, by virtue of it, to the possession of the lands upon the ceasing of the intermediate or precedent estate. They are contingent whilst the person to whom, or the event upon which, they are limited to take effect remains uncertain."

After a decision has been reached to the effect that a contingent future estate has been created, the time during which such estate will continue must be determined. This period is then compared with Section 230.15, Wisconsin Statutes, to decide for how long a time the alienation of the property is suspended. If the suspension is longer than a life or lives in being plus thirty years, the estate created is void. The principle is that, in order to make the future estate valid, the suspension of the power of alienation must under all circumstances terminate at or before the allowable period. It is not sufficient that it may so happen. It must so happen in every possible contingency.[41]

It is clear that the statute applies only to contingent future estates in which the person who will take is unascertained.[42] For example, if A by will gives a life estate to his son, B, and after the death of B a life estate to the children of B, with a remainder to the grandchildren of B, the remainder is contingent. If, at the death of A, B has no children, the remainder is invalid because of an unlawful suspension of alienation. The persons who will take the remainder cannot be ascertained within a life or lives in being plus thirty years. This same problem arises in a class gift which is vested subject to open. If B in the above hypothetical problem had two children alive when A died, the devise would be valid if A excluded any children B might have after A died. In this latter case, the allowable period would be measured by the life of B, his two children and thirty years thereafter. The remainder would vest within this period. If A did not exclude any possible afterborn children of B, the period might be measured by the life of a person not in being at the creation of the estate and the gift would be invalid.

The next problem is to determine what happens when a contingent future estate is held to be invalid. There will be a portion of the full fee which is not subject to the ownership of any person. The law must decide who will take this portion. If A devises land to B corporation and B is not in existence at the death of A, the devise will be

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[41] Eggleston v. Schwartz, 145 Wis. 106, 129 N.W. 48 (1911); Tyson v. Tyson, 96 Wis. 59, 71 N.W. 94 (1897).

[42] *Supra*, note 37.

invalid.[43] Since the devise is invalid the property remains a part of the testator's estate. However, when a future estate is created, a precedent estate, which is valid, must take effect. If the future estate is held invalid, this does not invalidate the intervening estate. There are two methods of treating the remainder.

First, the last preceding estate can be given the remainder so as to become a fee in the hands of the person taking the last precedent estate. This method will dispose of the problem in a fair manner if the prior estate is a conditional fee, but will do so in a way which is plainly contrary to the wishes of the person creating the estate if it is a life tenancy.

The second and better method for a life estate is to treat the remainder as a reversion. When a contingent future estate is held to be invalid the remainder will go back to the grantor, if living, or to the testator's heirs. In this way, the intention of the creator of the estate will be carried out as far as possible, but will not change the quantity of an estate which has been granted or devised. The above treatment will have the same effect as though a reversion had been expressly retained. There would seem to be no reason why Wisconsin would not follow this method of construing the intention of the person transferring the estate.[44]

There is no question but that in Wisconsin the common-law rule against perpetuities is ineffectual as regards personalty.[45] In 1925 the legislature passed the second portion of Section 230.14, which applies the rule against the suspension of the power of alienation to personalty, namely:

> ". . . Limitations of future or contingent interests in personal property are subject to the rules prescribed in relation to future estates in real property; provided, however, that this limitation upon interests in personal property shall not apply to any instrument which shall have taken effect prior to July, 1925."

The effect of the 1925 amendment was to subject personal property to the same rules to which real property was subordinate in regard to the suspension of alienation. Today, the same principles apply to both. The Supreme Court pointed out[46] "that the purpose of the amendment was to apply to future estates or interests in personal property, the same rules as had theretofore been applied by said section (230.14) to future estates in real estate, to the end that both future estates in real estate and future or contingent interests in personal property shall be void in their creation, which shall suspend the absolute power of alienation for a longer period than is prescribed in this chapter."

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[43] Giblin v. Giblin, 173 Wis. 632, 182 N.W. 357 (1921).
[44] See RESTATEMENT, PROPERTY sec. 228.
[45] *Supra*, note 34.
[46] Re Will of Schilling, 205 Wis. 259, 237 N.W. 122 (1931).

III. Conclusion

The Wisconsin law is not clear in many phases of this problem of restraints on the alienation of property. However, the general outline of this aspect of property law can be distinguished. The direct restraints on alienation are divided into three parts: disabling, forfeiture and promissory restraints. The first of these is invalid, the second is valid and the third is invalid in part. A promissory restraint on the sale of land is invalid, but a restraint against user is valid. Judging from the handling of restraints against user and on the sale of corporate stock, the Supreme Court relies a great deal on a test based on the reasonableness of the restraint.

In the field of indirect restraints no restraint is invalid if it cannot operate after a period measured by a life or lives in being plus thirty years. If the restraint will continue beyond this period, it is invalid only when the person or persons who shall take are unascertained. The common-law rule against perpetuities has never been expressly discarded in Wisconsin as to realty and would operate differently than the statutory rule. However, in view of decisions which have discarded the common-law rule as to personalty, it would not be logical to hold that the common-law rule does apply in Wisconsin as to realty.

When a future estate is declared invalid, the precedent estate becomes either a full fee simple or the gift over is treated as a reversion in the grantor or his heirs. The treatment given the invalid gift will depend on the court's construction of the grantor's intent.

The field of property law covered in this article has been the subject of much misunderstanding. The difficulty would largely disappear if consistent terminology is used in any discussion of the problems involved.

Douglas J. McClelland