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Case No. 1901-VCN

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

MICHAEL WELSH and AMY WELSH, his wife, Plaintiffs, v. HERITAGE HOMES OF DELAWARR, INC., a Delaware corporation, Defendant.	: : : : : : : : : : : :	**C.A. No. 1901-VCN**

MEMORANDUM OPINION

Date Submitted: January 22, 2008
Date Decided: February 15, 2008
Date Revised: February 19, 2008

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NOBLE, Vice Chancellor

Defendant Heritage Homes of DeLaWarr, Inc. ("Heritage Homes") is the developer of a forty-lot subdivision known as Lexington Mill, in Kent County, Delaware. It has erected all of Lexington Mill's thirty-one homes. The subdivision is unique because of its Colonial-style construction, a style reflecting the significant efforts of Heritage Homes' principals to learn about Colonial architecture and construction methods.

Plaintiffs Michael Welsh and Amy Welsh (the "Welshes") decided that they wanted to live in Lexington Mill. They purchased a lot (the "Property") from Heritage Homes and agreed that Heritage Homes would build their home. The parties, however, never agreed upon the full terms of a construction contract. When the Welshes hired another builder, the President of Heritage Homes, Donald Bloom, reviewed its plans under the architectural review provisions of the Declaration of Restrictions governing Lexington Mill and rejected them.

Because the parties had agreed that the Welshes would sell the Property back to Heritage Homes for the original price if a home was not built, Heritage Homes, approximately two years after closing on the lot sale, demanded that the Welshes re-convey the Property to it. The Welshes responded by filing this action in which they contend that the contractual duty to re-convey cannot be enforced because it would violate the rule against perpetuities and otherwise would be an undue restraint on alienation, that the agreement for construction of the home is

vague and, therefore, unenforceable, and that Heritage Homes, because of the bias of its principals, should not be allowed to enforce the restrictions against them and deny them a home built by a contractor of their choosing. In turn, Heritage Homes has counterclaimed for specific performance of the Welshes' duty to re-convey the Property to it.

The Welshes have moved for summary judgment.

I. BACKGROUND

On July 17, 2003, the Welshes and Heritage Homes entered into the "Agreement of Sale and Construction Agreement" (the "Agreement").[1] In addition to providing for the transfer of the Property, the Agreement reflected the parties' understanding that Heritage Homes also would construct a home for the Welshes on their newly acquired Property. Paragraph 2 of the Agreement provides:

> 2. The parties agree that Seller shall build and construct and furnish all labor and materials for a single family residence to be erected in accordance with the plans and specifications to be provided as soon as practical, which plans and specifications shall be incorporated herein. It is further agreed:
>
> a. A detailed construction agreement shall be executed at a later time, as a soon as practical, and shall be incorporated herein as part of this agreement.
>
> b. The price for the construction of the residence shall be $ TBD , to be paid out in accordance with the construction agreement, and/or the construction loan agreement, to be incorporated herein.

[1] Compendium of Exhibits to Plaintiffs' Opening Brief in Support of Plaintiffs' Motion for Summary Judgment ("Compendium") Ex. B.

> c. Buyers shall, as soon as possible, following the date of this instant agreement, make application for its construction loan in the amount of $ TBD . This entire agreement including lot sale, is contingent on Buyers obtaining a construction loan commitment by the TBD day of TBD A.D., 20 TBD . In the event that, after diligent effort, Buyer fails to get a construction loan commitment by the aforesaid date, then this entire agreement in [sic] null and void, and all deposit monies paid hereunder shall be returned to Buyer.[2]

The Agreement also granted Heritage Homes the right to reacquire the Property if the Welshes did not commence construction. Paragraph 3 of the Agreement provided:

> 3. Buyer agreed that in the event Buyer is unable to commence construction for any reason not attributed to Seller, Buyer agrees to re-convey the subject lot at the same price as sold to Buyer, within 30 days of receipt of Seller's request to re-convey.

The Agreement, however, establishes no period within which construction must commence.[3] Although the Welshes are obligated to re-convey the Property if requested by Heritage Homes, Heritage Homes is under no duty to buy the Property back.

Closing on the sale of the Property occurred on August 21, 2003. The deed did not include any reference either to the repurchase right or to the agreement that

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[2] The Agreement (at introductory paragraph 1) recites that "[i]t is the intent of [Heritage Homes] that it shall construct all homes on all lots sold." At times, this portion of the Agreement with the Builder Tie-In provision will be referred to as the "Construction Agreement."

[3] According to introductory paragraph 3 of the Agreement, "It is expected and a condition for all agreements hereunder that a home will be built on each lot sold immediately after sale, or within an agreed upon time following sale." At times, this portion of the Agreement will be referred to as the "Buyback Provision."

Heritage Homes would be the builder.[4] During the closing, there was some discussion of a three-year period within which construction would start. If there was agreement on that point, it evidently was not memorialized by any writing.

The parties subsequently were unable to reach agreement on the construction of a dwelling. The reasons for that failure are not clear. The Welshes contend that it was largely a matter of price. Heritage Homes asserts that the Welshes never provided sufficient details to allow it to develop a firm price. The Welshes, nonetheless, went forward with plans to build their home. They contracted with another builder.[5]

Lexington Mill is subject to a Declaration of Restrictions (the "Declaration"),[6] which, at paragraph 10, confers upon Heritage Homes as the Declarant a right of architectural review and contractor approval:

> (a) No building, . . . shall be commenced upon any lot . . . until the name of the contractor and the plans and specifications showing the nature, kind, shape, material and location thereof, including site plan and grading, shall have been submitted to the Declarant and shall have been approved in writing by Declarant.
>
> (b) Declarant shall have the right to refuse to approve such plans and specifications which are not, in its sole judgment, desirable for aesthetic or other reasons, and in so passing upon such plans and specifications it may consider, to the extent applicable, the suitability to the site of the proposed structure or alterations, the harmony thereof with the surroundings, the materials to be used, and the effect thereof

[4] Appendix to Reply Brief in Support of Plaintiffs' Motion for Summary Judgment ("Appendix") Ex. A.
[5] Compendium Ex. H.
[6] Compendium Ex. A.

> with the surroundings and upon the outlook from an enjoyment of adjacent or neighboring properties.
>
> (c) Declarant shall have the right to refuse to approve the proposed contractor if Declarant believes the contractor will not promptly complete the construction in a workmanlike manner.[7]

As a follow up to other discussions, the Welshes, in July 2005, submitted their builder's construction proposal for review by Heritage Homes under the Declaration. Shortly thereafter, Heritage Homes informed the Welshes that their plans had not been approved.[8] Several reasons were given, ranging from an "overall design of the house is not compatible with other homes in Lexington Mills" to a dislike of aluminum soffets. As its principal reason, however, Heritage Homes asserted the position that "[o]nly Heritage Homes is an authorized builder of new homes in Lexington Mills."

In addition to rejecting the Welshes' plans and their builder, Heritage Homes also purported to exercise its right to reacquire the Property. The Welshes have not re-conveyed the Property to Heritage Homes. This action followed.

II. CONTENTIONS

The Welshes seek to avoid the contractual obligation to re-convey the Property to Heritage Homes by arguing that the buyback terms of the Agreement violate the rule against perpetuities and constitute an undue restraint on alienation.

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[7] The Declaration, thus, contemplates builders in addition to Heritage Homes.
[8] Aff. of Donald Bloom Ex. C.

They point out that the Agreement does not establish any time period within which construction must begin, and it does not require Heritage Homes to repurchase the property within any specified period or at all. They next assert that the construction portion of the Agreement is unenforceable because there are so few terms and the text of agreement is so vague as to make it impossible to enforce. Finally, they contend that the decision of Heritage Homes to reject their plans and their builder was done in bad faith and that such inequitable conduct should be deemed to deprive Heritage Homes of its right to exercise architectural review authority over the Property.

Heritage Homes defends its entitlement to repurchase the Property by suggesting that the Court could impose a reasonable time limit and thereby avoid the rule against perpetuities issues. Moreover, it asserts that the Agreement creates a defeasible fee estate with a future interest in Heritage Homes and, therefore, does not violate the rule against perpetuities. As to the understanding that Heritage Homes would be the builder of the Welshes' home, Heritage Homes notes that the nature of the subdivision was readily apparent to the Welshes, that they had discussions before execution of the Agreement as to the average cost of a Heritage Homes-built house, and that the Welshes did not provide it with sufficient information to generate a full and complete construction contract. Finally, Heritage Homes asserts that it has acted in good faith in administering the

architectural review provisions of the Declaration and that whether it has acted in good faith is an open question of fact, thereby precluding summary judgment.

III. ANALYSIS

A. *The Summary Judgment Standard*

Summary judgment may be granted under Court of Chancery Rule 56 if there are no material facts in dispute and the moving party is entitled to judgment as a matter of law.[9] The movant must demonstrate that there is no issue of material fact and the Court must construe the facts in the light most favorable to the non-moving party.[10]

B. *Does Paragraph 3 of the Agreement Create a Conditional Option to Repurchase or Some Type of Defeasible Fee with a Concomitant Reversionary Interest that Survives Scrutiny under the Rule Against Perpetuities?*

The parties debate the legal effect of Paragraph 3 (the "Buyback Provision") of the Agreement, which provides:

> Buyer [the Welshes] agrees that in the event Buyer is unable to commence construction for any reason not attributed to Seller [Heritage Homes], Buyer agrees to re-convey the subject lot at the same price as sold to Buyer, within 30 days of receipt of Seller's request to re-convey.

[9] *Acciptier Life Sciences Fund, L.P. v. Helfer*, 905 A.2d 115, 122 (Del. Ch. 2006).
[10] *Eureka VIII LLC v. Niagara Falls Holdings LLC*, 899 A.2d 95, 106 (Del. Ch. 2006).

When applying a contract, the Court's goal is to ascertain the shared intent of the parties.[11] Delaware adheres to an objective theory of contracts.[12] Thus, where the language of a contract is clear and unambiguous, the ordinary meaning of the words chosen by the parties will establish their intent.[13]

The Welshes contend that the Buyback Provision simply is an option by which Heritage Homes could repurchase the Property if they failed to construct a home on the Property (the "Construction Condition").[14] That option is unlimited in its duration, purports to bind the Welshes and "their heirs, executors, administrors and assigns,"[15] and otherwise rests in a corporation, an entity of perpetual existence; accordingly, the Welshes argue, based on this Court's construction of the same contract provision in *Heritage Homes of De La Warr, Inc. v. Alexander*,[16]

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[11] *See, e.g.*, *Sassano v. CIBC World Markets Corp.*, 2008 WL 152582, at *5 (Del. Ch. Jan. 17, 2008).

[12] *See, e.g.*, *Seidensticker v. Gasparilla Inn, Inc.*, 2007 WL 4054473, at *2 (Del. Ch. Nov. 8, 2007).

[13] *See, e.g.*, *West Willow-Bay Court, LLC v. Robino-Bay Court, LLC*, 2007 WL 3317551, at *9 (Del. Ch. Nov. 2, 2007)

[14] Heritage Homes maintains that the Buyback Provision contemplates a three year time limit for a lot owner in Lexington Mill to begin construction of a home. Unlike in the contract at issue in *Heritage Homes of De La Warr v. Alexander*, 2005 WL 2173992 (Del. Ch. Sep. 1, 2005), *aff'd*, 900 A.2d 100 (2006) (TABLE), another case involving Heritage Homes and raising issues similar to those raised here, the three year time limit to begin construction is not expressly written in the Agreement. There is, however, some evidence that the parties had reached an oral understanding that construction would be commenced within three years of closing. For purposes of this memorandum opinion, the Court will assume, without deciding, that three years would be a reasonable time for the Welshes to have performed under the Agreement. *See, e.g.*, *Bryan v. Moore*, 863 A.2d 258, 261 (Del. Ch. 2004) ("If time is not of the essence in a contract, the court will allow a reasonable time to perform.").

[15] Agreement at ¶ 6.

[16] 2005 WL 2173992 (Del. Ch. Sep. 1, 2005), *aff'd*, 900 A.2d 100 (Del. 2006) (TABLE).

that the Buyback Provision violates the rule against perpetuities.[17] Thus, because the option might not be exercised, if at all, within the period prescribed by the rule, it is void and unenforceable.

Heritage Homes, on the other hand, contends that the Buyback Provision is not an option and, instead, should be construed as creating a defeasible fee estate. Specifically, it argues that the Buyback Provision creates a defeasible fee estate of either fee simple determinable or fee simple subject to a condition subsequent—interpretations that were not presented to the Court in *Alexander*. Despite the fee simple absolute conveyance language appearing on the face of the deed to the Property and Paragraph 1(c) of the Agreement, which required Heritage Homes to convey the Property in "free [sic] simple title, free and clear of liens and encumbrances,"[18] Heritage Homes asserts that, in fact, the Construction Condition in the Buyback Provision caused title to the Property to be conveyed in fee simple defeasible.[19] Accordingly, Heritage Homes argues that it either retained a possibility of reverter (fee simple determinable) or had a power to terminate (fee simple subject to condition subsequent) the Welshes' interest in the Property upon

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[17] The rule against perpetuities provides that "no interest is good unless it vests, if at all, not later than twenty-one years after some life in being at the creation of the interest." *Stuart Kingston, Inc. v. Robinson*, 596 A.2d 1378, 1383 (Del. 1991).

[18] Compendium Ex. B.

[19] *Cf. In re Estate of Barrett*, 1996 WL 120654, at *1 (Del. Ch. Mar. 8, 1996) (adopting Master's report determining that "where, as here, a deed or contract is free from ambiguity, a court is not permitted to construe its terms, although it may rule on the legal significance of terms used in it").

the happening of the Construction Condition. In either event, however, because that future interest in the Property is retained by Heritage Homes, as the grantor, it maintains that the Buyback Provision is outside the purview of the rule against perpetuities and is therefore valid and enforceable. In addition, Heritage Homes contends that, if the Buyback Provision is treated as an option, it should survive under modern notions about the effect of the rule against perpetuities on options.

Setting aside any question as to whether a valid defeasible fee can be created other than by deed,[20] the Court must determine what legal interest was created by the language of the Buyback Provision. There are, as the parties suggest, three possibilities: (1) a fee simple determinable estate (possibility of reverter); (2) a fee simple estate subject to a condition subsequent (right or reentry or power of termination); and (3) an option to repurchase the Property for a fixed price. If Heritage Homes is correct and the Buyback Provision created some type of defeasible fee with a reversionary or future interest resting in Heritage Homes, then

[20] *See, e.g.*, *Lynch v. Bunting*, 29 A.2d 155, 157 (Del. 1942) ("[I]t is essential that in order to introduce a determinable feature into a fee simple conveyance . . . the instrument itself *must*, on its face, contain a specific intent to do so . . . ." (emphasis added)). For purposes of this memorandum opinion, the Court will accept Heritage Homes' argument that it is "of no moment" that the limiting language does not appear on the face of the deed, at least as between Heritage Homes and the Welshes. *Cf.* 25 *Del. C.* § 109 ("If a conveyance of lands, tenements or hereditaments is absolute on its face and there is a defeasance, or written contract in the nature of a defeasance, or for a reconveyance of the premises, or any part thereof . . . [s]uch defeasance, or contract, shall be duly acknowledged, or proved, and recorded . . . or it shall not avail against a fair creditor, mortgagee or purchaser for a valuable consideration of or from the person to whom such conveyance is made . . . ."). Indeed, as will be discussed below, the precise document in which the language of the Buyback Provision is located is of no moment to this decision because regardless of where the language is found, it is, in all circumstances, an option in real property.

the Buyback Provision is not subject to the rule against perpetuities and would therefore be valid unless it is otherwise deemed to be an unreasonable restraint on alienation. On the other hand, if the Welshes are correct and the Buyback Provision is nothing more than an option of unlimited duration to repurchase the Property, then the rule against perpetuities would apply, and, as this Court explained in *Alexander*, the Buyback Provision would fail and be unenforceable.

1. The Buyback Provision Does Not Create a Fee Simple Determinable with a Possibility of Reverter in Heritage Homes

The Court first turns to the question of whether the Buyback Provision may properly be construed as creating a fee simple determinable estate with a possibility of reverter in Heritage Homes. It cannot. A fee simple determinable is "an estate that will *automatically* end and revert to the grantor if some specified event occurs."[21] In a fee simple determinable, the grantor conveys or transfers less than his full interest in the property, and he retains a future interest in the property

[21] BLACK'S LAW DICTIONARY 649 (8th ed. 2004) (emphasis added). *See also Lynch*, 29 A.2d at 176 (defining features of fee simple determinable estate); RESTATEMENT (FIRST) OF PROP.: FREEHOLD ESTATES § 44 (1936) [hereinafter RESTATEMENT: FREEHOLD ESTATES] ("An estate in fee simple determinable is created by any limitation which, in an otherwise effective conveyance of land, (a) creates an estate in fee simple; and (b) provides that the estate shall automatically expire upon the occurrence of a stated event."); RICHARD R. POWELL, POWELL ON REAL PROPERTY § 13.05[1], at 13-34 (Michael Allen Wolf ed. 2006) [hereinafter POWELL]. The following example illustrates the creation of a fee simple determinable estate: "A, owning Blackacre in fee simple absolute, transfers Blackacre 'to B and his heirs so long as Town C remains unincorporated.' B has an estate in fee simple determinable. A has a possibility of reverter despite the absence of specific words creating any interest in him. Town C is incorporated. B's estate expires automatically and A becomes entitled forthwith to possession of Blackacre." RESTATEMENT: FREEHOLD ESTATES, *supra*, § 44 at illus. 1.

for himself and his successors in interest, conditioned upon the occurrence of some future event. The future interest in a fee simple determinable estate is a reversionary interest known as a "possibility of reverter."[22] The hallmark of the fee simple determinable with a possibility of reverter, however, is that no further action is required on the part of the grantor to retake title to the property in fee simple absolute; the occurrence of the condition automatically vests such title back in the grantor.[23]

The Buyback Provision does not automatically vest title to the Property back in Heritage Homes upon occurrence of the Construction Condition. Instead, it specifies that the Welshes agree to reconvey the Property to Heritage Homes "within 30 days of receipt of [Heritage Homes'] request to re-convey." The Buyback provision mandates affirmative acts on the part of Heritage Homes to regain title to the Property—it must request reconveyance and repay the purchase

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[22] BLACK'S LAW DICTIONARY, *supra* note 21, at 1204 ("Possibility of Reverter: a reversionary interest that is subject to a condition precedent; specif., a future interest retained by a grantor after conveying a fee simple determinable, so that the grantee's estate terminates automatically and reverts to the grantor if the terminating event ever occurs."). *See also Lynch*, 29 A.2d at 176 (noting that possibility of reverter accompanies estate in fee simple determinable); RESTATEMENT (FIRST) OF PROP.: FUTURE INTERESTS § 154(3) (1936) [hereinafter RESTATEMENT: FUTURE INTERESTS] ("A possibility of reverter is any reversionary interest which is subject to a condition precedent."); POWELL, *supra* note 21, §§ 13.05[1], at 13-41 to -42, 20.02[1], at 20-8 to -9.

[23] Given modern notions restricting the use of "self help" to retake property, the "automatic" reversion is probably somewhat of an anachronism, if, indeed, it was ever so easy. Nevertheless, conceptually, the vesting of title back in the grantor is automatic, even if the actual retaking of physical possession is not.

price.[24] If it does not, title remains vested in the Welshes. Accordingly, because the Buyback Provision does not contain an automatic means by which title to the Property will revert to Heritage Homes, it is not, nor can it fairly be construed as creating, an estate in fee simple determinable with a possibility of reverter.

2. The Buyback Provision Creates an Option instead of an Estate in Fee Simple Subject to a Condition Subsequent with a Right of Reentry or Power of Termination in Heritage Homes

The more difficult question presented in this case is whether the Buyback Provision should be construed as an option to repurchase the Property or whether the provision may fairly be construed as creating an estate in fee simple subject to a condition subsequent with a "right of reentry" or a "power of termination" in Heritage Homes. The latter construction would take the Buyback Provision outside the rule against perpetuities;[25] given the Court's preference for construing agreements so as not to offend the rule where a consistent reading is possible, that reading of the Buyback Provision would be preferred.[26] The Court nevertheless concludes that the former reading is correct—the Buyback Provision is indeed an option to repurchase the Property. The reason for construing the Buyback

[24] Indeed, Heritage Homes is not even obligated to offer to buy back the property.

[25] RESTATEMENT (FIRST) OF PROP.: PERPETUITIES AND OTHER SOCIAL RESTRICTIONS § 372 (1936) [hereinafter RESTATEMENT: PERPETUITIES]. The Restatement (First)'s open hostility to options with an exercise date beyond the period allowed by the rule against perpetuities has not survived in recent years. *See* Part III(B)(3) *infra*. Its perspective on how a right should be characterized, whether as an option or as some type of future interest, does not appear, however, to have been undercut in a similar fashion.

[26] *See, e.g.*, *Stuart Kingston, Inc.*, 596 A.2d at 1383.

Provision as an option (and, thus, subject to the rule against perpetuities) may be viewed as a subtle one. The Court therefore will discuss together its reasons for rejecting Heritage Homes' argument for construing the Buyback Provision as creating an estate in fee simple subject to a condition subsequent and its reasons for determining that the Buyback Provision is, in fact, properly considered an option.

A fee simple subject to a condition subsequent is "[a]n estate subject to the grantor's power to end the estate if some specified event happens."[27] As in the fee simple determinable estate, the grantor in fee simple subject to a condition subsequent conveys less than his full interest in the property, and he retains a future interest in the property conveyed for himself and his successors in interest, conditioned upon the occurrence of some future event. The future interest retained by the grantor in a fee simple subject to a condition subsequent is known as a

[27] BLACK'S LAW DICTIONARY, *supra* note 21, at 649. *See also Lynch*, 29 A.2d at 176 (defining features of estate in fee simple subject to condition subsequent); RESTATEMENT: FREEHOLD ESTATES, *supra* note 21, § 45 ("An estate in fee simple subject to a condition subsequent is created by any limitation which, in an otherwise effective conveyance of land, (a) creates an estate in fee simple; and (b) provides that upon the occurrence of a stated event the conveyor or his successor in interest shall have the power to terminate the estate so created."); POWELL, *supra* note 21, § 13.05[2], at 13-44. The following example illustrates the creation of a fee simple estate subject to a condition subsequent: "A, owning Blackacre in fee simple absolute, transfers Blackacre 'to B and his heirs but on condition that if liquor is sold upon the premises conveyed, B's estate shall be subject to A's right to re-enter for breach thereof.' B sells liquor upon Blackacre. A, or his successor in interest, has the option of terminating the estate granted to B. RESTATEMENT: FREEHOLD ESTATES, *supra* note 21, § 45 illus. 1.

"power or termination"[28] or a "right of reentry."[29] Unlike the fee simple determinable with a possibility of reverter, however, the fee simple subject to a condition subsequent does not terminate automatically upon occurrence of the condition. Instead, the grantor must take an affirmative step to reclaim fee simple absolute title to the property; otherwise, title remains vested in the grantee.

In many respects, the Buyback Provision resembles a power of termination or a right of reentry that would follow an estate in fee simple subject to a condition subsequent. For example, the Buyback Provision is conditioned on the happening of a future event (*i.e.* the Construction Condition). It also requires Heritage Homes to take an affirmative step to reclaim title to the Property (*i.e.* it must request reconveyance to regain title). Indeed, until Heritage Homes does so, title remaines vested in the Welshes. Thus, there is some weight to Heritage Homes' suggested construction of the Buyback Provision. If the Buyback Provision only required the occurrence of the Construction Condition and Heritage Homes' bare assertion of its right to retake the Property, the Court might be persuaded that the provision

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[28] BLACK'S LAW DICTIONARY, *supra* note 21, at 1210 ("A future interest retained by a grantor after conveying a fee simple subject to a condition subsequent, so that the grantee's estate terminates (upon breach of the condition) only if the grantor exercises the right to retake it."). *See also Lynch*, 29 A.2d at 176 (noting that right of reentry accompanies estate in fee simple subject to condition subsequent); RESTATEMENT: FUTURE INTERESTS, *supra* note 22, § 155 ("A power of termination is the future interest created in the transferor, or his successor in interest, by a transfer of either an estate in land or an analogous interest in a thing other than land, subject to a condition subsequent."); POWELL, *supra* note 21, §§ 13.05[2], at 13-44, 20.03, at 20-24 to -29.

[29] BLACK'S LAW DICTIONARY, *supra* note 21, at 1350 ("See Power of Termination."). For a more thorough definition by reference to the synonymous term "power of termination," see generally authorities cited *supra* note 28.

could fairly be construed as creating an estate in fee simple subject to a condition subsequent. But the Buyback Provision requires something more.

The subtle, yet crucial, difference in the Buyback Provision that requires the Court to construe it as an option to repurchase, rather than as a fee simple subject to a condition subsequent, is that the Buyback Provision also requires Heritage Homes to pay *consideration* (the original purchase price) to the Welshes in order to reclaim title. It is that feature of the Buyback Provision that is fatal to Heritage Homes' argument and ultimately renders the Buyback Provision an option to repurchase the Property.

The Court has not found (nor have the parties cited) any Delaware authority drawing a distinction between an option and a right of reentry or a power of termination. Accordingly, the Court turns to the Restatement (First) of Property for guidance on this issue.[30] Section 394 of the Restatement provides:

> Option to Repurchase Reserved in Favor of the Conveyor. Subject to exceptions [not applicable here], the reservation of an option to repurchase the whole or any part of the interest conveyed, made in favor of the conveyor, is invalid, because of the rule against perpetuities, when, under the language and circumstances of the reservation, such option (a) may continue for a period longer than the maximum period described [by the rule against perpetuities]; and (b) would create an interest in land . . . but for the rule against perpetuities.[31]

[30] *See, e.g.*, *Libeau v. Fox*, 892 A.2d 1068, 1072 (Del. 2006) (affirming, with approval, this Court's application of "settled principles" from the Restatement (First) of Property).

[31] RESTATEMENT: PERPETUITIES, *supra* note 25, § 394. The Restatement's illustration of Section 394 demonstrates its antipathy to options that do not satisfy the rule's requirements: "A, owning Blackacre in fee simple absolute, makes an otherwise effective conveyance of Blackacre 'to B

Moreover, the Restatement goes on to state a constructional preference for construing provisions like the Buyback Provision as an option to repurchase, instead of a right of reentry or a power of termination. Comment c to Section 394 provides:

> Constructional preference. If the language and circumstances of a conveyance of an estate in fee simple are otherwise reasonably susceptible of two constructions, under one of which it creates either a possibility of reverter or a power of termination . . . and under the other of which it creates an option to repurchase (a type of interest within the rule stated in this Section) the latter of these two constructions is preferred. The fact that the exercise of the reserved privilege requires the parting of money or other consideration, by the reserving conveyor is sufficiently indicative of the intent of the conveyor to create an option, to prevent application [of the rule favoring construction of an ambiguous provision so as not to offend the rule against perpetuities].

The rationale for the rule stated in Section 394 of the Restatement is sound and in keeping with Delaware's public policy against unreasonable restraints on the alienability of land.[32] To be sure, a grantor ought not to be able to accomplish

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and his heirs, reserving, however, to A and his heirs the privilege at any time to repurchase an estate in fee simple absolute in Blackacre upon repaying to B, or to his successor in interest, the sum of $10,000 and reimbursing the then owner of Blackacre for the reasonable value of improvements made on Blackacre after this conveyance and still thereon at the time of such repurchase.' The option to repurchase attempted to be reserved is unlimited as to its duration. So long as it continues, if valid, the alienability of Blackacre is hindered. It is invalid, and B has an estate in fee simple absolute in Blackacre." *Id.* at illus. 1. *See also* POWELL, *supra* note 21, § 72.11[2], at 72-68 ("Options to purchase or to repurchase land, unconnected with a lease, commonly denominated options in gross, have generally been held bad under the common law rule against perpetuities, when not restricted in duration so as to comply with the permissible period under the rule.").

[32] *See, e.g.*, *Stuart Kingston, Inc.*, 596 A.2d at 1383 (noting public policy).

in a defeasible fee estate that which he would otherwise be prohibited from doing in a contract because the functional effect of the Buyback Provision is exactly the same regardless of the legal construct in which it exists.

The purpose of the Buyback Provision is clear: Heritage Homes may repurchase the Property for a fixed price upon the occurrence of the Construction Condition, but in no event is it required to do so. That is a textbook example of an option in real property[33] Thus, the proper reading of the Buyback Provision is that it creates a conditional option in real estate.[34] The Court must therefore consider the effect of the rule against perpetuities on the validity and enforceability of the Buyback Provision.

3. The Buyback Provision as an Option in Real Property Violates the Rule Against Perpetuities Because it is Unlimited in Duration

Having concluded that the Buyback Provision is an option and not a reversionary interest in the Property arising from a defeasible fee estate, the Court turns now to assess the Buyback Provision under the rule against perpetuities. "Options are regarded as having the effect of creating a future interest, depending upon the contingency of the exercise of the option. If it is possible that the option

[33] *See, e.g.*, *Central Del. County. Auth. v. Greyhound Corp.*, 588 A.2d 485, 488-89 (Pa. 1991) (looking to Section 394 of the Restatement and adopting its rationale where the deed provision could be construed either as a fee simple subject to a condition subsequent or as a conditional option to repurchase).

[34] This reading is also consistent with how a modern reader would understand the Buyback Provision. Given the choice between an arcane future interest and an option, a modern agreement of frequent use, it is difficult to accept that the parties intended to create any interest other than an option, especially in light of the express words that were chosen in this instance.

might not be exercised within the limits of the time allowed by the Rule against Perpetuities, the option is void."[35] This once well-settled principle of Delaware law has not fully withstood the test of time. In *Pathmark*,[36] an option held by a corporation could be exercised at any time during a period of thirty years. Notwithstanding that it was not required to be exercised within the period prescribed by the rule against perpetuities, the Court sustained the option as a reasonable commercial agreement between sophisticated parties. The Court, however, emphasized the limited duration of the option; indeed, it acknowledged that the Delaware Supreme Court "has implicitly determined [that] an unlimited time period is unreasonable."[37] *Pathmark* reflected this Court's effort to apply the rule against perpetuities to options in a nuanced fashion in circumstances in which the parties had agreed to a reasonable exercise period that otherwise would have violated the rule. Unlike Restatement (Third), it did not conclude that options are not subject to the rule.[38]

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[35] *Emerson v. Campbell*, 84 A.2d 148, 153 (Del. Ch. 1951).
[36] *Pathmark Stores, Inc. v. 3821 Assocs. L.P.*, 663 A.2d 1189 (Del. Ch. 1995).
[37] *Id.* at 1193.
[38] *See* RESTATEMENT (THIRD) PROPERTY: SERVITUDES § 3.3 (2000) ("The rule against perpetuities does not apply to servitudes or powers to create servitudes." The American Law Institute has defined "servitudes" to include options in real estate. *See id.* at cmt. a ("*Scope and Effect*. The rule stated in this section applies to options and rights of first refusal with respect to the purchase of land . . . ."). The Restatement (Third) focuses primarily on the reasonableness of an option as a restraint on the alienability of the burdened real estate. *Id.* § 3.4. Rather than summarily striking down an option of unlimited duration as violative of the rules against perpetuities and unreasonable restraints on alienation, however, the Restatement urges courts to adopt a more practical approach to implement the parties' intended agreement. Accordingly, the Restatement suggests that a court should seek to ascertain the shared intent of the parties, *id.*

The Buyback Provision is precisely the same option that was at issue in *Alexander*.[39] In that case, the Court held that the option violated the rule against perpetuities because it was unlimited in duration and otherwise rested in a corporation, an entity of perpetual existence. Heritage Homes argues that the Buyback Provision does not violate the rule because the option to repurchase must vest or fail within three years of settlement on the Property, the deadline by which the parties agreed that the Welshes would construct a home or else trigger Heritage Homes' right to repurchase the property. The future interest, however, that matters where an option is concerned is not necessarily the contingency of its ripening, but rather, and perhaps more importantly, the contingency of its exercise.

The Court agrees with Heritage Homes that the three year trigger on the Buyback Provision does not offend the rule. The right to exercise the option once triggered, however, still would be unlimited in duration; to be sure, there is nothing in the language of the Buyback Provision, the deed, or elsewhere in the Agreement

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§ 4.1, and then read into an option agreement a "reasonable" time for its duration, *id.* § 4.3(2).

Consistent with the modern view eschewing the draconian application of the rule against perpetuities to options in real estate, *Pathmark* signals this Court's willingness, in certain situations, to adopt a pragmatic approach. The Delaware Supreme Court, however, has not adopted the Restatement (Third)'s view that the rule against perpetuities never applies to options in real estate; as the *Pathmark* Court noted, an option of unlimited duration necessarily violates the rule under Delaware law, even under a more modern and flexible application. 663 A.2d at 1193. Thus, although parties are free to negotiate for an option in real estate that would endure for a period of time longer than that prescribed by the rule against perpetuities and although Delaware courts may uphold such options in certain circumstances, it is not for this Court under our existing law to craft a "reasonable duration" for an option where the parties failed to specify that term in their agreement.

[39] *See* 2005 WL 2173992, at *1.

that requires Heritage Homes to exercise the option within any fixed period of time. Moreover, as with the option at issue in *Alexander*, the Buyback Provision purports to bind the Welshes and their "heirs, executors, administrators, successors or assigns,"[40] and vests in Heritage Homes, a corporation with perpetual existence. Hence, it might continue forever. Accordingly, because there is no foreseeable horizon by which the option in the Buyback Provision must be exercised, "it is impossible to determine that this option might not be exercised, if at all, within the period prescribed by the rule against perpetuities."[41] Because an "unlimited time period" for the exercise of an option is unreasonable,[42] the Buyback Provision violates the rule and, thus, is void and unenforceable.[43]

C. *Is the Builder Tie-In Provision Enforceable?*

The Agreement contains a builder tie-in provision (the "Construction Agreement") whereby the Welshes purportedly agreed with Heritage Homes for the construction of a residence on the Property.[44] The Welshes contend that the Construction Agreement is exactly the same as the construction provision at issue

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[40] Agreement at ¶ 6.
[41] *Alexander* 2005 WL 2173992, at *2 (quotation omitted).
[42] *Pathmark*, 663 A.2d at 1193.
[43] The option period of thirty years in *Pathmark* was viewed as commercially reasonable. No purpose, reasonable or otherwise, for an option of indefinite duration has been identified by Heritage Homes.
[44] The terms of the Construction Agreement (paragraph 2 of the Agreement) are set forth *supra* in the text accompanying note 2. The Court struck down a similar agreement in *Alexander* because it found the builder tie-in provision to lack the essential and material terms of an agreement to construct a home, and so it was too vague to be enforced. *Alexander*, 2005 WL 2173992, at *3.

in *Alexander* and, as with that provision, is nothing more than a bare agreement to agree to a future contract governing the construction of their home. Specifically, they point out that the Construction Agreement lacks essential terms, such as the building plans and specifications and the price. Also, no time is specified for the parties to reach an agreement regarding the construction plans, and there is no timetable for completing construction.[45] Consequently, the Welshes argue that they are entitled to summary judgment on their claim for an injunction against enforcement of the Construction Agreement.

Heritage Homes argues that, unlike the situation in *Alexander* where only a few homes existed in Lexington Mill at the time the parties entered into their construction agreement, the Welshes had the benefit of a well-developed neighborhood with nearly thirty other homes to serve as examples for the design of their home.[46] Heritage Homes also claims to have provided the Welshes with the cost per square foot of several homes in the neighborhood, thereby providing a

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[45] The Court notes that Paragraph 3 of the Agreement might provide some guidance as to the timeframe involved here, given the parties' apparent understanding that construction would commence within three years. As discussed in the previous section, however, Paragraph 3 is unenforceable because it violates the Rule against Perpetuities, and, thus, it is excised from the parties' agreement. In any event, Paragraph 3 does not specify that the Welshes *must* construct a home within three years; rather, it simply states that the failure to begin construction within that time triggers the option to repurchase.

[46] Heritage Homes focuses its efforts on refuting the Welshes' claim that the Construction Agreement is vague and unenforceable. Heritage Homes has not contended that the Welshes failed to negotiate in good faith to implement the Construction Agreement in violation of the implied covenant of good faith and fair dealing. *See, e.g.*, *Dunlap v. State Farm Fire and Cas. Co.*, 878 A.2d 434, 441-42 (Del. 2005) (holding that the implied covenant of good faith and fair dealing "attaches to every contract.").

reasonable estimate of the cost of constructing the Welshes' home. In addition, the Court notes that Mrs. Welsh's sister had built a home in Lexington Mill; thus, there is a reasonable inference that the Welshes knew something about the nature of the community and Heritage Homes' construction effort.[47]

In *Alexander*, the Court concluded that this same contract term, with the same missing details, was "nothing more than a bare agreement to agree, one whose terms are so indefinite as to make the entire effort nugatory."[48] Heritage Homes has not presented a compelling argument for a different result here. The Court acknowledges that the Welshes may have had a better understanding of the construction parameters than the parties in *Alexander*, and, for purposes of this opinion, the Court will assume Heritage Homes' contention in that regard to be true. Thus, the Court will assume that the Welshes had reasonable knowledge regarding the general design of the homes in Lexington Mill, the general materials to be used in constructing a home in Lexington Mill, and a rough estimate of the cost per square foot for constructing a home in Lexington Mill. Nevertheless, the Construction Agreement still fails because it lacks essential terms and is too vague

[47] *See* Dep. of Donald Bloom pp. 33-34; Dep. of Michael A. Welsh pp. 22-23. *See also* Aff. of Donald Bloom ¶ 6 ("Mr. Welsh testified that the reason he and his wife wanted to move to Lexington Mill was because Amy Welsh's sister, Barbara Clendaniel, was builing a house in Lexington Mill. At the time the Welshes settled on the Property, the construction on the Clendaniel home had begun. The cost per square foot of the Clendaniel home was $115.02.").
[48] *Alexander*, 2005 WL 2173992, at *3.

to provide any reasonably objective controlling standards for determining a future agreement for the construction of the Welshes' home.

As with the builder tie-in agreement in *Alexander*, the Construction Agreement "does no more than merely memorialize the parties' intent to come to an agreement for the construction of a residence, leaving negotiation of all material terms for a later date."[49] As the Court stated in *Alexander*, "Delaware law requires that, 'to be enforceable, a contract to enter into a future contract must specify all its material and essential terms, and leave none to be agreed upon as the result of future negotiations . . . .'"[50] Construction of any home, much less a custom one, requires the parties to reach an agreement on numerous material and essential details beyond a general understanding that the home should be Colonial in style and have at least 1,500 square feet of living space. Thus, the Court concludes that the Construction Agreement is not enforceable, notwithstanding the Welshes' general knowledge regarding the style and cost of constructing a home in Lexington Mill.

Heritage Homes has submitted several photographs of other houses in Lexington Mill and argues that mere observation of those homes should have provided the Welshes with sufficient detail concerning the house Heritage Homes

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[49] *Id.*

[50] *Id.* (quoting *Raisler Sprinkler Co. v. Automatic Sprinkler Co. of Am.*, 171 A. 214, 219 (Del. Super. 1934)).

would construct for them.[51] The Court agrees with Heritage Homes that one can readily ascertain that the style of homes in Lexington Mill is colonial. Beyond that, however, the photographs actually confirm that the size and design of the homes vary from one house to the next. Moreover, there is nothing in the Construction Agreement that specifies whether the Welshes' home would be one particular model or another, what the materials would be, how many stories it would have, or whether it would be larger than the minimum size prescribed by the Declaration. Those are just a handful of examples, gleaned from the Court's review of the photographs, of the numerous "basic" (and essential) details one might consider in designing a home to be constructed in Lexington Mill.

Perhaps, most importantly, the Construction Agreement does not specify the essential term of price.[52] It may be true that Heritage Homes provided an estimate of the cost per square foot of other homes in Lexington Mill, including Mrs. Welsh's sister's home. But, in light of the wide variety of homes in Lexington Mill and the numerous details that go into constructing each (not to mention the normal variability in costs of material and labor), the cost per square foot of other homes in Lexington Mill is nothing more than a very rough guideline by which one might begin to estimate the cost of the Welshes' home. Without more specific

[51] Aff. of Donald Bloom Ex. A.
[52] *Alexander*, 2005 WL 2173992, at *2.

details as to the home to be built, however, a very rough estimate of the cost per square foot is not all that useful in terms of determining a definite price for *the Welshes' home* under the Construction Agreement.

In sum, the Court reaches the same conclusion regarding the sufficiency of the terms and the enforceability of the Construction Agreement that it reached in *Alexander* when it considered this same contract provision. "No reasonable person could find this provision a sufficient delineation of material terms, and, thus, it is not definite enough to be enforceable."[53] Accordingly, the Welshes are entitled to summary judgment and an injunction against the enforcement of the Construction Agreement.[54]

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[53] *Id.*

[54] This analysis assumes that Heritage Homes claims an independent right to enforce the Construction Agreement in the absence of an enforceable buyback provision. One could argue that the exclusive remedy for the Welshes' failure to build, as anticipated by the parties to the Agreement, was the return of the Property and, when that potential remedy failed because of the rule against perpetuities, that marked the end of the debate. With an enforceable buyback provision (one that probably would have been readily draftable with a limit on the duration of the option), Heritage Homes would have been able to reach its objective—Heritage Homes would either build the dwelling or regain the Property

None of this means that there cannot be enforceable "agreements to agree" or enforceable memoranda of understanding. *See, e.g.*, *PharmAthene v. SIGA Techs., Inc.*, 2008 WL 151855, at *13 (Del. Ch. Jan. 16, 2008). The critical inquiry is whether the material elements are provided or are readily ascertainable from an agreed upon source. Because of the build out of Lexington Mill, the sufficiency of the Construction Agreement here presents a closer question than in *Alexander* because a better understanding of the construction in the subdivision was readily available. The key terms, however, remain problematic here; they might have proved even more problematic if the Welshes were seeking to enforce what they had expected from Heritage Homes.

D. *Heritage Homes' Ability to Enforce the Declaration of Restrictions*

The Welshes argue that Heritage Homes rejected their plans and their builder in bad faith and, thus, should be denied the opportunity to enforce the Declaration. They rely primarily upon the equitable doctrine of unclean hands. Their motion for summary judgment with respect to this contention must be denied because the material facts are in dispute.[55] For example, Heritage Homes identified aesthetic and construction material shortcomings in the Welshes' proposal. In sum, there is no sufficient basis in the record for assessing the reasonableness or objectivity of Heritage Homes' conduct.

IV. CONCLUSION

For the foregoing reasons, the Welshes' Motion for Summary Judgment will be granted as to the Agreement's provisions regarding the buyback and the builder tie-in. Their motion as to Heritage Homes' enforcement of the Declaration will be denied. Counsel are requested to confer and to submit an implementing form of order.

[55] Moreover, the Declaration is not only for the benefit of Heritage Homes as the developer and Declarant, but it also serves to protect the other lot owners in Lexington Mill.