

## First Supplement to Memorandum 2009-25

### **Marketable Record Title: Notice of Option**

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Memorandum 2009-25 discusses the expiration of record notice of an option to purchase real property, pursuant to Civil Code Section 884.010.

Under Section 884.010 the expiration date for record notice of an option depends on whether the option itself has an expiration date:

884.010. If a recorded instrument creates or gives constructive notice of an option to purchase real property, the option expires of record if no conveyance, contract, or other instrument that gives notice of exercise or extends the option is recorded within the following times:

- (a) Six months after the option expires according to its terms.
- (b) If the option provides no expiration date, six months after the date the instrument that creates or gives constructive notice of the option is recorded.

Under subdivision (b), record notice of an open-ended option is only effective for six months. However, that period can be extended by recording a new notice before the expiration of the prior notice.

The need to extend the effect of record notice by recording a new notice every six months could be unreasonably burdensome, *if it is common for open-ended options to remain enforceable for longer periods of time*. If, on the other hand, it is common for such an option to be enforceable for only six months or less, then the six-month effective period shouldn't be a problem. Most option-holders would only need to record a single notice.

In discussing that issue, the staff indicated that it would try to determine whether there is any commonly accepted understanding of what constitutes a reasonable time to enforce an open-ended option to purchase real property. See Memorandum 2009-25, p. 4.

This supplement reports the result of that inquiry. Much of the research on this issue was conducted by Anne Shiau, a second year student at the King Hall School of Law at U.C. Davis. The staff greatly appreciates her assistance.

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Any California Law Revision Commission document referred to in this memorandum can be obtained from the Commission. Recent materials can be downloaded from the Commission's website ([www.clrc.ca.gov](http://www.clrc.ca.gov)). Other materials can be obtained by contacting the Commission's staff, through the website or otherwise.

## California Decisional Law

If an option has no expiration date, it can still become unenforceable through the passage of time. Such an option “must be exercised within a reasonable time, determined by the circumstances.” 1 B. Witkin, *Contracts* § 175, at 210 (10th ed. 2005). See also 54A Cal. Jur. 3d *Real Estate* § 750 (2009).

There are not many California appellate decisions discussing what amount of time is reasonable for the exercise of an open-ended option to purchase real property, and the facts in those cases vary so greatly that it is not possible to discern any reliable rule.

For example, in one case a 16-year delay in exercising an option was deemed reasonable. But the facts in that case were very unusual. The person granting the option was the option-holder’s trustee, and the court found that the trustee had misappropriated the option-holder’s money, leaving her with insufficient funds to exercise the option. *Hughes v. Heffner*, 29 Cal. App. 2d 382, 386-87, 84 P.2d 540 (1938).

In another case, the court found that 30 days was the reasonable period for enforcement of an open-ended option to purchase real property. Again, that decision was based on unusual facts. The original option to purchase had a 30-day time limit. That option had been extended a number of times, each time for an additional period of 30 days, with the same consideration paid by the option-holder. The final extension, for the same price, did not include a time limit. Nonetheless, based on the history of transactions between the parties, the court concluded that 30 days was the reasonable time for acceptance of that option. *Auslen v. Johnson*, 118 Cal. App. 2d 319, 321-22, 257 P.2d 664 (1953).

Obviously, outer boundaries of 16 years and 30 days do not provide much guidance. What they do demonstrate is the importance of the specific factual circumstances of the case in determining what is reasonable.

## National Decisional Law

Although the California cases on point are too few to provide the sort of rule of thumb that would be helpful in this study, there is some guidance to be gleaned from treatises that aggregate decisional law from all U.S. jurisdictions.

For example, the American Law Reports indicates that most states follow the same general rule regarding open-ended options:

Where the option is open-ended and does not specify a definite time of expiration, the courts have observed the rule that notice of

exercise of an option without a stated duration must be given within a reasonable time, and have focused their attention on just what constitutes a reasonable time under the circumstances.

87 A.L.R. 3d 805, § 2 (footnotes omitted).

The ALR emphasizes that these determinations typically turn on examination of the specific facts of the case, which can present a wide variety of different considerations:

The need to resolve this question has usually led the courts to examine the facts of the cases before them for situations that reflect favorably or unfavorably on the amount of time which actually elapsed between the time the option was given and the time it was exercised, such as the need of either party to perform acts preliminary to exercise, the optionor's responsibility for the delay in exercise, the parties' previous dealings with respect to the transaction at issue, a substantial increase in the market value of the subject property prior to exercise, the susceptibility of the subject property to sharp fluctuation in value, the optionee's practical construction of the option, the optionee's request for less time than in fact had elapsed prior to exercise, the optionee's failure diligently to perform an act prerequisite to exercise, the optionee's default in a major covenant under the option agreement, the optionee's long delay following a request by the optionor that the former exercise the option, the optionee's request for the option in the first place, the optionee's speculative purpose in acquiring the option, the optionor's substantial improvement of the subject property prior to exercise, the optionor's poor financial condition, the optionor's carrying of the risk of loss of the subject property prior to exercise, the apparent decision by either party or both parties to abandon the option, and the existence of long-standing rights in the subject property of parties unconnected with the transaction at issue.

*Id.*

Despite the heavy fact-dependency of the question, ALR's survey of reported cases identifies a strong trend:

[The] courts have unmistakably tended to uphold as reasonable time intervals of less than six months and to characterize as unreasonable time intervals of six months or more. Irrespective of the circumstances involved, the number of cases in which intervals of less than a half-year were found to be unreasonable have been disproportionately few, as have, by an even more impressive ratio, the number of cases in which longer intervals were held to be reasonable.

*Id.* See also 60 Am. Jur. Proof of Facts 3d 255, § 16 (2008) (“courts have shown an unmistakable tendency to uphold as reasonable nearly all intervals of less than six months and to find unreasonable nearly all intervals of six months or more, regardless of the factual circumstances on which the various rulings were based.”)

## **Conclusion**

The question of whether a given period of time for exercise of an option to purchase real property is reasonable is heavily dependent on the specific facts surrounding the option. Nonetheless, the national case law treatises have identified a strong tendency to find periods of up to six months reasonable, and periods of more than six months unreasonable.

To the extent that tendency holds true in California, it suggests that the six-month effective period for record notice of an open-ended option to purchase real property is appropriate. That national trend suggests that there should not be many cases in which an option-holder would need to extend the effective period of record notice of an open-ended option.

However, if it would make sense to provide a six-month grace period *after* expiration of an open-ended option (as is the rule under Section 884.010(a)), in order to give some leeway for recordation of notice of the exercise of the option, the six-month period in Section 884.010(b) could be extended to one year.

**The staff is inclined against that option.** It doesn’t appear that the existing six-month period has been causing any problems, and the staff is concerned that using two different time periods in Section 884.010 could be confusing. **We would stick with the existing six-month period for record notice of an open-ended option.**

Respectfully submitted,

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