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CLARIFYING THE NATURE OF LOUISIANA'S RIGHT OF FIRST REFUSAL IN THE TRANSFER OF IMMOVABLES

Introduction

A right of first refusal¹ is "a right to buy before or ahead of [an]other; . . . thus, [the contract gives] to the prospective purchaser the right to buy upon specified terms, but, and this is the important point, only if the seller decides to sell."² Although this right in certain ways resembles an option, there are at least two grounds on which the two types of contracts clearly may be distinguished. First, unlike an option, the right of first refusal "does not give the pre-emptioner the power to compel an unwilling owner to sell."³ Second, an option requires a stipulated time period for its exercise, and a right of first refusal does not. Despite the clear differences between these two contracts, Louisiana courts have had difficulty in drawing the distinction. This article will further explore that distinction in the context of the sale of immovable property.

First, the inapplicability of the rules pertaining to options to a right of first refusal will be analyzed. Second, some characteristics of Louisiana's right of first refusal will be considered. Finally, the jurisprudence classifying the right of first refusal as an option will be scrutinized.

Distinguishing Between a Right of First Refusal and an Option

First of all it should be noted that the confusion in the jurisprudence has not been over the enforceability of these contracts, but rather over their characterization.⁴ Professor Litvinoff's statement in his *Civil Law Treatise on Obligations* that "the enforceability of a *pacte de préférence* is unquestionable"⁵ is the prevailing view in Louisiana.⁶ The problem is that the Louisiana courts at times have incorrectly characterized the

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1. The right of first refusal is also known as a right of pre-emption or a *pacte de préférence*.

2. 40 ALR 3d 920, 924.

3. *Id.*

4. *Keene v. Williams*, 423 So. 2d 1065 (La. 1983); *Crawford v. Deshotels*, 359 So. 2d 118 (La. 1978); *Price v. Town of Ruston*, 171 La. 935, 132 So. 653 (1931).

5. 2 S. Litvinoff, *Obligations* § 104, at 188, in 7 *Louisiana Civil Law Treatise* (1975).

6. *Keene*, 423 So. 2d 1065; *Crawford*, 359 So. 2d 118; *Price*, 171 La. 935, 132 So. 653.

right of first refusal in the transfer of immovable property as an option,⁷ and at other times held that the right of first refusal is not an option.⁸

Louisiana Civil Code article 2462 governs option contracts involving the sale of immovable property. Specifically, the second paragraph addresses unilateral promises:⁹

One may purchase the right, or option to accept or reject, within a stipulated time, an offer or promise to sell, after the purchase of such option, for any consideration therein stipulated, such offer, or promise can not be withdrawn before the time agreed upon; and should it be accepted within the time stipulated, the contract or agreement to sell, evidenced by such promise and acceptance, may be specifically enforced by either party.¹⁰

Apparently, since a right of first refusal resembles an option, in that both allow one party to purchase a particular thing from another party at some point in the future, and since both are unilateral promises, the courts have struggled to apply the second paragraph of article 2462 to rights of first refusal. The difficulty in applying those provisions to rights of first refusal stems from the difference between the two contracts. A key characteristic of an option is a continuing obligation to sell if the option-holder accepts within the stipulated time. In a right of first refusal, however, the owner of the property is under no obligation whatsoever to offer the property to the holder of the right. Indeed, the property owner may decide never to sell the property. Further, it has been said that "[t]he distinction is clear in that a [right of first refusal] does not confer on the holder the power to compel an unwilling owner to sell, while an option does grant such power to the optionee."¹¹ Consequently, there is no "continuing right or option to accept (or reject) an extant offer or promise to sell - as contemplated by article 2462."¹²

Moreover, under Louisiana law an option contract must contain a "stipulated time" within which the option must be exercised, or the contract is void as against public policy.¹³ Problems arise when the

7. *Price*, 132 So. at 656.

8. *Crawford*, 359 So. at 122.

9. 2 S. Litvinoff, *Obligations* § 107, at 193, in 7 *Louisiana Civil Law Treatise* (1975).

10. La. Civ. Code art. 2462.

11. Boyer and Spriegel, *Land Use Control: Pre-Emptions, Perpetuities and Similar Restrictions*, 20 *U. Miami L. Rev.* 148, 154 (1965).

12. *Crawford*, 359 So. 2d at 122.

13. La. Civ. Code art. 2462. The policy is one against holding property out of commerce. Since an option of unlimited duration could perpetually deprive the owner of the right to alienate his property, such agreements are invalid as contrary to public policy. See *Delcambre v. Dubois*, 262 So. 2d 96 (La. App. 3d Cir. 1972); *Clark v. Dixon*, 254 So. 2d 482 (La. App. 3d Cir. 1971).

courts attempt to apply the "stipulated time" requirement of article 2462 to rights of first refusal. Rights of first refusal involve not one, but two time periods: the time between the formation of the contract and the point at which the owner manifests his desire to sell; and the time after the owner's offer to sell during which the holder must decide whether or not to accept. Although the second time period more closely resembles that involved in a option contract, the courts have favored applying the "stipulated time" requirement to the first time period.¹⁴ In *Price v. Town of Ruston*,¹⁵ for example, the Louisiana Supreme Court applied the "stipulated time" requirement to a first refusal clause, stating: "The stipulation limiting the time was that the option would be available whenever the [owner] might desire to sell the property"¹⁶

Since the owner who has granted a right of first refusal may never decide to sell, for Louisiana Civil Code article 2462 to apply, it must contemplate a point in time that commences upon the decision of one of the parties only. Because that article clearly does not contemplate such a time period, it appears that the court in *Price* misapplied it. Nevertheless, the court's decision is still consistent with the policy behind article 2462.¹⁸ Since the owner may sell the property at any time he desires, the contract does not take property out of commerce, and the reason for the "stipulated time" requirement is satisfied.

Justice Dixon in his concurrence in *Crawford v. Deshotels*,¹⁹ took the position that the "point in time" analysis does not fairly interpret 2462:

C.C. 2462 clearly contemplates that an option will be for only a "stipulated time," which I take to mean a time certain - a day on the calendar or a day on which it is contemplated that an event will occur which is *not* within the control of the person granting the option.²⁰

14. *Keene*, 433 So. 2d at 1069; *Price*, 132 So. at 656.

15. 171 La. 935, 132 So. 653 (1931).

16. *Id.* at 656.

17. *Id.*

18. See *supra* note 13.

19. 359 So. 2d 118 (La. 1978).

20. *Id.* at 123 (Dixon, J., concurring). Indeed, *Delcambre v. Dubois*, 262 So. 2d 96 (La. App. 3d Cir. 1972), supports Justice Dixon's view. In *Delcambre*, the plaintiff sought specific performance under a contract granting him the right to re-purchase land from the defendant. On original hearing the court invalidated the option as failing the "stipulated time" requirement. While the court said that "the time of an option could be until the occurrence of an event," when the occurrence of the event is entirely dependent on the optionholder's future conduct the event is uncertain and violates the "stipulated time" requirement.

While Justice Dixon's interpretation is arguably correct from both a textual and a policy standpoint when applied to options, it does not comport with the policy behind article 2462 when applied to a first refusal. This is so because that view would strike down a right of first refusal although it does not unreasonably restrict the alienation of property, since the owner may sell at any time. The tension between an appropriate literal application of article 2462 and fostering its policy could be avoided by finding that, since a right of first refusal is not an option, article 2462 simply does not apply. Moreover, the courts may still be faithful to the Civil Code, by holding that a right of first refusal is a valid innominate contract under Louisiana Civil Code article 1914.²¹

Characteristics of the Right of First Refusal

After concluding that a right of first refusal is not an option under article 2462, but rather a valid innominate contract, some additional characteristics of Louisiana's right of first refusal in the context of a transfer of immovable property may be analyzed.

The basic structure of a first refusal contract is that "one of the parties obligates himself to give the first choice to the other if he ever decides to sell his property."²² Thus, a first refusal is "a conditional promise of sale," the condition being "the owner's desire to sell."²³ This condition is not null even though it rests with the obligor.²⁴ Thus, initially neither party is really obligated to *do* anything, but rather the owner has a negative duty—that is, he may not sell the property without first offering it to the holder. The holder has no vested rights until the property is offered to him; until then the right is merely contingent. However, the complexion of the contract changes when the owner decides to sell the property and offers it to the holder. At this point the contract resembles an option. Once the offer is made, "the holder of the pre-emption does have the sole option to purchase and can compel the owner to convey or reconvey by an action for specific performance."²⁵ This leads to the problem presented by the time period within which the holder may accept or reject the offer.

Once the complexion of the contract changes, the obvious concern is whether the absence of a specified time for the holder to accept

21. La. Civ. Code Art. 1914: "Nominate contracts are those given a special designation such as sale, lease, loan or insurance. Innominate contracts are those with no special designation."

22. See Boyer and Spriegel, *supra* note 11, at 154.

23. See *id.* at 155.

24. See text accompanying *supra* note 5.

25. See Boyer and Spriegel, *supra* note 11, at 155.

invalidates the contract under article 2462 as an option in perpetuity. *Keene v. Williams*²⁶ addressed this issue and held that the failure to specify a time was not fatal to the contract, since "there was in the agreement an implied condition that Keene would be given a *reasonable amount of time* under the circumstances to either accept or reject the offer."²⁷

The idea of implying a reasonable period of time for the exercise of an option which fails to state a period of time is not new in Louisiana.²⁸ Further, it has been said that "[s]uch a conclusion would allow attainment of the same policy objectives but without overlooking the parties' intent."²⁹

Another interesting attribute of a right of first refusal is the application of the ten year liberative prescription period established in Louisiana Civil Code article 3447.³⁰ In *Roubichaux v. Boutte*,³¹ the court upheld a right of first refusal against an argument that the holders of the right "had 10 years within which to exercise their right of first refusal."³² Relying on the rule that "[f]or liberative prescription to be operative, a right or cause of action must exist in order for prescription to run,"³³ the court concluded that the right of action does not accrue and prescription does not begin to run until the owner decides to sell.

The Jurisprudence Concerning Rights of First Refusal

There are only three Louisiana Supreme Court cases concerning the characterization of a right of first refusal.³⁴ The earliest case on point is *Price v. Town of Ruston*,³⁵ in which Mrs. Price agreed to allow the Elks' Lodge to construct a third story on a building that she owned. The contract included a right of first refusal in favor of Mrs. Price. The court upheld the contract as an option against an argument that it was invalid because it contained no stipulated time within which it was to be exercised.³⁶

26. 423 So. 2d 1065 (La. 1983).

27. *Id.* at 1069, 1070.

28. This issue is explored in Note, *The Requirement of a Definite Time Period in Option Contracts*, 34 La. L. Rev. 668 (1974).

29. 2 S. Litvinoff, *Obligations* § 104, at 108 (Supp. 1979).

30. La. Civ. Code art. 3447: "Liberative prescription is a mode of barring of actions as a result of inaction for a period of time."

31. 492 So. 2d 521 (La. App. 3d Cir. 1986). See also *Terrell v. Messenger*, 428 So. 2d 1241, 1246 (La. App. 3d Cir. 1983), writ denied, 433 So. 2d 709 (La. 1983).

32. *Robichaux*, 492 So. 2d at 527.

33. *Id.*

34. *Keene v. Williams*, 423 So. 2d 1065 (La. 1983); *Crawford v. Deshotels*, 359 So. 2d 118 (La. 1978); *Price v. Town of Ruston*, 171 La. 935, 132 So. 653 (1931).

35. 171 La. 935, 132 So. 653.

36. *Price*, 132 So. at 656.

In *Crawford v. Deshotels*,³⁷ McDaniel conveyed half of her interest in certain immovable property to Crawford under an agreement stating that "should [McDaniel] desire to sell [her remaining one half interest] . . . [she] is herein obligated to offer to [Crawford] the first chance to buy."³⁸ The court rejected the contention that the contract was an invalid option:

The article [2462] and the jurisprudence on which relator relies, however, are not applicable here, for there is not here following "the purchase of such option" - or in this case entry of the contract - a continuing right or option to accept (or reject) an extant offer or promise to sell - as contemplated by Article 2462. Rather there is here what is more commonly described as a right of first refusal, or as the contract says, a right to be afforded a "first chance to buy" at a price equal to any bona fide offer which McDaniel should receive and be interested in accepting. Thus, the stipulated time requirement of Article 2462 is not applicable.³⁹

In other words, the court correctly distinguished a right of first refusal from an option and accurately set forth why Civil Code article 2462 does not apply. However, the court contradicted itself in the next paragraph by citing with approval *Price* and the language in that case which assumes that a right of first refusal is a valid option with a stipulated time.⁴⁰ The court then concluded that both of these reasons supported the validity of the contract. Clearly the two theories are mutually exclusive.

The most recent Supreme Court case on the subject is *Keene*.⁴¹ The court cited *Crawford* for the proposition that the "right of first refusal was valid under La.C.C. Art. 2462 which requires that an option have a stipulated time within which it must be accepted or rejected."⁴² It is particularly interesting that the court went out of its way to make clear its reliance on La. Civ. Code Art. 2462, since the court of appeals expressly held that article 2462 did not apply.⁴³

The first circuit literally applied *Keene* in *Travis v. Heirs of Felker*,⁴⁴ by upholding a right of first refusal as a valid option. In *Travis*, the court stated: "The Supreme Court has held the right of first refusal

37. 359 So. 2d 118.

38. *Crawford*, 359 So. 2d at 122.

39. *Id.*

40. *Id.*

41. 423 So. 2d 1065.

42. *Keene*, 423 So. 2d at 1069, n.2.

43. *Keene v. Williams*, 412 So. 2d 202, 205 (La. App. 3d Cir. 1982).

44. 482 So. 2d 5 (La. App. 1st Cir. 1985).

enforceable as an option under article 2462 of the Civil Code despite arguments that it states no specified time and that it is contrary to public policy because it is a perpetual option."⁴⁵ The court cited the trilogy of Supreme Court cases on the subject in support of this proposition.⁴⁵ Although the court's classification of the contract as an option was erroneous, the confusion is understandable.

Conclusion

The Louisiana courts have struggled to find codal authority for a right of first refusal and in so doing have erroneously classified it as an option under article 2462. The Supreme Court's statements in *Crawford* that a right of first refusal is not an option within the meaning of article 2462 remain the most accurate expression in the Louisiana jurisprudence of the distinction between the two contracts. The next step in clarifying the precise nature of the right of first refusal is to realize that its proper classification in the Civil Code is that of an innominate contract. This characterization will avoid the necessity of making strained interpretations of the "stipulated time" requirement of article 2462 when the danger the rule is designed to guard against is not present.

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45. *Id.* at 6.

