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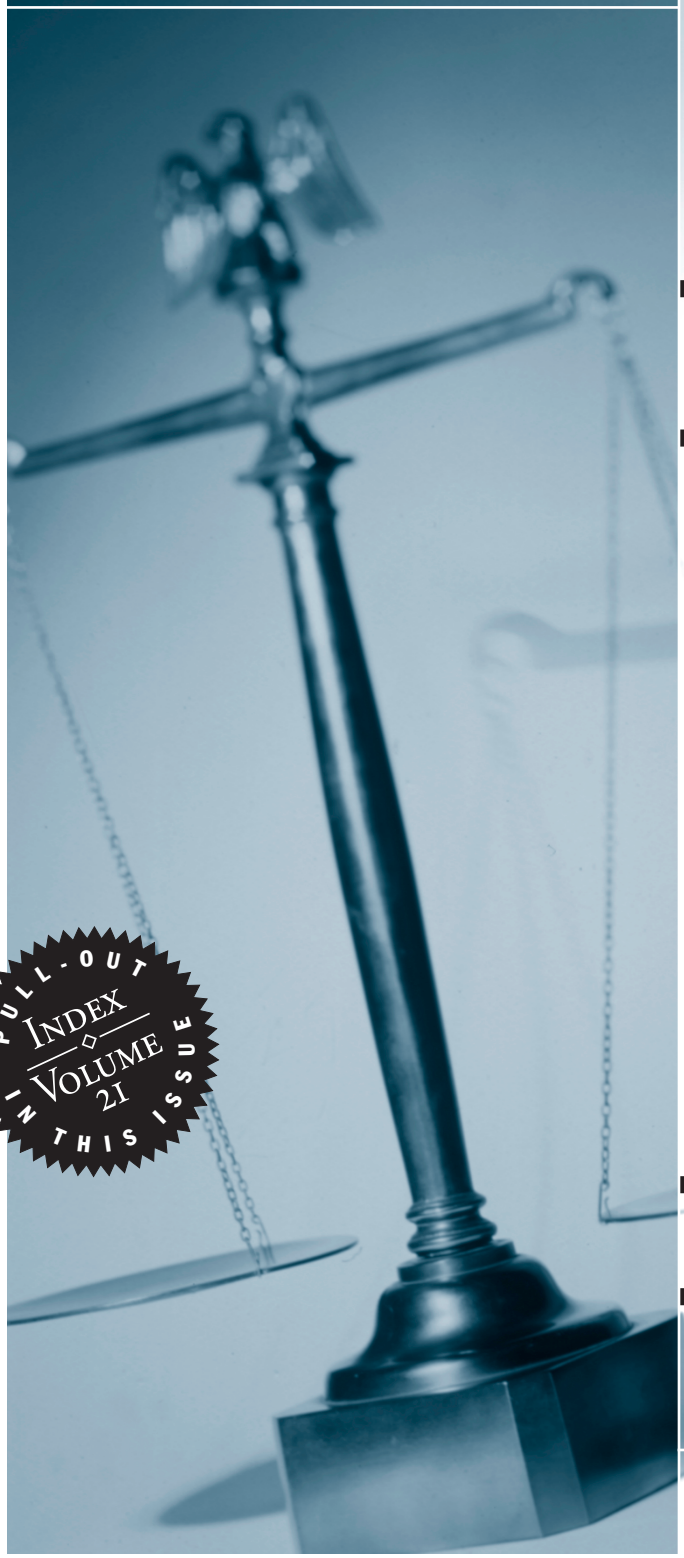

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Pitfalls of Incorporation by Reference in Sublease of Prime Lease Terms

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Subleases often contain the basic economic terms between the sublandlord and the subtenant and incorporate by reference the terms and conditions of the prime lease. Phrases such as "the subtenant agrees to perform all of the obligations of the sublandlord as 'tenant' under the prime lease" or "this sublease is subject to the terms and conditions of the prime lease" are commonly used to accomplish the incorporation of the prime lease terms. This practice is necessary because the subtenant is occupying the premises under, and subject to, the terms of the prime lease, and the sublandlord must require the subtenant to comply with the terms of the prime lease to prevent a default for which the sublandlord will be liable. Incorporation of the prime lease terms by reference also seems like a practical approach because it eliminates the need to restate in the sublease many "boilerplate" provisions already contained in the prime lease.

However, practitioners should be aware of the pitfalls of incorporation of prime lease terms by reference. Incorporation should not be a substitute for carefully reviewing each provision of the prime lease for the purpose of determining which provisions (or portions thereof) properly apply to the sublease transaction. Also, courts may not enforce waivers of certain legal rights by the subtenant if such waivers are contained in provisions of the prime lease that are incorporated into the sublease by reference.

A recent federal court case demonstrates that courts may decline to enforce sublease provisions containing waivers of important legal rights in cases where such provisions are not fully set forth in the sublease document, even though the prime lease provisions are incorporated into the sublease by reference. In *Urban Outfitters, Inc.* v. *166 Enterprise Corp.* and *IG Second Generation Partners, L.P.,* 2001 U.S. Dist. LEXIS 3646 (S.D.N.Y. 2001), the U.S. District Court in the Southern District of New York held that general incorporation language in a sublease does not include the original landlord/tenant agreement to waive the right to a jury trial in the event of litigation.

In *Urban Outfitters,* the plaintiff subtenant brought suit against the defendant prime landlord and defendant/sublandlord, arguing that the defendants breached various agreements between the parties by providing the plaintiff subtenant with commercial property that was unsuitable for the plaintiff's purposes. The plaintiff subtenant made jury demands for all issues triable by a jury. The defendants moved to strike the request for a jury trial on the grounds that such waiver of jury trial was included in the prime lease and all of the terms of the prime lease were incorporated by reference into the sublease.

The prime lease contained a fairly typical clause in which the tenant agreed to waive its right to trial by jury for matters arising under the prime lease. The sublease subsequently entered into by the plaintiff subtenant and defendant tenant/sublandlord provided in part that "This sublease is subject to all of the terms, covenants and provisions contained in the Prime Lease."

The court reasoned that jury waiver clauses must be construed strictly, as the right to a jury trial is a fundamental and protected right under the Seventh Amendment. Such a right can only be waived knowingly and intentionally, and such a waiver is not lightly inferred or extended. The court relied on *Cantor* v. *Techlease,* 59 A.2d 699 (N.Y. App. Div. 1977), in which the subtenant agreed only to a general incorporation of the prime lease terms agreed upon by the original tenant and its landlord. The *Cantor* court, in holding that the jury waiver in the prime lease was ineffective against the subtenant, made particular note that the prime lease agreement "provided only the that 'lessor and lessee' waived a jury trial in any action 'by either of them against the other.' " The *Cantor* court found that the general incorporation of these terms was insufficient to support the inference that the plaintiff subtenant had voluntarily waived its fundamental right to a jury trial.

Courts have also routinely held that warrants of attorney, in order to be enforceable, must be signed by the party against whom the warrant is being used. Executing a subsequent document in which a party assumes all of the obligations of another is not sufficient to permit enforcement of a warrant of attorney. See, e.g., *Wolf* v. *Gaines,* 179 N.E.2d 466 (Ill. App. Ct. 1961), in which the Illinois Court of Appeals held that a landlord could not utilize a warrant of attorney to confess judg-

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ment against the guarantor of a lease, when the guarantor did not sign the lease containing such warrant; see also *Frantz Tractor Co.* v. *Wyoming Valley Nursery,* 120 A.2d 303 (Pa. 1956), in which the Pennsylvania Supreme Court stated that a warrant of attorney to confess judgment must be self-sustaining; in order to be self-sustaining, it must be in writing and signed by the person to be bound by it, and the requisite signature must bear a direct relationship to the warrant and may not be applied extrinsically or imputed from an assignment of the instrument containing the warrant.

As *Urban Outfitters* and the other cases mentioned above demonstrate, courts may refuse to enforce waivers of important legal rights by subtenants unless those waivers are clearly made by subtenants in the sublease agreement. However, because subleases generally do not create privity between a prime landlord and a subtenant, such waivers may not be as effective as those between subtenants and prime landlord absent a joinder of the prime landlord in the sublease or a separate agreement between the subtenant and prime landlord (such as a consent and attornment agreement). Prime landlords who do not want to be in privity of contract with a subtenant but want the benefit of subtenant waivers should, at a minimum, require that the waivers made by the subtenants in the sublease be made for the benefit of the prime landlord as well as the sublandlord.

Another Illinois state court case demonstrates the confusion and misunderstanding that may arise when prime lease terms are incorporated into a sublease by reference using imprecise drafting and without a careful review of the applicability of the prime lease terms *vis-à-vis* the sublease parties.

In *Wright* v. *Mr. Quick, Inc.,* 472 N.E.2d 478 (Ill. App. Ct. 1984), the Illinois Court of Appeals, in reversing the trial court, held that, despite incorporation language which obligated the subtenant to be bound by the terms and conditions of the prime lease, but which did not obligate the tenant to maintain responsibility for repairs to the premises, the tenant sublandlord owed a duty to repair to a third party. The Supreme Court of Illinois reversed this decision in *Wright* v. *Mr. Quick, Inc.,* 486 N.E.2d 908 (Ill. 1985). In so doing, the Supreme Court of Illinois held, in relevant part, that the provisions in the sublease—providing that (1) the subtenant agreed to be bound by the terms and conditions of the prime lease and (2) the sublease is "subject to" the terms of the prime lease—did not constitute an incorporation of the provision of the prime lease that the tenant/sublandlord would maintain the premises where the sublease incorporated the terms and conditions of a store franchise agreement between the sublandlord and subtenant under which the subtenant assumed the duty to repair.

The plaintiff in *Wright* fell in the parking lot of her employer (the subtenant), who operated a fast food restaurant pursuant to a franchise agreement and sublease with the defendant sublandlord. The plaintiff was barred from bringing an action against her employer because her exclusive remedy against her employer was provided under the Workers' Compensation Act. She filed suit against the sublandlord on the basis that the sublandlord defendant owed a duty in tort to a person on the property as a result of incorporation language in the sublease. The incorporation language in the sublease read "Sublessee agrees *to abide by* and *be bound by* the terms and conditions of the lease above referred to, except insofar as its terms are changed and modified by this agreement?" Further, the sublease stated that it is subject to the terms and conditions of the prime lease.

In rejecting the plaintiff's arguments and reversing the court of appeals, the Supreme Court of Illinois stated that the general incorporation does not manifest an intention to incorporate the defendant's sublandlord's duty to repair as a covenant in the sublease. Such incorporation language was not in fact directed at the sublandlord and it does not extend any covenants to the sublandlord. The court reasoned that the terms "be bound by" and "abide by" indicate the parties' intention to place responsibilities on the subtenant and not to create rights in its favor. The court further stated that the incorporation language only bound the subtenant to the rights and obligations of the tenant under the prime lease. In addition, the court adopted the *Black's Law Dictionary* definition and held that the term "subject to" meant "subordinate, subservient, inferior to; governed or affected by." Thus, the sublease was subordinate to the prime lease in that the sublease could not conflict with the prime lease and could not extend beyond the term of the prime lease. Because the prime lease did not address the duty to repair as between the sublandlord and subtenant, the "subject to" language was irrelevant.

As is evident from the different decisions reached in this case by the various Illinois courts, drafters of subleases need to make sure that references in the prime lease to the landlord will constitute references to the sublandlord and that the references to the tenant will constitute references to the subtenant. It is imperative to set forth specifically which obligations under the prime lease are to remain obligations of the prime landlord and which are to be passed through to the sublandlord. Further, practitioners must not rely on general incorporation language to enforce waivers against the subtenant. Instead, practitioners should specifically set forth warrants of attorney and waivers of jury trial in the sublease. Otherwise, courts are likely to hold that such provisions are not incorporated into the sublease and are thus unenforceable against the subtenant.

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Designation Rights: A New Twist on an Old Impairment of Landlord's Rights in Bankruptcy Cases

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A significant power granted to debtors in bankruptcy cases is the ability to assume unexpired leases that benefit the estate and reject those that do not. If a lease is assumed, a debtor

may also assign the lease to a third party in exchange for the bonus value[1] of the lease. The power to assume and/or assign a lease gives a debtor flexibility in managing the estate, as leasehold interests may prove to be the most valuable assets in a bankruptcy case.[2]

A recent trend has developed in bankruptcy practice whereby a company attempts to create value for creditors through the sale of the right to direct the assumption or rejection of a lease, a so-called "designation right." A designation right can be best described as the exclusive right to determine whether a lease will be assumed or rejected by a debtor during a fixed period of time and to designate the assignee if the lease is assumed. The sale of designation rights has become prevalent in bankruptcy cases of large retailers who have determined to close a group of unprofitable locations.[3] These types of sales have gained acceptance because the process enables a debtor to maximize the value of its leasehold interests while eliminating potential risks. The sale of designation rights, however, contains many pitfalls for landlords, and may leave them in the unenviable position of permitting real estate speculators, rather than bankrupt tenants, to determine the fate of their property.

The Statutory Framework for the Assumption and Assignment of Leases

Recognizing the adverse impact of assumption and assignment of non-residential real property leases on landlords, Section 365 (b) of the Bankruptcy Code provides specific limitations on a debtor's right to assume or reject a lease. Prior to the assumption of a lease, the debtor must: (1) cure or provide "adequate assurance"[4] that it will promptly cure the default; (2) compensate or provide adequate assurance of prompt future compensation for actual pecuniary loss resulting from the default; and (3) provide adequate assurance of future performance under the lease. Further, in the case of shopping center leases, the Bankruptcy Code provides specific criteria to determine what constitutes "adequate assurance of future performance." In shopping center leases the debtor must provide adequate assurance:

> (A) of the source of rent and other consideration due under such lease, and in the case of an assignment, that the financial condition and operating performance of the proposed assignee ... shall be similar to [that of] the debtor as of the time the Debtor became the lessee under the lease;
> (B) that any percentage rent due ... will not decline substantially;
> (C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in any other [agreement] relating to such shopping center; and
> (D) that assumption or assignment ... will not disrupt any tenant mix or balance....

11 U.S.C. § 365(b)(3) (2001).

Another protection for landlords is the Bankruptcy Code's requirement that a debtor decide within 60 days of the commencement of the bankruptcy case whether to assume or reject a lease. 11 U.S.C. § 365(d)(4) (2001). The deadline may be extended by the Bankruptcy Court for cause shown. This component of the Bankruptcy Code was designed to protect owners of shopping centers from vacancies during the potentially lengthy period that debtor tenants of these centers took to decide whether to assume or reject their store leases. The protection afforded by this provision is frequently dismissed by large retailers, because courts ordinarily extend the deadline in those cases.[5]

How and When Designation Rights Arise

The sale of designation rights usually occurs in bankruptcy cases involving a large number of retail locations because, in such cases, a debtor is faced with the daunting task of marketing numerous leases in a short period of time. Ordinarily, and prior to the practice of selling designation rights, the debtor would attempt to market and sell the leases to a variety of end users in a process that could stretch out for many months. The debtor would continue to incur the carrying costs related to each lease throughout the sale process while facing the risk that one or more of the transactions might not close.

However, if the debtor-retailer chose to market and sell the designation rights, rather than the leases themselves, many of the carrying costs would be eliminated and the risks inherent to closing multiple transactions would be minimized. The debtor would thereby close one transaction affecting multiple locations with the purchaser of the designation rights and would receive the proceeds of that sale expeditiously. In essence, the sale of designation rights creates a one-stop shopping environment for the sale and purchase of a multitude of leasehold interests.

Sales of designation rights have, to date, only been employed in a small number of retail cases and the legitimacy of the right to transfer designation rights has not been squarely addressed by any court in a published opinion. Thus far, the only published opinion relating to the sale of designation rights is the case of *In re Ernst Home Center, Inc.*, 209 B.R. 974 (Bankr. W.D.Wash. 1997). Ernst Home Center was a leading home improvement retailer in the Northwestern United States and maintained over 80 retail locations at the inception of its bankruptcy case. During the pendency of the bankruptcy case, Ernst determined that it could no longer operate profitably and that an orderly liquidation was in the best interests of all interested parties. One of Ernst's most significant assets was its interest in its retail leases. However, the carrying costs for the group of leases was approximately $1.6 million per month and the retention of the leases for a protracted period would erode the value of the leases. Faced with these difficulties, Ernst negotiated a transaction with FADCO, LLC, in which Ernst agreed to sell to FADCO 3 fee interests and 59 leasehold interests. During a 14-month term, FADCO had the right to direct Ernst to assume and assign the leases to parties designated by FADCO and the right to direct Ernst to reject any lease. The transaction provided a guaranteed purchase price of $12 million to Ernst while eliminating any further losses due to carrying costs. The bankruptcy court approved the transaction finding that it was in the best interest of Ernst and its creditor body.

A group of landlords in *Ernst Home Center* appealed the bankruptcy court's order to the Ninth Circuit Bankruptcy Appellate Panel. Although the Appellate Panel determined that the appeal was moot, as the landlords failed to obtain a stay pending appeal, one judge wrote a concurring opinion that sheds some light on the legal issues surrounding designation rights. The concurring opinion found that the value of leasehold interests should be included in a bankruptcy estate and that a debtor has an ability to sell such an asset. Although not dispositive of the legitimacy of designation rights, at least the judge apparently opined that the process had credibility.

How to Attack Designation Rights

When the use of designation rights is employed in a bankruptcy case, a landlord is faced with the difficult prospect of attempting to persuade a bankruptcy court to reject a process that might generate millions of dollars for the creditor body and which may constitute the bulk of the recovery available to creditors. Although the landlord's rights are directly implicated by the sale of the designation rights, the momentum of approving a sale will be difficult to overcome. Despite the uphill battle, there appear to be several arguments which may convince a court that designation rights should not be employed.

The most basic attack on designation rights is an argument based on statutory construction. The Bankruptcy Code specifically states that a "trustee" is empowered to assume or reject a lease. However, when designation rights are implicated, the real party assuming and assigning the lease is the party who purchased the designation rights, not the trustee. Faced with an issue of statutory construction of the Bankruptcy Code, the U.S. Supreme Court, in the case of *Hartford Underwriters Insurance Co.* v. *Union Planters Bank,* N.A., ____ U.S. ____, 120 S.Ct. 1942 (2000), considered whether certain powers granted exclusively to a trustee in bankruptcy could be utilized by creditors in bankruptcy cases. The Supreme Court applied the plain meaning rule of statutory interpretation and concluded that the provision of the Bankruptcy Code at issue should be interpreted to empower only a trustee and not a third party to utilize a right created by Congress for the benefit of a trustee. The holding of *Hartford Underwriters* is directly applicable when analyzing designation rights, as it is contrary to the plain meaning of the Bankruptcy Code to interpret it to allow a third party to benefit from a right enacted for a trustee.

A related argument can also be advanced that the sale of designation rights offends traditional bankruptcy public policy principles by authorizing the sale of rights which are specifically granted to a debtor or trustee. It could be argued that authorizing the sale of special bankruptcy rights creates a dangerous precedent that might lead debtors to attempt to sell other debtor protections afforded by the Bankruptcy Code including the automatic stay (a cardinal principle of the Bankruptcy Code) or the ability to obtain financing over the objection of a prior secured creditor.

Another way to counter the use of designation rights is to limit the time the purchaser has to direct the assumption or rejection. As noted above, the Bankruptcy Court affixes a 60-day time period for the assumption and assignment of leases. The sale of designation rights will ordinarily require the debtor to file for an extension of its time to assume or reject. Landlords should oppose an extension and argue that the extension of the right should not be utilized to benefit a person who has no direct stake in the bankruptcy case. Similar to the arguments relating to the use of designation rights, a court should not extend the time to assume or reject solely for the benefit of a third party.

An additional argument against the sale of designation right is that the Bankruptcy Court lacks jurisdiction to authorize the assumption and assignment of the lease by the purchaser of the designation rights. Upon the sale of the designation rights, the debtor receives the consideration for the leases and no longer retains an economic interest in the disposition of the lease. Since the debtor's involvement in the lease effectively terminates upon the closing of the sale of the designation rights, the Bankruptcy Court may no longer have jurisdiction over the assumption and assignment of the lease to a new tenant (of course, a counter-argument could be made if the debtor is given a part of the profits earned by the designee). A potential purchaser of designation rights may have no interest in proceeding with the transaction if the landlord is able to convince the Bankruptcy Court that it lacks jurisdiction to require the landlord to accept the new tenant.

Conclusion

Since the sale of designation rights may well be a new method for real estate investing, landlords should certainly be cognizant of the broad implications of these rights and carefully review any document that purports to sell any real estate asset in a bankruptcy case. If a landlord does not act to protect its rights, it may well may lose the opportunity after the sale of the debtor's designation rights has been consummated.

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[1] A lease has a "bonus value" when "the capitalized then fair rental value for the remaining term of the lease, plus the value of any renewal right, exceeds the capitalized value of the rental the lease specifies." *Alamo Land & Cattle Co., Inc.* v. *Arizona,* 424 U.S. 295, 304, 96 S.Ct. 910, 916, 47 L.Ed.2d 1 (1976); *In re Ernst Home Center, Inc.,* 221 B.R. 243, 256(9th Cir. BAP 1998)

[2] *In re Shangra-La, Inc.,* 167 F.3d 843 (4th Cir.1999)

[3] The sale of designation rights has occurred in the following cases: *In re Bradlees Stores, Inc., et. al.* Case Nos.00-16033 and 00-16035 through 00-16036 (BRL)U.S. Bankruptcy Court for the Southern District of New York; *In re Montgomery Ward, LLC* Case No. 00-04667 (RTL) U.S. Bankruptcy Court for the District of Delaware; *In re The Grand Union Company et al.* Case Nos. 00-39613 (NLW) through 00-39616 (NLW) Jointly Administered, U.S. Bankruptcy Court for the District of New Jersey; *In re Hechinger Investment Company of Delaware, Inc., et al.* Case No. 99-02261 (PJW) Jointly Administered, U.S. Bankruptcy Court for the District of Delaware; *In re Service Merchandise Company, Inc. et al.* Case No. 99-02649 (GCP) U.S. Bankruptcy Court for the Middle District of Tennessee Nashville Division; *In re Best Products Co., Inc.* Case No. 96-35267-T U.S. Bankruptcy Court for the Eastern District of Virginia, Richmond Division; *In re Ernst Home Center, Inc.* Case No. 96-10129 U.S. Bankruptcy Court for the Western District of Washington; *In re Caldor, Inc.-NY, the Caldor Corporation, Caldor, Inc.-CT, et al.,* Case No. 95 B 44080 (JLG) Jointly Administered, U.S. Bankruptcy Court for the Southern District of New York.

[4] The Bankruptcy Code does not, define "adequate assurance of future performance" in situations involving non-shopping center leases. The legisla-

tive history indicates, however, that the focus is on the prejudice to the landlord.

If the trustee is to assume a contract or lease, the courts will have to insure that the trustee's performance under the contract or lease gives the other contracting party the full benefit of his bargain. H.R.Rep. No. 595, 95th Cong., 1st Sess. 348 (1977); S.Rep. No. 989, 95th Cong., 2d Sess. 59 (1978); *In re U.L. Radio Corp.*, 19 B.R. 537, 541 (Bankr.S.D.N.Y.1982).

[5] The amendments to section 365(d)(4) of the Bankruptcy Code proposed by the Senate through S.420 (passed by the Senate on March 15, 2001) and by the House of Representative through H.R. 333 (passed by the House of Representatives on March 1, 2001) will drastically change the landscape for designation rights as it constricts a Court's ability to extend the deadline to assume or reject leases. Under the proposed amendments, a debtor will initially have 120 days to assume or reject a lease and that period may be extended for an additional 90 days. A debtor may obtain additional extensions only upon prior written consent of the lessor. The proposed amendment to section 365(d)(4) reads as follows:

(4)(A) Subject to subparagraph (B), in any case under any chapter of this title, an unexpired lease of nonresidential real property under which the debtor is the lessee shall be deemed rejected, and the trustee shall immediately surrender that nonresidential real property to the lessor, if the trustee does not assume or reject the unexpired lease by the earlier of

(i) the date that is 120 days after the date of the order for relief; or

(ii) the date of entry of an order confirming a plan.

(B)(i) The court may extend the period determined under subparagraph (A), prior to the expiration of the 120-day period, for 90 days upon motion of the trustee or lessor for cause.

(ii) If the court grants an extension under clause (i), the court may grant a subsequent extension only upon prior written consent of the lessor in each instance.

The Meaning of California's Free Speech Clause in the Post-*Pruneyard* World

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Golden Gateway Center v. *Golden Gateway Tenants Association*, 26 Cal.4th 1013 (Golden Gateway), decided by the California Supreme Court in a four–three vote on August 30, 2001, presented the Court with the opportunity to clarify the boundaries of its landmark free speech case permitting leafleting and signature gathering on privately owned real property, *Robins* v. *Pruneyard Shopping Center*, 23 Cal.3d 899 (1979) (*Pruneyard*). In *Pruneyard*, the Court broke away from the free speech rulings of the U.S. Supreme Court, holding that the California Constitution, unlike the federal Constitution, prohibits the private owner of a large shopping center from banning signature gathering and leafleting on his property. The Court's sudden departure from established federal free speech jurisprudence, without having previously articulated any independent standard of its own, understandably created significant uncertainty among real estate owners as to the extent of their obligations to provide access.

The Court waited 22 years to clarify its *Pruneyard* holding in *Golden Gateway*. At issue in *Golden Gateway* was the right of a tenants' association to distribute leaflets door to door within a large apartment complex. Would the Court confine *Pruneyard* to large shopping centers, as have the Court of Appeal cases decided after *Pruneyard*, or did *Pruneyard* establish a broad right of free speech that could be invoked in other settings involving private parties? What kinds of private property might the Court consider a "public forum" for purposes of free speech rights?

Would the Court adhere to the traditional concept of the Bill of Rights as protecting individuals against government excess, or private conduct equivalent to government excess, known as the state action doctrine? *Golden Gateway* potentially held the key to all of these questions.

In the end, however, the justices could agree to very little. The Court voted four–three in favor of the apartment owner and against the tenants' association. However, only three of the seven justices voted to adhere to the state action doctrine, which would continue to impose significant limits on any expansion of Pruneyard. Three of the justices voted to abandon the state action doctrine altogether and open all private property to free speech where, in the Court's opinion, the free speech interests outweighed the private property interests. The seventh and deciding vote, a concurring opinion by Chief Justice Ronald George, expressly declined to decide the debate dividing the other six justices into two equal camps. Instead, Chief Justice George argued for a case-by-case determination based upon whether the property in question has been opened up to the public so as to constitute a public forum.

What does this mean for the future of free speech rights on private property in California? First, it means that we know very little about what the Court, as presently constituted, will decide outside of the context of a large shopping center and an apartment building. We may find out more in a year or so. The Court has before it another case exploring the boundaries of free speech on private property, *Waremart, Inc.* v. *Progressive Campaigns, Inc.*, pending as Supreme Court Case No. S094236 (*Waremart*). The issue before the Court in *Waremart* will be signature gathering on the privately owned sidewalk in front of a stand-alone, "big box" supermarket.

Second, it means that a change in one vote can result in a significant policy shift. For example, were one of the four-member majority to retire and be replaced by a judge favoring broader free speech rights, the *Golden Gateway* minority would become the majority, and the scope of free speech rights on private property could be expanded dramatically.

Third, there is a new, potentially significant variable that was not anticipated or considered by the Court in *Golden Gateway*—the events of September 11, 2001. Since September 11, 2001, security issues have assumed paramount importance at all levels of our society. We are now concerned about safety in public places such as airports, bus stations, post offices, office buildings and shopping centers. Safety is most difficult to control where access is most easily gained. Would the Court uphold the right of Bin Laden supporters to recruit or solicit donations in a shopping center?

Only time will tell.

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The Nature and Scope of Permissible Regulation of Union Access by Shopping Center Owners and Managers in the Wake of *Pruneyard*: The NLRB Has Spoken, But Legal Headaches Remain

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On August 23, 2001, the National Labor Relations Board (the "Board") issued its opinion in *Glendale Associates, Ltd. et al., National Association of Broadcast Employees and Technicians,* Case 31-CA-22759, 335 NLRB No. 8 (Aug. 23, 2001), affirming an Administrative Law Judge's ("ALJ") decision regarding the validity of two time, place and manner rules governing non-commercial expressive activity. Specifically, the Board agreed with the ALJ that the respondent therein had properly exercised its right under state law to maintain and apply a rule requiring advance identification of prospective participants in non-commercial expressive activity. However, the Board also agreed with the ALJ that the respondent violated Section 8(a)(1) of the National Labor Relations Act (the "Act") by maintaining and enforcing a rule prohibiting non-commercial expressive activities that identify by name the shopping center owner, manager or any tenant of the center.

In *Glendale,* representatives of the National Association of Broadcast Employees and Technicians, the Broadcasting and Cable Television Workers Sector of the Communication Workers of America, Local 57, AFL-CIO ("NABET"), distributed handbills at the Glendale Galleria (the "Center") to the Center's customers in order to garner support for their dispute with ABC, Inc., a wholly-owned subsidiary of Disney Enterprises, Inc. Since NABET's representatives refused to comply with the Center's rules, the Center's security director advised NABET's representatives that they might be subject to arrest for trespassing if they continued to distribute the improper handbill. Notwithstanding this admonition, representatives of NABET continued to distribute the handbill in question at the Center for approximately six hours.

NABET filed a charge. claiming that the respondent had engaged in certain unfair labor practices in violation of the Act. A complaint was issued, alleging that the respondent had violated Section 8(a)(1) of the Act by maintaining and enforcing a rule prohibiting the naming of any Center tenant in printed materials and a rule requiring the naming of all persons who will or may engage in certain non-commercial expressive activity in advance of the activity, and by threatening to arrest representatives of NABET for non-compliance with these rules.

The ALJ determined that the analytical framework for the matter presented was set forth in *Lechmere* v. *NLRB,* 502 U.S. 527, 112 S.Ct. 841 (1992), wherein the Supreme Court established a bright-line rule permitting employers to exclude non-employee union representatives attempting to distribute literature on their property, unless the union is attempting to communicate with the employer's employees and the location of the employees' workplace and living quarters place them beyond the reach of reasonable union efforts to communicate with them. Nevertheless, even after acknowledging that Lechmere controlled this matter, the ALJ held that NABET's purported First Amendment and Section 7 rights outweighed the respondent's property rights. The ALJ did not cite any authority to support his use of a balancing test, or his conclusion that NABET had rights under the First Amendment and Section 7 to engage in its activity at the Center.

The ALJ went on to hold that the respondent's prohibition against naming a tenant of the Center was an unlawful content-based restriction rather than a time, place and manner restriction permitted under *Robins* v. *Pruneyard Shopping Center,* 23 Cal. 3d 899, 153 Cal. Rptr. 854 (1979), affd, 447 U.S. 74, 100 S.Ct. 2035 (1980) (*"Pruneyard"*). Contrarily, the ALJ also found that the respondent did not violate the Act by maintaining and enforcing a rule requiring advance identification of prospective participants in non-commercial expressive activity at the Center. On review, the Board adopted both of the ALJ's findings.

Citing *Bristol Farms,* 311 NLRB 437 (1993), the Board expressly stated that it looks to state law to determine whether a party has a property right sufficient to exclude non-employee union representatives because "it is [s]tate law, not the Act, that creates and defines [the] property interest." The Board adopted the ALJ's finding and affirmed that the rule requiring advance notice of prospective handbillers is consistent with legitimate time, place and manner purposes under state law. Indeed, the Board recognized that the California Court of Appeal in *Union of Needletrades, Industrial & Textile Employees, AFL-CIO* v. *Superior Court,* 56 Cal. App. 4th 996, 65 Cal. Rptr. 2d 838 (1997) ("UNITE"), upheld the "prior identification" rule as a permissible regulation under California law. Hence, the Board agreed with the ALJ that "properly exercised its entitlement under state law to maintain and apply a reasonable time, place and manner regulation."

With respect to the second rule at issue, the respondent's prohibition against the naming of a Center tenant, the Board implicitly did not rely favorably on *H-CHH Associates* v. *Citizens For Representative Gov't,* 193 Cal.App.3d 1193, 238 Cal.Rptr. 841 (1987), *cert. denied,* 485 U.S. 971, 108 S.Ct. 1248 (1988), which held that, under state law, the prohibition against soliciting money—a recognized content-based restriction—was sanctioned as being appropriate for a privately owned shopping center. The Board's rejection of H-CHH and finding of a violation of Section 8(a)(1) of the Act was allegedly based upon an inadequate record, stating that "[a]s a practical matter, it appears that the purpose and effect of the rule, as applied here, was simply to shield the [r]espondent's tenants, such as the Disney Store, from bring the subject of otherwise lawful handbilling."

In sum, the Board's decision in *Glendale*, while undoubtedly a partial victory for shopping center owners and managers previously left adrift to craft enforceable time, place and manner rules in the wake of *Pruneyard,* also evidences the ongoing tussle between the Board and the courts of appeals on the issue of permissible regulation of access to private property. Should the Board and/or respondent seek enforcement

and/or review, respectively, of the Board's decision in *Glendale,* there will be occasion to document the next chapter in this legal conundrum.

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Rhode Island v. *Palazzolo*: The Next Step in the Law of Regulatory Takings

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The U.S. Supreme Court took the next small step in the continuing development of the doctrine of regulatory takings in its decision this year in *Rhode Island* v. *Palazzolo,* 121 S. Ct. 2448 (2001). The petitioner in *Palazzolo,* Anthony Palazzolo, owned 18 acres of waterfront land in Westerly, Rhode Island. In 1985, he sought permission from the Rhode Island Coastal Resources Management Council to construct a private beach club on the parcel. This development would have required the filling of 11 acres of coastal wetlands. Acting pursuant to a statute enacted seven years prior to the time that Palazzolo acquired title to the property, the Council rejected the proposed development. Palazzolo brought suit, claiming that the application of the state's wetlands regulations to his property constituted a taking. He lost at both the trial and the Rhode Island Supreme Court levels, and then sought review by the U.S. Supreme Court.

Palazzolo appealed four holdings of the Rhode Island Supreme Court. The court had held (i) that his claims were not ripe; (ii) that he had no right to challenge regulations that were established prior to his taking title to the property; (iii) that, in any event, the action of the State did not amount to a taking under the standard of *Lucas* v. *South Carolina Coastal Council,* 505 U.S. 1003 (1992), because it did not deprive him of all economically beneficial use of the property; and (iv) that, even under the broader standard of *Penn Central Transp. Co.* v. *New York City,* 438 U.S. 104 (1978), Palazzolo had no claim because, given that the wetlands regulations were enacted before he acquired title, he could not have had "reasonable investment backed expectations" of developing the property free of such regulations.

The U.S. Supreme Court held:

(i) that Palazzolo's claims were ripe;

(ii) that the right to challenge the wetland regulations was not barred by Palazzolo's having taken title after the regulations were enacted;

(iii) that he had not been deprived of all economically beneficial use of his property and thus could not sustain a takings claim on the basis of the standard articulated in Lucas; and

(iv) that the holding of the Rhode Island court that he could not have had any reasonable, investment-backed expectations regarding the development of the property in any manner other than that provided by the regulations needed to be re-examined on remand, in light of the Court's holding in item (ii).

The second of these holdings is Palazzolo's contribution to the evolution of the law of regulatory takings. The Court summed up the holding of the lower court in this way: "A purchaser or a successive title holder like petitioner is deemed to have notice of an earlier-enacted restriction and is barred from claiming that it effects a taking" *Palazzolo,* 121 S. Ct. at 2448.

The argument that supports this conclusion is restated by the Court in these terms: "Property rights are created by the State. *[citations omitted]* So . . . by prospective legislation the State can shape and define property rights and reasonable, investment backed expectations, and subsequent owners cannot claim any injury from lost value. After all, they purchased or took title with notice of the limitation." *Palazzolo,* 121 S. Ct. at 2462.

The Court rejected this reasoning. It noted (without argument or citation) that in "certain circumstances . . . a particular exercise of the State's regulatory power" can be "so unreasonable or onerous as to compel compensation." *Id.* The mere passage of time cannot change this.[1] "A State would be allowed, in effect, to put an expiration date on the Takings Clause. This ought not to be the rule. Future generations, too, have a right to challenge unreasonable limitations on the use and value of land." *Palazzolo,* 121 S. Ct. at 2463.

The Court cited its opinion in *Nollan* v. *California Coastal Commission,* 483 U.S. 825 (1987) in support of the step it took: "The principal dissenting opinion [in *Nollan*] observed it was a policy of the California Coastal Commission to require the condition [allowing lateral beach access to the public], and that the Nollans, who purchased their home after the policy went into effect, were 'on notice that new developments would be approved only if provisions were made for lateral beach access.' *[citation omitted].* A majority of the Court rejected the proposition. 'So long as the Commission could not have deprived the prior owners of the easement without compensating them . . . the prior owners must be understood to have transferred their full property rights in conveying the lot." *Palazzolo,* 121 S. Ct. at 2463–2464.

Palazzolo took the loose thread of this exchange between the dissent and the majority in Nollan and wove it into the main strand of regulatory takings law.

Background of Regulatory Takings Law

"Contemporary regulatory takings law has its origins in *Pennsylvania Coal Co.* v. *Mahon,* 260 U.S. 393 (1922). Writing for the Court, Justice Holmes staked out the limits of the question: "Government could hardly go on if to some extent values incident to property could not be diminished without paying for every such change in general law. As long recognized, some values are enjoyed under an implied limitation and must yield to the police power." *Id.* at 413.

"The general rule at least is that while property may be regulated to a certain extent, if regulation goes too far it will

be recognized as a taking." *Id.* at 415. ". . . this [the extent to which the police power can be exercised without effecting a taking] is a question of degree—and therefore cannot be disposed of by general propositions." *Id.* at 416.

Holmes then concluded that the statute in question went too far, and effected an uncompensated taking.

In *Penn Central Transp. Co.* v. *New York City*, 438 U.S. 104 (1978), the Court considered whether a New York City landmarks preservation law, which prohibited the owner (*Penn Central*) from constructing a 50-story office tower over Grand Central Terminal, effected a taking. Penn Central was denied an approval under the landmarks law of its proposal to construct the office tower. Penn Central had opposed, but had not further challenged, the designation of the Terminal as a landmark, and neither challenged the factual findings behind the denial of approval for the tower nor sought approval of a smaller tower. Instead, Penn Central filed suit alleging an uncompensated taking. The trial court awarded declaratory judgment and injunctive relief to Penn Central. The New York Supreme Court, Appellate Division, reversed the trial court, and the New York Court of Appeals (the highest New York State court) affirmed the decision of the Appellate Division. The U.S. Supreme Court upheld the decision of the New York Court of Appeals, finding that there had not been an uncompensated taking of Penn Central's property.

In reaching its decision, the Court noted the difficulty it had encountered in providing guidance on regulatory takings matters, which the Court described as essentially *ad hoc*, factual inquiries. *Penn Central,* 438 U.S. at 124. The Court identified "several factors that have particular significance" in determining whether a government regulatory action constitutes a taking:

(i) "the economic impact of the regulation" on the property owner;

(ii) "the extent to which the regulation has interfered with distinct investment-backed expectations"; and

(iii) "the character of the governmental action." *Id*. at 124.

In *Loretto* v. *Teleprompter Manhattan CATV Corp.,* 458 U.S. 419 (1982), the Court found occasion to reach beyond the multi-factor approach to regulatory takings questions that it had articulated in *Penn Central* and formulated a bright-line rule. A New York statute required owners of residential rental property to allow cable television companies to install cables and related equipment on and in their buildings. Jean Loretto, the owner of a five-story apartment building in Manhattan, brought a class-action suit alleging, in part, that the statute effected a taking without just compensation. Both trial and appellate courts upheld the statute and found that it did not effect a taking. The Supreme Court overturned the ruling of the state court, and found that the statute did work a taking of Loretto's property. Note that the dissent in *Loretto* asserted that the "19th-century precedents relied on by the Court lack any vitality outside the agrarian context in which they were decided." *Loretto,* 458 U.S. at 446. The *Loretto* issues, indeed virtually the *Loretto* fact pattern, are enjoying a reincarnation in a number of so-called "forced-access" or "non-discriminatory access" cases that grow out of the recent federal and state deregulation of the telecommunications industry. See, e.g., *Gulf Power Company* v. *United States,* 187 F.3d 1324 (11th Cir. 1999); *Greater Boston Real Estate Board et al.* v. *Massachusetts Department of Telecommunications and Energy et al.,* Massachusetts Superior Court, Civil Action No. 00-4904-A. (2001).

In *Nollan* v. *California Coastal Commission,* 483 U.S. 825 (1987), the Court considered a situation confronted by most developers in recent decades: the appending of an onerous condition to an approval that grants the right to build. The Nollans wished to exercise an option they held to acquire an oceanfront lot. A condition to the exercise of that option was that the Nollans demolish an old, small house on the lot and replace it with a new structure. They sought approval to construct a larger, three-bedroom house. The California Coastal Commission granted a permit for the house, but as a condition to the permit, required that the Nollans grant the public a permanent easement to pass laterally (that is, parallel to the shoreline) across their beach. The Nollans brought suit alleging a taking of their property without compensation. After several administrative and lower court rulings, the Nollans' claim was rejected by the California Court of Appeal. They then appealed to the U.S. Supreme Court.

The Court, in an opinion written by Justice Scalia, began with the position (which it did not believe could seriously be disputed) that, if California had simply required that the Nollans grant the public an easement across their property (unconnected to the grant of any permit), such a requirement would be a taking. *Nollan,* 483 U.S. at 831. The Court's opinion then stated that, in some circumstances, requiring such an easement as a condition to a permit would not constitute a taking. It reasoned, however, that if there is a "lack of nexus" between a condition imposed on a permit and the purpose that would have been served by an outright prohibition on the activity authorized by the permit, the condition "is not a valid regulation of land use but 'an out-and-out extortion.'" *Nollan,* 483 U.S. at 837. The Court then found that the required grant of lateral access along the shore bore no relation to the asserted public purpose of increasing public access from inland to the water. It concluded that, if California "want[ed] an easement across the Nollans' property, it must pay for it." *Nollan,* 483 U.S. at 842.

In *Lucas* v. *South Carolina Coastal Council,* 505 U.S. 1003 (1992) (in which the Court's opinion was, as in *Nollan,* written by Justice Scalia), the Court considered whether a taking was effected by a South Carolina regulation that, in the view of the trial court, eliminated all of the economic value of the property in question. Lucas owned two lots on an island off the coast of South Carolina, on each of which, when he acquired them in 1986, he would have been able to construct a single family home. In 1988, South Carolina enacted the Beachfront Management Act, "which has the direct effect of barring petitioner from erecting any permanent habitable structures on his two parcels." *Lucas,* 505 U.S. at 1007. Lucas brought suit, and the trial court found that a taking had occurred and ordered Lucas to be compensated. The Supreme Court of South Carolina reversed the trial court and found that no compensation was due, because the regulation at issue was designed to prevent serious public harm.

In his consideration of this matter, Justice Scalia surveyed the Court's consideration of the problem of regulatory takings

from *Pennsylvania Coal* v. *Mahon* through the present. The Court's opinion then turned to a fundamental consideration that pointed away from a finding that a taking had occurred—the view that there is no taking, and that thus no compensation is required when a regulation is an exercise of the police power designed to prevent a serious harm to the public. In its further analysis, the Court noted, however, that whether a regulation is designed to prevent a harm or to confer a benefit is often largely matter of perspective. The same effect can be described as an avoidance of harm or the conferring of a benefit. Further, the same end (e.g., restriction of development on a particular parcel) may equally well be accomplished by an explicit taking (e.g., of a development easement) or by imposition of a regulation (e.g., restricting development in wetlands). Thus, a finding by a state court or a recitation by a state legislature that a regulation is necessary to avoid a harm, even if true, is not enough by itself to support the conclusion that such regulation is not a taking.

The Court went on to articulate a rule to distinguish "regulatory 'takings'—which require compensation—from regulatory deprivations that do not":

"Where the State seeks to sustain regulation that deprives land of all economically beneficial use, we think it may resist compensation only if the logically antecedent inquiry into the nature of the owner's estate shows that the proscribed use interests were not part of his title to begin with." *Lucas,* 505 U.S. at 1027.

". . . regulations that prohibit all economically beneficial use of land . . . cannot be newly legislated or decreed (without compensation), but must inhere in the title itself, in the restrictions that background principles of the State's law of property and nuisance already place upon land ownership." *Lucas,* 505 U.S. at 1029.

The Court remanded the case for the state court to determine the relevant background principles. In *Dolan* v. *City of Tigard,* 512 U.S. 374 (1994), the Court returned to the general question it confronted in *Nollan* v. *California Coastal Commission:* When does a condition attached to the grant of a permit go so far as to constitute a taking? Dolan owned a 9,700-square-foot plumbing and electrical supply store located on a 1.67 acre parcel. A creek flowed across one corner and along one boundary of the parcel, and a portion of the parcel was within the 100-year flood plain of the creek. Dolan sought a permit to demolish the existing structure; construct a new store almost twice as large; create paved parking; and, in a later phase, construct some additional commercial space. The city granted the needed approvals, but imposed conditions that included two dedications of property to the public:

(i)All portions of the parcel within the 100-year flood plain of the creek were to be dedicated to the city as a greenway; and

(ii)A strip 15 feet wide, measured landward from the limit of the 100-year floodplain, was to be dedicated to the city for use as a pedestrian/bicycle pathway.

The issuance of the permit included findings that (i) the required dedication of the floodplain area was related to "the applicant's plan to intensify development on the site" and (ii) the pedestrian/bicycle pathway 'could offset some of the traffic demand on [nearby] streets and lessen the increase in traffic congestion.' " *Dolan,* 512 U.S. at 381–382.

Dolan appealed, arguing that "the city's dedication requirements were not related to the proposed development," and thus were an uncompensated taking. *Dolan,* 512 U.S. at 382. The Land Use Board of Appeals, the trial court and both Oregon appellate courts rejected her claim. In its consideration of the case, the Court held that a two-stage determination was required:

(i)". . . we must first determine whether the 'essential nexus' exists between the 'legitimate state interest' and the permit condition exacted by the city."

(ii)"If we find that a nexus exists, we must then decide the required degree of connection between the exactions and the projected impact of the proposed development." *Dolan,* 512 U.S. at 386.

The Court noted that, in *Nollan* v. *California Coastal Commission,* it had not considered the second requirement, because the exaction demanded in *Nollan* did not meet the first requirement. In *Dolan,* however, the Court found that the "essential nexus" test was clearly met. It then turned to the second step in the analysis: "to determine whether the degree of the exactions demanded by the city's permit conditions bears the required relationship to the projected impact of the petitioner's proposed development." *Dolan,* 512 U.S. at 388. The Court found that while "keeping the floodplain open and free from development would likely confine the pressures on Fanno Creek created by petitioner's development, . . . [t]he city ... never said why a public greenway, as opposed to a private one, was required in the interest of flood control." *Dolan,* 512 U.S. at 393.

Similarly, with regard to the required dedication of land for a pedestrian/bicycle pathway, the Court found that "the city ha[d] not [met] its burden of demonstrating that the additional number of vehicle and bicycle trips generated by petitioner's development reasonably relate[d] to the city's requirement for a dedication of the pedestrian/bicycle pathway easement." *Dolan* at 395. The Court concluded: "No precise mathematical calculation is required, but the city must make some effort to quantify its findings in support of the dedication for the pedestrian/bicycle pathway beyond the conclusory statement that it could help offset some of the traffic demand generated." *Dolan,* 512 U.S. at 395–396.

With that, the case was remanded.

Palazzolo **in Context**

Since *Pennsylvania Coal,* the Court's principal decisions on the issue of regulatory takings fall into two categories: The first addresses per se takings, such as *Loretto* (physical occupation) and *Lucas* (deprivation of all economic value). The second addresses circumstances that require a case-specific analysis in order to determine whether a taking has occurred, such as *Penn Central* (economic impact, investment-backed expectations and character of the government action), *Nollan* (essential nexus) and *Dolan* (essential nexus and rough proportionality).

Palazzolo increases the possibility of successfully prosecuting a regulatory takings claims under both categories. While *Lucas* supported the position that what appears to be a per se taking (e.g., because of deprivation of all economic value) may, after analysis be no taking at all, if the analysis shows that background principles of title included a reservation of

the interest affected by the state action being challenged, "*Palazzollo* raises the threshold to entry into that Pantheon of "background principles."

Similarly, what appears to be valid regulation of the use of property, pursuant to a scheme in place long before a claimant acquired title, may now be subject to challenge. The reasonableness of the claimant's investment-backed expectations will be measured not against the regulatory scheme in place at the time of acquisition, but against the background principles of the state's law of property, as those principles may be articulated in light of the case then before the court.

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[1] It may be worth noting that the mere passage of time is a necessary element, under the doctrine of adverse possession, in converting trespass into ownership.

In Practice

Electronic Signatures and Commercial Real Estate Transactions

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Internet e-mail is used frequently to negotiate and exchange documents for commercial real estate transactions such as sales, leases and loans. Nonetheless, most such transactions are not consummated until the final documents are printed, signed and exchanged. The need for handwritten signatures often delays the deal. New federal legislation, the Electronic Signatures in Global and National Commerce Act (Pub. L. No. 106-229, 114 Stat. 464 [2000]), clears the way for consummation of real estate transactions, simultaneously, by parties sitting at computers in different places and time zones, without the need for handwritten signatures on printed documents.

Handwritten and Electronic "Signatures"

Handwritten signatures are creations of the physical world, a unique interaction of brain, body, pen and paper, a distinctive flow of lines and swirls that can be replicated only by the signatory. Certain unique characteristics of the person are imbedded in each handwritten signature. A signature may authenticate an object, such as that of an artist on a painting. If an object is a legal document, it also confirms agreement to its terms.

A signed document authenticates and preserves the agreement of the parties. The document is authenticated through use of a distinctive mark, sometimes with witnesses and notarization, which confirms that the person who signed is the same as the person whose mark appears on the document, i.e. the person is not an imposter and the signature is not a forgery. A handwritten signature also maintains the integrity of a document. By initialing pages, the use of special paper and the exchange of executed originals, parties may assure that the document is not altered after it is signed.

A new world has emerged in recent years, one without physical characteristics, which exists through the confluence of minds and human energy connected by the Internet. Ingenious technology for electronic signatures has emerged from this new world. Although many types of electronic signatures are being developed, most lack any consistent traits. To understand these new electronic signatures, think of them as a process by which documents in digital format are authenticated, rather than as a distinctive physical mark such as a handwritten signature.

An electronic signature may be hidden in a document, woven intricately throughout the fabric comprising its digital code, and invisible when the document is viewed on a computer screen or printed. Nonetheless, the unique characteristics it imparts to the digital version of the document confirm its authenticity and preclude its alteration, in most instances, much more effectively than with handwritten signatures and printed documents.

Significance and Limitations of the E-Sign Act

The Electronic Signatures in Global and National Commerce Act ("E-Sign Act"), which became effective on October 1, 2000, provides that an electronic signature or document has the same legal effect as a printed signature or document. A signature or contract relating to a transaction may *not* be denied legal effect, validity or enforceability solely because (a) it is in electronic form or (b) an electronic signature was used in its formation (Section 101[a]). The term "transaction" includes the sale, lease, exchange or other disposition of any interest in real property (Section 106[13][B]). This gives the electronic medium the same legal status as the paper medium. The simple but sweeping provisions of the E-Sign Act create a legal environment within which new computer technologies may flourish.

The E-Sign Act also provides that any legal requirement for a notarization or acknowledgment, either verified or under oath, may be satisfied by the electronic signature of the person authorized to perform those acts (Section 101[g]). These provisions are of particular significance to the real estate industry, since many conveyancing documents must be notarized prior to recording.

What Is an Electronic Signature?

The E-Sign Act defines an "electronic signature" to include "… an electronic sound, symbol or process, attached to or logically associated with a contract … by a person with the intent to sign.…" "Electronic" is defined as relating to technology having electrical, electronic, magnetic, wireless, optical, electromagnetic, or similar capabilities." The definition is intentionally broad as to what is an electronic signature, and includes the following:

- handwritten signature on a fax transmittal;
- image of a handwritten signature, scanned and digitized;

- "smart cards" that identify the user;
- encrypted "digital signature" with public and private keys;
- voiceprint, retinal scan, fingerprint or DNA comparison.

There are many types of electronic signatures. Some are crude and unreliable while others are complex and extremely effective. New electronic signature technologies emerge constantly. Many of these technologies are combined with password features, date recording and document encryption.

Encryption, the process by which the digital version of a document is scrambled and encoded, is central to "digital signatures," currently the most sophisticated type of electronic signatures. Special computer software with algorithms encode the digital version of a document so that it may be read or modified only by authorized individuals using the same software. This software creates two different "keys," which may be passwords, smart cards, retinal scans or other methods of identification. One set of "private" keys is used by the parties to lock the document through encryption. A separate "public" key is shared with others to unlock and read the document. Only the parties to a transaction, together with their private keys, may alter the document once it has been encrypted.

Which of the electronic signature technologies will become most popular, by providing the right combination of security and ease of use, will be determined in the marketplace.

Consumer Protection Provisions

The E-Sign Act contains extensive provisions to protect consumers. A "consumer" is someone who obtains products or services primarily for personal, family or household purposes (Section 106[1]). Disclosures are required, and procedures established, pursuant to which consumers may consent to the use of electronic signatures and records (Section101[c]). The procedures include verification that the parties use compatible computer software. These special consumer provisions apply to transactions such as home mortgage loans and residential leases, but do not apply to business-to-business transactions such as shopping center leases or project construction loans. Nonetheless, since the E-Sign Act does not require anyone to use electronic signatures, all parties to a commercial real estate transaction must consent to their use.

Even though the consumer protection provisions of the E-Sign Act do not apply to commercial transactions, the cautious drafter of a commercial real estate document utilizing electronic signatures nonetheless may wish to include similar provisions. This would reduce the likelihood that a party to the commercial contract might challenge its enforceability based on the argument that there was not an effective consent to utilization of electronic signatures.

Exceptions and Special Provisions

In addition to the consumer protections, specific provisions are also included in the E-Sign Act in response to concerns expressed by representatives for insurance agents and brokers, governmental agencies such as the Securities and Exchange Commission, the Federal Communications Commission and the banking industry. Certain types of transactions are specifically excepted. These include wills and testamentary trusts, family law matters, certain provisions of the Uniform Commercial Code, court orders and notices, terminations of utility services, repossession or foreclosure of rental property or a primary residence, termination of health or life insurance, product recalls, documents relating to hazardous materials, and standards and format requirements of governmental agencies relating to the filing of records (Section 103 and 104).

One purpose of the E-Sign Act is to eliminate the uncertainty caused by non-existent or inconsistent state electronic signature laws. Generally, this new federal legislation preempts conflicting state laws, and specifically overrides those that requires the use of, or favors, a specific technology for electronic signatures and records (Section 102). The E-Sign Act includes additional provisions governing the maintenance of electronic records.

Conclusion

The E-Sign Act is designed to eliminate legal barriers to the development of new and innovative digital signature technologies. It opens the doors for private businesses and entrepreneurs to develop these technologies, and will impact e-commerce dramatically in the future, including transactions of the commercial real estate industry.

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Of Interest

Articles

Afarin, "Section 365—Executory Contracts and Unexpired Leases," 2001 *Ann.Surv. Bankr.L.*421 (2001/2000).
Baxter, "Recent Developments in Executory Contracts," 10 *J. Bankr.L. & Prac.* 121 (Jan.–Feb. 2001).
Kupetz, Real Estate Leases in Bankruptcy: Landlord/Tenant Issues Under the Bankruptcy Code," 2000 *Ann.Surv. Bankr.L.* 331 (2001/2000).
McIntosh, "Insolvency Act 2000—Landlords' Right of Peaceable Re-entry (United Kingdom)," 17 *Insolvency L. & Prac.* 48 (March–April, 2001).
St. James, "Landlord Beware: Will a Security Deposit Survive a Bankruptcy?" 26 *Cal.Bankr.J.*44 (2001).
Sankaraan, "Rejection Versus Termination: A Sublessee's Rights in a Lease Rejected in a Bankruptcy Proceeding Under 11 U.S.C. 365 (d)(4)," 99 *Mich.L.Rev.* 853 (Feb. 2001).

Cases

Assignment

A court could address a debtor's motion to extend the time to accept or reject a lease after the 60-day period for assumption or rejection had passed, as long as the motion was made before the 60-day period had passed. *In re Travel 2000, Inc.*, 264 B.R. 451 (Bankr.. W.D. Mich. 2001)

A tenant subleased the premises under a sublease which contained a clause providing that the obligation to pay rent

was an independent covenant. The subtenant vacated the premises and the tenant assigned its rights under the prime lease to a third party 12 days afterward. The tenant then sued the subtenant, claiming the subtenant owed rent for the balance of the term, less the amount of rent paid by the third party. The court held that the subtenant was only liable for rent for the 12 days during which the tenant had received no rent. The tenant appealed and the appellate court affirmed, finding that the clause in the sublease, which provided that the obligation to pay rent was an independent covenant, did not entitle the tenant to recover the balance of rent due under the entire term of the sublease. Under that kind of provision, a landlord's breach generally does not relieve the tenant of the obligation to pay rent, while the tenant remains in possession of the premises. In this case, the subtenant vacated the premises and the tenant assigned the prime lease for its own benefit, thereby relieving the subtenant of further obligations under the sublease. *Queensboro Dodge, Ltd.* v. *Queens J.K. Management Corp.,* 284 A.D.2d 383, 725 N.Y.S.2d 398 (2d Dep't 2001).

Bankruptcy

The requirement in Section 365 (d) that a trustee or debtor-in-possession timely perform the debtor's obligations under any unexpired nonresidential lease applied specifically to the debtor, a lessee, in its obligations as the lessee. The obligation could not be extended to the debtor as the sublessor, requiring it to use its best efforts to obtain a non-disturbance agreement from the prime lessor for the benefit of the debtor's sublessee. *In re BCE West, L.P.,* 264 B.R. 578 (9th Cir. BAP 2001).

A landlord moved for administrative rent for the 60-day postpetition period before rejection of the lease and the debtor objected on the grounds he had surrendered the property prepetition. The court found that proof of actual use and benefit of the premises was not required and held the landlord was entitled to administrative priority expense for 60 days of the postpetition rent. *In re CHS Electronics, Inc.,* 265 B.R. 339 (Bankr..S.D.Fla. 2001).

A landlord's motion to compel a debtor-in-possession to pay real estate taxes under unexpired commercial leases was denied on the grounds that the bankruptcy statute requiring the debtor-in-possession to timely perform postpetition obligations obligated the debtor to reimburse the landlord only for those real estate taxes which *accrued* postpetition, regardless of when they were billed. *In re GC Companies, Inc.,* 261 B.R. 594 (Bankr..D.Del. 2001).

The tenants/debtors filed a voluntary petition for bankruptcy protection and remained in possession of the premises. In the course of seeking buyers for their leases, they sought to extend the time to assume or reject their unexpired leases and filed three motions to extend the time. The debtors filed the last extension four days late. "Lend Lease" was the landlords' agent for the lease and objected to the extensions. It argued that granting the debtors' motion would open the floodgates and allow debtors seemingly infinite time to assume or reject leases. The court rejected its argument, noting that the touchstone of its analysis was the balance of prejudice to Lend Lease and the debtors (rather than all landlords and debtors). The court held that it was entitled to use its equitable powers under 11 U.S.C. §105(a) to grant the debtor's motions to extend time to assume or reject the new lease. It considered that under equity principles, debtors can have additional time to decide whether to assume or reject a particular lease, citing *In re Channel Home Centers, Inc.,* 989 F.2d 682, 686-88 (3d Cir. 1993). The court limited its ruling to the particular facts of this case, and noted that its decision was generally not to permit debtors to have an infinite amount of time to decide to assume or reject a lease. *In re GST Telecom, Inc.,* 2001 WL 686971, Case No. 00-1982-GMS (D. Del. 2001).

A debtor/tenant's obligation for rent had crystallized on the first of the month, which was one day before it filed its bankruptcy petition. The landlord filed a motion to compel payment of rent, and the court granted the motion and held that the Bankruptcy Code obligated the debtor to timely perform any lease obligations arising during the postpetition, prerejection period, for rent relating to its postpetition occupancy on a pro rata basis. *In re Travel 2000, Inc.,* 264 B.R. 444 (Bankr..W.D.) Mich. 2001.

Contracts

A developer entered into a contract with, and drafted primarily by, an anchor tenant, which incorporated the site plan by reference and provided that the developer would not build structures other than those represented in the site plan, without the consent of the anchor tenant. The lease was amended three times and a new site plan indicated a renumbered pad for a "Proposed Future Store," rather than a Proposed Future Department Store, whose "Actual Configuration and Size May Vary," although the parking ratio would be maintained. When the developer sought to build a substantially larger store on the pad, the anchor tenant objected and sued to enjoin construction. The trial court granted the developer's motion for summary judgment and the anchor tenant appealed. The appellate court examined the lease language and decided the site plan expressly provided that the actual size and configuration of the store might vary. In addition, there were no limits on the size of the future store, whereas other provisions in the lease contained specific language limiting the size of certain premises. The appellate court affirmed the summary judgment in favor of the developer. *Belk, Inc.* v. *Warner Robins Zamias Ltd. Ptrshp.,* __ S.E.2d __, 2001 WL 1112113, A01A0929 (Ga. App. 2001).

A tenant requested permission to assign its lease and entered into an agreement with the lease which incorporated by reference "all relevant terms of the lease," provided that the tenant would "repair and restore the Leased Premises as required by the Lease," and contained specific terms dealing with roof repairs. A dispute arose regarding certain repairs, and the landlord sued the tenant for breach of the agreement. The trial court granted the landlord's motion for summary judgment and awarded attorney's fees and expenses. The tenant appealed, arguing that the agreement did not incorporate by reference the entire lease, but only selected terms. The appellate court found the language "doubtful" and applied contract law to interpret the agreement against the drafter, i.e., the landlord. It concluded that the lease was not adopted in its entirety and that the attorney's fee provision had not been included. It, therefore, reversed the trial court's award of attorney's fees to the landlord. The appellate court did find that the tenant's repair obligations were clearly incorporated but that

there were questions of fact about the cost of some repairs. It thus affirmed in part and reversed in part. *Farnsworth* v. *Faulkner,* 2001 WL 892817, No. W2000-02031-C0A-R3-CV (Tenn. Ct.App. 2001).

A contract vendee of the right to purchase property assigned that right for $30,000. The contract vendee terminated the contract and negotiations ceased. The assignee then contacted the seller directly and agreed to purchase the property for the same amount as the contract vendee had agreed to pay. The contract vendee then sued the alleged holder of the oral assignment, claiming unjust enrichment and seeking the alleged amount agreed upon for the sale of the assignment of the right to purchase the subject property. The trial court denied the assignee's motion for summary judgment, but the appellate court reversed, holding that once the contract to purchase had been terminated by the contract vendee, the assignee was entitled to negotiate a contract directly with the seller. *J.E. Capital* v. *Karp Family Assoc.,* 726 N.Y.S.2d 663, 2001 N.Y. Slip Op. 06079 (1st Dept. 2001).

Two condominium buildings were connected by an alleyway. The ground floor of the buildings was occupied by commercial units and the upper floors were residential. One of the commercial units operated a coffee shop that used half the connecting alleyway for its tables and chairs. When this use caused disruption to the residential units, one of the residents sued the developer, the condominium association and the association president, claiming that the coffee shop had no right to use the area in which its tables and chairs were located. The coffee shop owner intervened. The trial court agreed with the plaintiff and granted an injunction that limited, but did not prohibit, use of the alleyway. The resident appealed and the appellate court examined the condominium bylaws and lease with the coffee shop. It concluded the coffee shop had the right to use the sidewalk, but found that according to both the condominium bylaws and the coffee shop lease, the disputed area was not a sidewalk. The appellate court thus affirmed the trial court's finding regarding the right to use the disputed area . However, it reversed the partial injunctive relief and granted an injunction prohibiting entirely the use of the area by the coffee shop. *Lacassagne* v. *Friedrichs Square Condominium Association, Inc.,* 792 So.2d 914 (La. App. 5 Cir., 2001).

The Johnstons agreed to sell Dixie Village Shopping Center to Equity, which transferred the contract to Lake Mary. After closing, Mr. Johnston was concerned that Lake Mary would not remit certain overage rents, CAM charges and taxes that were due prior to closing. He retained over $96,000 in rent checks. As a result, Lake Mary refused to fulfill some of its post-sale obligations and sued the Johnstons for breach of contract, conversion, and unfair and deceptive trade practices. The trial court granted a directed verdict in favor of Mrs. Johnston on the claims for breach of contract, conversion, and unfair and deceptive trade practices but against Mr. Johnston. It awarded Lake Mary the amount of the retained rent and refused to award attorney fees. Both parties appealed, and the appellate court affirmed the findings in favor of Lake Mary with regard to conversion of the rent checks and unfair and deceptive trail practices. It also affirmed Lake Mary's method of calculating the tax reimbursement. Finally, the appellate court found that under state law, despite the contract provision allowing attorney fees, there was no basis for allowing them in a contract case, and the court had sole discretion to award them in an unfair trade practices claim. *Lake Mary Ltd. Ptrshp.* v. *Johnston,* No. 551 S.E.2d 546 (N.C. App. 2001).

A broker was entitled to a commission for leasing a developer's property. The property owner agreed to pay the commission but sold the property, and the buyer assumed the owner's obligation. The developer and the broker sued the buyer for the amount of commission due, and the buyer claimed the developer was barred from collecting the commission because he was not a licensed real estate broker. The theories of recovery allegedly included breach of a contract to pay a commission, of which the developer was the intended beneficiary. The trial court granted summary judgment to the buyer, but the appellate court reversed, finding that the developer neither sought indemnity nor sought to recover a commission unearned as a licensed real estate broker. Rather, the developer was seeking damages from a party who allegedly had assumed the obligation to pay the commissions. *McDonald Windward Partners, L.P.* v. *Wenzhold, L.P.,* 552 S.E.2d 92 (Ga. App. 2001).

A purchase agreement for property to be developed for use as a shopping center provided for deposit of money into escrow, a time period within which the purchaser, Crown Capital, could inspect the property to determine if it was satisfactory for the use intended under the agreement, and an additional deposit if the purchaser did not give notice of its intent to terminate after inspection of the property. Crown, which drafted the contract, gave notice of termination after the potential anchor tenant for the proposed shopping center withdrew its interest. Crown did not inspect the property, but concluded it was no longer economically suitable to develop as a shopping center and sought to terminate the purchase agreement. The seller sued and the trial court granted summary judgment to Crown. The seller appealed. The appellate court found that the contract was ambiguous regarding the meaning of the phrase "satisfactory for the purchaser's intended use." The court followed the rules of contract construction, whose goal is to give a fair and reasonable construction that upholds a binding contract. It concluded the parties did not mean that a satisfactory use was an unrestricted discretionary use that would permit the destruction of the contract. The appellate court decided the seller was entitled to summary judgment and reversed the trial court's grant of summary judgment to Crown. *Sheridan* v. *Crown Capital Corp.,* 2001 WL 946488, A01A1675 (Ga. App. 2001).

Covenants

Lemstone's, a shopping center tenant, had a lease that provided it would use its premises only for the sale of religious and inspirational books. About 18 months prior to the expiration of the lease, the landlord leased premises to a competing tenant. Lemstone's business declined and it abandoned the premises about six months before the lease expired. The landlord sued for damages for breach of lease and Lemstone counterclaimed. The court granted the landlord's motion for summary judgment and Lemstone appealed. Lemstone argued the restriction in the lease was ambiguous, but the court disagreed, finding the restriction applied only to Lemstone's and

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not to the landlord's right to control its tenant mix. The court also rejected Lemstone's argument that the landlord had tortiously interfered with its lease by leasing premises in the shopping center to a competing tenant. However, the court reviewed Ohio law extensively and concluded that a commercial lease is a contract under which a landlord has a duty to mitigate. It remanded for findings on whether the landlord had made reasonable efforts to do so. *Frenchtown Square Partnership* v. *Lemstone, Inc.*, 2001 WL 503068, Case No. 99 C.A. 300 (Ohio App. 7 Dist. 2001).

A lease contained a clause prohibiting the landlord from leasing to an entity that "shall be utilized as an amusement center or other usage substantially similar to" the tenant's use. The landlord leased to a similar operation, and the tenant's profits immediately began to decrease. The tenant sued both the landlord and the competitor, but the competitor was dismissed from the suit. A jury awarded the tenant damages and attorney's fees, and the landlord appealed. The landlord argued that the restrictive covenant was so broad that it unreasonably restricted competition, but the court examined the covenant in the context of the lease and concluded that the covenant was a reasonable restriction on competition and the landlord had violated it. The court then addressed the argument by the landlord's general partner that he should have been dismissed on the basis of an exculpatory clause in the lease. The court noted that exculpatory clauses waive substantial rights and, therefore, must be "explicit, prominent, clear and unambiguous." The covenant in the instant lease lacked an indicia of prominence and was unenforceable. The appellate court also found that the tenant was not in default. Furthermore, the evidence regarding the diminished value of the leasehold with a broken covenant properly included operating losses, lost profits and loss of investment. *Parkside Center, Ltd.* v. *Chicagoland Vending, Inc.*, 552 S.E.2d 557 (Ga. App. 2001).

A tenant and successor landlord signed an "Amended and Restated Lease," which incorporated an exclusive use provision prohibiting the landlord from leasing to a "bar restaurant or food service establishment of any kind." The successor landlord leased to a tenant which sold an item that the original tenant sold. However, when notified that the landlord responded, it was not a competing use. The original tenant sued for a declaration that the landlord was violating the exclusive use provision and that the tenant was, therefore, entitled to a 50% rent abatement. The trial court granted the landlord's motion for summary judgment, finding that the abatement provision was an unenforceable penalty. The appellate court reversed, reasoning that the clause was negotiated at arms' length and did not favor one party over the other. The clause might result in an underestimation of the tenant's damages and did not guarantee a windfall to the tenant. The court distinguished the principal case cited by the landlord and found that the provision in the instant case was neither one-sided nor obviously intended to impose a penalty to coerce performance. The court did, however, find the language "food service establishment of any kind" unclear and, thus, reversed summary judgment on the question of whether the exclusive covenant applied to the allegedly competing tenant. *Red Sage Ltd. Ptrshp.* v. *Despa Deutsche Sparkassen Immobilien-Anlage-Gasellschaft MBH*, 254 F.3d 1120 (7th Cir. 2001).

Environment

When the owner of a shopping center sought to refinance the property, the lender required payments for site testing and environmental insurance as a condition of the load. The shopping center owner sought reimbursement of the costs from a tenant that operated a dry-cleaning business, claiming the costs were incurred as a result of chemical spills in the tenant's business. The tenant refused and the owner filed suit for breach of lease. The court found the costs were incurred as a result of the owner's decision to refinance rather than as a result of the tenant's conduct. Furthermore, the court found that the lease agreement did not include indemnification for such costs. The owner appealed and the appellate court affirmed, finding that under the terms of the lease, the tenant was not obligated to pay the costs of site testing and environmental insurance. *D&J Co.* v. *Stuart*, Court of Appeals No. L-00-1357, Ohio Ct. App., 6th App.Dist, September 14, 2001.

Fees

A landlord was not entitled to attorney fees where the lease did not contain a general attorney's fees provision, and the circumstances of the case did not fall under the default clause in the lease. A 10-year lease provided that the tenant would be responsible for buildout costs if it terminated the lease within three years. Less than three years into the lease, the tenant sent notice that it wanted to terminate the lease on a date that was the commencement of the third year. The landlord and tenant tried, but were unable, to negotiate a new lease. Eventually, the landlord sued for the buildout costs, and the court held that because the tenant gave notice within the first three years of the lease, it was liable for the costs. The landlord then made a motion and was granted attorney's fees. The tenant appealed, and the court held the lease did not provide for fees under the circumstances of the case. There was no general provision, and default provision did not apply. That provision required the tenant to pay fees if the landlord terminated the lease due to the tenant's default. The instant case did not involve the landlord's termination; it was the tenant that wanted to terminate. Thus, the award of fees to the landlord was reversed. *Midway Warehouse Ltd. Ptrshp.* v. *Ramsey Action Programs, Inc.*, 2001 WL 605076, C1-00-1985 (Minn. App. 2001).

A landlord purchased property with an apartment that was occupied by the original owner of the property who built the apartment. The landlord subsequently discovered the apartment violated the city's ordinances and was illegal. The landlord then commenced a Forcible Entry and Detainer (FED) action and obtained a default judgment. The tenant's attorney moved to set aside the default judgment and after a trial, it was determined the tenant had offered a forged certificate of occupancy for the apartment. The trial court then held that there was no breach of lease, awarded possession to the landlord and denied the landlord's request for attorney fees in excess of $90,000. The landlord appealed and the court recognized that attorney fees are not recoverable as damages in the absence of a contract or statute. The state's FED statute provided for the award of attorney fees as part of the compensatory damages to the prevailing party in an FED action. The trial court had found that the landlord's claim was based on the illegality of the lease, but the appellate court disagreed. It

concluded the claim and relief granted were for FED and that the landlord was entitled to fees. It therefore remanded for a determination and award of reasonable attorney fees to the landlord. *Wilcox* v. *Clark*, 2000 WL 33542592, Court of Appeals No. 99CA0994 (Colo. App. 2001).

Guarantees

A guarantor of the debtor corporation's secured debt was subrogated to the rights of a secured creditor to the extent that the guarantor personally paid the debt owed to the creditor. Moreover, the surplus remaining after the proceeds from the sales of the debtor's assets and the guarantor's residence were used to satisfy the debt, belonged to the guarantor. *In re Cornmesser's, Inc.*, 264 B.R. 159 (Bankr..W.D.Pa. 2001).

A lessor wanted individuals to guarantee a corporate tenant's lease personally. The tenant presented two officers as guarantors, one of whom was broke and submitted an outdated financial statement. The lessee defaulted on the lease and the lessor sued both the tenant and one of its officers, claiming the officer knew about and participated in a scheme to defraud the lessor. The trial court granted the officer's motion for summary judgment and awarded attorney fees. The lessor appealed and the court affirmed. The court noted an officer could be personally liable for fraud and there was evidence the officer knew that the guarantor's financial situation was questionable. However, the court found no evidence to prove that the officer knew about the scheme to defraud the lessor. In addition, the court rejected the lessor's argument that the claim was not based on the lease and thus not governed by the clause awarding attorney fees to the prevailing party. It therefore affirmed all but the award of prejudgment interest on the attorney fees. *DGHI Enterprises* v. *Contini*, 2001 WL 1187151, No. 47383-2-I (Wash. App. Div. 1, 2001).

A lease signed and personally guaranteed by the president of the corporate tenant expired, and the tenant held over for more than two years. The parties then signed a "lease agreement and extension" that was retroactive to the expiration date. No personal guarantee of the extension was executed, but the guarantor of the original lease signed the extension in his capacity as vice president. After the tenant defaulted, the landlord sued the guarantor. At trial, the court granted summary judgment for the guarantor. On appeal, the landlord argued the lease was extended and the guarantee should continue. The appellate court disagreed, finding that the lease was not an extension but a new lease and that the guarantee could not continue without the unambiguous agreement of the guarantors. However, the court concluded that the facts might support a finding of estoppel against the vice president who signed the contract because he would benefit from the continuation of the business at the same location. The court remanded for a trial on the issue of estoppel. *The Sherwin-Williams Co.* v. *ASBN Inc.*, 550 S.E.2d 527 (N.C. App. 2001).

A lessor sued the lessee and guarantor for unpaid rent, and the guarantor raised the affirmative defense of failure of consideration. The guarantor argued the lease did not expressly require his guarantee or mention a guarantee by a third party. The guarantee, however, stated it was made for "good and valuable consideration . . . and in consideration of the landlord entering into the Lease. . . ." The court framed the issue as the adequacy of consideration for the execution of the guarantee, not execution of the lease. The guarantor objected to the admission of parol evidence to prove consideration, but the court found that caselaw supported its admission in these circumstances. The court reviewed the evidence and the cases cited by the guarantor to support his argument that execution of a lease cannot serve as consideration when the lease was signed before the guarantee. It determined that agreements that are collateral to, not inconsistent with, and that do no vary or contradict, the contract's terms, are enforceable. The guarantee in the instant case fulfilled those criteria and was, thus, enforceable. It concluded there was sufficient evidence there was consideration given to enforce the guarantee. *Windham* v. *Cal-Tim, Ltd.*, 47 S.W.2d 846 (Tex. App.-Beaumont, 2001).

Landlord & Tenant

A landlord signed a lease with a prospective tenant who had purchased an existing profitable business and wanted to move to the landlord's strip center because he thought it would be a more profitable location. The new space had numerous building code violations, and the tenant wanted additional improvements made before he would occupy the space. The lease enumerated the improvements, and the tenant stated repeatedly that time was of the essence and he could not afford interim rent. The landlord submitted plans that did not remedy the building code violations and the building inspector rejected them. The renovations were never completed, and the tenant was not able to open for business because of the landlord's delays in construction. The tenant sued the landlord for breach of contract, seeking lost profits. The jury returned a verdict in the tenant's favor and the landlord appealed, arguing the amount of the verdict was too high and there was no evidence to support breach of the lease. The appellate court examined the lease, agreed it was ambiguous and found that extrinsic evidence regarding the parties' intent had been necessary, and the trial court had not erred in refusing to grant judgment notwithstanding the verdict. The court then reviewed the law of contracts and held that lost profits were recoverable if they were within the contemplation of the parties, were the probable result of the breach and were not speculative. The court concluded that all three criteria were met, especially because the tenant had bought an existing business with a proven track record of profits. It, therefore, affirmed the verdict in the tenant's favor. *Abboud* v. *Robertson*, 2001 WL 876191, No. 78028 (Ohio App. 8 Dist., 2001).

A tenant leased premises to operate a restaurant and was assured by the leasing agent that she could open by a certain date. The opening was delayed because the tenant was unable to obtain the necessary permits due to a restrictive covenant requiring her to obtain a variance for parking spaces. She opened well after the original date. When the restaurant began to fail, she ceased paying rent. The landlord sued for eviction and won by default. He then sued for damages and argued that the court's judgment in the eviction case was *res judicata* and barred the tenant's counter-claim for damages. The appellate court rejected the landlord's argument, finding that summary procedure statutes do not provide for the determination of all issues between the parties. The tenant was not

obligated to and did not assert all equitable defenses. Therefore, there was no adjudication of the merits of her counter-claim. In addition, the court rejected the argument that the tenant could not claim she was defrauded because the restrictive covenant was a matter of public record. A search for a restrictive covenant is not expected to be performed as standard procedure by a party before entering a commercial lease. *Camena Investments and Property Management Corp.* v. *Cross,* 791 So.2d 595 (Fla. App. 3 Dist. 2001).

A month-to-month tenant notified the landlord he intended to vacate the premises due to the landlord's failure to make certain repairs. The landlord sent a letter outlining the terms of a new five-year lease that was to commence the following day. The tenant vacated, but not before the deadline imposed by the landlord had passed. Four years later, the landlord sued for unpaid rent under the five-year lease. The tenant counter-claimed, alleging the suit was frivolous and groundless. The tenant then filed a motion for summary judgment on statute of limitations grounds and alleged there was no evidence to support a valid and enforceable lease and no evidence of damages. The trial court granted the tenant's summary judgment motion and the landlord appealed. He argued there was no evidence he had been served with a copy of the summary judgment motion and the tenant had failed to provide him with evidence of service. The appellate court rejected both arguments, finding there was no evidence of a meeting of the minds to form the lease and no evidence of ratification merely because the tenant failed to vacate the premises in less than 24 hours. *Dhingra* v. *Mendelow,* 2001 WL 1136149, No. 14-00-00770-CV (Tex.App. - Hous. (14 Dist.) 2001).

The previous landlord sold the property that the tenant occupied on a month-to-month basis, to a third party (the "new landlord"). The new landlord increased the rent on the month-to month lease. The tenant paid the increased rent for one month, then reverted back to payment of the prior monthly rent. The new landlord served the tenant with an eviction notice after the tenant failed to pay the increased rent for five months. The landlord sued the tenant for unpaid rent and other expenses, and the tenant counter-claimed and filed a third-party complaint against the previous landlord, claiming that the tenant and previous landlord had an oral agreement regarding the tenant's right of first refusal on an option to purchase the property. The tenant claimed that he had made improvements to the property in reliance on the oral agreement. The tenant argued that the improvements he made constituted part performance that should remove the oral agreement from the Statute of Frauds. The landlord's motion for summary judgment was granted, and the tenant appealed. In addition to certain procedural rulings, the appellate court held that the landlord never waived its right to collect unpaid rent by accepting the tenant's payment of the lower rent as partial payment. Furthermore, the improvements made by the tenant were not sufficient to obviate the Statute of Frauds because there was no proof that the improvements were made in reliance on the oral agreement and not for some other purpose. The tenant's subjective belief that he might purchase the property at some point in the future was insufficient to obviate the Statute of Frauds. *Edgbarton Investment Co., LLC* v. *Target Expediting Inc., et al.,* 757 N.E.2d 380 (Ohio 2001).

A tenant leased premises to operate a restaurant and bar. The landlord filed a rent and possession claim when the tenant failed to pay rent for several months. At trial the tenant offered to pay the back rent, and the landlord agreed to dismiss the case. Before the case was dismissed, the landlord terminated the lease and filed an unlawful detainer action. The trial court awarded the landlord possession of its property, and the tenant appealed. The tenant argued the landlord had elected its remedies by filing a rent and possession action. The court of appeals disagreed. It held that the election of remedies doctrine applies where the remedies are inconsistent. In this case, rent and possession are not inconsistent with unlawful detainer. Moreover, case law has held that summary proceedings are cumulative and not inconsistent. Thus, the doctrine of election of remedies did not apply, and the court affirmed the lower court's decision not to dismiss the unlawful detainer action. *Ellsworth Breihan Bldg. Co.* v. *Teha Inc.,* 48 S.W.3d 80 (Mo. App. E.D., 2001).

A tenant at will gave less than the 30 days' required notice before he vacated the premises, owing utilities arrearage. The landlord changed the lock on the premises, and the tenant subsequently broke the lock to enter the room where some of the tenant's furniture had been stored. The landlord swore out a warrant for criminal trespass, but by the time the sheriff arrested the tenant the statute of limitations had run out and no indictment could be issued. The tenant then sued the landlord for malicious prosecution, defamation and false imprisonment. The trial court granted summary judgment to the landlord, and the appellate court affirmed. It found that there was probable cause for the warrant when it was issued and, thus, there was no question of fact regarding the malicious prosecution claim. It also affirmed summary judgment on the claims of defamation and false imprisonment. Defamation could not be based on privileged court documents and the tenant had not been unlawful and, thus, could be falsely imprisoned or detained because the warrant had been validly issued. *Erfani* v. *Bishop,* 553 S.E.2d 326 (Ga. App. 2001)

A landowner failed to pay taxes on commercial property and the property was sold at a tax sale. Before the sale was confirmed, the landowner signed new leases with the tenants and continued to collect rents. After confirmation of the sale, the purchaser and tenants negotiated for a new lease, but were unable to agree. The purchaser began to charge a higher rent, and the tenants refused to pay the increase and would not vacate the premises. The purchaser sued to evict them, and the trial court ordered the tenants to pay the rent deficiency and vacate the premises. The tenants appealed, arguing they had a prior lease with the original owner and that the purchase was the owner's agent. The appellate court rejected their arguments, finding that the tax sale and confirmation extinguished any existing leases on the property, that there was no evidence of an agency relationship, and that the purchaser and tenants entered into a tenancy at will on a month-to-month basis. The appellate court affirmed the finding in favor of the purchaser. *Euclid Plaza Assoc., LLC* v. *African American Law Firm, LLC,* 58 S.W.3d 446 (Mo. App. E.D. 2001).

A landlord served the tenant with a notice to cure, alleging the tenant was in breach of its lease by operating a video and computer game arcade without a license. The tenant filed an

action seeking a declaration that he was not in breach of the lease and made a motion for a preliminary injunction preventing the landlord from terminating the lease (Yellowstone injunction). The trial court denied the motion for the injunction and the tenant appealed. The appellate court found that the tenant had established he had the ability and was willing to cure the alleged defaults listed on the notice sent by the landlord by any means short of vacating the premises. The court reversed and granted the Yellowstone injunction. *Heon Lee* v. *TT & PP Main Street Realty Corp.*, 729 N.Y.S.2d 775, 2001 N.Y. Slip Op. 07020 (2d Dep't 2001).

The owner of almost 25% of the beneficiary interest in a trust whose major asset was a shopping center sued the trustee for breach of fiduciary duty. The complaint alleged the breach involved entering into substandard leases with the majority of the shopping center tenants. The trial court entered judgment in favor of the beneficiary, and the trustee appealed. The appellate court affirmed as to all counts except the one involving the shopping center leases. It held there was no evidence that it was standard in the industry to obtain triple net leases from the tenants. Nor was there evidence that the rents the trustee negotiated were below market. The appellate court thus found there was insufficient evidence to prove the trustee was negligent in failing to obtain triple net leases from the tenants. *Hochhauser* v. *Jacobson,* 795 So.2d 232 (Fla. App. 4 Dist. 2001).

A landlord hired a contractor to repair the tenant's roof. The contractor left holes in the roof, resulting in leaks that damaged the tenant's premises. Despite the tenant's complaints, the landlord, its managing agent nor the contractor took steps to repair the holes. The tenant sued the landlord for breach of the lease's covenant of quiet enjoyment and the landlord, managing agent and contractor for negligence. The court recognized the landlord's common-law duty to avoid negligent acts, which would include reasonable care in choosing an independent contractor and to ensure the work was done properly. The manager owed the same duty to the tenant as the landlord because it was the landlord's agent. The contractor also owed a common-law duty to the tenant to avoid foreseeable harm. The court held that the tenant stated an adequate claim against the three defendants. The court, however, dismissed the claim for punitive damages and held that the exculpatory clause in the lease was void as against public policy, according to the state's Landlord and Tenant Act. *Hinkle Engineering, Inc.* v. *175 Jackson LLC,* 2001 WL 1246757, 01 C 5078 (N.D. Ill. 2001).

A tenant's parking lot lease expired after several renewals, and the tenant ceased paying rent. After 11 months, the landlord demanded further rent, claiming the tenant was holding over. When the tenant failed to respond to the landlord's demands, the landlord sued. The tenant moved for summary judgment, which the trial court granted, rejecting the landlord's arguments that the tenant was holding over. The landlord contended that the tenant had erected a fence, shrubs and curb bumpers, and continued to pay real estate taxes. The tenant responded that the fence was erected to separate and protect the landlord's property and that he offered to remove it when the landlord informed him it was on the landlord's property. The tenant also claimed that it installed shrubs and bumpers pursuant to local ordinances and that it had erroneously paid the taxes. It stored no equipment or vehicles on the property after the lease expired and pointed out that the landlord had not demanded rent for 11 months after the lease expired. The landlord appealed the summary judgment, and the appellate court affirmed. It found that a holdover requires an implied agreement that the tenant intends to continue the landlord/tenant relationship. It held that the evidence did not support an intent to hold over. *Inzetta* v. *The Ohio Bell Telephone Co.,* 2001 WL 438700, No. 00AP-1084 (Ohio App. 10 Dist. 2001).

A lease obligated the tenant to pay guaranteed minimum rent and taxes, and permitted the landlord to evict the tenant if rent went unpaid for 10 days after notification of nonpayment. The tenant paid the overdue taxes but did not pay the rent, and the landlord evicted him. The tenant filed bankruptcy and later sued the landlord for wrongful eviction, fraud and breach of an oral modification of the lease. The jury found for the tenant and the landlord appealed. The appellate court found that there was no evidence of new consideration to support the alleged oral modification of the lease, allowing the tenant to pay rent beyond the 10 days after notice. The appellate court also concluded the trial court had erred in admitting the bankruptcy court's opinion to prove the existence of the oral modification because the landlord was not a party to the bankruptcy proceedings. The court also held that because the landlord had no duty to disclose the sale of the premises, it had not committed fraud by failing to do so. Finally, the appellate court held that there was some evidence that the landlord may have waived enforcement of the lease provisions regarding the due date of the rent, and it affirmed the jury's finding against the landlord. The court remanded for a new trial of the claim for wrongful eviction. *McCutchin* v. *Addison Texas, Inc.,* 2001 WL 910940, No. 05-98-0918-CV (Tex. App. - Dallas 2001).

The sole tenant in the landlord's building operated a woodworking business that produced a quantity of sawdust on a daily basis. The tenant claimed its employees shut off all power and cleaned up the sawdust each day. When a fire destroyed the building, the Fire Marshall ruled the cause of the fire was unknown, but a private investigator concluded the tenant's negligence caused the fire. The landlord sued the tenant for breach of lease based on the tenant's negligence and its obligation to insure the building and its contents. The trial court found for the tenant and the landlord appealed, arguing that the court should have found the tenant negligent as a matter of law and the court erred in not applying *res ipsa loquitor* to infer the tenant's negligence caused the fire. The landlord also contended the court erred when it failed to consider the accumulation of sawdust as a cause of the fire. The appellate court disagreed. It found that the trial court understood and correctly applied the doctrine of *res ipsa loquitor,* that the court was never asked to find the tenant negligent as a matter of law, and that there was evidence in the record from which the trial court could conclude the origin of the fire was unknown. The court was not required to draw the inference that the tenant's negligence caused the fire. *Wilson* v. *Cooke,* 26 P.3d 822 (Or. App. 2001).

Leases

A lease provided that nonpayment of rent was a default and after notice of three such defaults within 12 months, no further

notice was necessary and the landlord could re-enter the premises, terminate the lease or terminate the tenant's possession. After three notices of nonpayment, the landlord filed an action for summary ejectment. The tenant admitted it did not pay rent because it thought the landlord was overcharging and the landlord was not fulfilling its obligations under the lease. The trial court granted the landlord's motion for summary judgment, and the tenant appealed. The appellate court rejected the tenant's arguments that the trial court had no subject matter jurisdiction, that genuine issues of fact existed regarding the landlord's overcharge for late fees and obligation to make repairs, and that the tenant had been constructively evicted. However, the appellate court agreed that the landlord failed to terminate the lease properly and, therefore, had no authority to file an action for summary ejectment. The three notices of default were not sufficiently clear and unequivocal to notify the tenant that the landlord was terminating the lease. A dissenting opinion reasoned that the landlord's words were clear enough to cause the tenant's leasehold estate to have "ceased" pursuant to statute. *ARE-100/800/801 Capitola, L.LC.* v. *Triangle Laboratories, Inc.*, 550 S.E.2d 31 (N.C. App. 2001).

A tenant suffered losses due to a fire caused by arson and subsequent vandalism. It sued the landlord, alleging its failure to secure the leased premises after an initial fire had caused further damage. The tenant sought damages for lost business, equipment, improvements and business opportunity. The landlord argued the tenant had delayed in calling the fire department, and the delay absolved the landlord of liability for damages to the tenant's property. The landlord moved for summary judgment; the tenant objected, arguing there was a question of fact regarding whether the provision would protect the landlord from its own negligence. The court reviewed the law regarding contracts and ambiguity, examining the lease language in question. It concluded there was no ambiguity. The use of the words "any" and "all" to describe the allocation of risk left no doubt that the risk of loss fell on the tenant. It granted the landlord's motion for summary judgment. *B &D Associates, Inc.* v. *Russell*, 2001 WL 822545, CV980263199S (Conn. Super. 2001).

A tenant leased a space for use as an antique warehouse and flea market. It had previously been used for a non-retail warehouse and the city determined that the building now needed emergency exits, lighting, additional off-street parking, handicapped restrooms and sprinklers. The tenant claimed the landlord was responsible for installing the sprinkler system, never occupied the interior of the building and eventually stopped paying rent. The landlord sued for nonpayment of rent, and the trial court granted the landlord's motion for summary judgment. The tenant appealed, arguing the lease required the landlord to do the initial cleanup and repair. The landlord replied that it had done so, and the tenant was required to give written notice of any inadequacy in the cleanup. The court disagreed with the landlord and found that the provision requiring notice did not apply to the initial cleanup, but to subsequent defective conditions of which the landlord would not be aware. The court thus reversed summary judgment for the landlord regarding its responsibility for code compliance. The parties knew the condition of the building when they signed the lease and did not allocate to the landlord the responsibility for any improvements. Instead, the tenant undertook the responsibility to make the space suitable for its intended use. The final objection concerned the use of the premises as an apartment and the landlord's obligation to make it suitable for that use. The court found no obligation of the part of the landlord for the residential use. *Baird* v. *Kelley*, 551 S.E.2d 810 (Ga. App. 2001).

A landlord sued for money damages arising out of the breach of two restaurant leases. The tenants did not answer or appear and the court entered a default judgment against both tenants in a combined amount greater than $27 million. The tenants appealed, arguing that the trial court erred in denying their motion for relief from the judgment based on "mistake, inadvertence, surprise or excusable neglect." The appellate court rejected the argument because there was no evidence to support it and because under the state law those defenses are inapplicable once legal counsel is retained in the case. The tenants also argued fraud, misrepresentation or misconduct based on the landlord's failure to serve notice of substitution of parties or of the motion for default judgment. The court rejected both contentions. The appellate court found merit in the tenant's final argument, however, that the landlord had a duty to mitigate before enforcing the acceleration clause in the lease. The court reversed the decision and remanded for a hearing to determine whether the landlord had mitigated and whether the tenant was entitled to a credit for payment of certain funds. *Castle Hill Holdings VII, LLC* v. *Midland Food Services, II, LLC*, 2001 WL 1194804, , Case No. 2001AP010003 (Ohio App., 5 Dist. 2001).

A lease to a laundromat tenant provided that 15% of the coin receipts would be paid as rent to the lessor semiannually. The lessor wrote the lessee in January saying that although he had accepted three late payments in the past, future payments were due on January 2 and July 2 of each year. When no rent was paid on July 2, the lessor sent a five-day notice to pay rent or quit. When no rent was paid within the five-day period, the lessor filed a Forcible Entry and Detainer action, seeking rent and possession. The trial court granted the lessee summary judgment but the appellate court reversed. It reviewed both dictionary and caselaw definitions of "semiannually" and found that it ordinarily means "at the expiration of each half year from the date of the agreement." To accept the lessee's definition that rent could be paid at any two times a year would be inconsistent with Illinois law and any reasonable commercial bargain that requires a regular accounting. Furthermore, the lessor remedied any possible waiver of his right to enforce the lease by writing the letter and sending the five-day notice. *Fox* v. *Commercial Coin Laundry Systems*, 2001 WL 1061798, No. 1-00-3820 (Ill. App. 1 Dist. 2001).

A lease contained an option providing for one five-year term at the "then prevailing market rental rate as determined by the landlord in good faith." The tenant filed suit in district court but then filed a Chapter 11 proceeding. The amount of rent owed under the lease was central to determining the reorganization plan. The landlord filed a proof of claim for rent and costs under the lease and the tenant objected. The bankruptcy court allowed the landlord rent, late fees and attorney fees, and the tenant requested reversal of attorney fees

because the landlord had not prevailed on the issue of rent. The tenant argued the landlord did not set the rate in good faith. The landlord moved for summary judgment, arguing it was undisputed that the tenant had not paid any increase, but the amount of rent due remained a question. The tenant also objected to the award of attorney fees. The federal district court concluded that the bankruptcy judge had heard and received evidence and determined the rate for the renewal period. He also heard evidence regarding attorney fees and made findings as to allowable fees pursuant to a proof of claim. The federal district court would not disturb the finding of the state district court and bankruptcy court that there was no bad faith. It therefore affirmed the award of attorney fees to the landlord. *In re 44 H Inc.* v. *Catellus Development Corp.*, Civil Action No. 157 F.Supp.2d 1175 (D.C. Colo. 2001).

A lease required the tenant to procure insurance on the landlord's real property and authorized the landlord to obtain the insurance and require the tenant to reimburse the landlord for the premiums. It further required delivery of certificates of insurance. The tenant failed to obtain the insurance and, after a tornado damaged the leased premises, the landlord sought to recover damages based on the tenant's failure to procure the insurance. The tenant claimed his understanding was that he would insure his personal property and the landlord would insure the real property. Neither party delivered certificates of insurance to the other at the lease signing. The landlord's attorney did request proof of insurance, but did not follow up on the request. The appellate court found there were questions of fact regarding whether the landlord decided to purchase its own real property casualty insurance, and the tenant's failure to do so was a result of the landlord's representations and failure to enforce the lease requirement that the landlord obtain insurance. There was also a question regarding whether the landlord had waived the requirement or was estopped from enforcing it. The court found the non-waiver provision in the lease ambiguous as to whether the landlord's failure to insist upon strict performance of a provision waived enforcement of a past performance but not of future performance. *Mahsa, Inc.* v. *Al-Madinah Petroleum, Inc.* 552 S.E.2d 876 (Ga. App. 2001).

A tenant leased about 4-$^1/_2$ % of an industrial complex under a lease that listed as part of the CAM fees "5% of all tenant rents collected at the industrial complex from all tenants." The tenant paid the fees for three years without objection, but filed a complaint against the landlord for breach of contract and declaratory judgment, claiming the landlord had overcharged for fees not permitted in the lease. The tenant's president testified at trial that he was unaware the fees would be 5% of all rent collected from the complex. The trial court found in the landlord's favor. The tenant appealed, and the appellate court determined that parol evidence could be used because the contract was unclear. Testimony by real estate professionals established that 5% of all income was reasonable. Moreover, the tenant had an attorney, had the right to obtain an accounting and did not question the fees until it filed suit. The appellate court affirmed the decision in favor of the landlord. *Mentor Industrial Complex Ltd. Ptrshp.* v. *North Coast Wood Products Inc.*, 2001 WL 822450, Case No. 2000-L-116 (Ohio App. 11 Dist. 2001).

A lease provided that rent would be paid in exchange for the use of "approximately 8,700 square feet." The tenant occupied the premises for three years without complaint and then discovered the premises were not 8,700 square feet. The tenant complained to the landlord about the square footage and the payment of management fees and electric charges, and sued the landlord for breach of contract and fraud. At trial, the tenant presented evidence that the premises were 7,235 square feet and it was not customary to charge management fees as additional rent. The landlord's representative testified that the lease was not based on the square footage and that it was customary to charge management fees as additional rent. The jury found that the landlord had breached the lease, but found that the tenant was not harmed by the breach. It awarded the tenant attorney's fees. On appeal, the court found that the main issue of the case was about money, i.e., whether the tenant had been overcharged. Because the jury had not awarded the tenant monetary damages, the tenant was not the prevailing party under the lease and, therefore, was not entitled to attorney's fees under the lease. The appellate court ruled that the landlord was entitled to damages and remanded to the trial court to determine the amount of fees due. *Pinehurst/ Fairmount Ptrs. LP* v. *Concrete Productions, Inc.*, 2001 WL 832351, No. 05-00-01223-CV (Tex. App. - Dallas (2001).

A mortgage company leased premises under a lease signed by its branch operators, who were not officers of the corporation. The landlord filed an action for Forcible Entry and Detainer against the corporation and then amended the complaint to include the branch operators, alleging breach of lease and nonpayment of rent. The trial court found that the corporation had ratified the lease and entered judgment against the corporation and branch managers. The corporation appealed, arguing the trial court erred in finding it liable because the branch operators personally guaranteed the lease and had agreed with the corporation to be personally liable for rent due under the lease. The corporation also objected to the finding of ratification. The appellate court initially noted that any agreement between the corporation and the branch operators had no effect on the contract between the landlord and the corporation. It was an indemnification agreement and was, in fact, the basis for the corporation's cross-claims against the operators. The appellate court then stated that because there was no transcript of the proceedings below it was obligated to presume the proceedings were correct and affirm the judgment of the trial court. *Taranga Properties, Ltd.* v. *Ohio Mortgage Co.*, 2001 WL 1105136, No. 78979 (Ohio App. 8 Dist. 2001).

Shop-Rite, a tenant in a shopping center, sued Chestnut Hill, the landlord, and another tenant, Odd Job, for breach of contract and tortious interference with its lease with Chestnut Hill. The Shop-Rite lease contained an exclusive covenant to sell groceries, and Odd Job was selling items that Shop-Rite considered to be groceries. Odd Job's lease with Chestnut Hill obligated Chestnut Hill to pay Odd Job's costs and fees if it were brought into litigation because of Chestnut Hill's acts or omission. Odd Job sought costs and fees from Chestnut Hill on the grounds that Chestnut Hill leased to Odd Job without informing Odd Job of the restrictions in Shop-Rite's lease. The court examined Chestnut Hill's arguments and concluded that Odd Job was entitled to summary judgment because it was

operating within the confines of its own lease and that it was "dragged into this suit solely because of Chestnut Hill's claimed act or omission," i.e., Chestnut Hill's alleged breach of the Shop-Rite exclusive covenant. The court noted that only one of Chestnut Hill's arguments was worthwhile, i.e., that Odd Job's lease prohibited it from selling grocery items. However, the court doubted the argument was made in good faith and was not supported by its prior acts concerning other tenants' leases. It, therefore, granted Odd Job's motion for summary judgment. *Wakefern Food Corp.* v. *Chestnut Hill Plaza Holdings Corp.*, 2001 WL 515069, No. 18040 (Del. Ch. 2001).

Lenders

A contract provision for a prepayment premium as part of a lender's oversecured claim was unreasonable and would not be allowed. It represented roughly 18% of the debtor's prepayment, and the lender presented no evidence regarding the change in interest rates since the loan was made or the damages it had sustained due to the debtor's prepayment. *In re Schwegmann Giant Supermarkets Ptrshp.*, 264 B.R. 823 (Bankr..E.D.La. 2001).

Options

The tenants leased commercial space for a ten-year, five-month, term, with a five-year renewal option. The renewal option provided that the new rent "shall be the greater of (a) base rent for the last year of the original term or (b) the then existing market rental rate for comparable shopping centers." The landlord informed the new tenant that the new rent would be $29.50 per square foot, which was comparable to the rent charged in other shopping centers. The tenants objected and filed a declaratory judgment action. The trial court severed the clause providing that the renewal rent would be the market rental rate for comparable properties. The parties agreed that under state law the provision was vague and indefinite because it provided no method by which a certain price could be calculated. The trial court concluded that the provision was an unenforceable portion of the lease agreement and determined that part (a) was the appropriate rent. The appellate court reversed, holding that although part (b) of the renewal option was unenforceable because it was indefinite language, it was also an integral part of the lease agreement and could not be severed because it provided a formula for determining the price of the lease. The appellate court held that severability was inappropriate in this case. *AMB Property, L.P. et al.* v. *MTS, Inc.*, 551 S.E.2d 102 (Ga. App.2001).

J.S.K. entered a contract with New Plan Realty Trust for a tax-free exchange and a leaseback to J.S.K. of one of two tracts of shopping center property. J.S.K. sued for a declaratory judgment that there was an oral option to purchase the leased tract and for rescission on the grounds that New Plan misrepresented that it would grant J.S.K. an option to purchase. The district court held that J.S.K. failed to prove a meeting of the minds existed with respect to the option agreement and also failed to meet its burden of proof for rescission on the grounds that New Plan misrepresented that it would grant J.S.K. an option to purchase. On appeal, the Fourth U.S. Circuit Court of Appeals held J.S.K. concluded that the evidence supported the finding that there was no meeting of the minds regarding an oral option documented by notes on a file folder. The parties should have known the statute of frauds requires a written agreement; the lease contained a merger clause, which was clear and unambiguous, requiring no parole evidence. Furthermore, because J.S.K. failed to prove New Plan misrepresented there was an enforceable oral option to purchase, it did not justifiably rely on the option to purchase real property. *J.S.K. Realty Co.* v. *New Plan Realty Trust*, 9 Fed. Appx. 89 2001 454512 (4th Cir. 2001).

A court was asked to enforce a consent decree that confirmed the right of State Teachers' Retirement System (STRS) to purchase a shopping center from Kenwood Plaza Limited Partnership (KPLP). The parties disputed the amounts that could be deducted from the purchase under the option which permitted reductions for "closing costs and normal prorations" and the payment of attorney fees and expenses by the party that failed to comply with the consent decree. STRS argued that it should receive a reduction for asbestos removal, but the trial court held that asbestos removal had been considered in the purchase price and was not a normal proration. The court also found that it was custom and practice for each party to pay its accounting and legal fees unless the document clearly provided otherwise. The remaining payments on a lease termination agreement for a below-market lease were also the purchaser's responsibility because the purchaser benefited from the empty space. Percentage rent should be apportioned based on the number of days each party owned the property. The appellate court affirmed the trial court's findings and concluded that because the purchaser did not prevail in its appeal, it was the non-complying party under the consent decree and, therefore, responsible for attorney fees and costs. *Kenwood Plaza Ltd. Ptrshp.* v. *State Teachers' Retirement System Board of Ohio*, 2001 WL 1077939, Appeal No. C-000730 (Ohio App. 1 Dist. 2001).

An option to extend a lease required written notification six months before expiration of the lease term. The tenant failed to notify the landlord until more than six-and-a-half months beyond the date required in the lease. The landlord rejected the tenant's notification and informed the tenant that the building was being sold to the tenant's competitor. The tenant then sued the landlord for breach of fiduciary duty, unfair trade practices, and breach of the covenant of good faith and fair dealing, *inter alia*. Six weeks later, while the tenant's action was pending, the landlord sued to evict the tenant. The tenant counter-claimed, alleging breach of the landlord's fiduciary duty. The court granted the landlord's motion to dismiss the tenant's counter-claim under the prior pending action doctrine. The tenant appealed the dismissal and the appellate court found that the present case and prior pending case involved the same parties, the same factual background, and sought the same goals or obligations. It held the tenant was continuing to litigate the question of the landlord's fiduciary duty in the prior pending action and could not argue it before this court. It affirmed dismissal of the counter-claim and grant of summary judgment. *Modzelewski* v. *William Raveis Real Estate, Inc.*, 2001 WL 1053544, AC 20580, 21150 (Conn. App. 2001).

A lease for a laundry room in an apartment complex gave the lessor, John Hancock, the option to terminate if the lease were assigned without the lessor's permission. The lessee's assets, including the laundry room lease, were purchased by CoinMach, which took immediate possession and began to

operate the machines. No approval for the assignment was ever obtained from the lessor, John Hancock, and three years later, the lessor sold the apartment complex to KCC. KCC then informed CoinMach it was exercising its option to terminate the lease unless CoinMach provided documents showing the assignment was approved. KCC signed a lease with Jetz conditioned upon proper termination of the lease with CoinMach, but CoinMach refused to vacate the premises. Jetz filed a petition to quiet title and moved for summary judgment.. The trial court granted Jetz's motion and CoinMach appealed. The appellate court held that John Hancock, KCC's predecessor, had failed to exercise its option to terminate in a timely manner. There was evidence that John Hancock knew about the assignment and did not terminate the lease. KCC's terminating the lease three years later would prejudice CoinMach by depriving it of its justifiable expectations. The appellate court reversed the grant of summary judgment to Jetz and remanded. *Jetz Service Co., Inc.* v. *KC Citadel Apartments, LLC,* 2001 WL 1220921, WD 59696 (Mo..App. W.D. 2001).

Permits

There was no due process violation by a county that denied a developer's application for a comprehensive plan amendment to permit a planned unit development with residential, retail and office space in a rural area. *Martin County* v. *Section 28 Partnership Ltd.,* 772 So.2d 616 (Fla. Dist. Ct. App. 2000).

Owners who had a valid permit made substantial changes to property and incurred substantial expenses. Where they had undertaken construction in good faith and relied on ordinances in existence at the time the permit was issued, and the town later approved the phased construction of the project, the owners had a vested right to complete the construction. *Sahl* v. *Town of York,* 760 A.2d 266 (Maine 2000).

Public Access

A supermarket was charged with Unfair Labor Practices by the NLRB when it sought to exclude union members from passing out leaflets in the store pickup area and adjacent parking lot and dismissed an employee associated with the Union movement. The supermarket appealed the NLRB's order and the Fourth U.S. Circuit Court of Appeals affirmed in part and denied in part. The Fourth Circuit basically held that the employer could not threaten to close the store or dismiss an employee for his union activities. However, the court reviewed the lease language giving the supermarket the right to prevent trespassing and noted the union had alternative means of communicating with employees. The court also examined relevant caselaw and stated that under *Hudgens* v. *NLRB,* 424 U.S. 507 (1976), a shopping center owner can prevent picketing on private property. The court concluded that because union organizers were not "members of the public who might benefit" the supermarket, their intrusion was unlawful. The court, therefore, refused to enforce the parts of the NLRB's order that required the supermarket "to renounce the authority to prevent handbilling by the union organizers." *Weis Markets, Inc.* v. *NLRB,* 265 F.3d 239 (4th Cir. 2001), *Cert. Den'd* at 120 S.Ct. 54 (2001).

Receivership

The guarantor of the purchaser of a building made several payments to the seller pursuant to the guarantee and then sued the purchaser to recover the payments. Subsequently, the guarantor moved for the appointment of a receiver to collect rents, pending settlement of the suit. The court granted the request in an order that directed the receiver "to take any and all steps necessary to gain access to unoccupied portions of the subject property…and allow secured parties and their authorized agents…access." When the receiver petitioned to be dismissed and requested fees, the guarantor objected to the fee request, arguing that the receiver had exceeded the authority granted by the order because he had done more than be a passive collection agent and gatekeeper. The trial court found that the situation required the receiver to do more, that the order contemplated that he might do more and that he should be compensated. The appellate court affirmed, noting that the award of fees is within the trial court's discretion and would not be reversed absent a showing of abuse. The court rejected all the arguments advanced by the guarantor and affirmed the trial court's award. *Mycon* v. *Mycon,* No. 2001 WL 537873, No. 46525-2-1 (Wash.App., Div 1.2001).

Tort Liability

A tenant's employee was injured when he walked into an air-conditioning unit on the leased premises. He sued the landlord to recover for personal injuries, and the court denied the landlord's motion for summary judgment. On appeal the court found that a landlord court be liable for a dangerous or defective condition on leased premises if it "contracted by a covenant to be responsible for repairs, if performance of the covenant would have presented an unreasonable risk of harm, and if the landlord failed to exercise reasonable care to perform his obligations under the lease." In this case, the tenant had installed the air- conditioning units after taking possession, and the lease required the tenant to repair and maintain the units. Consequently, the tenant, not the landlord, was responsible for any injuries caused by a defective condition created by the air-conditioning units. *Brilliant* v. *DCVM Realty,* 284 A.D.2d 289, 725 N.Y.S.2d 372 (2d Dep't 2001).

A minor suffered injuries after he entered a storage area closed to the general public in a shopping mall and became caught in a conveyor belt system. The minor's father, a tenant of the shopping mall, sued the landlords, *inter alia,* alleging that the landlords should have foreseen harm to the child, that the landlords owed the child a duty of reasonable care and that the landlord's negligence was the proximate cause of the child's injuries. The court dismissed the case, granting the landlord's summary judgment motion. The court, citing *Kahn* v. *James Burton Co.,* 5 Ill. 2d 614, 615, 126 N.E. 2d 836 (1955), held that children generally have no greater rights to trespass than adults. The owner had no duty to trespassers unless he knew, or should have known, that children frequent the area; that a defective or dangerous condition was present, which was likely to injure children; and that the expense of repair was slight when compared to the danger to children. In this case, the landlord could not have known that children frequent an area of the shopping mall that was closed to the public. Furthermore, the court held that the plaintiff failed to demonstrate, either through argument or supporting affidavits, which parts of the belt were unreasonably dangerous to hold the defendant-manufacturer responsible for the child's

injuries. The court also found that the landlord was not the proximate cause of the child's injuries because it was not reasonably foreseeable that a child would enter an area of the mall that was closed to the public. *Luu* v. *Kim,* 752 N.E.2d 547 (Ill. App. 1 Dist. 2001).

A woman was injured when she slipped on oil spilled in the aisle of a Home Depot. She sued the store but the trial court granted Home Depot's motion for summary judgment, on the grounds there was no liability. She appealed. No oil was sold in the aisle where she fell, but the department manager and loss prevention supervisor saw some teenagers playing in the aisle that sold oil where the injured customer slipped. Home Depot's policy was to monitor teens so that they did not cause a hazard to other shoppers. The appellate court held there were issues of fact regarding Home Depot's liability. There was evidence that employees knew that these non-shoppers regularly played in the store and had spilled things before. It was, therefore, foreseeable that they might spill something that could be hazardous to shoppers. There was also evidence that Home Depot did not follow its own policies when the loss prevention manager failed to ask the teens to leave. Thus, the appellate court reversed the grant of summary judgment to Home Depot and remanded for a trial on liability. *Medley* v. *The Home Depot,* Inc., 2001 WL 1083734, (Ga. App. 2001).

A landlord may have breached its duty to maintain a safe premises by failing to erect a firewall on the leased premises. *Walter Champion Co.* v. *Dodson,* 2001 WL 1231007, A01A1204, A01A1205 (Ga. App. 2001).

From Canada

Negotiating in Good Faith or Negligence—Is Any Duty Owed?

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The Supreme Court of Canada, in the decision of *Martel Building Ltd.* v. *Her Majesty the Queen* (1997), 129 F.T.R. 239; Aff'd. [1998] 4 F.C. 300; Rev'd [2000] S.C.J. No. 60 (F.C.) (*"Martel"*), dismissed the notion that one party to lease negotiations can claim pure economic damages as a result of the negligence of the other party in those negotiations. In addition, it laid to rest, at least for now, the notion that one party to lease negotiations has a duty to negotiate in good faith with the other.

There are two previous cases in Canada where the courts have determined that under an ongoing lease, the duty of good faith existed:

- *Empress Towers Ltd.* v. *The Bank of Nova Scotia* (1990), 73 D.L.R. (4th). In this case, the renewal clause provided that rent for the renewal term would be the market rent as agreed upon between the parties. The British Columbia Court of Appeal determined there was an implied covenant that the parties would negotiate in good faith for the renewal rent and that neither party would act unreasonably in withholding its agreement on a proposed market rent; and
- *Gateway Realty Ltd.* v. *Arton Holdings Ltd.* (1991), 106 N.S.R. (2d), 180 (F.C.); *Aff'd.* 122 N.S.R. (2d) 180 (C.A.). In this case the issue was whether the landlord was acting reasonably in withholding its consent to a proposed assignment. The Nova Scotia Court of Appeal determined that there was an implied duty on the landlord to act in good faith in looking at the tenant's request.

The *Martel* decision differs from these previous decisions in that the issue in *Martel* was whether there was a duty of good faith in the conduct of commercial negotiations to a lease, as opposed to the previous cases, which dealt with an obligation of good faith between parties to an existing lease.

Martel Facts

In *Martel*, the landlord leased in essence all of its office building, under a ten-year lease, to the federal government as tenant. The lease did not contain an option to renew, but did contemplate the possibility of a renewal lease. Approximately two years before the expiration of the term of the lease, the landlord contacted the tenant to commence negotiations regarding a renewal lease.

The facts of the negotiations between the landlord and the tenant are somewhat convoluted, but the following are the salient points:

- The landlord was continually kept in the dark by the tenant during the approximately one-and-one-half years of negotiating regarding the tenant's position with respect to many items, including whether the tenant was intending to go to a tender process, or would instead decide to renew with the landlord, and the tenant's bottom line;
- At a crucial meeting, the landlord was led to believe that if it could meet a certain rental rate, the tenant would not go to tender and would accept the landlord's offer.

On the strength of this understanding, the landlord renegotiated its mortgage, and then advised the tenant that the landlord could offer the rental rate identified by the tenant. However, after advising the landlord of the tenant's drop dead date, and after receiving the above offer from the landlord, the tenant wished to negotiate further regarding the landlord's proposed retrofit details.

The tenant requested numerous pieces of information regarding these details, and only allowed the landlord three hours to obtain this information. The landlord was unable to meet this three-hour deadline. The tenant then proceeded to tender, and ultimately notified the landlord that the tenant had decided to accept the tender of a competitive landlord, and had rejected the landlord's tender because the tenant's fit up costs were higher for the landlord's building than for the landlord's competitor. This was the first time the landlord had been made aware of the requirement of any fit up costs on the part of the tenant.

Martel Decision

The landlord sued the tenant, arguing:

1. There was a breach of an implied term in the lease that there would be a renewal of the term;
2. The tenant had failed to negotiate in good faith;

3. The tenant's actions during the negotiations amounted to negligence, giving rise to damages.

The trial court, the Court of Appeal and the Supreme Court of Canada all rejected the landlord's first argument. With respect to the duty to negotiate in good faith, the Court held that no duty yet existed in Canadian law. It is interesting to note that the Supreme Court of Canada did leave the door open that perhaps sometime in the future such duty could be found to exist in Canadian law.

With respect to negligence, the trial court concluded that the tenant owed the landlord a duty of care, and the tenant had breached that duty of care during the conduct of its negotiations. However, the tenant's negligence did not cause the landlord to lose the lease renewal, and therefore there was no proximity between the landlord's damages and the tenant's negligence.

The Federal Court of Appeal overturned the trial court decision and held that a duty of care existed, that duty of care had been breached by the tenant, and that there was a link between the landlord's loss of the renewal and the tenant's negligence; therefore, the tenant was liable to the landlord for damages.

The tenant appealed to the Supreme Court of Canada.

In looking at the negligence claim, the Supreme Court of Canada first ascertained that the landlord's damages amounted to a pure economic loss (i.e., a loss not accompanied by other physical harm or property damage). The Court also concluded that the alleged negligence of the tenant in the lease did not fall within the existing five recognized categories of actions that would give rise to compensable pure economic damages. The Court, therefore, embarked on a discussion as to whether a new category ought to be created for this type of negligence.

The Supreme Court of Canada refused to create such a new category based upon the following policy considerations:

The goal of parties to commercial negotiations is to realize a financial gain at the expense of another party. Socially and economically useful conduct would be deterred by depriving a party of its ability to maintain any advantageous bargaining position in commercial negotiations. Labeling a party's failure to disclose during negotiations its bottom line, its motives or its final position as negligent conduct would defeat the essence of negotiations. Tort law would become after-the-fact insurance against the failure by either party to act with due diligence in commercial negotiations. Alternatively, in order to hedge the risk of failed commercial negotiations, courts would be asked to scrutinize the details of pre-contractual conduct. Recognizing this as a new category would create needless litigation, and should be discouraged.

For all of the above reasons, the Court concluded that any duty of care owed by the tenant to the landlord was outweighed by the disastrous effects that would be occasioned by extending this duty of care into the conduct of commercial negotiations, where the alleged damages amounted to pure economic loss.

In summary, according to *Martel*, the Court concluded that a duty of care existed between the tenant and the landlord because the landlord and the tenant had a long-standing (ten-year) relationship; the tenant was in essence the only tenant in the landlord's building; the tenant was a dominant player in the office leasing market in the geographical area where the landlord's building was located; and the lease itself contemplated the possibility of a renewal lease.

The Court nevertheless held that it is not possible for a landlord or tenant to claim damages stemming from the other's negligence in the lease negotiations because the landlord's damages were only economic and were not accompanied by other physical harm or property damage; the conduct of the tenant did not fall within the existing recognized category of conduct that gives rise to successful claims for pure economic loss, and the Court, on policy reasons, did not wish to create a new category. The issue of whether there is an implied covenant between parties to commercial negotiations, each to act in good faith toward the other, has not yet been prohibited and, perhaps in the future, this is where parties will have success.

Judicial/LegislativeDevelopments

Cases

ALBERTA

The tenant argued that it was induced into entering the lease as a result of negligent misrepresentations made by the landlord at the time of the lease negotiations. The tenant's claim for damages was dismissed because the tenant failed to present any evidence regarding misrepresentations upon which the tenant acted to its detriment. *Pasta Franchised Developments Ltd.* v. *Omers Realty Corporation* [2001] A.J. No. 596 (Court of Queen's Bench, March 30, 2001, Beilby J.).

The owners of certain lands attempted to circumvent the municipality's subdivision controls through various schemes wherein tracts of land were leased—as opposed to being sold outright. The schemes were illegal because they violated the purposes of the municipality's subdivision control legislation. *Half Moon Lake Resort Ltd.* v. *Strathcona (County)* [2001] A.J. No. 220 (Alberta Court of Appeal, February 27, 2001, McClung, Hunt and Berger JJ.A.).

The tenant was not liable for injuries sustained by an individual who slipped and fell on a public sidewalk adjacent to the tenant's business despite the fact that a municipal by-law required the tenant to remove snow and ice from the sidewalk. The tenant was not an occupier under the applicable legislation because the tenant was not in physical possession of the sidewalk. Further, the tenant did not owe the individual a duty of care at common law because that duty does not arise from an obligation imposed by a municipal by-law to clear snow and ice. *Koch* v. *Slave Lake Jewellers Ltd.* [2001] A.J. No. 685 (Court of Queen's Bench, May 22, 2001, Burrows J.).

The lease provided that the tenant could exercise its option to renew six (6) months prior to the end of the Primary Lease Term. The tenant argued that this meant it could exercise the

option at any time *during* the six-month period prior to the expiry of the initial term. The landlord's interpretation was upheld: the tenant could only exercise the option *prior* to the commencement of the last six months of the term. *McEwen Square Ltd.* v. *Ellis* [2001] A.J. No. 691 (Court of Queen's Bench, April 24, 2001, Master Funduk).

A caveat filed by an assignee of a lease was sufficient to protect its interest in the lease despite the fact that the original tenant had not filed a caveat. The caveat was also sufficient to protect the assignee's renewal option although no specific reference had been made to the renewal in the caveat. *Golden View Investments Ltd.* v. *Centrecorp Management Service Ltd.*, A.J. No. 1500 (Court of Queen's Bench, December 12, 2000, Acton J.).

MANITOBA

It was alleged that the Municipal Board of Manitoba failed to consider, as required by statute, whether certain business assessments bore a fair and just relationship to the assessed value of all business premises in the City of Winnipeg. The common complaint was that the assessor included a notional common area maintenance charge in determining the annual rental value for some, but not all, business premises. Leave to appeal was denied on the grounds that there was evidence before the Board to support its finding that the statutory requirements had been met. *Black Photo Corp.* v. *Winnipeg (City) Assessor* [2001] M.J. No. 275 (Manitoba Court of Appeal, June 11, 2001, Philp J.A.) together with various others.

A supermarket breached its lease by failing to operate its business in the premises despite the fact that the lease did not contain a continuous operating clause. The supermarket, being an anchor tenant, had an obligation to the landlord and to the other merchants in the shopping centre to remain open for business. *Nickel Developments Ltd.* v. *Canada Safeway Ltd.* [2000] M.J. No. 614 (Manitoba Court of Appeal, May 29, 2001, Twaddle, Kroft and Monnin JJ.A.).

NEW BRUNSWICK

At a meeting between the parties, the landlord proposed that the tenant could renew its lease for a term of four years. A formal renewal agreement was never executed but the tenant began to perform some of its obligations under the verbal renewal agreement. The landlord subsequently sought to terminate the tenancy, taking the position that the offer it had proposed to the tenant contained only the minimum terms that the landlord was willing to accept and that there were to be additional terms to be discussed. The landlord's claim was dismissed because an existing agreement to lease was found to be in place. The verbal agreement was enforceable as it had been partly performed. While it was not clear that the landlord had advised the tenant that there were additional terms to be negotiated, there was an onus upon the landlord to present those terms to the tenant in a timely fashion. *505292 N.B. Ltd. (c.o.b. Create A Stir)* v. *Tri Wave Holdings Ltd.* [2001] N.B.J. No. 214 (Court of Queen's Bench, May 30, 2001, Glennie J.).

NOVA SCOTIA

The landlord's distress was legal despite some irregularities. The irregularities included a failure to show the proper amount of rent on the notice of distress and a failure to obtain sworn appraisals. Despite the irregularities, damages were not awarded because the tenant had failed to prove that it sustained special damages—as is required under the *Tenancies and Distress for Rent Act*. *Elia* v. *Treger* [2001] N.S.J. 196 (Nova Scotia Supreme Court, May 28, 2001, Hamilton J.).

The new owner of a commercial property sought possession of the tenant's premises on the grounds that the tenant was a month-to-month tenant. The tenant asserted that it had entered into a five-year lease with the prior owner, notwithstanding the fact that a formal agreement had not been executed. A review of the correspondence exchanged between the prior owner and the tenant revealed that the correspondence amounted to a binding offer to lease. It was irrelevant that the prior owner and the tenant had not reached an agreement on several ancillary issues. *Delvay Construction Inc.* v. *Kelly Insurance Services Inc.* [2001] N.S.J. No. 163 (Nova Scotia Supreme Court, May 8, 2001, Goodfellow J.)

ONTARIO

The lease did not provide a mechanism for apportioning hydro, gas and water disposal charges to the tenant. The tenant argued that it should have been charged an amount that was fair and reasonable— having regard to the tenant's actual use and not on a proportionate share basis. The tenant's claim was dismissed on the basis, *inter alia,* that the parties had, in fact, agreed that the tenant would pay its proportionate share, notwithstanding its actual use. The tenant's claim for relocation costs was also dismissed on the grounds that the costs were not recoverable by the tenant because they had been personally incurred by the tenant's principal and not by the tenant. *1005285 Ontario Ltd.* v. *1118531 Ontario Ltd.* [2001] O.J. No. 2879 (Ontario Superior Court of Justice, July 5, 2001, McDermid J.).

The franchisee of a Mr. Submarine outlet was granted an order declaring a neighbouring Quizno's store to be in breach of a restrictive covenant that was registered on title and which prevented the sale of "food, food products or meals." An injunction was also granted prohibiting Quizno's from selling those food products that were in *direct competition* of those sold by Mr. Submarine. The restrictive covenant was enforceable despite the fact that Mr. Submarine had acquiesced in allowing other neighboring units to sell food products in violation of the covenant. *1012728 Ontario Inc.* v. *Falconvest Inc.* [2001] O.J. No. 1488 (Ontario Superior Court of Justice, April 20, 2001, B. Wright J.).

The tenant wished to exercise its option to renew but failed to give written notice to the landlord within the time period set out under the lease. Having failed to comply strictly with the terms of the lease, the tenant had no legal entitlement to continue the tenancy. In addition, there were no equitable grounds upon which the tenant could remain in possession of the premises. *1175220 Ontario Inc.* v. *Steve Rossi Ltd.* [2001] O.J. No. 2643 (Ontario Superior Court of Justice, June 25, 2001, Pitt J.).

The tenant had withheld the payment of rent for several months, arguing that the landlord's ongoing failure to repair a leaking roof adversely affected the tenant's business. The matter was ordered to be resolved by way of a trial because the landlord and the tenant had advanced conflicting views regarding the state of repair of the roof of the leased premises. In the meantime, an injunction was granted preventing the landlord from distraining for arrears of rent or from otherwise interfering with the tenancy until the conclusion of the trial. The tenant was also ordered to pay approximately one-half of its monthly rent into court and the other half to the landlord. *1352879 Ontario Inc.* v. *Del Rosso* [2001] O.J. No. 3064 (Ontario Superior Court of Justice, Motions Court, July 30, 2001, Somers J.).

The landlord was not able to distrain against the tenant's goods after the tenant failed to pay rent strictly in accordance with the terms of the lease. It could not be said that the tenant was in arrears because, *inter alia,* despite the usual conduct between the parties, the landlord had made no effort to contact the tenant to collect the rent. In addition, the landlord's conduct in acquiescing to payment of rent on any day of the month was sufficient to permit the tenant to think that its payment method was acceptable. *1401231 Inc.* v. *Computer Mind Inc.* [2001] O.J. No. 1679 (Ontario Superior Court of Justice, April 8, 2001 (released April 25, 2001), Platana J.).

The owners of two shopping centres failed to repay their loans on the due date. The bank issued a notice of intention to enforce its security nearly three months after the loan due date and also sought an accounting of the rents that had been collected over the three-month period. The debtor owners were not obligated to account for the rents because the relevant wording of the assignment of leases and rents did not result in the bank's acquiring an absolute assignment of the rents *prior* to issuing a notice of its intention to enforce its security. *Canadian Imperial Bank of Commerce* v. *Conway* [2001] O.J. No. 3027 (Ontario Superior Court of Justice, July 26, 2001, Molloy J.).

The tenant was prejudiced when new trustees of an association were elected and the former trustees would not turn over to the new trustees the tenant's post-dated rent cheques (title to the property was held by the trustees on behalf of the association). The new trustees subsequently distrained for arrears of rent. The distress was unlawful because the tenant was not in breach by refusing to pay rent to the new trustees. *Divinec* v. *526799 Ontario Ltd. (c.o.b. Europa Catering)* [2001] O.J. No. 925 (Ontario Superior Court of Justice - Divisional Court, March 15, 2001, Then, Carnwath and Lederman JJ.).

Dylex Bankruptcy

The bankruptcy of Dylex initially began with a stay of proceedings under the *Companies' Creditors and Arrangement Act.* The stay was subsequently terminated and replaced with an Order appointing Richter & Partners Inc. as Interim Receiver of Dylex under the *Bankruptcy and Insolvency Act*. Pursuant to this second Order, the Receiver was given control of all leased premises and was authorized to solicit offers to purchase all or parts of the BiWay and Fairweather chains. All lease transfers were to be in accordance with the terms of the respective leases. The Receiver was also given the ability to repudiate any lease upon not less than seven days' notice. The Order also contained stringent terms regarding the payment of occupation rent by the Receiver (including a "Landlords' Charge" in respect of any unpaid occupancy rent), and the right of the Receiver to remove fixtures from the leased premises.

By way of an Order imposed by Justice Spence on September 4, 2001, the court approved the sale of several BiWay stores to Dollarama A.M.A. Inc. and others to Denninghouse Ltd., subject to the rights of landlords to be paid arrears of rent as a condition of any assignment of lease and also subject to the rights of landlords under the respective leases (i.e., respecting use, assignment).

On September 28, 2001, a further order was granted authorizing the sale of the Fairweather chain to an unspecified purchaser, but without the requirement that the corresponding assignments be conditioned on payment of rental arrears, and upon the further clarification that the approval order did not constitute approval within the meaning of Section 38(2) of the *Bankruptcy and Insolvency Act*. Immediately following the making of that order, a receiving order was issued and Dylex Limited was adjudged bankrupt (with effect as of September 28, 2001). *Dylex Proceedings Under the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act,* Court File Nos. 01-CL-4216 and 31-OR-206758-T.

The tenant operated a cinema for almost 30 years before it closed for business in violation of a continuous operating covenant in the lease. The lease expired almost 18 months later, at which point the tenant sought to remove its trade fixtures. The landlord argued that title to the trade fixtures had passed to the landlord and that the tenant had no right to remove them. A review of the lease revealed that the tenant was entitled to remove its trade fixtures. *Famous Players Inc.* v. *J.D.S. Investments Limited/Vista Sudbury Hotels Inc.,* Court File No. A-9319/01 (Ontario Superior Court of Justice, July 27, 2001, P.C. Hennessy J.).

Without notice, in response to the tenant's announcement that it would soon be closing its store, the landlord forcibly removed the tenant from the premises and terminated the lease. Thereafter, the landlord did not allow the tenant to

remove its goods from the premises on the grounds that title passed to the landlord under the terms of the lease. The landlord could not prohibit the tenant from removing its goods because the lease provision upon which the landlord sought to rely only applied in circumstances where the tenant abandoned the premises and left its goods behind. It did not give the landlord title to the tenant's goods where the tenant had been forcibly removed from the premises. *Fortino's Supermarket Ltd.* v. *Mount Albion Plaza Inc and Fengate Property Management Ltd.*, Court File No. 00-2648 (Ontario Superior Court of Justice, November 29, 2000, Philp, J).

The landlord applied for a writ of possession for the premises. The landlord complained that there were several incidents of nuisance that occurred outside of the tenant's premises. The application was dismissed on the basis that any of the other businesses in the landlord's strip mall could have been the cause of the nuisance. *Golden Mine Construction Co.* v. *Golden Cue Billiards & Sports Bar Ltd.* [2001] OJ No. 2161 (Ontario Superior Court of Justice, May 30, 2001, E. Macdonald J.).

The tenant purported to grant a sublease but, in fact, made an assignment of the lease because the tenant failed to reserve part of the term. Having assigned the lease, the option to purchase passed to the so-called subtenant at the time of the assignment and, as such, it was no longer exercisable by the tenant. The tenant was unsuccessful in arguing that Section 3 of the *Commercial Tenancies Act* allows for the granting of a sublease without the necessity of having to reserve part of the term. *Goldman* v. *682980 Ontario Ltd.* [2001] O.J. No. 3005 (Ontario Superior Court of Justice, July 23, 2001, Hawkins J.).

An agreement entered into in 1992 served to renew the existing lease between the parties and did not serve as an entirely new lease. However, the tenants were not required to pay the landlord's insurance premiums because it was incumbent on the landlord to show that the premiums were properly chargeable. Having failed to present any evidence with respect to the nature of the insurance charges, the landlord failed to discharge its legal burden. *Humber* v. *Associated Respiratory Services Inc. (c.o.b. ARS Vitalaire)* [2001] O.J. No. 1970 (Ontario Court of Appeal, May, 30, 2001, Osborne A.C.J.O., Doherty and MacPherson JJ.A).

The head landlord exercised a right of termination contained in the lease as an alternative to consenting to the head tenant's application for consent to an assignment. The head landlord's option to terminate was not a right of re-entry or forfeiture and, as such, the subtenant was not entitled to apply for relief under Section 21 of the *Commercial Tenancies Act*. Further, Section 98 of the *Courts of Justices Act*, which also provides for relief against penalties and forfeitures, was likewise inapplicable. *Maverick Professional Services Inc.* v. *592423 Ontario Inc.* [2001] O.J. No. 1877 (Ontario Court of Appeal, May 18, 2001, Morden, Catzman and Feldman JJ.A.).

The landlord successfully appealed a decision of the Federal Court Trial Division, which had been called upon to determine the rents payable under certain land leases. The landlord's contention was that the trial judge applied a 40% discount factor to the fair market value of the lands in question without basing it on any finding of fact (contrary to the Supreme Court of Canada's decision in *Musqueam Indian Band* v. *Glass)*. A new trial was ordered. *St. Martin* v. *Canada (Ministry of Indian Affairs and Northern Development)* [2001] F.C.J. No. 1052 (Federal Court of Appeal, April 4, 2001, Isaac, Sexton and Sharlow JJ.A).

QUEBEC

The tenant registered its original lease on title but failed to register several subsequent amending agreements whereby the tenant pre-paid its rent to the landlord. When the property was later sold, the purchaser sought to recover rent from the tenant. The tenant was required to pay rent to the purchaser despite the fact that it had already been paid to the previous landlord. The purchaser was only bound by the registered lease and not by the unregistered amendments. *2682982 Canada Inc.* v. *Compagnie 390 Saint Jacques, Nova Scotia,* CA 500-09-010008-001.

The lease required Zellers to pay a tax on capital—but did not provide a method of calculating the tax. After GE Capital acquired the property, it sought to recover federal and provincial capital taxes from Zellers. The court held that the provision was unenforceable due to the fact that it was vague. *GE Capital Realty Management Inc.* v. *Zellers Inc.*, CA 500-09-000522-946.

The vendor and purchaser had tried to avoid the payment of mutation tax through the use of a scheme wherein the property was first transferred to a newly incorporated subsidiary of the vendor. The scheme was not exempt from mutation tax. *Produits Forestiers Alliance Inc.* v. *Donnacona (Ville de).*, CA 200-09-002588-991.

A guarantor of a commercial lease was not responsible for rent that remained unpaid while the tenant had been overholding. Articles 1881 and 2345 of the Civil Code provide that the obligations of a guarantor do not apply to the extension or renewal of a term. *Iberville Developments Leasing Ltd.* v. *Koutsoulis,* CQ 500-02-093269-012.

SASKATCHEWAN

The owner of a commercial property was granted an interim injunction, thereby preventing a neighbouring Canadian Tire store from proceeding with its expansion plans. The proposed expansion by Canadian Tire would interfere with the adjacent owner's access and parking rights as granted under an agreement between the parties. *Westcor Properties Inc.* v. *Canadian Tire Corp.* (2000), 201 Sask. R. 125 (Q.B.).

The tenant argued that the landlord failed to repair the roof of the premises. The landlord had not breached its repair covenant but, in any event, the tenant was not entitled to withhold the payment of rent on account of the alleged breach. Additionally, the landlord could not charge the tenant for rent after it had effectively terminated the lease by taking possession of the premises. *Yuan* v. *Mah Investments Ltd.* (2001), 205 Sask. R. 22 (Q.B.).

Legislation

MANITOBA

The Board of Revision and the Municipal Board have the ability to alter assessments and to otherwise determine the fair market value of an assessment for a property. In certain circumstances, the Bill also makes it mandatory for assessors to give notice when the assessor wishes to request the Municipal Board to increase an assessed value. The Bill comes into force on January 1, 2002.

ONTARIO

Oak Ridges Moraine Protection Act, 2001, S.O. 2001, c. 3—The Act essentially froze all development on the Oak Ridges Moraine for the period commencing May 17, 2001, and ending November 17, 2001.

Bill 90–Waste Divirsion Act, 2001—The Bill seeks to establish and develop a waste diversion program for the Province of Ontario. The program will be run and administered by a corporation named Waste Diversion Ontario. Companies that produce or are otherwise connected to certain types of waste may be required to help fund the program.

Bill 67–Ontario Energy Board Amendment Act (Electricity Rates), 2001—The Bill limits the increases that the Ontario Energy Board can approve with respect to the rates that distributors charge for distributing electricity to consumers in certain prescribed years. The limits mirror the percentage annual increase in the Consumer Price Index for Canada (all items).

Bill 70–Occupational Health and Safety Amendment Act (Workplace Violence), 2001 (Private Member's Bill)—The Bill amends the Occupational Health and Safety Act such that significant duties are placed on employers and employees with respect to acts of workplace violence (which includes both physical and psychological violence). The Bill, *inter alia*, requires that employers develop a written code of conduct with respect to workplace violence and that employees receive adequate training in connection with their rights and obligations under the legislation. Employees are also required to report to their employer all acts of workplace violence.

Bill 24–Municipal Amendment Act (Adult Entertainment Parlours), 2001 (Private Member's Bill)—The Bill seeks to regulate adult entertainment parlours. The Bill requires that the operators of such parlours obtain licenses from the local municipality. The Bill also gives municipalities the power to pass by-laws requiring persons to be licensed to work in an adult entertainment parlour. The Bill also prohibits an operator from employing someone who is under 18 years of age.

Bill 6–Protection of Minors from Sexually Explicit Goods and Services Act, 2001 (Private Member's Bill)—The Bill prohibits the sale of sexually explicit goods or services to minors.

SASKATCHEWAN

The Land Titles Act, 2000 S.S. 2000, c. L-5.1; *The Land Surveys Act, 2000* S.S. 2000, c. L-4.1; and *The Condominium Property Act, 1993* S.S. 1993, c. C-26.1—The legislation serves to assist the Province of Saskatchewan in the implementation of its revamped land registry system. The new system includes an automated system for Land Titles and converts the existing information in Land Titles offices into an electronic database. Under the new system, Duplicate Certificates of Title will no longer be required for transactions in the Land Titles system.

This update was prepared by Natalie Vukovich and Joseph Grignano (Daoust Vukovich Baker-Sigal Banka LLP, Ontario) with the assistance of Blair C. Yorke-Slader (Bennett Jones LLP, Alberta), Murray F. Tait (T&T Properties, Alberta), Douglas J. Mathews (Stewart McKelvey Stirling Scales, Nova Scotia), Stephen J. Messinger (Goodman and Carr LLP, Ontario), Glen R. Peters (Fillmore Riley, Manitoba), Fredric L. Carsley (Mendelsohn, Rosentzveig, Shacter, Quebec), and R. Neil MacKay (MacPherson Leslie & Tyerman, Saskatchewan).

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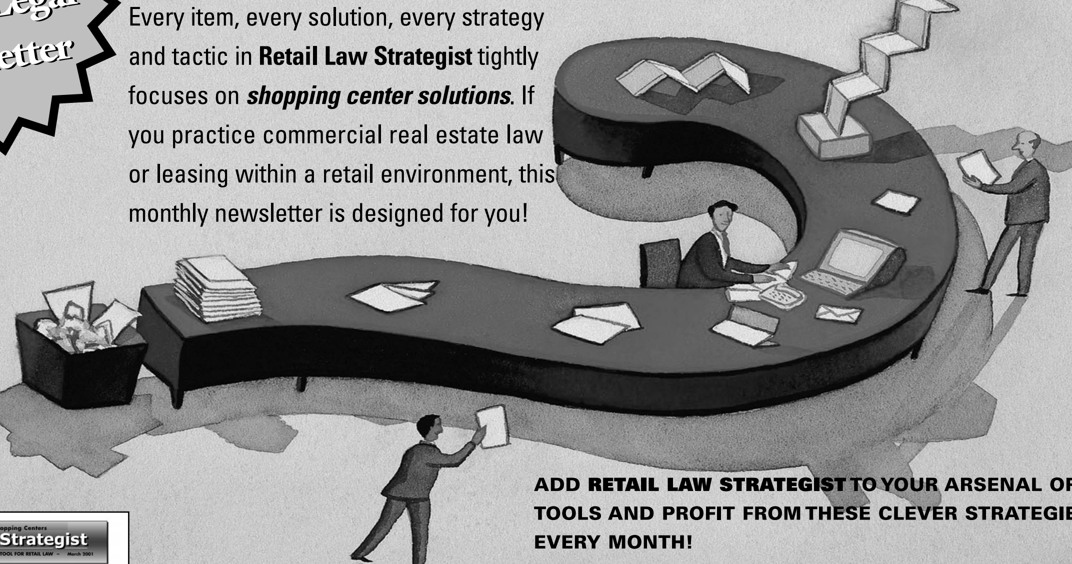

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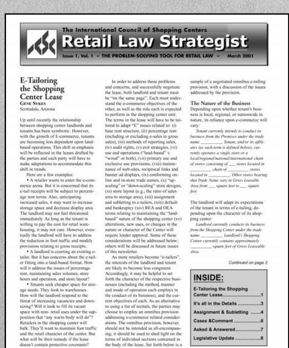

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