

IN PRACTICE

COMMERCIAL LEASING

By GARY K. WOLINETZ

Can Untimely Attempts To Exercise Renewal Options Be Enforced?

The timely exercise of an option to renew a long-term commercial lease can be a trap for the unwary. See *Goodyear v. Kin Properties*, 276 N.J. Super. 96, 102 (App. Div.), cert. denied, 139 N.J. 290 (1994). Renewal option clauses are often complex and may cross-reference not only a master lease but a sublease or even a sub-sublease. Since the lease is long-term and subject to assignment, the parties who created — and understood — the renewal option are often not the parties who must exercise the option years later.

There are a variety of reasons why a landlord may elect to enforce strictly the cutoff date in a renewal option. Obviously, a tenant who refuses to commit to a renewal term in hopes of finding a better deal leaves the landlord, perhaps subject to a mortgage or a lease if it is also a tenant, little choice but to enforce the renewal option and secure a new tenant if the existing tenant does not act timely.

Additionally, a landlord receiving below-market rent from a tenant entitled to exercise one or more renewal options may seek any opportunity to eliminate the tenant. The landlord may wait patiently for years until a longtime tenant, through a clerical or computer error, fails to properly exercise a renewal option before seeking to remove the tenant from the premises or extracting a significant rent increase as a

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condition of allowing the tenant to renew.

Needless to say, the failure to exercise a renewal clause in a timely fashion may have disastrous consequences for the delinquent tenant if the landlord is intent on strict enforcement of the lease. At best, assuming the landlord did not waive any rights, the tenant can hope for an increase in rent and possibly a more onerous lease. At worst, the tenant may be forced to vacate the premises, with the possible destruction of business.

The Central Conflict

At its heart, the issue of failure to give timely notice focuses on the conflict faced by courts in many commercial tenancy disputes: enforcing a lease as written to preserve business stability and the sanctity of contract versus saving parties from their inadvertent blunders on equitable grounds. See, *Liqui-Box v. Estate of Edelman*, 238 N.J. Super. 588, 600 (App. Div.), cert. denied, 122 N.J. 142 (1990); *Sosanie v. Perneti Holding Corp.*, 115 N.J. Super. 409, 416 (Ch. Div. 1971) ("the function of a court is to enforce a lease as it is written not to write for the parties a different or better contract"). Typically, the relevant inquiry will focus on the length of the tenant's delay in exercising its renewal rights and whether the landlord will be prejudiced if it is forced to accept the late notice. Id. at 416.

Three Chancery Division cases that illustrate these principles are *Goldberg Corp. v. The Goldberg Realty & Investment Co.*, 134 N.J. Eq. 415 (Chan. 1944); *Marjer v. Layfmen*, 140 N.J. Eq. 68 (Chan. 1947); and *Sosanie v. Perneti Holding Corp.*, 115 N.J. Super. 409. In *Goldberg*, a department

store tenant had the option to renew a 10-year lease for 18 months before the lease expired. *Goldberg*, supra, 134 N.J. Eq. at 417. Claiming that the premises were in need of extensive improvements, the tenant failed to exercise the renewal option in a timely fashion. After several unsuccessful attempts to work out the terms of a new lease, the landlord advised the tenant that it must vacate the premises at the end of the lease because the landlord had rented the premises to a new tenant. Shortly thereafter, claiming the possible destruction of its business, the tenant sought an injunction to bar the landlord from terminating its tenancy and granting it a reasonable time to exercise the renewal option.

Noting the length of the delay (approximately 18 months), and that the negotiations between the parties concerned a new lease and not the option to renew the

At issue is a conflict: enforcing a lease to preserve business stability and the contract's sanctity versus saving parties from their inadvertent blunders on equitable grounds.

existing lease, the court refused to grant the injunction. The court did recognize that "considerations of righteousness, justice or morality must exist to enable a court of equity to rescue parties from the natural and reasonably probable consequences of their own imprudence." Id. at 422-23. However, absent conduct intended to lull the tenant into a false sense of security, such equitable notions could not compel the court to "make a contract for litigants *sui juris* or compel them to contract with each other." Id.

Given the length of the delay and the landlord's reliance on the tenant's conduct, the result in *Goldberg* is hardly surprising. Yet, the case aptly illustrates a court's reluctance to rewrite the leases of commercial parties, even where a tenant's business is threatened.

Marjer v. Layfmen and *Sosanie v. Perneti Holding Corp.* represent the other end of the spectrum. In *Marjer*, a tenant sent the renewal notice in a timely fashion but failed to sign it. 140 N.J. Eq. at 70. The landlord claimed that the notice was ineffective because, contrary to the lease, the unsigned notice did not "irrevocably indicate the tenant's taking up and exercising [the] option." Id. Shortly thereafter, the tenant sought injunctive relief to compel the landlord to renew the lease.

Citing 32 *Am. Jur.*, Landlord and Tenant, sections 975-979, the court articulated the principles that would guide New Jersey courts in evaluating claims of late renewal notices through the present:

There is unanimity in the decisions that equity will relieve against the consequences of a failure to give a notice at the time or in the form and man-

precedent to the renewal of the lease, when such failure results from accident, fraud, surprise, or mistake and there are other special circumstances which have been held to warrant a court of equity in granting relief against the consequences of the lessee's failure to notify the lessor within the stipulated time or in the specific form or manner prescribed. It has been said that equity will not relieve against mere forgetfulness and will not intervene where there is no fraud, accident, or mistake on account of which the lessee neglected to avail himself of the option, and he assigns no explanation or excuse for the delay except his negligence or that of his agent. The matter is one largely of discretion.

Id. at 71-72.

Relying on these principles, and, specifically, the absence of any prejudice to the landlord by the tenant's failure to sign her renewal notice and the possible destruction of the tenant's business, the Chancery Court granted the tenant's application for a preliminary injunction.

Similarly, in *Sosanie*, 115 N.J. Super. 412, operators of a neighborhood pharmacy had the option to renew a five-year lease if they gave the landlord written notice six months before the lease expired. One month after the renewal period expired, the landlord advised the tenants that they had to vacate. Days later, the tenants attempted to exercise the renewal option and sought injunctive relief.

Duty To Remind?

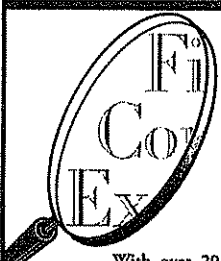
Initially, the court rejected the tenants' argument that the landlord had a duty to remind the tenants that their time to exercise the renewal option was expiring. However, reiterating the standards articulated in *Marjer*, the court emphasized that the tenants' failure to give timely renewal notice may be excused "if fraud, accident, surprise or mistake are shown, or where there are other special circumstances..." Id. at 413.

The *Sosanie* court held that the following factors constituted the requisite "special circumstances" to permit the tenants to exercise the renewal option:

- The tenants would suffer substantial harm if they were forced to relocate;
- The landlord did not change its position in reliance on the tenants' delay;
- The tenants' delay was caused by an honest mistake of fact;
- The delay (approximately one month) was slight and the loss to the landlord insignificant; and
- The landlord had no expectation that the tenants did not intend to renew. Id. at 416.

Sosanie was the last reported case in New Jersey to confront directly whether a tenant who belatedly exercised an option to renew a lease could nevertheless enforce the renewal provision. However, an unreported decision from Judge McGann on this topic, and several recent Appellate Division cases considering closely analogous situations, deserve mention.

In *Food Circus Supermarkets, Inc. v. Mayfair Supermarkets, Inc.*, No. MON-C-82-92 (N.J. Super. Ct. Ch. Div. May 19,



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COMMERCIAL LEASING

CONTINUED FROM PAGE 10

1992), the tenant supermarket (Food Circus) sought to exercise its renewal option approximately three months late. The landlord refused and demanded that the tenant vacate the premises at the expiration of the lease. The tenant sought injunctive relief, claiming that its business would be destroyed (along with many jobs) if it were not permitted to exercise the renewal option.

Judge Patrick McGann Jr. rejected the tenant's excuses and strictly enforced the renewal provision. Relying on *Brick Plaza, Inc. v. Humble Oil*, 218 N.J. Super. 101 (App. Div. 1987), discussed *infra*, Judge McGann explained that the parties were sophisticated entities represented by counsel that had bargained for specific renewal provisions. The judge concluded that, consistent with the clear terms of the lease, Mayfair had the right to enforce those provisions.

Brick Plaza exemplifies the truism that a commercial contract should be enforced as it is written. There, the tenant had a three-month window to exercise an option to purchase contained in a lease.

Purportedly relying on an early draft lease (even though the original was in the possession of its attorney), the tenant sought to exercise the option over five months late. During its occupancy of the leased premises, the tenant had constructed several buildings and spent approximately \$70,000 in repairs.

No Excuse

The Appellate Division rejected the tenant's attempt to exercise the purchase option because "we are presented here not with a 'slight' delay, but one which extended almost five and a half months beyond the expiration of the three month period limited for the giving of notice." *Id.* at 104. The Appellate Division emphasized that "[w]hen an option has been exercised long after the expiration of a specified time, even a party's 'honest mistake of fact' will not excuse its own neglect:

Business people do not enter into agreements to provide grist for the work of the courts. They do so to bring order and predictability to

their affairs. Giving full credit to plaintiff's claim of mistaken honest belief that the option clause made no provision for notice, and taking into account its consequent hardship, to recognize such neglect as excusable and now order the Chancery Division to balance the equities would introduce intolerable uncertainty into a carefully structured contractual relationship. Parties should not be obliged to speculate about how the conscience of a court may define their rights and obligations when an option has been exercised long after the expiration of a specified time. Where the clearly fixed obligations of an optionee have been so grossly breached our interest in preserving the stability of business arrangements outweighs whatever equitable purpose may be served by relieving plaintiff from the consequences of its own neglect

Id. at 105 (emphasis added).

In a slightly different twist, the

Appellate Division recently held in *Goodyear v. Kim Properties*, 276 N.J. Super. 96, that a tenant's notice to exercise a renewal notice was effective even though it was premature. Applying the *Marjer* special circumstances test, the Appellate Division emphasized that this result was appropriate because: the premature notice was the fault of a single employee; the tenant would suffer substantial hardship; and the plaintiffs did not change their position in reliance on the early notice. *Id.* at 103.

New Jersey's treatment of untimely renewal cases reflects a conflict between the strict enforcement position advocated in *Brick Plaza* and the careful weighing of the equities discussed in *Sosanie*. All too often, as *Brick Plaza* notes, the ultimate result depends upon the "conscience of the court," with the obvious uncertainty that causes.

Counsel can reduce this uncertainty. For example, because many long-term tenants fail to give timely notice in a lease because of clerical errors or honest confusion, tenants' counsel should consider incorporating a lease provision imposing a "duty to remind" upon landlords before a tenant loses its right to enforce a renewal option. Alternatively, counsel representing a landlord legitimately affected by a tenant's failure to exercise a renewal option in a timely fashion should advise the landlord to ensure that it carefully document how it changed its position in reliance on the tenant's mistake. ■