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Real Property - Landlord and Tenant - Need for Lessee Who Transfers Whole Term to Base Right of Re-Entry on Condition of "Substantial Advantage" to Him

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REAL PROPERTY—LANDLORD AND TENANT—NEED FOR LESSEE WHO TRANSFERS WHOLE TERM TO BASE RIGHT OF RE-ENTRY ON CONDITION OF "SUBSTANTIAL ADVANTAGE" TO HIM—Plaintiff lessee transferred his interest in the first floor and basement of certain commercial premises for the full remaining period of his own lease, retaining his interest in the second floor, where he lived. This transfer was in form a sublease, under which plaintiff as sublessor reserved power to cancel the sublease and take possession without notice if the premises were used for any purpose other than an off-sale liquor store. Plaintiff's transferee later assigned all his interest to defendant corporation, which immediately began converting the premises into an ice cream store. After defendant had spent over $10,000 in remodeling, plaintiff gave notice that he considered the lease violated, and brought an unlawful detainer action to recover possession. The trial court found for plaintiff. On appeal, *held,* reversed, with direction to enter judgment for defendant. A sublessor who transfers all or part of the premises for the full term may reserve a right of re-entry for failure to perform covenants or conditions in the sublease.[1] This rule applies, however, only if such covenants or conditions contain undertakings of substantial advantage to the sublessor. *Kostakes v. Daly,* (Minn. 1956) 75 N. W. (2d) 191.

When a lessee transfers his interest in leased premises for the full remaining duration of his own lease under an agreement intended as a sublease, the courts have had some difficulty in maintaining a consistent categorization of the transferee's interest in terms of Anglo-American tenurial relationships.[2] If the original landlord's rights are in issue, such a transfer is almost

1 Davidson v. Minnesota Loan & Trust Co., 158 Minn. 411, 197 N.W. 833 (1924); 32 A.L.R. 1418 (1924).

2 See generally Ferrier, "Can There Be a Sublease for the Entire Unexpired Portion of a Term?" 18 CALIF. L. REV. 1 (1929).

always held an assignment of the lease, placing the transferee in privity of estate with the landlord.[3] This privity enables the landlord to assert his landlord's remedies against the transferee for the latter's breach of any obligations which run with the leasehold.[4] The same result is reached when the lessee's entire interest in only a physical part of the premises is transferred, the legal effect being an assignment *pro tanto*.[5] Under this orthodox doctrine, the intended sublease is deemed an assignment because the lessee has reserved no part of the duration of the head lease. A reversionary interest in the lessee transferor is required to support a new tenurial relationship, and reservation of a different rent or of a power of re-entry for breach of covenants or conditions by the transferee does not usually constitute such a reversionary interest.[6] The courts, however, have often allowed a lessee to enforce a right of re-entry—essentially a landlord's remedy—against his transferee under a "sublease" for the entire remaining term. This result may be reached either on the ground that a power of re-entry in the lessee is a "contingent reversionary interest" sufficient to support the sublessor-sublessee relation,[7] or perhaps, more frankly, on the ground that where the parties contract for a sublease, their intention to deal as sublessor and sublessee should be controlling *inter se*.[8] In the principal case the court was

3 Sexton v. Chicago Storage Co., 129 Ill. 318, 21 N.E. 920 (1889); *contra,* Davis v. Vidal, 105 Tex. 444, 151 S.W. 290 (1912); 42 L.R.A. (n.s.) 1084 and note (1913).

4 32 AM. JUR., Landlord and Tenant §371 (1941). The landlord also has a cause of action against his original lessee, who remains liable for infractions of leasehold obligations by privity of contract. Oswald v. Fratenburgh, 36 Minn. 270, 31 N.W. 173 (1886).

5 Wiedemann v. Brown, 190 Minn. 33, 250 N.W. 724 (1933). See also 99 A.L.R. 220 (1935).

6 Sexton v. Chicago Storage Co., note 3 supra; 32 AM. JUR., Landlord and Tenant §317 (1941). *Contra:* Dunlap v. Bullard, 131 Mass. 161 (1881); Davis v. Vidal, note 3 supra. Yet even a token reservation of a day or less will prevent the transfer from being an assignment for any purpose. See Ferrier, "Can There Be a Sublease for the Entire Unexpired Portion of a Term?" 18 CALIF. L. REV. 1 at 17-19 (1929). Also see discussion in 8 MINN. L. REV. 609 (1924) pointing out the hyper-technicality of the rule requiring a reversionary interest to support the sublessor-sublessee relationship.

7 Dunlap v. Bullard, note 6 supra; Davis v. Vidal, note 3 supra. Traditionally, a right of re-entry is not regarded as an estate in land. See discussion of the problem in note, 50 MICH. L. REV. 946 (1952). See also Wallace, "Assignment and Sublease," 8 IND. L. J. 359 (1933), showing how courts have undermined the requirement of a reversion in the lessee to support a subtenancy between him and his transferee by recognizing exceptional contingent and technical "reversionary interests," in efforts to effectuate the contracting parties' intent to create a subtenancy. Shumer v. Hurwitz, 49 Misc. 121, 96 N.Y.S. 1026 (1905).

8 Coles Trading Co. v. Spiegel, Inc., (9th Cir. 1951) 187 F. (2d) 984. See Stewart v. Long Island R.R. Co., 102 N.Y. 601, 8 N.E. 200 (1886), where it is pointed out at 607-608 that classification of a sublease for the entire remaining term as a sublease or an assignment may depend upon whether the original lessor's or the lessee's rights are being asserted against the transferee. The problem is further complicated in the present case by the fact that the defendant was not a party to the contract of sublease, but rather is an assignee of the contracting sublessee. The question is thus whether or not defendant should be bound by the status of sublessee which his transferor had bargained for with the lessee. This extension was made in Davidson v. Minnesota Loan & Trust Co., note 1 supra. Of course the same result follows from the Massachusetts and Texas courts' willingness to call a power of re-entry a "contingent reversionary interest," note 7 supra.

faced with a clear Minnesota precedent allowing a lessee who had "sublet" for the full remaining term to enforce a right of re-entry in the sublease against a defendant who had succeeded to the transferee's interest and had refused to pay any rent other than that reserved in the head lease.[9] The court purported to follow this rule, but added that it is applicable only if performance of the covenants or conditions would be "of substantial advantage to the plaintiff [sublessor],"[10] and distinguished the principal case by deciding as a matter of law that restricting use of the premises to a liquor store was not of substantial advantage to plaintiff. The most that can be said of this distinction is that it is novel. The result may well be defended on its facts,[11] but the asserted grounds of decision are untenable. The court was apparently unwilling to renounce its prior decision and revert to the orthodox approach of denying plaintiff the status of sublessor for lack of a recognizable reversionary interest, thereby refusing to enforce his right of re-entry against defendant. Such unwillingness is to be commended if based on a continued desire to overcome conceptualism in favor of the intent of the parties to the sublease.[12] Yet the case puts a new obstacle in place of the old by requiring the intended sublessor to demonstrate that performance of the covenants or conditions elicited from his transferee would be to his "substantial advantage." This new obstacle cannot help but yield uncertainty. To say as a matter of law that a covenant to pay increased rent is, but a condition restricting use of premises is not, of "substantial" advantage seems more arbitrary than instructive, and undoubtedly will leave a lessee-transferor puzzling over how much and what kind of proof of advantage he must offer in order to obtain enforcement of his right of re-entry. Moreover the restriction on use of the premises, clearly set out in the sublease defendant claimed under, was fully known to all parties.[13] The decision in effect deprives plaintiff of his right to bargain for what he deemed to be to his advantage. It may even be ventured that many might urge as substantially advantageous a provision designed to assure the continued existence of a liquor store downstairs. At any rate, it is regrettable that the court chose this new doctrine rather than reaching the same result upon

9 Davidson v. Minnesota Loan & Trust Co., note 1 supra. Under the "sublease" in that case, the transferee had covenanted to pay the lessee more rent than was reserved in the head lease.

10 Principal case at 194. Note that the court continually refers to the original lessee as "sublessor," although it had previously stressed that he was rather an assignor.

11 The court stressed the unappealing picture presented by the plaintiff, who apparently watched defendant's expensive remodeling operations for almost two months before notifying defendant that he considered the lease broken by use of the premises for other than a liquor store. This was perhaps the real reason motivating the court to adopt its new rationale.

12 See Wallace, "Assignment and Sublease," 8 IND. L. J. 359, especially pp. 384-386 (1933).

13 The court's opinion appears to place no significance on the fact that defendant was an assignee of the transferee rather than the transferee himself, but see note 8 supra.

more candid grounds of estoppel or waiver.[14] That would have preserved the court's prior approach of looking to the contracting parties' intent to create a subtenancy despite feudal concepts of privity, without interjecting new and unpredictable prerequisites to relief.

John A. Beach, S. Ed.

[14] See note 11 supra; Swartz v. Meier, 136 Md. 72, 110 A. 202 (1920); 76 A.L.R. 304 at 317 (1932).