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Judicial relief still not likely upon late or otherwise deficient exercise of an option to renew a lease or purchase premises

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Leases frequently include an option permitting the tenant to renew the term of the lease or to purchase the premises. This article reviews the decision of the New Jersey Supreme Court in *Brunswick Hills Racquet Club v. Route 18 Shopping Center Associates*, 182 N.J. 210 (2005), and subsequent cases addressing the issue of whether an option to renew or purchase in a lease should be honored despite failure to exercise the option in accordance with the precise terms of the lease. Although initially it appeared that *Brunswick Hills* signaled a change in the law in favor of tenants, review of subsequent decisions suggests that *Brunswick Hills* was decided upon its peculiar facts and that equitable relief is rare in these cases.

In *Brunswick Hills*, the Supreme Court reversed the Appellate Division and granted relief to the tenant despite its failure to exercise the option in strict accordance with the terms of the lease. There, the lease contained an option to purchase or convert to a 99-year lease at the end of 25 years upon timely notice of intent to exercise the option by the tenant, together with the payment of \$150,000. The tenant gave timely notice, but did not make the payment, mistakenly believing it was due at closing. The landlord failed to mention the missed payment during the succeeding year and a half, or to respond to the tenant's communications regarding the lease option until the deadline for payment had passed, at which time the landlord announced the option had lapsed. The Court in *Brunswick Hills* granted relief to the tenant, finding that breach of the covenant of good faith and fair dealing was clearly evidenced by a series of evasions and delays by the landlord that lulled the tenant into believing it had properly exercised the option. Although the court ruled in favor of the tenant, it recognized that deference should ordinarily be accorded to the terms negotiated by the parties to an agreement. The court stated: "Ordinarily, we are content to let experienced commercial parties fend for themselves and do not seek to 'introduce intolerable uncertainty into a carefully structured contractual relationship' by balancing equities." However, the court opined that it was not establishing a new duty for commercial landlords to act as calendar clerks for the tenants. The court stated:

Courts generally should not tinker with a finely drawn and precise contract entered into by experienced business people that regulates their financial affairs. Equitable relief is not available merely because enforcement of the contract causes hardship to one of the parties. [Citation omitted.] A court cannot 'abrogate the terms of a contract' unless there is a settled equitable principle, such as fraud, mistake, or accident, allowing for such intervention.

The court observed each case is fact-sensitive so it cannot catalogue the myriad forms of conduct that may constitute a violation of the covenant of good faith and fair dealing.

Significantly, in reaching its decision, *Brunswick Hills* distinguished *Brick Plaza v. Humble Oil & Refining Co.*, 218 N.J. Super. 101 (App. Div. 1987), where the tenant failed to give notice of its intent to exercise an option to purchase the premises until five months after the deadline had passed. There, the tenant who had constructed improvements on the land explained that its late exercise of the option was an "honest mistake" resulting from its president's reliance on an unexecuted draft of the lease agreement. In contrast, in *Brunswick Hills* the court found that the tenant did not sit on its rights as in *Brick Plaza*, but gave notice of its intent to renew well in advance of the option deadline.

Several unpublished decisions subsequent to *Brunswick Hills* suggest that, consistent with prior law, relief will not readily be granted to a tenant who fails to exercise its option pursuant to the terms of its lease.

In *Kings Supermarkets v. Stop & Shop Supermarket Company*, 2006 N.J. Super. LEXIS 2844 (App. Div. 2006), the court found that hardship alone was not sufficient to excuse late exercise of an option contained in a sublease. Kings, as sublessee, gave notice to sublessor Stop & Shop of its intent to exercise the option nine months late, which the sublandlord refused to accept. In an effort to have the court recognize its exercise of the option, Kings argued that it spent substantial monies for store renovations, that it was an important fixture in the community for almost 25 years, and that Stop & Shop knew Kings wanted to extend the sublease. The Appellate Division adopted the reasoning of the trial court, which found that a court cannot abrogate the terms of a contract unless there is a settled equitable principle, such as fraud, mistake or accident allowing for such intervention. The court found no evidence of bad faith and found that Kings' investment of monies and renovations did not alone make it inequitable to enforce the terms upon which the parties had agreed.

The trial court in *Kings* observed that it must be remembered that in *Brunswick Hills*, the court stated that it was not establishing a new duty for commercial landlords to act as calendar clerks for tenants who had slept on their rights, that disregard of contractual terms under the guise of equitable principles is not so easy, and that unlike *Brunswick Hills*, no breach of the covenant of good faith and fair dealing was shown. The Appellate Division in *Kings* distinguished *Sosanie v. Perneti Holding Corp.*, 115 N.J. Super. 409, 414 (Ch. Div. 1971), where the Chancery Division had ruled that where the business was dependent on its location, a slight delay in providing notice of renewal would not prevent the effective exercise of the option.

In *Four Winds Plaza Corporation v. SonValley Developers*, 2008 N.J. Super. LEXIS 705 (App. Div. Aug. 7, 2008), the Appellate Division affirmed a trial court decision refusing to relieve a tenant from its failure to timely exercise its option to purchase. The optioner sought to excuse the purported late exercise of the purchase option because of the supposed ambiguity of the terms and alleged financial hardship. But the *Four Winds* court found the case analogous to *Brick Plaza v. Humble Oil & Refining Co.*, and held the failure to timely exercise an option is not excusable because of a mistaken interpretation of the clear language of the lease.

In *Pegill v. 4 Palms*, 2013 N.J. Super. LEXIS 389 (App. Div. Feb.??21, 2013), the tenant operated a restaurant in the premises which had been purchased from a seller having the same principal as landlord. The Appellate Division rejected the tenant's assertion that it effectively exercised its option to purchase pursuant to the lease when the tenant failed to tender the \$275,000 deposit required under the lease. The court affirmed that the deposit was a material element of the option, and the tenant was obligated to strictly comply with the option provision. Nonetheless, the court considered the hardship to the tenant. The Appellate Division observed that the trial judge considered that his decision would not result in the tenant's losing the restaurant business because the lease continued in force for another 19 years, with an option to extend for another 20 years, and gave the tenant a right of first refusal if the landlord decided to sell. The court observed: "Consequently, defendants still had ample protection against a forfeiture of their investment in the business." Perhaps this court would have decided in the tenant's favor if the tenant would have lost its business without judicial relief. Nevertheless, two subsequent cases granted relief.

In *Window Shapes v. Toma Realty*, 2009 N.J. Super. LEXIS 2047 (App. Div. 2009), unlike the previously cited cases, the Appellate Division applied equitable considerations in rejecting the landlord's refusal to honor an option to purchase based on the tenant's failure to maintain insurance in compliance with the terms of the lease. Noting the landlord had been indifferent to the insurance deficiencies, the court held that the trial judge properly exercised his discretion to enforce the tenant's rights and avoid forfeiture.

Similarly, in *New West Caldwell Dental Group v. PARS Enterprises*, 2010 N.J. Super. LEXIS 1945 (App. Div. Aug. 11, 2010), the Appellate Division affirmed the trial court's decision that an option to purchase had been effectively exercised. There the court interpreted the lease according to its terms and held the exercise of the option effective despite the landlord's claim that the option was ineffective because the tenant and another tenant planned to transfer the property to a new legal entity consisting of the two tenants.

When *Brunswick Hills* was decided, it suggested a change in the law with respect to affording relief to a tenant failing to exercise its option in accordance with the specific terms of a lease. However, subsequent cases indicate that tenants still should not ordinarily count on equitable relief. Although excusing the tenant's failure to comply with the option terms, *Brunswick Hills* and later cases appear to confirm the general rule that an option to renew a lease or purchase the property will be strictly enforced according to its terms absent very special circumstances. Each case is fact-sensitive. In applying equitable principles, courts will consider the covenant of good faith and fair dealing, bad faith, the degree of lateness, hardship to the tenant and the sophistication of the parties. Cases involving imperfect exercise of an option arise not infrequently. The ultimate lesson of these cases is for a tenant to find a way not to overlook the timing and other requirements in its lease in the exercise of the option.

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