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Assignment and Sublease Restrictions: The Tribulations of Leasehold Transfers

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ASSIGNMENT AND SUBLEASE RESTRICTIONS: THE TRIBULATIONS OF LEASEHOLD TRANSFERS

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PREFACE

This Article deals with a variety of issues concerning restrictions on assignments and subleases contained in non-residential real property leases. The Article was prepared to provide the California Law Revision Commission\(^1\) with background information for its study of this subject. The opinions, conclusions and recommendations contained in this Article are entirely those of the Author and do not necessarily represent or reflect the opinions, conclusions or recommendations of the Commission. The purpose of the study is to determine whether there is a need to codify, clarify or modify California law by legislation.

The Article is divided into six distinct but related studies. Part 1 deals with the validity and interpretation of restrictions imposed by a lessor on a tenant’s ability to transfer the leasehold. It also covers related issues involved in a lessor’s remedies following breach and abandonment by a tenant. Part 2 examines the remedies available to a lessor when a tenant wrongfully violates a transfer restriction. Part 3 covers the remedies available to a tenant when a lessor wrongfully refuses to consent to a transfer by a tenant. Part 4 deals with the application of transfer restrictions to involuntary transfers. Part 5 considers the relationship and distinction between a restriction on transfer and a restriction on use. Finally, Part 6 examines the enforceability of a transfer restriction against a tenant’s successor.

I thank Glen (Tim) Neal, my student research assistant, for his extremely competent and creative assistance on this project. I also thank the real property lawyers around the state who have taken the time to review and comment on my work.

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1. The California Law Revision Commission is created by statute (Cal. Gov't Code §§ 8280-8297) and is composed of a member of the California Senate, a member of the California Assembly, seven members appointed by the Governor with the advice and consent of the Senate, and the Legislative Counsel ex officio. It is directed to examine the common law and the state statutes and judicial decisions for the purpose of discovering defects and anachronisms in the law and recommending reforms.
PART 1
RESTRICTIONS ON LEASE TRANSFERS:
VALIDITY AND RELATED REMEDIES ISSUES
(MUST CONSENTING ADULTS BE REASONABLE?)

I. Scope of Part

Assume that a lessor and tenant enter into a commercial lease of real property. Later, the tenant transfers or attempts to transfer all or part of the leasehold to a third party. The transfer will be in the form of either an assignment to an assignee, or a sublease to a subtenant. A clause in the lease between the lessor and tenant restricts the tenant’s ability to transfer to a third party. The lessor refuses to allow the transfer. The tenant and the third party either complete the transfer despite the lessor’s objections, or the deal between the tenant and the third party is ended due to the lessor’s objections. A dispute between the lessor and the tenant ensues. The third party will also be involved in the dispute if the transfer was completed, and perhaps be involved even if it was not completed.

This is the basic factual situation that triggers the issues involved in the Article. The same issues are involved when the transfer restrictions are contained in a sublease from the tenant to a subtenant, and it is the subtenant who wishes to transfer to a third party over the tenant/sublessor’s objections. The restrictions on transfer can take a variety of forms, discussed in detail below. Generally, restrictions come in two forms. First, there are direct restrictions, such as a prohibition against transfer without the lessor’s consent. Second, there are indirect restrictions, such as a lessor’s option to recover possession of the premises if a transfer is proposed, or a lessor’s right to participate in profits from the third party if a transfer is completed. There are other factual variations which will be discussed where appropriate. The Article is limited to non-residential leases and the word “commercial” will be used in the broad sense to include all types of non-residential leases. There is, however, a limited discussion of the distinct factors present in a residential transaction.

The Article examines existing California law, and in some instances proposes clarifications or modifications of the law, dealing with the following general issues:

1. What are the limitations, if any, on a lessor’s ability to restrict a transfer by a tenant?

2. Suppose the restriction provisions are silent about the standard governing the lessor’s right to object to a transfer. What standard will be used—reasonableness or sole discretion?
3. Suppose the parties agree to provisions that expressly provide for a standard of sole discretion for the lessor's right to object to transfer. Will that provision be enforceable, or will a mandatory reasonableness standard be imposed?

4. What are the limitations, if any, on a lessor's ability to provide for an option to recover the premises when a transfer is proposed?

5. What are the limitations, if any, on a lessor's ability to provide for a right to part or all of the profits from the third party if a transfer is completed?

6. What is the relationship between transfer restrictions and a lessor's remedies for breach and abandonment by a tenant?

II. INTRODUCTION

In 1983, a relatively dormant area of California lease law was reexamined and thrust into the limelight. In Cohen v. Ratinoff, a California court of appeal reviewed and rejected a portion of the common-law and current majority view regarding lease transfer restraints. In 1985, in Kendall v. Ernest Pestana, Inc., the California Supreme Court did the same.

There are three basic components to the common-law and majority view. First, the tenant's leasehold interest is freely transferable, unless the parties agree to a restriction. Second, the parties are free to absolutely prohibit transfer or to condition transfer upon obtaining the lessor's consent, which may be withheld in the lessor's sole discretion. Third, if the parties agree that the lessor's consent is required for a transfer, but fail to expressly provide for a reasonableness standard, the lessor can withhold consent in his or her sole discretion. The holdings in Cohen and Kendall are limited to changing the third component by imposing a reasonableness standard when the clause does not express a standard.

This change should be examined. If the change is a good one, the propriety of applying the change to leases finalized prior to Cohen and Kendall should be examined.

Although dicta, there is broad language in Kendall that sends mixed signals about the continued validity of clauses that absolutely prohibit

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4. See infra notes 54-60 and accompanying text for a complete discussion of the common-law and majority view.
5. Kendall, 40 Cal. 3d at 506-07, 709 P.2d at 849, 220 Cal. Rptr. at 830; Cohen, 147 Cal. App. 3d at 330, 195 Cal. Rptr. at 89.
LEASEHOLD TRANSFER RESTRICTIONS

6. Kendall, 40 Cal. 3d at 496, 709 P.2d at 841-42, 220 Cal. Rptr. at 822-23.
10. Id. § 1951.4(b).
11. C. MOYNIHAN, INTRODUCTION TO THE LAW OF REAL PROPERTY § 8, at 94 (2d ed.)
retains a contingent right to recover possession, there is a jurisdictional split on the result. In California, the result is a sublease.\textsuperscript{12}

The tenant remains liable to the lessor for breaches of the lease that occur after either an assignment or a sublease.\textsuperscript{13} This is based on their privity of contract which continues unless the lessor releases the tenant. Consent to an assignment or sublease does not in itself release the tenant from liability to the lessor.\textsuperscript{14}

An assignee and the lessor become liable to one another for breaches of their respective real covenant obligations that occur during the period that the assignee has the leasehold.\textsuperscript{15} This is based on privity of estate between the lessor and assignee, which arises when the assignee takes over the tenant’s estate. Absent an assumption, the assignee is not liable for breaches that occurred before the assignment or occur after a reassignment.\textsuperscript{16}

Generally, a subtenant is not directly liable to the lessor.\textsuperscript{17} Absent an assumption by the subtenant, there is no privity of contract or estate between the lessor and subtenant. However, if the lease obligations are not performed, the lessor can terminate the lease and recover possession from the tenant and the subtenant.\textsuperscript{18} Generally, the lessor is not directly liable to the subtenant for breaches of the prime lease obligations. However, direct liability might arise in situations where the lessor consents to a sublease and the subtenant assumes the obligations of the prime lease.\textsuperscript{19}

There are significant differences in the relationship between a tenant/assignor and an assignee on the one hand, and a tenant/sublessor and a subtenant on the other. A sublease creates a new tenancy relationship and privity of estate, as well as contract, between the tenant as sub-


\textsuperscript{14} Peiser v. Mettler, 50 Cal. 2d 594, 598 P.2d 953 (1958); 2 R. Powell, supra, note 11, at 372.112.

\textsuperscript{15} CAL. CIV. CODE § 822 (West 1982); 2 R. Powell, supra, note 11 at 372.94-96; Rohan, supra note 11 § 501, at 5-5 to 5-6.

\textsuperscript{16} CAL. CIV. PROC. CODE § 1466 (West 1982).

\textsuperscript{17} See Erickson v. Rhee, 181 Cal. 562, 185 P. 847 (1919); C. Moynihan, supra note 11, at 96; Rohan, supra note 11, at 5-5 to 5-6.

\textsuperscript{18} CAL. CIV. PROC. CODE §§ 1161(3), 1164 (West 1982); id. § 1174 (West Supp. 1988).

lessor and the third party as subtenant. An assignment leaves the tenant/assignor with no further interest in the property. The relationship between the tenant/assignor and the assignee is purely contractual. Examples of important ramifications of this distinction are the right to bring an unlawful detainer action and the right to exercise purchase or renewal options contained in the lease. The tenant/sublessor has a right to bring an unlawful detainer action against the subtenant to recover possession of the property if the subtenant breaches obligations to the tenant/sublessor. The tenant/assignor cannot bring an unlawful detainer action against the assignee. When a sublease occurs, generally the tenant/sublessor retains the right to exercise purchase or renewal options contained in the lease. When an assignment occurs, the option rights generally pass to the assignee.

There are important differences in the nature and effect of an assignment and a sublease. The lessor, tenant and third party may have important reasons to prefer one form of transfer over the other, and these preferences may conflict. However, for the purpose of testing the standard that should apply to a restriction on transfer, an assignment and sublease are generally treated identically.

IV. TYPES OF RESTRICTION CLAUSES

There are several types of lease clauses that restrict, directly or indirectly, a transfer of all or part of the leasehold by the tenant. They typically fall into one or more of the following categories:

1. Silent Consent Standard. The tenant must obtain the lessor's consent to a transfer, but there is no express standard governing the lessor. The clause does not expressly require the lessor to be reasonable, nor does it expressly permit the lessor to refuse consent in his sole discretion. The Cohen and Kendall cases involve this type of clause.

2. Express Reasonable Consent Standard. The tenant must obtain the lessor's consent to a transfer, and a reasonableness standard is expressly imposed upon the lessor. The common phrase that "consent shall not be unreasonably withheld" is an example.

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20. The tenant's interest in the property, which is necessary for privity of estate, ceases upon assignment. ROHAN, supra note 11, § 501, at 5-4 to 5-5.
23. Kendall, 40 Cal. 3d at 492 n.2, 709 P.2d at 839 n.2, 220 Cal. Rptr. at 820 n.2.
3. **Express Sole Discretion Consent Standard.** The tenant must obtain the lessor's consent to a transfer, and the lessor is expressly given sole discretion to grant or withhold consent. For example, the clause might provide that "consent may be withheld in the sole and absolute subjective discretion of the lessor."

4. **Express Specific Requirements.** The tenant's right to transfer, and the lessor's consent, are conditioned upon express specific requirements. The requirements vary depending upon the facts of the particular lease transaction. For example, the tenant and third party may be required to furnish evidence that the third party meets certain minimum credit or operational experience requirements.

5. **Consent Required But Exceptions.** The lessor's consent is required per one of the above alternatives, but specific types of transactions are exempted from the future consent requirements. For example, an exemption for subleases to the tenant's franchisees or an exemption for transfers among related corporate entities may be appropriate in some situations.

6. **Absolute Prohibition.** Transfer is prohibited. There is no mention of consent or compliance with requirements.

7. **Possession Recovery.** If the tenant wishes to transfer, the lessor may elect to recover possession of the property. The tenant is free to transfer to the third party only if the lessor chooses not to exercise that option.

8. **Profit Shift.** The lessor is entitled to receive part or all of the profit generated by the transfer transaction.

There are sophisticated variations of the "Possession Recovery" and the "Profit Shift" types of clauses. Also, these two types can be combined with other types of clauses. For example, the "Express Reasonable Consent Standard" clause and the "Profit Shift" clause could readily be combined. The lessor would have the right to impose reasonable objections, and if the transfer goes through, the lessor shares in the profit from the third party. The "Express Reasonable Consent Standard" clause could be combined with a variation of the "Possession Recovery" clause. For example, the lessor could either make reasonable objections to the transfer, or recover possession by exercising a right of first refusal matching the terms of the third party offer. There are variations of the other clauses as well. For example, there may be a provision granting the tenant an option to terminate the lease if the lessor refuses consent for a reason not set forth in the lease, or one that does not meet the test of
commercial reasonableness.\textsuperscript{25}

V. Motives of the Parties

The tenant's desire for free transferability, and the lessor's desire for restrictions on transferability, involve a variety of motives. These motives show that the transferability issue is an important one for the parties to a commercial lease. Several of these motives are discussed below.

A. Tenant Motives

The tenant who operates a business on the premises may wish freedom to transfer when he or she wishes to retire from the business or move to another location. The need to transfer may be unanticipated due to illness of the tenant or the business. If the business conducted on the premises is healthy, the proposed leasehold transfer may also involve a sale of the business. If a sale of the tenant's business is involved, the location may be so important to the particular business that it is difficult to separate a sale of the business from a transfer of the leasehold.

The tenant's space needs may create the desire for freedom to transfer. A tenant may anticipate a need to expand in the future and lease more space than initially needed. Until the expansion occurs, the tenant would like to defray the rental cost of the additional space by subletting. On the other hand, the tenant may initially use all of the space rented but later have reduced needs. A reduction in business or changes in the business technology may eliminate the need for some of the leased premises. Rather than negotiate a termination of the existing lease and move to a different location, the tenant may wish to remain and rent the excess space.

Corporate family events may create the need for a leasehold transfer. For example, there may be an assignment of the lease involved in a merger of the corporate tenant or a sublease involved in the creation of a subsidiary. A partnership tenant may wish to incorporate and transfer to the new entity.

Personal family events may also create a transfer incentive. For example, a parent may wish to transfer the leasehold and family business to a child. This might occur as part of a retirement plan or as part of an estate plan.

The tenant may wish to use the leasehold as security for a loan. This could involve three separate steps of transfer. First is the transfer of

\textsuperscript{25} See F & L Center Co. v. Cunningham Drug Stores, 19 Ohio App. 3d 72, 482 N.E.2d 1296 (1984).
a security interest in the leasehold. Second is the potential foreclosure or
trustee's sale transfer. Third is the retransfer by the lender if it acquired
the leasehold at the foreclosure or trustee's sale.

A variety of other motives may arise out of the many types of com-
cmercial lease transactions; however, the motives described above are the
most common.

B. Lessor Motives

The lessor's motives are called into question by the cases involving
leasehold transfer restrictions. At this point, the reader should avoid
placing a value judgment of reasonable or unreasonable on any particular
motive. Moreover, it is important to note that transfer restrictions are
not the only way a lessor can protect some of these motives. For exam-
ple, the lessor might rely on a clause compelling, preventing or regulating
certain uses on or alterations of the premises. When the profit motive is
involved, there are several alternatives available, as discussed below.

The lessor is virtually unrestricted by law, except for prohibitions
against discrimination, in evaluating and choosing a tenant in the first
instance. The lessor would like the same freedom to evaluate and choose
any new occupant, or to retain the original tenant. The tenant is a
known and chosen quantity, and the lessor may prefer not to deal with a
virtually unknown transferee chosen by the tenant.

Various facets of income protection concern lessors. Creditworthi-
ness of the new occupant is a typical concern. If the rent is based on a
percentage of profits, the new occupant's ability to generate profits is a
major consideration. This involves factors such as management ability,
business experience and type of business. The particular agreed per-
centage set forth in the lease is generally based on the tenant's particular
type of business. There is a wide variation among rates based on the type
of business, and a change of tenant and business can significantly affect
percentage rental income. The lessor may want to preserve the draw-
ing power of a certain tenant in a shopping center. That drawing power
brings people to the center and generates profits for other tenants who
are paying percentage rentals. The drawing power also helps to maintain

27. A loss of percentage rentals was involved in one of the post-Kendall cases discussed
below. John Hogan Enter., Inc. v. Kellogg, 187 Cal. App. 3d 589, 231 Cal. Rptr. 711 (1986);
see infra notes 255-65 and accompanying text.
EXECUTIVES REPORT, 8 (Mar. 1, 1987).
the overall economic health of the center and facilitates renting space in the center.

The variety and balance of tenants is another important consideration to a shopping center lessor. Control over the mix of uses is important to the lessor for two reasons. First, the mix can have an important effect on the degree of economic success of the center. Also, the lessor wants to avoid violating any exclusive rights or non-competition protection given to other tenants. The lessor may wish to avoid competition from a new occupant to protect the lessor’s business whether in a shopping center situation or not. In addition to mix, the lessor may want to maintain a certain image for a center or a building. This involves more than just a control over the general type of business. It can involve factors such as name recognition, quality of goods and services, ethnic character of goods and services, and reputation for unique goods or services.

A different occupant may increase the burden on the building or common areas, or may increase demand for lessor services. For example, the new occupant may require use of heavy equipment which causes noise and vibrations which disturb other tenants. The new occupant’s business may require the use of a forklift, which causes extreme bearing weight on small areas and accelerates deterioration of pavement and floors. There may be a substantial increase in the use of parking areas, elevators and other common areas and facilities. There may be an increased demand for lessor-furnished services such as electricity, water and trash pick-up. Insurance costs and its availability may change. Use by a new occupant may involve alterations to the building such as partition walls and signs.

The transaction itself may cause an unwanted increase in the lessor’s real property tax burden. Certain assignments and subleases can cause an increase in assessed valuation and thus an increase in property taxes. The lessor may wish to avoid a transfer of a security interest in the leasehold, which could lead to a transfer upon foreclosure or trustee’s sale, and a retransfer by a lender who acquired the leasehold at the foreclosure or trustee’s sale. The lessor may be concerned about having the leasehold involved in an involuntary forced sale and ending up with an unknown new tenant at the end of the process. Also, the lessor may be concerned about meeting certain conditions the lender has required for making the loan.

30. This latter concern was involved in one of the post-Kendall cases discussed below. Airport Plaza, Inc. v. Blanchard, 188 Cal. App. 3d 1594, 234 Cal. Rptr. 198 (1987); see infra notes 269-82 and accompanying text.
Another concern is that a sublease reduces the lessor's ability to clear the lease title and recover possession before expiration of the term. Even if the tenant/sublessee may be willing to voluntarily surrender his leasehold, the subtenant can block recovery of the premises.31

Another consideration is the competition in renting out space. A lessor may have a large inventory of unrented space and may desire to avoid competition from existing tenants who put space up for sublease. A tenant who subleases and becomes a sublessee may want to restrict transfer by the subtenant for many of the same motives discussed above. In addition, the tenant/sublessee will be concerned that the new occupant chosen by the subtenant may do something which creates a breach of the prime lease and jeopardizes the tenant's position under the prime lease.

C. Profit Motive

The tenant and lessor share the motive to profit from an appreciation in the rental value of the premises. When the rental value increases above the agreed rent in the lease, the difference creates a leasehold bonus value. So long as there is no transfer, the tenant indirectly enjoys the benefit by occupying property which is worth more rent than he is obligated to pay. However, when a transfer occurs, both the landlord and the tenant would like the profit generated from the third party who comes into the premises with a higher rental value. It is at that point that a dispute is likely to occur, and questions of express language and reasonableness become involved.

VI. Standards Governing Restrictions

A. The Two General Standards

In theory, leasehold transfer restrictions could be banned altogether if doing so were to serve some compelling public policy. This draconian approach has not been taken in the past and it is not likely to occur in the future. Since transfer restrictions are not prohibited, the question becomes what type of standard to apply to them. There are two basic standards involved in the clauses and discussed by the courts: reasonableness and sole discretion. The reasonableness standard requires the lessor to conform to objective commercial reasonableness. The sole discretion standard allows the lessor to have subjective, personal reasons for deny-

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ing transfer, which do not have to meet an objective test of commercial reasonableness.

The sole discretion standard does not allow the lessor total freedom. For example, he or she cannot engage in prohibited discrimination.\textsuperscript{32} California recognizes that a power that may be exercised without reason should not be exercised for a bad reason.\textsuperscript{33}

\textbf{B. Sole Discretion Standard: Perhaps Not an Unreasonable Choice}

The words "arbitrary" or "capricious" are sometimes used in describing the subjective standard instead of "sole discretion."\textsuperscript{34} These words evince an unnecessary negative prejudgment. The phrase "sole discretion" is a more impartial and descriptive label for the subjective standard.

Does a lessor who chooses and negotiates for a sole discretion standard do so to be unreasonable? It is simplistic to believe that all lessors who bargain for a clause without a reasonableness standard wish to be unreasonable. For example, a lessor with a small transaction and a short-term lease may simply wish to avoid the expense and time involved in evaluating new parties during the lease term, or may wish to avoid litigation over reasonableness.

The ultimate decision of whether a lessor has acted reasonably rests with a judge or jury. There may be two distinct questions in litigation concerning compliance with the reasonableness standard. First, is the specific requirement reasonable? Second, have the third party and the tenant reasonably complied with the requirement? For example, suppose a lessor requires the third party to have good credit and sufficient experience to operate a particular business on the premises. Are credit and experience reasonable requirements? What is "good" credit and "sufficient" experience? What credit and experience does the proposed third party have?

Some requirements are vague and perhaps somewhat personal. For example, a lessor may wish to create and maintain a certain "image" for his shopping center or building. This appears perfectly reasonable and even necessary to the lessor. However, the prospect of having a jury of

\begin{thebibliography}{99}
\bibitem{32} CAL. CIV. CODE § 51 (West Supp. 1988).
\bibitem{33} Schweiger v. Superior Court, 3 Cal. 3d 507, 516-17, 476 P.2d 97, 102-03, 90 Cal. Rptr. 729, 734-35 (1970).
\end{thebibliography}
people with no interest in the property evaluate the reasonableness of his or her image and its enforcement may not be appealing to the lessor.

Even specific requirements that seem to be clearly reasonable may be subject to attack. For example, consider the requirement that the third party have good credit. There is a comment in the Kendall case that commercially reasonable grounds for refusing consent include objections to the financial stability of the third party. This seems obvious and beyond serious challenge, leaving open to dispute and litigation only the factual question of the particular financial stability required of the third party. However, the tenant and third party might still mount an attack on the financial stability requirement itself.

The tenant remains liable to the lessor after the transfer occurs, so the tenant's financial stability remains accessible to the lessor. Could the tenant and third party argue that since the lessor will continue to have the same financial protection from the tenant after the transfer, it is unreasonable to insist that the third party independently have financial stability? Would this be requiring greater protection for the lessor than he or she would have had in the absence of a transfer? The lessor is legitimately interested in performance by the party in possession, not in instituting collection litigation against an absentee party. Even though the lessor can mount arguments to counter an attack on the apparent reasonableness of the requirement, he might still end up having to litigate the issue. Therefore, it may be reasonable for a lessor wishing to avoid litigation to do so by expressly providing for a sole discretion standard.

Another example of apparently clear reasonableness is the lessor's desire to protect percentage rentals. A California court of appeal has held that as a matter of law the lessor who objects to an assignment that will result in a loss of percentage rentals acts reasonably. Suppose that a lease provides for percentage rentals, but it does not contain a clause limiting use of the premises to any specific business or it contains a clause allowing the tenant to conduct any lawful business on the premises. Or, suppose there is a restriction against use for other than a specific business, but there is no clause compelling the tenant to continue in business

35. Kendall, 40 Cal. 3d at 501, 709 P.2d at 846, 220 Cal. Rptr. at 826.
36. Id. at 500, 709 P.2d at 844, 220 Cal. Rptr. at 825.
37. A lessor’s refusal based on financial stability of the third party has been held unreasonable when the original tenant offers to act as guarantor. See Adams, Harkness & Hill, Inc. v. Northeast Realty Corp., 361 Mass. 552, 281 N.E.2d 262 (1972); Annotation, Construction and Effect of Provision in Lease that Consent to Subletting or Assignment Will Not be Arbitrarily or Unreasonably Withheld, 54 A.L.R. 3d 679 (1973) [hereinafter Annotation, Construction and Effect].
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on the property. Also, suppose that there is a substantial minimum rent so that it is unlikely that a court will impose an implied obligation on the tenant to operate a particular business, or to operate at all. 39 A change in the type of business by the tenant could result in a drop in or loss of percentage rentals; a cessation of business would result in a loss of percentage rentals. Does the lessor have a legally enforceable expectation to rent over and above the agreed minimum rent? Could the tenant and third party argue that the lessor is unreasonable to insist that he receive more protection upon transfer than he would have had without one? This argument is not just an example of a potential attack on an apparently reasonable requirement; it is also an example of the need to consider using other clauses when drafting or applying a transfer restriction clause. A clause limiting use to a specific business and compelling continuous operation would go a long way toward protection upon transfer.

There are a variety of transactions that fall into the commercial lease category. There may be a short-term lease used to provide a small shop for a sole proprietor or a long-term lease used as a financing tool for a major project developer. There may be periodic heavy use such as seasonal income tax assistance, or steady and intense use such as an industrial factory. The goals of the parties, and the lease provisions as the bargained compromises of those goals, are also varied and often complex. No one size fits all.

The California Supreme Court has recognized the difficulties of applying a reasonableness standard to commercial leases. In Mattei v. Hopper, 40 a seller attempted to get out of a real property sale contract on the ground that the buyer's obligation was subject to the broker being able to arrange satisfactory leases of shopping center buildings. The seller claimed that this made the buyer's promise illusory and thus, the contract failed for lack of consideration. 41 The court mentioned the "multiplicity of factors" involved in a commercial lease and declined to apply a "reasonable man" standard to the satisfaction clause. 42 The court pointed out that "it would seem that the factors involved in determining whether a lease is satisfactory to the lessor are too numerous and varied to permit the application of a reasonable man standard." 43 The court went on to uphold the contract since the buyer, although not held to a

41. Id. at 121-22, 330 P.2d at 626.
42. Id. at 123, 330 P.2d at 627.
43. Id.
A dissenting opinion in a 1981 Idaho Supreme Court decision points out some of the practical problems that result from a reasonableness standard. The case involved a "Silent Consent Standard" type clause. The clause required the tenant to obtain the lessor's consent to a leasehold transfer, but it did not contain an express standard of either reasonableness or sole discretion. The majority inferred a reasonableness standard. The dissenting justice commented:

[T]he effect of the decision is to potentially subject every denial of consent to litigation and approval by a judge. Rather than the lessor being sure of his right to control his property by retaining an unrestricted right to deny consent to assign or sublease, by its decision today this Court has destroyed that right and vested in the courts the power to determine what the lessor should have intended and award control of the property based upon that determination. Certainly, as evidenced by this case, the parties will rarely agree on what is reasonable under particular circumstances. Is there any assurance that judges will be unified in their opinions on what is reasonable? The only assurance to be gained by the rule adopted by the majority today is that the parties' attempt to write their lease to avoid litigation will be frustrated.

A lessor may want to avoid the expense, delay and uncertainty of litigation. He or she may want to avoid having his or her judgment second-guessed in a trial, perhaps years after exercising his or her judgment, by persons with no interest in the property. The lessor may also wish to avoid exposure to a risk of substantial punitive damages.

C. Basic Issues in Choice of Standards

The tension between freedom of contract and public policy is a core issue underlying transfer restriction questions. Beyond that broad issue, there are two basic questions.

First, if a clause prohibits transfer of the leasehold without the les-

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44. Id. at 126, 330 P.2d at 628.
46. See supra note 24 and accompanying text.
47. Funk, 102 Idaho at 522, 633 P.2d at 587.
48. Id. at 526, 633 P.2d at 591 (Bakes, C.J., dissenting) (emphasis in original).
49. See supra notes 26-31 and accompanying text for a discussion of other lessor motives for placing restrictions on lease transfers.
sor's consent, but does not expressly provide for a standard, is a reasonableness or a sole discretion standard applicable? A "Silent Consent Standard" type clause is the most common example; the tenant is prohibited from assigning or subletting "without the lessor's prior written consent." In addition to the freedom of contract versus public policy issue, there is an interpretation question involved: Have the parties agreed to one standard or the other by not saying more, or have they left an omission which must be construed and furnished?

Second, can the parties expressly negotiate and provide for a sole discretion standard, or are there compelling public policy reasons to take away the freedom to contract and mandate a reasonableness standard? The "Express Sole Discretion Consent Standard" type clause and the "Absolute Prohibition" type clause are the most common examples.

VII. VIEWS OUTSIDE CALIFORNIA

A. Common-law and Majority View

The common-law and majority rule can be simply summarized: leasehold transfers are freely allowed unless restricted; restrictions are permitted, but strictly construed.

The leasehold is a transferable property interest. Absent a valid restriction in the lease, the tenant may assign or sublease without the lessor's consent and without complying with any particular standards or restrictions. In a rare situation, a restriction might be implied. The lessor is permitted to negotiate an agreement that restricts transfer of the leasehold. Although the common-law prohibition against restraints on fee transfers is virtually absolute, restrictions on leasehold transfers are allowed because of the lessor's continuing interest in the property during and after the term of the lease.

The scope of a restriction clause is strictly construed in order to allow maximum freedom to the tenant. Thus, a particular transaction will generally escape the restriction unless the clause expressly takes it into consideration. For example, a simple prohibition against assignment

50. See supra note 24 and accompanying text.
51. See supra notes 24-25 and accompanying text.
52. Id.
53. See supra Section IV.
55. C. MOYNIHAN, supra note 11, at 32; 2 R. POWELL, supra note 11, at 372.97.
or subleasing does not take into consideration the type of entity (e.g., a corporate tenant that continues to hold the lease while its stock is transferred), the type of interest transferred (e.g., a license or easement) or the type of transfer (e.g., an involuntary transfer by death). A restriction on one type of transfer does not lead to an inferred restriction on other types of transfers.

The basic issues involved in the choice of standards are resolved in the following manner:

1. If a clause prohibits transfer of the leasehold without the lessor’s consent, but does not expressly provide for a reasonableness standard, the lessor is bound only by the sole discretion standard.

2. The parties may expressly provide for a sole discretion standard and this will be enforceable.

B. Minority View

Some jurisdictions have reconsidered the common-law and majority view and rejected it in part. In Kendall, the court commented that “[t]he traditional majority rule has come under steady attack in recent years.” The Kendall opinion goes on to state:

A growing minority of jurisdictions now hold that where a lease provides for assignment only with the prior consent of the lessor, such consent may be withheld only where the lessor has a commercially reasonable objection to the assignment, even in the absence of a provision in the lease stating that consent to assignment will not be unreasonably withheld.

The following states are referred to as being in this minority: Alabama, Alaska, Arkansas, Florida, Idaho, Illinois, New Mexico and

60. 2 R. Powell, supra note 11, at 372.97.
62. Id.
Ohio.\textsuperscript{70} Three other states are mentioned for conflicting or uncertain authority.\textsuperscript{71} Ohio subsequently reversed its position.\textsuperscript{72} Also, a later Ohio case supports the common-law and majority view.\textsuperscript{73} There also have been cases in Arizona\textsuperscript{74} and Colorado\textsuperscript{75} supporting the minority position. Recent cases considering the issue have not universally adopted the minority view,\textsuperscript{76} and the ones adopting the minority view are not all without dissent.\textsuperscript{77} However, this is not necessarily due to a disagreement with the merits of the minority view. It may be due to the belief that the legislature, rather than the court, should make the change.\textsuperscript{78} There may also be a belief that the minority is the better view, but that changes to the standard should not be adopted retroactively. An exact count of states is much less important than determining exactly what the minority cases do and what they do not do.

Each of the cases mentioned above involved a "Silent Consent Standard"\textsuperscript{79} type clause that prohibited transfer without the lessor's consent but did not expressly state either a reasonableness or a sole discretion standard. None of those cases involved a clause expressly providing for a sole discretion standard and none of those cases hold that an express sole discretion standard would be unenforceable. Thus, the attack of the minority upon the traditional common-law and majority view has been aimed at only one of the two major components of that rule.\textsuperscript{80}

The minority cases stand for the proposition that a reasonableness

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\textsuperscript{71} The three states are Louisiana, Massachusetts and North Carolina, mentioned in Kendall, 40 Cal. 3d at 496 n.9, 709 P.2d at 841-42 n.9, 220 Cal. Rptr. at 822-23 n.9 (1985).
\textsuperscript{73} F & L Center Co. v. Cunningham Drug Stores, Inc., 19 Ohio App. 3d 72, 482 N.E.2d 1296 (1984).
\textsuperscript{78} See, e.g., Homa-Goff Interiors, 350 So. 2d at 1041.
\textsuperscript{79} See supra note 24 and accompanying text.
\textsuperscript{80} See supra notes 59-60 and accompanying text for a discussion of the components of the rule.
\end{flushright}
standard will be implied to govern the lessor in the absence of an express standard. The cases change the effect of a "Silent Consent Standard" type clause. Absent an express standard, the common-law and majority permit the lessor to have sole discretion. The minority requires the lessor to meet an objective standard of commercial reasonableness. A major argument for the common-law and majority treatment of this type of clause is that the language is clear, so there is no basis for implying a reasonableness standard. The clause does not expressly mention sole discretion or reasonableness. The tenant could have bargained for a reasonableness standard, in which case it would be expressed in the lease. Since it is not in the lease, it was not bargained for, and the lessor is left with a sole discretion standard. The minority does not find the "Silent Consent Standard" unambiguous regarding the governing standard. If the clause is considered unclear, two basic policies lead to a reasonableness standard. One is the implied covenant of good faith and fair dealing. The other is the dislike and strict construction of restrictions on transfer.

Many of the minority-view cases use strong language to criticize the sole discretion standard. However, the cases do not directly hold that the parties cannot bargain and expressly provide for such a standard. There is no trend of holdings abolishing the part of the common-law and majority rule that leaves the sole discretion standard to the agreement of the parties.

The minority view is directed at avoiding unpleasant surprises for the tenant at the time of transfer—the "Silent Consent Standard" surprise. It is directed at encouraging disclosures and clarifying expectations. It does not override the freedom of contract of the parties, nor does it prohibit a negotiated express sole discretion standard.

81. See, e.g., Kendall, 40 Cal. 3d at 496-98, 709 P.2d at 841-43, 220 Cal. Rptr. at 822-23.
82. See supra note 24 and accompanying text.
83. See supra note 59 and accompanying text.
84. See, e.g. Kendall, 40 Cal. 3d at 500, 709 P.2d at 845, 220 Cal. Rptr. at 826.
86. See Kendall, 40 Cal. 3d at 502, 709 P.2d at 846, 220 Cal. Rptr. at 827.
87. Id. at 502-03, 709 P.2d at 846, 220 Cal. Rptr. at 827.
88. Id. at 500, 709 P.2d at 844, 220 Cal. Rptr. at 825-26.
89. Id. at 498-99, 709 P.2d at 843-44, 220 Cal. Rptr. at 824-25.
90. See, e.g., id. at 501-04, 709 P.2d at 845-48, 220 Cal. Rptr. at 826-28.
VIII. RESTATEMENT POSITION

The Restatement (Second) of Property adopts the following approach to leasehold transfers and restrictions:

The interests . . . of the tenant in the leased property are freely transferable, unless . . . the parties to the lease validly agree otherwise.91

A restraint on alienation without the consent of the landlord of the tenant's interest in the leased property is valid, but the landlord's consent to an alienation by the tenant cannot be withheld unreasonably, unless a freely negotiated provision in the lease gives the landlord an absolute right to withhold consent.92

The strict construction approach of the common-law and majority is continued in the Restatement.93 Thus, the language will be construed in favor of the tenant and transferability absent clear words of restriction.

The Restatement distinguishes among three types of restraints, categorized by the remedies available to the lessor.94 First, if a prohibited transfer is made, the "forfeiture restraint" allows the lessor either to terminate the lease or to forego his objections to the transfer and enforce the lease provisions.95 Second, the "disabling restraint" allows the lessor to keep the lease in effect and prevent the transfer from taking place.96 Third, the "promissory restraint" ends up almost as one of the other two types, depending on the remedy available and chosen for breach of the promise.97 If the lessor can and does terminate the lease, the effect is the same as a forfeiture restraint, but with the additional right to damages. If the lessor can and does seek specific performance of the promise, the effect is the same as a disabling restraint. Although the lessor may prefer to have the option to negate the transfer, the disabling restraint is more disliked than a forfeiture restraint. The disabling restraint prevents transfer while the forfeiture restraint involves either a transfer back to the lessor or a permitted transfer to the third party. California appears to adopt the forfeiture restraint remedy, despite language in the clause indicating either a disabling or a promissory restraint.98

92. Id. § 15.2.
93. Id. at comment e.
94. Id. at comments b, c & d.
95. Id. at comment b.
96. Id. at comment c.
97. Id. at comment d.
98. See, e.g., People v. Klopstock, 24 Cal. 2d 897, 151 P.2d 641 (1944); Chapman v. Great
Kendall and several of the other minority-view cases refer to the Restatement and use it to support their use of the reasonableness standard. The Restatement reflects the minority view by imposing a reasonableness standard on the “Silent Consent Standard” type clause. It leaves the common-law and majority view intact where the parties have agreed to and have expressly provided for a sole discretion standard. The Restatement position allows the lessor to have a provision for “an absolute right to withhold consent” if it is “freely negotiated.” Under the Restatement, if the tenant has “no significant bargaining power in relation to the terms of the lease,” it is not freely negotiated. A clause that lacks free negotiation is not totally void; transfer is still restricted but a reasonableness standard applies.

The policy toward recovery of the premises by the lessor, triggered by an attempted transfer, depends on the manner in which recovery is accomplished. There might be a provision allowing the tenant to terminate the lease (as an exclusive remedy) if the lessor unreasonably withholds consent. This is sufficiently close to a sole discretion standard to require that the clause be freely negotiated. A Restatement comment distinguishes this from a lessor’s right of first refusal to acquire the tenant’s interest on the same terms offered by a third party. The comment states that “[s]uch right of first refusal is valid though its exercise will prevent the transfer by the tenant to another.” Since the tenant will receive basically the same deal from the lessor or the third party, there is no significant damper on transferability.

The Restatement position, like the minority view, is directed at avoiding unpleasant surprises for the tenant at the time of transfer—the “Silent Consent Standard” surprise; it is directed at encouraging disclosures and clarifying expectations. It does not override the freedom of contract of the parties, nor prohibit a negotiated express sole discretion standard.

100. RESTATEMENT, supra note 91, § 15.2(2).
101. Id. § 15.2 comment i.
102. Id.
103. Id.
IX. CALIFORNIA PRIOR TO KENDALL

A. Statutes

California Civil Code section 711 provides that "[c]onditions restraining alienation, when repugnant to the interest created, are void." There is nothing in this statute, enacted in 1872, to indicate that anything but the common-law rule was being adopted. Restraints on alienation were considered repugnant to a fee simple interest. They were not considered repugnant to a leasehold interest. California Civil Code section 820 provides in pertinent part that "[a] tenant for years or at will has no other rights to the property than such as are given to him by the agreement or instrument by which his tenancy is acquired." This statute, enacted in 1872, emphasizes the lease as the source of the tenant's rights.

B. Cases Prior to Kendall

*DeAngeles v. Cotta*, decided in 1923, has been cited as an early suggestion that restrictions must relate to the lessor's legitimate interests. The lessor brought an unlawful detainer action based on the alleged breach of a "Silent Consent Standard" type clause which prohibited transfer without the lessor's consent. The four original tenants, through a series of individual assignments, had transferred their interests in the lease to two new parties. The trial court found that the original tenants did not jointly assign the leasehold and the clause did not prohibit assignment of their individual interests.

The court of appeal reversed, interpreting the clause as a joint and several covenant not to assign. The court stated that "[o]wners of property are justly solicitous as to the character of its occupants and restrictions upon the right of a lessee to substitute another tenant without the lessor's consent are reasonable covenants which ought to be rationally construed." The court referred to the California statute that re-
quires strict construction of a condition involving forfeiture,"¹¹⁵ but went on to say that "[t]his does not mean that courts must resort to scholastic subtleties to save tenants from the consequences of their deliberate breach of their covenants."¹¹⁶ The court approved the view that courts should not make a different contract for the parties or defeat their clear intent by resorting to strained and unnatural construction.¹¹⁷ A petition for hearing in the California Supreme Court was denied.¹¹⁸

_Deangeles_ does not involve a court-imposed reasonableness standard. It does not analyze and express a preference against a sole discretion standard. The case merely shows that strict construction of a restriction on transfer does not prevent a common-sense interpretation of the purpose of the clause to protect a lessor.

_Kendis v. Cohn_,¹¹⁹ decided in 1928 by the court of appeal, involved a clause that prohibited assignment or subletting without the lessor's consent.¹²⁰ The clause provided that "lessees may, with the written consent of . . . lessors, assign . . . to any person or persons of good character and repute and satisfactory to the lessors."¹²¹ The court pointed out that a reasonableness standard was not expressed and would not be inferred. The lessor "is the sole judge of his own satisfaction, subject only to the limitation that he must act in good faith."¹²² The lessor was the sole judge of good character and repute, without testing that judgment against the ordinary reasonable person. However, if he or she were in fact satisfied, he or she could not act in bad faith by deceitfully denying satisfaction.¹²³

The _Kendis_ opinion states that a lessor is still bound by a requirement of good faith even though he or she does not have to be judged by an objective reasonableness standard.¹²⁴ A person may be unreasonable but still act in good faith. Reasonableness is an objective test based on common experience of the ordinary reasonable person. "Good faith, in contrast, suggests a moral quality; its absence is equated with dishonesty, deceit or unfaithfulness to duty."¹²⁵

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¹¹⁵. CAL. CIV. CODE § 1442 (West 1982).
¹¹⁷. _Id._ at 695-96, 217 P. at 823.
¹¹⁸. _Id._ at 696, 217 P. at 823.
¹¹⁹. 90 Cal. App. 41, 265 P. 844 (1928).
¹²⁰. _Id._ at 48-49, 265 P. at 846-47.
¹²¹. _Id._ at 49, 265 P. at 847.
¹²². _Id._ at 66, 265 P. at 854.
¹²³. _Id._ at 67, 265 P. at 854.
¹²⁴. _Id._
The clause in *Richard v. Degen & Brody, Inc.*,\(^{126}\) decided in 1960, prohibited assignment or subleasing without the lessor's written consent, and it did not expressly provide a consent standard. The tenant contended that the lessor could not "arbitrarily" refuse consent to a sublease.\(^{127}\) The court rejected the tenant's contention with the comment that it was "untenable" and followed the traditional majority view;\(^{128}\) the "Silent Consent Standard" type clause was governed by a sole discretion, not a reasonableness, standard.\(^{129}\) The court did not discuss the merits of that view, nor the reasons that might support a contrary view.\(^{130}\)

In 1981, a court of appeal panel imposed a reasonableness standard on a condominium association.\(^{131}\) In *Laguna Royale Owners Association v. Darger*,\(^{132}\) a condominium association attempted to block a mini-time-share division by one of the condominium owners. The association asserted the absolute right to withhold consent while the unit owner asserted the absolute right to transfer.\(^{133}\) The court rejected both absolutes and allowed transfer restrictions subject to a reasonableness standard.\(^{134}\) The association argued that the traditional rule allowing absolute restrictions on a tenant applied because the unit owner was technically a sublessee.\(^{135}\) The condominium was developed pursuant to a 99-year ground lease, and buyers of the units received an undivided interest in the leasehold.\(^{136}\) The court took a passing shot at the traditional rule when it stated: "Even assuming the continued vitality of the rule that a lessor may arbitrarily withhold consent to a sublease . . . there is little or no similarity in the relationship between a condominium owner and his fellow owners and that between lessor and lessee or sublessor and sublessee."\(^{137}\) The common law has long recognized a distinction between a leasehold interest upon which restrictions are clearly allowed, and a fee ownership interest upon which restrictions are virtually prohibited.\(^{138}\) Since the court distinguished the condominium unit interest from the

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127. *Id.* at 297, 5 Cal. Rptr. at 268.
128. *Id.* at 299, 5 Cal. Rptr. at 269.
129. *Id.*
130. *Id.*
132. *Id.*
133. *Id.* at 679, 174 Cal. Rptr. at 142.
134. *Id.* at 680, 174 Cal. Rptr. at 142.
135. *Id.* at 681, 174 Cal. Rptr. at 143.
136. *Id.* at 673, 174 Cal. Rptr. at 138.
137. *Id.* at 681, 174 Cal. Rptr. at 143.
typical leasehold interest, the rule in the Richard case was also distinguished.  

In Cohen v. Ratinoff, a court of appeal squarely faced and rejected the traditional rule decided in 1983. A commercial lease clause prevented assignment or subleasing without the lessor's prior written consent, and there was no express consent standard—a “Silent Consent Standard” type clause. After several requests by the tenant for consent to an assignment, the lessor’s attorney informed the tenant that the lessor could be “as arbitrary as he chooses.” This colorful framing of the issue may have encouraged reevaluation of the traditional rule for the court held that a lessor may refuse consent only where he or she has an objectively reasonable objection.

The Cohen case was followed in quick succession by five cases dealing with the same issue: Schweiso v. Williams in 1984; Prestin v. Mobil Oil Co. in 1984 (applying a federal court’s perception of California law); Sade Shoe Co. v. Oschin & Snyder in 1984; Hamilton v. Dixon in 1985; and, Thrifty Oil Co. v. Batarse in 1985. All five cases involved commercial leases. All five involved clauses restricting transfer without the lessor’s consent, but with no express consent standard—a “Silent Consent Standard” type clause. Schweiso and Prestin imposed a reasonableness standard on the lessor. In Schweiso, the lessors referred to the restriction clause as a “license to steal” and they demanded a “transfer fee” as “blood money.” Some might consider this subtle choice of words used to frame the issue as the verbal equivalent of an obscene gesture.

The Sade Shoe Co. decision seems to stand for the proposition that a sole discretion refusal is permitted, but that it may constitute tortious interference with prospective economic advantage. This prompted the

139. Laguna Royale Owners Ass'n, 119 Cal. App. at 681, 174 Cal. Rptr. at 143.
141. Id. at 328, 195 Cal. Rptr. at 88.
142. Id. at 325, 195 Cal. Rptr. at 86.
143. Id. at 330, 195 Cal. Rptr. at 89.
145. 741 F.2d 268 (9th Cir. 1984).
149. Prestin, 741 F.2d at 269; Thrifty Oil Co., 174 Cal. App. 3d at 772, 220 Cal. Rptr. at 286; Hamilton, 168 Cal. App. 3d at 1006, 214 Cal. Rptr. at 640; Sade Shoe Co., 162 Cal. App. 3d at 1177, 209 Cal. Rptr. at 125; Schweiso, 150 Cal. App. 3d at 886, 198 Cal. Rptr. at 240.
150. Prestin, 741 F.2d at 273; Schweiso, 150 Cal. App. 3d at 886-87, 198 Cal. Rptr. at 240.
151. Schweiso, 150 Cal. App. 3d at 885, 198 Cal. Rptr. at 239.
152. Sade Shoe, 162 Cal. App. 3d at 1179-80, 209 Cal. Rptr. at 126-27.
The lease in *Hamilton* was executed in 1970. The court expressed the view that *Richard v. Degen & Brody* was "clearly the law" at that time, and it would be improper to rewrite the bargained rights and reasonable expectations fifteen years later. The court also commented that the abrogation of the freedom to bargain for a sole discretion standard should come from the legislature, and not the courts.

It should be noted that the facts in *Hamilton* show that it is improper to always characterize the tenant as riding the white horse of virtue in a joust with a greedy lessor. Picture the lessor as a sixty-seven year old widow living alone in a mobile home. Her income came from social security and rent from the leased property. Her fixed rent had become a "pittance" due to "shocking double-digit inflation" during the fifteen years since the lease was executed.

The dispute in the *Thrifty Oil* case involved a "Silent Consent Standard" type clause in a sublease. The subtenant subleased to third parties without even asking for the sublessor's consent. The sublessor brought an unlawful detainer action against the subtenant and third parties to recover possession. After a hearing, which took place about three months before the *Cohen* decision, the trial court ruled in favor of the sublessor based on the *Richard* case. After the *Cohen* decision, the subtenant and third parties cited it in a petition to be relieved from forfeiture under California Civil Procedure Code section 1179. This section allows relief from forfeiture in limited hardship situations. The trial court denied the petition because the subtenant had not requested consent. The court of appeal found it unnecessary to decide whether *Richard* or *Cohen* applied when interpreting the "Silent Consent Standard" clause, because no consent had been sought. Regardless of

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154. Id. at 1006, 214 Cal. Rptr. at 640.
155. Id. at 1009, 214 Cal. Rptr. at 642 (citing *Richard v. Degen & Brody*, Inc., 181 Cal. App. 2d 289, 5 Cal. Rptr. 263 (1960)).
156. Id. at 1010, 214 Cal. Rptr. at 643.
157. Id. at 1011, 214 Cal. Rptr. at 643.
159. Id.
160. Id. at 773, 220 Cal. Rptr. at 287.
161. Id.
162. Id. at 774, 220 Cal. Rptr. at 288.
163. CAL. CIV. PROC. CODE § 1179 (West 1982).
165. Id. at 776, 220 Cal. Rptr. at 289.
which case applied, the court of appeal in *Thrifty Oil* stated that the subtenant and third parties "properly could not prevail in the unlawful detainer action because of the fact there was a failure to seek consent for the assignment."\(^{166}\) However, the court held that the failure to seek consent was not an absolute bar to relief against forfeiture under section 1179.\(^{167}\) The matter was remanded to the trial court to weigh the facts for forfeiture relief.\(^{168}\) The court gave examples of factors to consider. One factor is not that consent was not sought but *why* consent was not sought.\(^{169}\) Another example was the degree of arbitrariness or unreasonableness, if any, of the sublessor.\(^{170}\) It seems strange that the failure to ask for consent would block the subtenant and third parties from winning the unlawful detainer, yet not block them from relief against forfeiture. Comments in the case indicate that the court might have been giving the subtenant and third parties the opportunity to prove that asking for consent would have been a futile gesture.\(^{171}\)

In *Don Rose Oil Co. v. Lindsley*,\(^{172}\) decided in 1984 by the court of appeal, the court cited *Cohen* and *Prestin* with approval, and commented that "[t]he trend in the law is toward assignability of contract rights."\(^{173}\) However, this case involved a dispute concerning the right to assign a petroleum franchise.\(^{174}\) The characteristics of a business franchise and a commercial lease are sufficiently different so that the case did nothing to resolve leasehold transfer issues.

This was the variegated background faced by the California Supreme Court when the *Kendall* case came before it.

**X. Kendall v. Ernest Pestana, Inc.**

**A. Facts**

There were four transactions leading up to the suit in *Kendall*.\(^{175}\) The following outline may help to identify the transactions and parties discussed below:

1. Lessor (City) ——— lease ——— Tenant (Perlitchs).
2. Tenant (Perlitchs) ——— sublease ——— Subtenant (Bixler).

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166. *Id.*
167. *Id.* at 777, 220 Cal. Rptr. at 290.
168. *Id.* at 775, 220 Cal. Rptr. at 288.
169. *Id.* at 778, 220 Cal. Rptr. at 290.
170. *Id.*, 220 Cal. Rptr. at 291.
171. *Id.* at 776, 220 Cal. Rptr. at 289.
173. *Id.* at 759, 206 Cal. Rptr. at 674.
174. *Id.* at 755, 206 Cal. Rptr. at 671.
3. Tenant (Perlitchs) — assignee (Pestana).
4. Subtenant (Bixler) — proposed assignee (Kendall & O'Haras).
5. Proposed assignees of the sublease, Kendall and O'Haras, vs. Assignee of the prime lease, Pestana.

First, the City of San Jose (lessor) leased airport hanger space to the Perlitchs (prime tenants). Second, the Perlitchs (prime tenants) sublet to Bixler (subtenant). Third, the Perlitchs (prime tenants/sublessors) assigned all interest in the prime lease to the Pestana corporation (assignee of the prime lease and successor sublessor). Fourth, Bixler (subtenant) proposed to assign his interests in the sublease, as part of a sale of his business, to Kendall and the O'Haras (proposed assignees of the sublease). Kendall and the O'Haras had a stronger financial position than Bixler (subtenant). Bixler (subtenant) requested consent to the proposed assignment from Pestana (assignee of the prime lease and successor sublessor). Consent was denied, and Pestana allegedly demanded increased rent and other deal sweeteners as a condition of consent.

Kendall and the O'Haras (proposed assignees of the sublease) brought an action against Pestana (assignee of the prime lease and successor sublessor) for declaratory and injunctive relief as well as damages. They contended in effect that Pestana was bound by a reasonableness standard and that it had unreasonably withheld and conditioned consent. The trial court sustained a demurrer to the complaint without leave to amend and, on appeal, this was deemed to include a judgment of dismissal of the action. The California Supreme Court reversed.

The plaintiffs, Kendall and the O'Haras, were the proposed assignees of a sublease. The defendant, Pestana, was the assignee of the prime lease and a successor sublessor. The disputed clause was

176. Id. at 493, 709 P.2d at 839, 220 Cal. Rptr. at 820.
177. Id.
178. Id.
179. Id., 709 P.2d 840, 220 Cal. Rptr. at 821.
180. Id.
181. Id. at 494, 709 P.2d at 840, 220 Cal. Rptr. at 821.
182. Id.
183. Id.
184. Id.
185. Id. at 493 n.3, 709 P.2d at 839 n.3, 220 Cal Rptr. at 820 n.3.
186. Id. at 507, 709 P.2d at 849, 220 Cal. Rptr. at 830.
187. Id. at 493, 709 P.2d at 840, 220 Cal. Rptr. at 820.
188. Id. at 494, 709 P.2d at 840, 220 Cal. Rptr. at 821.
contained in the sublease.\textsuperscript{189} It prohibited assignment, sublease or other specific actions without prior written consent of the sublessor.\textsuperscript{190} It was a "Silent Consent Standard" type clause, and did not expressly provide for a reasonableness or a sole discretion standard.\textsuperscript{191} Other clauses provided for: a five-year term with options for four additional five-year terms; a rent escalation every ten years proportionate to the prime lease rent increase; and use of the premises as an aircraft maintenance business. The sublease was apparently drafted and executed in 1969 (with a term to commence January 1, 1970).\textsuperscript{192}

The dispute concerned a successor sublessor's refusal to consent to assignment of the subleasehold by a subtenant.\textsuperscript{193} It will be easier to deal with the issues in the more common context of a lessor, tenant and third party dispute. Assume that the lessor of a commercial lease used a "Silent Consent Standard" type clause to refuse or condition consent to a proposed transfer by the tenant to a third party. The court in Kendall used this context in its discussion.\textsuperscript{194} The issues and their resolution will be the same. Also, although the parties in the case were fighting over a proposed assignment, the court expressly extended its holding to subleases.\textsuperscript{195}

\section*{B. Kendall Rule and Reasons}

The facts involved a "Silent Consent Standard" type clause.\textsuperscript{196} The lease required the tenant to get the lessor's consent for a transfer of the leasehold. The clause did not expressly provide for either a reasonableness standard or a sole discretion standard.\textsuperscript{197} Faced with the narrow issue of which standard to use, the majority of the court in Kendall adopted the minority view that a reasonableness standard should be implied.\textsuperscript{198} The decision imposes a reasonableness consent standard on the lessor of a commercial lease containing a clause that restricts assignment or subleasing without lessor's consent, and that has no express consent

\bibitem{189} Id. n.5.
\bibitem{190} Id.
\bibitem{191} Id.
\bibitem{192} Id. at 493, 709 P.2d at 839, 220 Cal. Rptr. at 820.
\bibitem{193} Id. at 494, 709 P.2d at 840, 220 Cal. Rptr. at 821.
\bibitem{194} Id. at 495, 709 P.2d at 841, 220 Cal. Rptr. at 822.
\bibitem{195} Id. at 492 n.2, 709 P.2d at 839 n.2, 220 Cal. Rptr. at 820 n.2.
\bibitem{196} Kendall v. Ernest Pestana, Inc., 40 Cal. 3d 488, 492, 709 P.2d 837, 839, 220 Cal. Rptr. 818, 820 (1985); see supra note 24 and accompanying text for an explanation of this type of clause.
\bibitem{197} Kendall, 40 Cal. 3d at 494 n.5, 709 P.2d at 840 n.5, 220 Cal. Rptr. at 821 n.5.
\bibitem{198} Id. at 506-07, 709 P.2d at 849, 220 Cal. Rptr. at 830.
standard. The lessor in that situation must have a commercially reasonable objection to justify refusal to consent.

The court relied on dual bases for the result, flowing from the dual nature of a lease as a conveyance and as a contract. First, the Kendall court stated that in California unreasonable restraints on alienation are prohibited. The court borrowed from the "due on transfer" loan security situation in Wellenkamp v. Bank of America to support and amplify this proposition. The justification for the restriction is compared with the quantum of restraint to determine reasonableness. The court saw no modern justification for allowing leases to be exempt from the general policy.

Second, the duty of good faith and fair dealing is implied in contracts in California. The contractual nature of a lease brings that duty into the lease. The court concluded that where the lessor retains the discretionary power to grant or withhold consent to an assignment or sublease, the power should be exercised in accordance with commercially reasonable standards.

C. Common-law Rule Arguments Rejected

When a clause requires the lessor's consent, the common-law and majority view would allow the lessor to permit or block transfer in its sole discretion in the absence of an express reasonableness standard. The Kendall court addressed arguments supporting the traditional common-law rule.

First, the traditional rule emphasizes the lessor's freedom of personal choice in selecting the tenant. The unconsenting lessor is not obligated to look to someone else for performance. The court said that the values used in personal selection are preserved by the commercially reasonable grounds used for withholding consent. Also, the original tenant remains liable to the lessor despite the assignment or sublease. The court also pointed to certain lease-breach remedy legislation, discussed below in section E, as support for limits on the lessor's freedom of

199. Id. at 498, 709 P.2d at 843, 220 Cal. Rptr. at 824.
200. Id.
201. Id. (citing Wellenkamp v. Bank of America, 21 Cal. 3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978)).
202. Id.
203. Id. at 500, 709 P.2d at 844-45, 220 Cal. Rptr. at 825-26.
204. Id., 709 P.2d at 845, 220 Cal. Rptr. at 826.
206. Id. at 502, 709 P.2d at 846, 220 Cal. Rptr. at 827.
Another justification the court cited for the traditional rule is that the absence of an express reasonableness standard results in an unambiguous reservation of sole discretion. The tenant failed to bargain for a reasonableness standard, so the law should not rewrite the contract. The court implied that the clause was not unambiguous. Also, it pointed out that recognition of the implied duty of good faith and fair dealing is not a rewriting of the contract. It is important to keep in mind the type of clause that the court was dealing with when considering the ambiguity argument: the clause did not expressly provide any consent standard. Thus the court's discussion was dicta.

D. Use of "Silent Consent Standard" Clause to Increase Profit is Improper

Sometimes the rental value of property increases beyond the agreed rent. Sometimes a lessor uses a proposed assignment or sublease as a device to demand increased rent as a condition of consent. This was apparently the situation in Kendall. The court rejected the argument that the lessor has the right to the increase in rental value in this situation. The lessee made his bargain and could not reasonably anticipate any greater benefit of increased value than that granted by the lease. It is important to keep the court's criticism of the lessee's profit motive in the perspective of the facts. The lessee apparently surprised the tenant with a demand for money that it was not otherwise entitled to under the terms of the lease. It was attempting to improve, not just maintain, its economic position without the benefit of an express clause. The lessee could have initially bargained for and expressly included frequent periodic rent increases in the lease; it could have used other express clauses to increase its return. In the Kendall lease, there was a provision for rent escalation every ten years. Apparently, however, there was no express provision for a rent increase upon assignment or subleasing, nor

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207. Id. at 501-02, 709 P.2d at 845-46, 220 Cal. Rptr. at 826-27; see infra notes 217-32 and accompanying text.
208. Kendall, 40 Cal. 3d at 501-02, 709 P.2d at 845-46, 220 Cal. Rptr. at 826-27.
209. Id. at 503, 709 P.2d at 847, 220 Cal. Rptr. at 827-28.
210. This accounts for the profit motive shared by both lessor and tenant. See supra subsection V(C).
212. Id. at 504, 709 P.2d at 848, 220 Cal. Rptr. at 829.
213. Id. at 494, 709 P.2d at 840, 220 Cal. Rptr. at 821.
214. Id. at 504-05, 709 P.2d at 848, 220 Cal. Rptr. at 829.
215. Id. at 493, 709 P.2d at 839, 220 Cal. Rptr. at 820.
was there any provision for the lessor to receive part or all of the profit derived by the tenant from the transaction.216 Thus, the lessor had little intrinsic support for contending that it was proper to demand higher rent as a condition for permitting the transfer.

E. Inferences From Remedy Legislation

In 1970, the California Legislature adopted a comprehensive revision of the lessor's remedies upon termination of a lease.217 Parts of that legislation are cited for support by both the Kendall majority218 and dissent.219 Civil Code section 1951.2 provides that, except as provided in section 1951.4, a lease terminates if either of two situations occur: (1) the tenant breaches and abandons; or (2) the tenant breaches and the lessor terminates the tenant's right to possession.220 Section 1951.2 further provides that the lessor may recover the excess of the post-termination unpaid rent over the amount of rental loss that the tenant proves could have been reasonably avoided.221 Thus, the tenant may reduce or avoid these damages by proving what the lessor could receive by reletting to another tenant. The Kendall majority opinion commented that this "duty to mitigate damages" undermines the lessor's freedom to look exclusively to the tenant for performance.222

Civil Code section 1951.4 permits the lessor to keep the lease in effect and to continue enforcing its terms against the tenant.223 This lock-in remedy must be included in the lease to apply. Also, it is available only "if the lease permits" the tenant to sublet, assign, or both, subject only to reasonable limitations.224 If the lessor's consent is required, the lease must provide that consent "shall not unreasonably be withheld."225 The remedy is available only if the lessor expressly subjects himself or herself to a reasonableness standard. The Kendall dissent argued that the legislature provided the remedy as an incentive to forego the right to

216. Id. at 504, 709 P.2d at 848, 220 Cal. Rptr. at 829.
219. Id. at 510, 709 P.2d at 851-52, 220 Cal. Rptr. at 832-33 (Lucas, J., dissenting).
220. CAL. CIV. CODE § 1951.2.
221. Id. § 1951-2(a)(2).
222. Kendall, 40 Cal. 3d at 502, 709 P.2d at 846, 220 Cal. Rptr. at 827.
223. CAL. CIV. CODE § 1951.4.
224. Id.
225. Id.
withhold consent unreasonably.\textsuperscript{226} It follows, the dissent argued, that the legislature must have recognized the contractual right to withhold consent unreasonably.\textsuperscript{227} The majority called this speculation.\textsuperscript{228} The majority stated that implied statutory recognition of a common-law rule that is not the subject of the statute does not codify the rule.\textsuperscript{229} Also, such implied recognition does not prevent a court from reexamining the rule.\textsuperscript{230}

The majority and dissent positions can be reconciled. The dissent argued that the legislature provided the lock-in remedy in part as an incentive for a lessor to forego the right to withhold consent in his or her sole discretion.\textsuperscript{231} The majority did not prohibit an express sole discretion standard. It implied a reasonableness standard where there was no express contrary language.\textsuperscript{232} Thus, the lessor has the incentive to give up a sole discretion standard in order to obtain the lock-in remedy, but if the lessor does not wish to forego the sole discretion standard, the lease must expressly provide for it.

There is another argument based on section 1951.4; one that was not specifically mentioned by the dissent. In order for the lock-in remedy to be available, the lease must permit the tenant to sublet, assign, “or both.” The statute clearly requires that the lessor allow either a sublease or an assignment or both, without restriction or with reasonable restrictions. It just as clearly allows the lessor to prevent either a sublease or an assignment without the reasonableness standard limitation. This argument can also be reconciled with the majority position by emphasizing the narrowness of the majority’s holding—in the absence of an express standard, reasonableness will be implied.

The remedy legislation package adopted in 1970 was the product of an extensive review by the California Law Revision Commission.\textsuperscript{233} It seems that the Commission and the legislature assumed the existence of the traditional rule in California, but did not specifically consider whether it should be followed or rejected. The remedies revision was a major undertaking and understandably occupied their attention. Now

\textsuperscript{226} Kendall, 40 Cal. 3d at 510, 709 P.2d at 852, 220 Cal. Rptr. at 833 (Lucas, J., dissenting).
\textsuperscript{227} Id. (Lucas, J., dissenting).
\textsuperscript{228} Id. at 506, 709 P.2d at 849, 220 Cal. Rptr. at 830.
\textsuperscript{229} Id.
\textsuperscript{230} Id.
\textsuperscript{231} Id. at 510, 709 P.2d at 852, 220 Cal. Rptr. at 833 (Lucas, J., dissenting).
\textsuperscript{232} Id. at 506-07, 709 P.2d at 849, 220 Cal. Rptr. at 830.
\textsuperscript{233} See Abandonment or Termination of a Lease, 8 CAL. L. REVISION COMM’N REP. 701 (1966); 9 CAL. L. REVISION COMM’N REP. 401 (1968); 9 CAL. L. REVISION COMM’N REP. 153 (1969).
that issues concerning restraints on leasehold transfers have become
more pronounced, Civil Code section 1951.4 should be re-examined.
This will be done below.

F. Guidelines for Reasonableness

The Kendall decision points out some factors that may be consid-
ered in applying the reasonableness standard. They are: financial re-
sponsibility of the new party; legality and suitability of the use of the
premises; need for alterations of the premises; and nature of occu-
pancy.\textsuperscript{234} The court mentioned other situations where courts have con-
sidered the lessor's objection to be reasonable. These situations were:
the desire to have one lead tenant in order to preserve the building image;
the desire to preserve tenant mix in a shopping center; and the belief that
a proposed specialty restaurant would not succeed at the location.\textsuperscript{235}
The court considered it unreasonable to deny consent "solely on the basis
of personal taste, convenience or sensibility," or for the purpose of charg-
ing more rent than originally agreed.\textsuperscript{236} Other examples can be found in
cases involving clauses that contain an express reasonableness standard.

Once a reasonableness standard has been negotiated or imposed, the
question of what is reasonable is generally one of fact.\textsuperscript{237} This Article is
concerned with the more basic question of when a reasonableness stan-
dard will be imposed. Therefore, there will not be an extensive discus-
sion of cases applying the reasonableness standard.

G. Application to Types of Restriction Clauses

Section D of this Article describes eight different types of transfer
restriction clauses. The Kendall case involved the "Silent Consent Stan-
dard" type clause.\textsuperscript{238} The clause did not contain an express standard for
consent. The court only had to decide whether to infer a reasonableness
or a sole discretion consent standard in the absence of any express stan-
dard. It inferred a reasonableness standard and thus, departed from the
common-law and majority view on this particular issue. The case has no
impact on the "Express Reasonable Consent Standard"\textsuperscript{239} type clause,
except for language in the case discussing what may or may not be con-

818, 826 (1985).
\textsuperscript{235} Id. at 502, 709 P.2d at 846, 220 Cal. Rptr. at 827.
\textsuperscript{236} Id. at 501, 709 P.2d at 845, 220 Cal. Rptr. at 826.
\textsuperscript{237} Id.
\textsuperscript{239} See supra notes 24-25 and accompanying text.
sidered reasonable. Supra note 240. The “Express Sole Discretion Consent Standard,” Supra note 241 “Absolute Prohibition” Supra note 242 and “Possession Recovery” Supra note 243 type clauses were not expressly involved in the Kendall case. Drawing inferences from language used to resolve the narrow issue actually involved in the case is dangerous. There may be clues in the case to predict the attitude of the court members who decided Kendall. However, such divining by crystal ball must take into consideration that four out of five in the majority are no longer on the court Supra note 244 and both of the dissenters are still sitting. Supra note 245 Some feel that the change in court personnel will favor lessors, at least where questions of reasonableness arise.

The Kendall court used broad general language to both criticize the traditional common-law rule and to support a reasonableness standard. Supra note 246 Much of that language could be applied to an express sole discretion standard clause. On the other hand, the court referred to the Restatement as support for modern rejection of the traditional common-law rule. Supra note 247 The Restatement infers a reasonableness standard in a “Silent Consent Standard” type of clause, but it also allows a freely negotiated “absolute right to withhold consent.” Supra note 248 The court clearly recognized the impact of the Restatement position. It commented that the Restatement rule would validate a clause giving the lessor “absolute discretion” or the power of “absolutely prohibiting” an assignment (or sublease). Supra note 249 However, the court added that the case does not involve the question of the validity of those clause types. Supra note 250

Kendall did not deal directly with the “Express Specific Requirements” type clause. If there is a question about the reasonableness of a specific requirement, the general discussion of reasonable objections will be of help. If there is a question whether the parties can expressly agree to a specific requirement that does not meet a reasonableness test, the clue search mentioned above is involved again. Kendall applies directly to the “Consent Required But Exemptions” type clause if the clause is silent on the consent standard. If there is an express reasonableness stan-

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240. Kendall, 40 Cal. 3d at 501, 709 P.2d at 895, 220 Cal. Rptr. at 826.
241. See supra notes 24-25 and accompanying text.
242. Id.
243. Id.
244. Justices Bird, Reynoso, Grodin, and Kaus.
246. Kendall, 40 Cal. 3d at 501-05, 709 P.2d at 845-48, 220 Cal. Rptr. at 826-29.
247. Id. at 499-500, 709 P.2d at 844, 220 Cal. Rptr. at 825.
248. RESTATEMENT, supra note 91, § 15.2(2).
250. Id.
251. See supra notes 24-25 and accompanying text.
dard, Kendall has no impact except for language discussing the meaning of reasonableness. If there is an express sole discretion standard, there is no direct answer in the case.

Footnote seventeen in Kendall appears to show approval of a "Profit Shift" type clause that gives the lessor the right to profit from the assignment or sublease transaction. The Court stated in that footnote:

[Amicus counsel request[s] that we make clear that, "whatever principle governs in the absence of express lease provisions, nothing bars the parties to commercial lease transactions from making their own arrangements respecting the allocation of appreciated rentals if there is a transfer of the leasehold." This principle we affirm; we merely hold that the clause in the instant lease established no such arrangement.

Footnote seventeen also indicated that the court was aiming its broad criticism of the common-law rule at clauses that do not contain express language, not clauses that clearly put the tenant on notice of what to expect.

XI. CALIFORNIA AFTER THE KENDALL CASE

John Hogan Enterprises, Inc. v. Kellogg, decided in 1986 by the court of appeal, involved a percentage rent lease with a clause that limited use of the premises to a women's ready-to-wear shop. The tenant had been operating at a stable profit for several years and producing percentage rentals above the minimum rent. The tenant entered escrow to assign the lease to a third party who proposed to operate an antique store as a hobby. There would not be sufficient revenue to produce percentage rentals, so only the minimum rent would be paid by the third party for the remaining nine years of the term. The third party agreed to pay the tenant $150,000. This amount was "equivalent to the difference over the remaining nine years of the lease between the minimum rent and the actual rents the Lessor had historically received." The

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252. Id.
253. Kendall, 40 Cal. 3d at 505 n.17, 709 P.2d at 848 n.17, 220 Cal. Rptr. at 829 n.17.
254. Id.
256. Id. at 591-92, 231 Cal. Rptr. at 712.
257. Id. at 592, 231 Cal. Rptr. at 712. The original lease provided for a minimum monthly rent of $2,750. During the three years prior to the lessee's attempt to assign the lease, the average monthly rent, based on the percentage formula consistently exceeded the minimum monthly rent. In 1981, the average monthly rent exceeded $4,200; in 1982, it exceeded $4,000; and in 1983, it exceeded $3,700. Id. at 591, 231 Cal. Rptr. at 712.
258. Id. at 592 n.2, 231 Cal. Rptr. at 712 n.2.
lessor used a "Silent Consent Standard"\textsuperscript{259} type clause in the lease to object to the transfer.

The court applied \textit{Kendall} and subjected the lessor to a reasonableness standard.\textsuperscript{260} It made an irrefutable comment in holding, as a matter of law, that the lessor met the reasonableness standard: "Refusing to consent to highway robbery cannot be deemed commercially unjustified."\textsuperscript{261} The court drew an important distinction: a lessor's refusal to consent in order to increase his or her return above that provided in the lease is generally considered unreasonable.\textsuperscript{262} However, it is reasonable to object to a transfer that would place the lessor in a worse financial position than he or she bargained for and could expect to continue under a percentage lease.\textsuperscript{263}

The \textit{Hogan} court did not directly deal with the use clause. The clause limited use to a women's ready-to-wear shop.\textsuperscript{264} The third party intended to use the premises as an antique shop.\textsuperscript{265} Probably, the court considered the proposed change of use issue as included in, and overpowered by, the loss of rent issue. There does not seem to be a legitimate basis in the case to speculate that the court would have allowed the change in use if there had not been a drop in rent.

In \textit{Northridge Hospital Foundation v. Pic 'N' Save No. 9, Inc.},\textsuperscript{266} a 1986 court of appeal decision, the court cited \textit{Kendall} for the proposition that a lease is a contract and as such contained the duty of good faith and fair dealing implied in all contracts.\textsuperscript{267} However, the case did not discuss transfer restrictions. Instead, it involved a lessor and tenant attempting to eliminate a sublease by a voluntary surrender of the prime lease.\textsuperscript{268}

\textit{Airport Plaza, Inc. v. Blanchard},\textsuperscript{269} a 1987 court of appeal decision, is another case involving the question of reasonableness. Blanchard was the lessor of a seventy-five year ground lease. Airport Plaza, a corporation with two shareholders, was the successor tenant of the ground lease.\textsuperscript{270} The tenant, as required by the lease, built a shopping center.\textsuperscript{271}

\textsuperscript{259} See supra text accompanying note 24.
\textsuperscript{260} John Hogan Enters., 187 Cal. App. 3d at 593, 231 Cal. Rptr. at 713.
\textsuperscript{261} Id. at 594, 231 Cal. Rptr. at 714.
\textsuperscript{262} Id. at 593, 231 Cal. Rptr. at 713.
\textsuperscript{263} Id. at 593-94, 231 Cal. Rptr. at 713-14.
\textsuperscript{264} Id. at 591, 231 Cal. Rptr. 712.
\textsuperscript{265} Id. at 592, 231 Cal. Rptr. at 712.
\textsuperscript{266} 187 Cal. App. 3d 1088, 232 Cal. Rptr. 329 (1986).
\textsuperscript{267} Id. at 1100, 232 Cal. Rptr. at 336.
\textsuperscript{268} Id. at 1092, 232 Cal. Rptr. at 331.
\textsuperscript{269} 188 Cal. App. 3d 1594, 234 Cal. Rptr. 198 (1987).
\textsuperscript{270} Id. at 1597, 234 Cal. Rptr. at 199.
\textsuperscript{271} Id. at 1597-99, 234 Cal. Rptr. at 199-201.
Airport Plaza wanted to borrow money to recoup some of its investment in the property. It proposed to hypothecate its leasehold as security for the loan. The loan money was not to be reinvested in the center.\textsuperscript{272} Airport Plaza also proposed to dissolve the corporation and distribute its assets, including the hypothecated leasehold, to its two shareholders.\textsuperscript{273} The lessor objected to the hypothecation and the dissolution.\textsuperscript{274} 

A lease clause stated that the tenant could not transfer in whole or part without the lessor’s consent, except as otherwise provided in the lease.\textsuperscript{275} This is a “Silent Consent Standard” type clause governed by the \textit{Kendall} requirement of reasonableness.\textsuperscript{276} The lease provided that the tenant could hypothecate for purposes of improving the premises.\textsuperscript{277} It also provided that the tenant could assign the entire leasehold without the lessor’s consent if Airport Plaza remained liable until all encumbrances against the property had been paid off.\textsuperscript{278} 

The \textit{Airport Plaza} court held that the lessor was reasonable in objecting to the hypothecation because the lender required terms that varied substantially from the lease.\textsuperscript{279} The court also held that the lessor was reasonable in objecting to the dissolution of the corporation and assignment of its assets to its shareholders\textsuperscript{280} because the lessor’s security would have become impaired; the corporate assets would have become personal assets of the shareholders and would have been used for purposes other than the shopping center.\textsuperscript{281} The court recognized that, generally, a technical change of ownership or legal form is not a violation of a transfer restriction when the change does not affect the rights of the landlord.\textsuperscript{282} 

\textit{Multiplex Insurance Agency, Inc. v. California Life Insurance Co.},\textsuperscript{283} decided in 1987 by the court of appeal, involved an action by a general insurance agent against an insurance company for failure to pay commissions. The court relied on \textit{Kendall} concerning the propriety of bringing a tort action for breach of contract.\textsuperscript{284} The \textit{Cohen v. Ratinoff} case, by

\begin{thebibliography}{9}
\bibitem{272} Id. at 1597-98, 234 Cal. Rptr. at 199-200.
\bibitem{273} Id. at 1597, 234 Cal. Rptr. at 199.
\bibitem{274} Id. at 1597-98, 234 Cal. Rptr. at 199-200.
\bibitem{275} Id. at 1599, 234 Cal. Rptr. at 201.
\bibitem{276} Id.
\bibitem{277} Id. at 1599, 234 Cal. Rptr. at 200.
\bibitem{278} Id. at 1602, 234 Cal. Rptr. at 202.
\bibitem{279} Id. at 1601, 220 Cal. Rptr. at 202.
\bibitem{280} Id. at 1604, 220 Cal. Rptr. at 204.
\bibitem{281} Id. at 1603, 234 Cal. Rptr. at 203.
\bibitem{282} Id. at 1602, 234 Cal. Rptr. at 203.
\bibitem{284} Id. at 931, 235 Cal. Rptr. at 15.
\end{thebibliography}
reversing a judgment on the pleadings and remanding, allowed the tenant to proceed with a bad faith breach of contract cause of action and claim for punitive damages. Footnote eleven in Kendall pointed this out, expressed no view on the merits of the punitive damages claim in Cohen, and noted that not every breach of the good faith and fair dealing covenant results in a tort action.

Golden State Transit Corp. v. City of Los Angeles is a 1987 decision by a federal district court. An applicant for a taxicab franchise renewal sought an order that the franchise could be transferred without City restriction, other than good moral character of the transferee. The court refused to eliminate all restrictions and pointed out that the franchisee was adequately protected by the Kendall requirement of reasonableness.

Superior Motels, Inc. v. Rinn Motor Hotels, Inc., a 1987 court of appeal decision, involved whether an anti-receivership provision in a lease was an invalid restraint on alienation. The disputed lease clause provided that the appointment of a receiver to take possession of the tenant's assets would constitute a breach of the lease. The tenant attacked the clause as an unreasonable restraint on alienation, relying on Civil Code section 711, which provides: "Conditions restraining alienation, when repugnant to the interest created, are void." The court said that section 711 prohibits only restraints that are unreasonable, those not necessary to protect, or prevent impairment of, a security. The court cited Kendall and two secured loan transaction cases as authority for this proposition. The court further stated that it could not resolve in the abstract whether the clause was valid and there was no evidence regarding the necessity of the provision to protect security interests.

286. Id. at 330, 195 Cal. Rptr. at 89.
289. Id. at 575.
290. Id. at 575-76.
292. Id. at 1042, 241 Cal. Rptr. at 489.
293. Id. at 1059, 241 Cal. Rptr. at 500.
298. Id.
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Kreisher v. Mobil Oil Corp.,\textsuperscript{299} a 1988 court of appeal decision, deals with the retroactivity of the Kendall standard of reasonableness. It is discussed below at Section M of this part of the Article.

XII. PUBLIC POLICIES

The Kendall court relied on two distinct policies to support implying a reasonableness standard.\textsuperscript{300} The first is the contract policy of implying a covenant of good faith and fair dealing into every contract. The second is the real property policy against restraints on alienation.

A. Rule Against Restraints on Alienation

1. Common-law background and development

The real property rule against restraints on alienation has ancient origins in the law of England. It is older than the perennial favorite of property historians, the rule against perpetuities.\textsuperscript{301} It is possible that the policy of free alienability developed as a side effect of rules that were developed for quite different purposes.\textsuperscript{302} The first major statute dealing with the subject was a product of the English feudal system. Quia Emptores, adopted in 1290, provided that:

[I]t shall be lawful to every freeman to sell at his own pleasure his lands and tenements, or part of them; so that the feoffee shall hold the same lands or tenements of the chief lord of the same fee, by such service and customs as his feoffor held before.\textsuperscript{303}

This statute was aimed at freeing fee simple estates from the early English practice of subinfeudation. Subinfeudation involved the creation of layered continuing obligations to successive grantors.\textsuperscript{304}

Examination of the historical origins of the rule in early England does little to explain its vitality in the United States today. An early rationale, which was codified in California,\textsuperscript{305} is the “repugnancy” argument. Since a fee simple property interest is transferable, it is repugnant

\begin{thebibliography}{99}
\bibitem{Restatement} RESTATEMENT, supra note 91, Introductory note to Part II, at 142.
\bibitem{Id} Id.
\bibitem{Moynihan} For a general discussion of the common law background, see C. MOYNIHAN, supra note 11, at 1-24.
\bibitem{CalCivCode} CAL. CIV. CODE § 711 (West 1982).
\end{thebibliography}
to the nature of the fee simple interest to restrain transfer.\textsuperscript{306} One prominent commentator has found this rationale to be less than persuasive.\textsuperscript{307} He argues that if the interest is created subject to an express provision for forfeiture upon alienation, the very nature of the interest includes its inalienability.\textsuperscript{308} Thus, he argues, the repugnancy rationale is a poor expression of a policy of opposition to such restraints.\textsuperscript{309}

Another rationale for the rule against restraints is that there are only a certain number of recognized estates in real property. If the grantor of a fee simple could eliminate its characteristic of alienability, he or she would be able to create a new type of estate.\textsuperscript{310} Today, such a formalistic reason seems hollow as a basis for following the rule.

Courts and treatise writers have cited several social and economic policies to justify a rule against restraints on fee alienation. For example: (1) the average market price of property may be increased; (2) wealth may be increasingly concentrated if owners are unable to alienate property; (3) improvement of property will be discouraged if the owners cannot realize any increased value by a sale; and (4) creditors will suffer if they cannot reach the asset through security interests.\textsuperscript{311} Further, alienability increases productivity—if an owner is unable to make land productive, he or she will usually sell it to someone who can. If the owner cannot transfer to a more productive user and is reluctant to make improvements, the property will not be devoted to its highest and best use.\textsuperscript{312}

Some courts and commentators have recognized that restraints on alienation are not necessarily entirely bad. Restraints may actually facilitate development or have some other legitimate purpose that outweighs the impact of the restraint.\textsuperscript{313} For example, a restraint imposed on all purchasers of property in a residential development or interests in a con-

\begin{footnotes}
\item[306] C. MOYNIHAN, supra note 11, at 143; \textit{see}, e.g., Bonnell v. McLaughlin, 173 Cal. 213, 159 P. 590 (1916); McCleary v. Ellis, 54 Iowa 311, 6 N.W. 571 (1880); Pattin v. Scott, 270 Pa. 49, 112 A. 911 (1921).
\item[307] 6 AMERICAN LAW OF PROPERTY § 26.19, at 439 (A.J. Casner ed. 1952) [hereinafter PROPERTY].
\item[308] \textit{Id.}
\item[309] \textit{Id.}
\item[310] 3 Simes & Smith, \textit{The Law of Future Interests} § 1134 (2d ed. 1956).
\item[311] 6 PROPERTY, supra note 307, § 26.3, at 412-14.
\item[313] Northwest Real Estate Co. v. Serio, 156 Md. 229, 236-39, 144 A. 245, 247-48 (1929) (Bond, C. J., dissenting); 3 Simes & Smith, \textit{supra} note 310, § 1115, at 8.
\end{footnotes}
dominium or cooperative may secure mutual protection of the purchasers' investments and common expectations. This recognition of legitimate uses for restraints tends to militate against an absolute prohibition of restraints. Instead, it results in a balancing of the negative impact of the restraint against the positive purpose of the restriction.

The duration of the restraint and the effect of violation are also factors to consider. A restraint on a fee simple for a limited period may be viewed more favorably than a perpetual restraint. A forfeiture type restraint results in either a waiver of objection to the transfer or a forfeiture resulting in re-transfer. The forfeiture restraint is viewed more favorably than a disabling restraint, which negates the restricted transfer.

Although a perpetual restraint on a fee simple is void, Kentucky, and perhaps other states, would allow a forfeiture restraint of limited duration on a fee simple.

The principal target of the rule against restraints on alienation has been the fee simple estate. In contrast, most courts uphold forfeiture restraints on life estates. The life estate is not as alienable as the fee simple even absent restriction, and there are additional reasons why a grantor may want to restrict transfer of a life estate.

The rule against restraints on alienation was not directed against restrictions on transfers of leasehold estates, except with respect to the strict construction of restriction language. According to one commentator, "[t]he common-law hostility to restraints on alienation had a large exception with respect to estates for years. A lessor could prohibit the lessee from transferring the estate to whatever extent he might desire." The lessor's continuing interest in the property, both during and after the lease term, is a major interest and a strong incentive for control.

314. Restatement, supra note 91, Introductory note to Chap. 4, at 158-59.
316. 6 Property, supra note 307, § 26.9, at 419.
317. Id. § 26.15, at 430; see, e.g., Cushing v. Spalding, 164 Mass. 287, 41 N.E. 297 (1895); Stansbury v. Hubner, 73 Md. 228, 20 A. 904 (1890).
318. Robertson v. Simmons, 322 S.W.2d 476 (Ky. 1959); Cammack v. Allen, 199 Ky. 268, 250 S.W. 963 (1923); Francis v. Big Sandy Co., 171 Ky. 209, 188 S.W. 345 (1916).
319. See, e.g., Conger v. Lowe, 124 Ind. 368, 24 N.E. 889 (1890); Ford v. Ford, 230 Ky. 56, 18 S.W.2d 859 (1929); Lariverre v. Rains, 112 Mich. 276, 70 N.W. 583 (1897).
320. 6 Property, supra note 307, § 26.48, at 485.
321. 2 R. Powell, supra note 11, § 246, at 372.97.
322. For a more complete discussion of the common-law and majority rule with respect to leaseholds, see supra Section G.1.
2. California rule against restraints

In 1872, the California legislature adopted California Civil Code section 711 which states: "Conditions restraining alienation, when repugnant to the interest created, are void." The common-law rule against restraints, discussed above, considered restraints repugnant to a fee simple interest, but not repugnant to a leasehold interest. There is nothing in the statute to indicate it was doing something other than adopting the common law. Thus, it must be construed as a continuation of the common law, not as a new enactment.

In 1978, the California Supreme Court, in *Wellenkamp v. Bank of America*, clearly adopted a balancing test for the validity of restraints affecting alienation of fee simple estates. The *Wellenkamp* family of cases involved secured credit transactions with restrictions on the encumbrance, installment sale and conveyance of a fee simple estate. The cases involved deeds of trust securing loans and creating security interests in fee simple estates. Clauses in the deeds of trust permitted the lenders to accelerate the due date and call the loans upon transfer (or encumbrance) of an interest in the property. The *Wellenkamp* court recognized that section 711 does not prohibit all restraints, only unreasonable ones. A balancing test is applied to determine reasonableness. The justification for the restriction is compared with the quantum of restraint in order to determine reasonableness. Although *Wellenkamp* applied the rule against restraints to transactions apparently not contemplated by the common-law rule, loan security interests, the case can be viewed as liberalizing the common-law rule against restraints on fee simple estates. The restraints are not automatically void; they are subject to a balancing test.

*Cohen v. Ratinoff*, decided in 1983, was the first California appellate decision to apply section 711 to a leasehold. The court stated that only unreasonable restraints are invalid and cited the *Laguna Royale*

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323. CAL. CIV. CODE § 711 (West 1982).
324. See supra notes 301-22 and accompanying text.
325. CAL. CIV. CODE § 5 (West 1982).
326. 21 Cal. 3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978).
328. *Wellenkamp*, 21 Cal. 3d at 948, 582 P.2d at 973, 148 Cal. Rptr. at 382 (citing Coast Bank v. Minderhout, 61 Cal. 2d 311, 392 P.2d 265, 38 Cal. Rptr. 505 (1964)).
329. Id. at 949, 582 P.2d 973-74, 148 Cal. Rptr. at 382-83.
330. Id., 582 P.2d at 973, 148 Cal. Rptr. at 382.
332. An earlier case is distinguishable because it involved a condominium development.
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case. Laguna Royale involved basically a condominium transaction, not a typical leasehold transaction. The Cohen court concluded that the "Silent Consent Standard" type of clause was not inherently repugnant to the leasehold interest because the lessor has an interest in the character of the proposed transferee. However, the court held that there is an unreasonable restraint if the clause is implemented in such a manner that "its underlying purpose is perverted by the arbitrary or unreasonable withholding of consent." In a footnote, the court commented that the tenant argued that the reasoning of Wellenkamp should apply to leases. The court went on to say: "Since Wellenkamp did not involve a leasehold interest, it is distinguishable from the instant case." However, the court did not explain its extension of the common-law rule against restraints, and section 711, to leaseholds. Note that the court used the implied covenant of good faith and fair dealing, discussed below, as an independent basis for imposing a reasonableness standard on the lessor.

The Kendall court saw no modem justification for exempting leases from a general policy prohibiting unreasonable restraints on alienation. It borrowed the balancing test from Wellenkamp and stated: "Reasonableness is determined by comparing the justification for a particular restraint on alienation with the quantum of restraint actually imposed by it." The court quoted a commentator's doubts about the continued vitality of the common-law treatment of leaseholds:

A lessor could prohibit the lessee from transferring the estate for years to whatever extent he might desire. It was believed that the objectives served by allowing such restraints outweighed the social evils implicit in the restraints, in that they gave to the lessor a needed control over the person entrusted with the lessor's property and to whom he must look for the performance of the covenants contained in the lease. Whether this reasoning retains full validity can well be doubted. Rela-

336. Id.
337. Id. at 328 n.2, 195 Cal. Rptr. at 88 n.2.
338. Id.
339. Id. at 330, 195 Cal. Rptr. at 89.
tionships between lessor and lessee have tended to become more and more impersonal. Courts have considerably lessened the effectiveness of restraint clauses by strict construction and liberal applications of the doctrine of waiver.\textsuperscript{341} The Kendall court also cited with approval the Restatement proposition that the lessor’s consent to transfer by the tenant cannot be withheld unreasonably, unless a freely negotiated lease provision gives the lessor the absolute right to withhold consent.\textsuperscript{342}

There is no question that the Kendall decision uses strong language to criticize the common-law and majority rule which allows the lessor to retain sole discretion over a leasehold transfer. Similarly, there is no question that the result in Kendall can be accomplished without completely overturning the common-law and majority rule. The case involved a “Silent Consent Standard” type clause, one which did not expressly state that consent could be withheld in the lessor’s sole discretion.\textsuperscript{343} An application of strict construction of restriction clauses and fair disclosure to the tenant would justify imposition of a reasonableness standard, absent an express provision to the contrary. This would satisfy the legitimate concerns expressed in Kendall, but leave the parties free to bargain and expressly provide for a sole discretion standard, or for other clauses that expressly exempt the lessor from the scrutiny of a reasonableness standard. Such a result would be consistent with the developing minority view and the Restatement position cited in Kendall.\textsuperscript{344} It may also be concluded that it is “reasonable” to allow the parties to bargain and expressly provide for a sole discretion standard or specific requirements that are not subject to litigation.\textsuperscript{345}

The imposition of a reasonableness standard in the absence of an express sole discretion standard or specific set of requirements seems to be a fair and logical extension of the strict construction of restraints on leasehold transfers. This would reduce the chances of unpleasant surprises for the tenant at the time of transfer, and it would encourage lessors to bargain for an express clause if they want to avoid the reasonableness standard. There is some question concerning the fairness of retroactivity, but otherwise this development in Kendall appears justified. However, it seems unnecessary and undesirable to extend this de-

\textsuperscript{341} Id. at 499, 709 P.2d at 844, 220 Cal. Rptr. at 825.
\textsuperscript{342} Id. at 499-500, 709 P.2d at 844, 220 Cal. Rptr. at 825. For a discussion of the Restatement position, see supra notes 91-103 and accompanying text.
\textsuperscript{343} Kendall, 40 Cal. 3d at 503, 709 P.2d 847, 220 Cal. Rptr. at 828.
\textsuperscript{344} See supra notes 247-49 and accompanying text; see also supra notes 54-103.
\textsuperscript{345} See supra notes 34-49 and accompanying text.
development beyond the facts of *Kendall* to a mandatory reasonableness standard test for all types of leasehold transfer restrictions, regardless of express contrary language in the lease. Such an extension is not supported by the holdings in the developing minority view cases, and it is not supported by the Restatement position.

One of the reasons mentioned for curtailing restrictions is the shortage of vacancies. Vacancies fluctuate with time and place, and there are major factors at work in producing or reducing them. An economic outlook report in early 1988 was entitled “Slow growth, higher vacancies cast ominous shadows over commercial real estate in '88.”\(^\text{346}\) The report mentions several factors contributing to vacancies reaching up to 40% in some areas of Los Angeles County, but does not mention free transferability of leaseholds as one of them.\(^\text{347}\)

It is possible to hypothesize public ills resulting from restraints on leasehold transfers, or to encounter anecdotal incidents of individual problems. However, this Author found no empirical study that showed that the common-law view, majority view or the Restatement modified common-law view in fact caused problems serious enough to warrant removing the freedom of contract.

The California Supreme Court has recognized that intellectual criticism of a rule may not accurately reflect an actual problem. In particular, in *Keys v. Romley*,\(^\text{348}\) an action was brought for damages caused by surface water run-off.\(^\text{349}\) The court admitted that the rule followed in California since 1873 tended to inhibit the improvement of land.\(^\text{350}\) The court stated:

> [N]o documentation has been produced to establish that the rule has in fact impeded urban development in the state. A number of highly urbanized states follow the rule, and California’s phenomenal growth rate, to which no one can be oblivious and of which this court may take judicial notice, appears un-stunted by the existence and application of the civil law rule since 1873.\(^\text{351}\)

Justice Mosk, who was one of the two dissenters in *Kendall*, made this comment in the unanimous *Keys* decision.

It is naive to assume that all lessors would win a negotiation for a

\(^{347}\) Id.
\(^{348}\) 64 Cal. 2d 396, 412 P.2d 529, 50 Cal. Rptr. 273 (1966).
\(^{349}\) Id. at 398, 412 P.2d 530, 50 Cal. Rptr. at 274.
\(^{350}\) Id. at 402, 412 P.2d at 533, 50 Cal. Rptr. at 277.
\(^{351}\) Id. at 406-07, 412 P.2d at 535, 50 Cal. Rptr. at 279 (footnote omitted).
clause lacking a reasonableness standard. Even if a lessor won such a negotiation, California already has a built-in statutory protection against lessors making massive use of clauses removing the reasonableness standard. California Civil Code section 1951.4 allows a lessor to use the important lock-in remedy upon breach and abandonment by a tenant only if the lease permits the tenant to transfer, subject only to limits that meet a reasonableness standard.352 Some lawyers feel that this remedy is so important that it makes any discussion of Kendall and sole discretion standards moot.

Another factor to consider is the remedy available to a lessor for violation of the restraint by a tenant. California appears to limit the lessor to a forfeiture remedy.353 This limitation is traditionally viewed more favorably than a disabling restraint, which would nullify an attempted transfer.354

There appears to be good reason to impose a reasonableness standard in the absence of an express contrary agreement of the parties. There does not appear to be a compelling reason to change the rule against restraints on alienation and take away freedom of contract by prohibiting an express provision for sole discretion.355 The Restatement position reflects these conclusions.356

Although there are some shorter limits for certain types of leases, the maximum duration allowed for a lease in California is ninety-nine years.357 An argument could be made that extremely long-term leases approach the practical duration of a fee simple, and thus, should be subject to the same strict prohibition against restraints. It seems that long-term leases tend to be complex, highly negotiated transactions and best left to the agreement of the parties. However, if there is a realistic, compelling reason to impose a mandatory reasonableness standard on long-term leases, the problem could be solved by a time limit after which a mandatory reasonableness standard would govern. A time limit would be a more direct solution than an absolute rule applicable to all leases regardless of duration. However, the exact time picked for a time limit appears to be a rather arbitrary choice.

352. See infra notes 451-78 and accompanying text for further discussion of section 1951.4.
354. 6 PROPERTY, supra note 307, §.26.9, at 419; RESTATEMENT, supra note 91, § 15.2, comments b-d, n.4.
355. “If it ain’t broke, don’t fix it.” Source unknown.
356. See supra notes 91-103 and accompanying text.
Before leaving the alienability issue, it is interesting to note that a strong and enforceable leasehold transfer restriction clause will probably enhance the alienability of the lessor’s reversion.

B. Implied Covenant of Good Faith and Fair Dealing

The Kendall court used the implied covenant of good faith and fair dealing as a basis for implying a reasonableness standard into the “Silent Consent Standard” type clause.³⁵⁸ The covenant of good faith and fair dealing is implied into every contract in California.³⁵⁹ Basically, the covenant requires that neither party do anything to deprive the other of the contemplated benefits of the agreement.³⁶⁰ A lease is considered to be a contract as well as a conveyance.³⁶¹ Thus, every lease includes an implied covenant of good faith and fair dealing.

The covenant of good faith and fair dealing focuses on the bargain of the parties and their expectations flowing from that bargain. It has been said that “[g]ood faith performance... occurs when a party’s discretion is exercised for any purpose within the reasonable contemplation of the parties at the time of formation—to capture opportunities that were preserved upon entering the contract, interpreted objectively.”³⁶² If the clause imposes a consent requirement, but does not expressly state a reasonableness standard or a sole discretion standard, Kendall would find a reasonableness standard contemplated by the tenant and imply that standard based on good faith and fair dealing.

It is rather easy to use good faith and fair dealing to imply a reasonableness standard in the absence of an express agreement to the contrary. This is what the Kendall court did and nothing else. It would be quite a different matter to use good faith and fair dealing to mandate a reasonableness standard in the face of express language to the contrary.

Generally, courts will not find an implied covenant regarding a subject in a contract when the contract comprehensively covers that subject.³⁶³ For example, in Commercial Union Assurance Companies v.

³⁶⁰. Kendall, 40 Cal. 3d at 500, 709 P.2d at 844, 220 Cal. Rptr. at 825; see also Seaman’s, 36 Cal. 3d at 768, 686 P.2d at 1166, 206 Cal. Rptr. at 362.
³⁶¹. Kendall, 40 Cal. 3d at 498, 709 P.2d at 843, 220 Cal. Rptr. at 824; CAL. CIV. CODE. § 1925 (West 1985).
³⁶³. See Lippman v. Sears, Roebuck & Co., 44 Cal. 2d 136, 280 P.2d 775 (1955); Cousins
Safeway Stores, Inc., the California Supreme Court declared that the extent of the duty of good faith and fair dealing depends upon the nature of the bargain struck and the legitimate expectations of the parties arising from the contract. Moreover, in the Seaman's case, the court stated that although the parties may not be permitted to disclaim the covenant of good faith and fair dealing, they are free, within reasonable limits, to agree upon the standards by which application of the covenant is to be measured.

A 1933 New York decision is credited with the first statement of the now standard doctrine of good faith and fair dealing. More recently, in VTR, Inc. v. Goodyear Tire & Rubber Co., a federal district court in New York referred to general contract principles in Corbin's treatise on contracts to make very specific comments on the relationship between the covenant of good faith and fair dealing and express provisions in the contract. The court commented:

The general rule [regarding the covenant of good faith and fair dealing] . . . is plainly subject to the exception that the parties may, by express provisions of the contract, grant the right to engage in the very acts and conduct which would otherwise have been forbidden by an implied covenant of good faith and fair dealing.

. . . .

No case has been cited and I know of none which holds that there is a breach of an implied covenant of good faith and fair dealing where a party to a contract has done what the provisions of the contract expressly give him the right to do . . . . As to acts and conduct authorized by the express provisions of the contract, no covenant of good faith and fair dealing can be implied which forbids such acts and conduct.

. . . .

The allegations that the defendants acted in bad faith are mere characterizations by the plaintiffs and add nothing to their claim for relief. Whether or not the acts and conduct of the


365. Id. at 918, 610 P.2d 1041, 164 Cal. Rptr. at 712.

366. Seaman's, 36 Cal. 3d at 769, 686 P.2d at 1167, 206 Cal. Rptr. at 363.

367. See Burton, supra note 362, at 379, where the author states that the doctrine was first formulated in Kirké La Shelle Co. v. Paul Armstrong Co., 263 N.Y. 79, 188 N.E. 163 (1933).

defendants are in bad faith is to be determined here by whether or not they had the right to engage in them under the contract. Since they had such right, defendants cannot be said to have acted in bad faith.\textsuperscript{369}

The court also mentioned that merely because a party agreed to a bad bargain does not change the result.\textsuperscript{370}

If the lessor bargains for and gets an express clause negating the reasonableness standard on a transfer restriction, the tenant is put on notice that the reasonableness standard is not one of his or her contractual expectations. It may be considered reasonable for a lessor to want such a provision.\textsuperscript{371} A later claim by the tenant that the lessor should be subject to a reasonableness standard despite express contrary language would be an attempt to deny the lessor the benefit of his or her bargained contractual expectations.

Thus, there appears to be good reason, based on the implied covenant of good faith and fair dealing, to impose a reasonableness standard in the absence of an express contrary agreement of the parties. However, if there is an express agreement to the contrary, there does not appear to be a compelling reason to take away the freedom of contract by mandating a reasonableness standard. The Restatement position reflects these conclusions.\textsuperscript{372}

\textbf{C. The Restatement Compromise}

The Restatement position seems to strike the best compromise between freedom of contract and public policy. It imposes a reasonableness standard unless the parties freely negotiate and expressly provide to the contrary.\textsuperscript{373} It places the emphasis on reasonable expectations and disclosure, rather than on mandating a reasonableness standard in the face of contrary language.\textsuperscript{374}

This position is a carefully considered solution to the criticisms leveled against the traditional common-law rule. The Restatement is the source most often referred to by courts that move away from the traditional rule. If the traditional rule is considered inadequate in some respects by more states, the Restatement position will have an advantage

\textsuperscript{369} Id. at 777-80.
\textsuperscript{370} Id. at 480.
\textsuperscript{371} See supra notes 344-45 and accompanying text.
\textsuperscript{372} See supra notes 91-103 and accompanying text.
\textsuperscript{373} RESTATEMENT, supra note 91, § 15.2.
\textsuperscript{374} Id.
over other possible solutions: it will develop a national body of interpretations.

There is a phrase in the Restatement position that could use some clarification. The Restatement requires that a clause providing for the absolute right of the lessor to withhold consent be "freely negotiated."\textsuperscript{375} It is clear that total equality of bargaining power is not required; however, the Restatement does not consider a clause freely negotiated if the tenant has "no significant bargaining power in relation to the terms of the lease."\textsuperscript{376} The relationship between the phrase "freely negotiated" in the Restatement and the contract law adhesion doctrine in California is unclear. California has a well developed body of law defining the parameters of the adhesion doctrine as a means of protecting one contracting party from overreaching by the other.\textsuperscript{377} Stability and predictability in contractual relationships are important, especially when dealing with real property interests. If the Restatement position is adopted in California, consideration should be given to clarifying the requirements of "freely negotiated." One means of clarification would be to adopt the adhesion doctrine as the test. Since this doctrine is already an integral part of California law, there would be no problem of unfairness created by retroactive application.

Another factor involved in the stability and predictability of contracts is the burden of proof. Contracts and contract provisions should not be easily set aside. The tenant should have the burden of establishing the lack of free negotiation, which would result in the invalidity of the express language. This approach to valuing contract stability has been taken in other legislation crafted by the California Law Revision Commission.\textsuperscript{378}

XIII. RETROACTIVITY

The document containing the disputed "Silent Consent Standard" clause in Kendall was drafted and executed in 1969 (with a term commencing January 1, 1970).\textsuperscript{379} At that time, the most recent California case dealing specifically with the consent standard issue was Richard v. Degen & Brody, Inc.\textsuperscript{380} That case also involved the "Silent Consent Stan-

\textsuperscript{375} Id. comment i.
\textsuperscript{376} Id.
\textsuperscript{378} Cal. Civ. Code § 1671(b) (West 1985).
\textsuperscript{380} 181 Cal. App. 2d 289, 5 Cal. Rptr. 263 (1960).
It clearly followed the common-law and majority rule that the lessor was not bound by a reasonableness standard if the clause did not express one. There were no California cases adopting a different view at the time. It was not until fourteen years after the disputed document in Kendall was executed before a California court, in Cohen v. Ratinoff, squarely faced and rejected the common-law and majority rule.

The Kendall dissent argued that the lessor’s counsel was entitled to rely on the traditional rule as the state of the law in California when the document was executed, and it was unfair to reject the common-law rule retroactively. The dissent expressed the view that the contract was being rewritten by a retroactive rejection of the traditional rule. Also, it suggested that if a change was warranted, it should be made by the legislature.

The majority responded that the traditional rule had not been universally followed and that it had never been adopted by the California Supreme Court. The court commented that “the trend in favor of the minority rule should come as no surprise to observers of the changing state of real property law in the 20th century.” This is a noble thought, but can it be applied realistically to a lawyer drafting a lease in 1969?

Prior to the Cohen case, the “due on transfer” or encumbrance clause in a loan security document was the transfer issue receiving attention in California. The Wellenkamp decision in 1978 was relied upon heavily in Kendall. It was certainly possible to draw analogies from the “due on transfer” or encumbrance cases. However, it does not seem unreasonable that an attorney would conclude that a clause in a deed of trust restraining alienation of a fee simple interest would be distinguishable from a lease clause restraining assignment and subletting of a lease-

381. Id. at 292, 5 Cal. Rptr. at 265.
382. Id. at 299, 5 Cal. Rptr. at 269.
384. Kendall, 40 Cal. 3d at 508-09, 709 P.2d at 850-51, 220 Cal. Rptr. at 831-32 (Lucas, J., dissenting).
385. Id. at 511, 709 P.2d at 851, 220 Cal. Rptr. at 832 (Lucas, J., dissenting).
386. Id. (Lucas, J., dissenting).
387. Id. at 496, 709 P.2d at 852, 220 Cal. Rptr. at 823.
388. Id. at 504, 709 P.2d at 847, 220 Cal. Rptr. at 828.
389. Id. at 498, 709 P.2d at 843, 220 Cal. Rptr. at 824 (citing Wellenkamp v. Bank of Am., 21 Cal. 3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978)). Wellenkamp was given only limited retroactivity. It was not applied when, prior to the date the decision became final, the lender had enforced the clause by foreclosure, or waived enforcement in return for a modification agreement.
hold. Indeed, the Cohen court made such a distinction.\(^{390}\) Also, it seems that the California Supreme Court did not clearly start its journey toward Wellenkamp until 1971 when it decided La Sala v. American Savings & Loan Association.\(^{391}\) This was after the Kendall document had been executed.

An Article in the January, 1970 issue of the Hastings Law Journal, criticized the application of the traditional rule to residential leases and argued for change.\(^{392}\) However, it pointed out that “[e]xcept for dictum in a Massachusetts district court case, and an apparently controlling decision in Louisiana, this harsh rule is accepted everywhere.”\(^{393}\) Additionally, there was a particularly perceptive prediction in a 1980 Article in the California State Bar Journal.\(^{394}\) The Article reviewed the cases and concluded that the principles in the Wellenkamp loan security case should govern leasehold transfer restrictions.\(^{395}\) Both of these articles criticizing the traditional rule were published after the document in Kendall was executed.

Clearly, some lawyers believed California followed the traditional rule. The lawyers on the court in the unanimous, but vacated, court of appeal decision in Kendall expressed no doubts. The appellate court, referring to the “Silent Consent Standard” clause, stated:

\[\text{[I]t is obvious that the attorney for the lessor agreeing to such a term was entitled to rely upon the state of the law then existing in California. And at such time (Dec. 12, 1969) it is clear that California followed the “weight of authority” in these United States and allowed such consent to be arbitrarily or unreasonably withheld absent a provision to the contrary.}\]

That court expressed the view that it would be rewriting the contract of the parties to apply the minority view to the lease.\(^{397}\) It suggested that if California was going to adopt the minority view, it should be done by

\(^{390}\) Cohen, 147 Cal. App. 3d at 328 n.2, 195 Cal. Rptr. at 88 n.2. When dealing with deeds of trust, distinctions are important. A trustee under a deed of trust has been distinguished from an ordinary bearer. See Stephens, Partain & Cunningham v. Hollis, 196 Cal. App. 3d 948, 955 n.4, 242 Cal. Rptr. 251, 255 n.4 (1987).

\(^{391}\) 5 Cal. 3d 864, 489 P.2d 1113, 97 Cal. Rptr. 849 (1971).


\(^{393}\) Id. at 519.

\(^{394}\) Kehr, supra note 110.

\(^{395}\) Id. at 112-14.


\(^{397}\) Id. at 138.
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legislation. The unanimous court of appeal in the now disapproved decision in *Hamilton v. Dixon* opined that the *Richard* case (following the traditional rule) was "clearly the law" at the time a lease was signed in 1970, and it would be improper to rewrite the bargained rights and reasonable expectations of the parties. The unanimous opinion of the court of appeal in *Thrifty Oil Co. v. Batarse* referred to a trial court hearing that took place in July, 1983 (about three months before the *Cohen* decision), and commented that "[a]t that time the law was clearly in accord with *Richard v. Degen & Brody, Inc.*"

A practice handbook published by the California Continuing Education of the Bar in 1976 contains a sample of a "Silent Consent Standard" clause with the following comment:

A tenant should insist that the landlord agree not to unreasonably withhold its consent to a proposed assignment, encumbrance, or subletting, and most landlords agree to give such a clause. Without such an agreement the landlord can arbitrarily withhold its consent or attach conditions to the granting of its consent, and the tenant is without recourse.

Until the time that the *Cohen* case was decided in 1983, major treatises expressed the view that California followed the common-law and majority view.

It seems realistic to recognize that the law regarding leasehold restraints changed in the 1980s. A change based, at least in part, on the implied covenant of good faith and fair dealing should give careful consideration to the reasonable expectations of the parties at the time the bargain was struck. In February, 1988 a California court of appeal decided *Kreisher v. Mobil Oil Corp.* The unanimous decision contains a strong and thorough argument against retroactive application of *Kendall.* It is significant that the current California Supreme Court denied review.

In *Kreisher*, the trial court entered judgment against lessor Mobil,

398. *Id.*
400. *Id.* at 1009, 214 Cal. Rptr. at 642.
402. *Id.* at 773, 220 Cal. Rptr. at 287.
403. M. DEAN, F. NICHOLAS, R. CAPLAN, COMMERCIAL REAL PROPERTY LEASE PRACTICE § 3.110, at 159 (Cal. CEB 1976) [hereinafter LEASE PRACTICE].
406. *Id.* at 396-97, 243 Cal. Rptr. 666-67.
based on a jury verdict, for $214,000 compensatory damages and $2,002,500 punitive damages.\textsuperscript{407} The tenant, a Mobil station franchisee, based his causes of action on the lessor’s failure to comply with a reasonableness standard when the lessor refused to consent to a transfer of the tenant’s leasehold and gasoline service station franchise.\textsuperscript{408} The lease and franchise agreements both contained a “Silent Consent Standard” clause.\textsuperscript{409} One third party offered the tenant $28,000 for the transfer, and another offered $31,000.\textsuperscript{410}

The relationship between the parties was based on two related documents: a franchise agreement and a station lease.\textsuperscript{411} The relationship continued through a series of three-year term contracts going back to 1971.\textsuperscript{412}

The sequence of events leading to litigation started with a notice of default from the lessor to the tenant. The notice referred to the tenant’s breach of a continuous operation clause and stated the lessor’s intention to terminate if the default was not cured.\textsuperscript{413} The tenant responded with a notice of a third party’s offer of $28,000 for a transfer and a request for the lessor’s consent.\textsuperscript{414} The lessor refused without stating a reason, other than the lessor’s intention to terminate the lease and franchise.\textsuperscript{415} The lessor then learned of an additional breach, the failure to maintain insurance, and of revocation of the tenant’s resale permit by the State Board of Equalization.\textsuperscript{416} After giving an additional notice of termination for default, the lessor served the tenant with a three-day notice to quit.\textsuperscript{417} The tenant then notified the lessor of the second third party offer, this one for $31,000, and asked if the lessor wished either to meet that offer or consent to the transfer.\textsuperscript{418} The lessor rejected both proposals and commenced an unlawful detainer action.\textsuperscript{419} The tenant vacated prior to any further judicial action.\textsuperscript{420}

The tenant then filed an action against the lessor for compensatory

\textsuperscript{407} Id. at 395, 243 Cal. Rptr. at 666.
\textsuperscript{408} Id. at 393-94, 243 Cal. Rptr. at 664-65.
\textsuperscript{409} Id. at 392, 243 Cal. Rptr. at 664.
\textsuperscript{410} Id. at 393, 243 Cal. Rptr. at 664.
\textsuperscript{411} Id. at 392, 243 Cal. Rptr. at 664.
\textsuperscript{412} Id.
\textsuperscript{413} Id.
\textsuperscript{414} Id.
\textsuperscript{415} Id.
\textsuperscript{416} Id. at 392-93, 243 Cal. Rptr. at 664.
\textsuperscript{417} Id. at 393, 243 Cal. Rptr. at 664.
\textsuperscript{418} Id.
\textsuperscript{419} Id. at 393, 243 Cal. Rptr. at 665.
\textsuperscript{420} Id.
and punitive damages based on eight causes of action.\textsuperscript{421} The three causes of action that ultimately went to the jury and led to the judgment were: breach of contract and the implied covenant of good faith and fair dealing; intentional interference with prospective economic advantage; and intentional infliction of emotional distress.\textsuperscript{422}

The \textit{Kreisher} court indicated that contract execution, consent refusal and jury verdict all occurred before the \textit{Kendall} decision was filed on December 5, 1985.\textsuperscript{423} That case subjected lessors to a reasonableness standard, implied into "Silent Consent Standard" clauses.\textsuperscript{424} The court reviewed the principles involved in retroactivity, including foreseeability, reliance, public policy and fairness.\textsuperscript{425} It then concluded:

\begin{quote}
Our weighing of the relevant considerations comes down to this. At all relevant times, the prevailing rule of law was that a lessor could withhold assent to a proposed assignment for any reason whatsoever. Mobil displayed considerable and justifiable reliance on that rule. . . . The strength and extent of that reliance is only partially offset by Mobil's inability to foresee the nonjudicial portents of a change in the rule. By contrast, there is no evidence that plaintiff had any inkling of a judicial change of the rule. . . . Public policy supporting the change will not be advanced by applying the change to completed contractual arrangements involving the stability of real property titles. As regards the fairness factor, we perceive no satisfying basis for making plaintiff the windfall beneficiary of a change he did not foresee or help bring about. Conversely, it is patently unfair to penalize Mobil for its nonconformity with standards which took effect only after it conscientiously determined the state of the law and relied upon it in reasonable good faith.\textsuperscript{426}
\end{quote}

The court reversed the judgment because the refusal to give consent was at the heart of all the causes of action.\textsuperscript{427}

Since \textit{Kreisher} involved a petroleum dealer franchise, as well as a lease, the court also discussed California Business \& Professions Code section 21148.\textsuperscript{428} That section prohibits a franchisor from withholding consent to a transfer of the franchise unless certain requirements are

\begin{itemize}
\item \textsuperscript{421} \textit{Id.} at 393-94, 243 Cal. Rptr. at 665.
\item \textsuperscript{422} \textit{Id.} at 394, 243 Cal. Rptr. at 665.
\item \textsuperscript{423} \textit{Id.} at 396, 243 Cal. Rptr. at 667.
\item \textsuperscript{424} \textit{Kendall}, 40 Cal. 3d at 506-07, 709 P.2d at 849, 220 Cal. Rptr. at 830.
\item \textsuperscript{425} \textit{Kreisher}, 198 Cal. App. 3d at 403-04, 243 Cal. Rptr. at 672.
\item \textsuperscript{426} \textit{Id.} at 404, 243 Cal. Rptr. at 672.
\item \textsuperscript{427} \textit{Id.} at 405, 243 Cal. Rptr. 673.
\item \textsuperscript{428} \textit{Id.} at 403-04, 243 Cal. Rptr. at 671-72.
\end{itemize}
The section became effective on January 1, 1981, and was expressly made prospective in operation. The statute therefore did not apply to the pre-statute franchise in the case. Note that there could be a problem if a station dealer had both a franchise and a lease from a petroleum company and the two were subject to inconsistent transfer restrictions. This problem appears to be avoided by California Business & Professions Code section 21140 (a)(1). It defines a “franchise” to include the related lease. Thus, the same limitations on transfer restrictions apply to the dealer’s lease.

In the Kendall case, the lease, the refusal to consent and the trial all occurred before the Supreme Court opinion was filed. However, the tenant in that case did help bring about the change. This Article has mentioned some of the reasons a lessor may have for wishing to avoid application of a reasonableness standard. Another reason might be the desire to avoid the potential of a punitive damage jury award. Note that the highest price offered for a transfer in Kreisher was $31,000. The punitive damage award was $2,002,500.

XIV. THE SURPRISE PROFIT DEMAND

Unanticipated demands by lessors for profit from a transfer seem to stir the passions and cause a strong motivation to reject the common-law and majority view. The Cohen and Kendall cases are good examples. The same is true in other states. A demand unsupported by express lease provisions comes as a surprise to the tenant. That creates the problem. It is not created because the lessor seeks to benefit from an appreciation in the value of his property. In fact, if some lessors had not asked

429. CAL. BUS. & PROF. CODE § 21148 (West 1987).
430. Kreisher, 198 Cal. App. 3d at 403, 243 Cal. Rptr. at 671.
432. Id.
434. Id. at 493-94, 709 P.2d at 839-40, 220 Cal. Rptr. at 820-21.
435. See supra notes 34-49 and accompanying text.
436. Kreisher, 198 Cal. App. 3d at 393, 243 Cal. Rptr. at 664.
437. Id. at 394, 243 Cal. Rptr. at 665.
for more money than was specifically provided for in their leases, sometimes with colorful ambush language,\textsuperscript{440} probably little judicial attention would have been given to this area of the law.

There seems to be agreement that the reasonableness standard is satisfied when a lessor seeks to protect his or her expectations for the agreed rental return.\textsuperscript{441} However, when he goes beyond protecting the agreed rent and seeks to sweeten the deal without the benefit of an express clause, problems develop. The profit involved in the dispute typically arises because of an increase in the rental value of the property in excess of the amount of the agreed rent. The tenant indirectly enjoys the benefit of this bonus value while occupying premises worth more than the rent he or she pays. At the time of transfer, the tenant wants to profit directly from this bonus value by charging consideration for an assignment or higher rent for a sublease. The lessor wants to use the transfer as an event to profit from the increased value.

The desire to profit from an appreciation in property is not intrinsically evil or lacking in good faith. Both the lessor and the tenant have a motive to profit from the appreciation. For example, the lessor may argue that the tenant should look to his business, not the property, for profit. Conversely, the tenant may argue that he or she bears the risk of a decrease in rental value so he or she should have the benefit of an increase. Neither party is intrinsically entitled to the appreciation profit. The benefit of that profit is one to be derived from the bargain made between them.

A lessor who desires that the rent keep pace with the value of the property has always had more effective ways of doing so than to withhold consent under a “Silent Consent Standard” clause.\textsuperscript{442} Rent escalation based on periodic reappraisals is one way. Rent escalation based on a formula or one of the consumer price indices, although not directly tied to market value of the premises, is another way. A short-term lease, either with or without a right of first refusal, will keep bringing the rent up to a market rate. These methods can be bargained for and expressly set forth in the lease. The increase in rent and the tenant’s loss of bonus value resulting from these methods come as no surprise to the tenant.

The “Silent Consent Standard”\textsuperscript{443} clause does not have this charac-

\textsuperscript{440} Lessors have referred to the transfer restriction as a “license to steal” and to a demanded transfer fee as “blood money.” Schweiso v. Williams, 150 Cal. App. 3d 883, 885, 198 Cal. Rptr. 238, 239 (1984).
\textsuperscript{442} See supra note 24 and accompanying text.
\textsuperscript{443} Id.
teristic of express disclosure to the tenant. Preventing its use for unanticipated exaction of a profit that has not been bargained for is understandable. It is the surprise factor, imposed on the tenant's deal without prior negotiation and warning, that creates the problem and not the profit motive itself.

Judicial decisions designed to avoid the "Silent Consent Standard" surprise should not be extended to prevent the parties from expressly agreeing on a profit to the lessor triggered by a transfer. Such an extension would be economic policy making—a mandatory transfer of value from the lessor to the tenant at the time of transfer despite an express contrary agreement. It would also lead to incongruous results. The policy would be adopted to protect the profit of tenants. Lessors would probably place more reliance on drafting perfectly acceptable devices to raise the rent more effectively and more frequently. With a clause providing for a lessor profit upon transfer, the tenant at least, in most circumstances, can control the time when the additional profit to the lessor arises. Also, a tenant may want a "sweetheart" lease with initial rent below market for a particular tenant, but increasing to market upon transfer.444

At one extreme is the "Silent Consent Standard" clause involved in cases that reject the common-law and majority view and impose a reasonableness standard. After imposing the reasonableness standard, cases such as Cohen and Kendall typically hold that it is unreasonable to use the clause to extract additional profit.445 At the other extreme is the "Profit Shift" clause which expressly allows the lessor to participate in profit generated at the time of transfer.446 This profit is part of the original bargain, and it does not come as a late surprise hit on the tenant. Somewhat in between is the "Express Sole Discretion Consent Standard" type clause.447 This type of clause does not mislead the tenant into believing that the lessor is subject to a reasonableness standard. Rather, it has been held that a lessor can seek to improve, rather than just maintain, his or her position with this type of clause.448

Maybe the "Express Sole Discretion Consent Standard"449 would be

444. Cukierman v. Mechanic's Bank (In re J.F. Hink & Son), 815 F.2d 1314 (9th Cir. 1987).
446. See supra notes 24-25 and accompanying text.
447. Id.
449. See supra notes 24-25 and accompanying text.
less objectionable to some, and be less subject to litigation, if it could not
be used to exact additional profit. This would free the clause from the
demands and litigation of a reasonableness standard governing other de-
cisions by the lessor. It would leave the parties free to negotiate and expres
sly provide for lessor profit upon transfer. Such a compromise rule
would merely require fair disclosure of future profit entitlements. How-
ever, a prohibition against requiring additional money as a condition of
consent would not be without problems.

If a lessor has a reasonable justification for refusing consent, he
could be in jeopardy if he proposes a waiver of his or her objection in
return for a change in the economic terms of the lease. For example,
suppose it reasonably appears to a lessor that the proposed transferee
poses greater risks due to weak credit or inexperienced management.
Could the lessor agree to take on the greater risk for a greater return?
The frequency of this type of problem could be reduced by requiring the
lessor to have either an express increase in profit clause or a reasonable
justification to support a deal sweetener. Lessors would still be en-
couraged to rely on negotiation and express disclosure clauses in order to
avoid litigation over reasonableness.

There is another problem which is more difficult to avoid, and that
could provide a fruitful source of litigation. If there is a prohibition
against the use of the “Express Sole Discretion Consent Standard”
clause\textsuperscript{450} to demand greater profit, it would allow a tenant to attack a
refusal based on the lessor’s motivations. There would be difficulties
proving the lessor’s motivations. Since a lessor need not justify refusal to
consent, a tenant could have difficulty establishing the prohibited motive
unless the lessor openly stated it. On the other hand, a lessor could have
difficulty defending against a charge of secret profit motive without prov-
ing a reasonable justification for a refusal. Thus, a clause intended to be
simple and to avoid litigation could end up creating more practical
problems and litigation than it avoids.

XV. THE LOCK-IN REMEDY: CIVIL CODE SECTION 1951.4

A. The Remedy Legislation in General

This Article previously discussed certain remedy legislation,
adopted in 1970, and discussed the conflicting conclusions the Kendall
majority and dissent drew from it.\textsuperscript{451} The California Law Revision Com-
mission went through a lengthy and comprehensive process of reviewing

\textsuperscript{450} Id.

\textsuperscript{451} See supra notes 217-33 and accompanying text.
and proposing modifications to common-law remedies for tenant breaches. With few changes, the resulting legislation is contained in California Civil Code sections 1951 through 1951.8. These sections attempt to eliminate some of the problems with the common law and to create remedies that are essentially fair to both the lessor and the defaulting tenant.

The basic plan of the legislation, contained in section 1951.2, is to have upon tenant breach an immediate termination of the lease and an immediate cause of action for damages, including prospective rental loss damages. The contract rule of mitigation of damages is built in by allowing the tenant to prove post-termination rental loss that the lessor could have reasonably avoided. The termination of the lease is triggered by either of two situations: (1) the tenant breaching and abandoning the premises; or (2) the tenant breaching and the lessor terminating the tenant's right to possession of the premises.

According to the basic remedy, the tenant can unilaterally trigger a termination of the lease by breach and abandonment. The lessor is given the opportunity by section 1951.4 to prevent this termination and provide for a lock-in remedy. If the lease specifically provides for the remedy and this section is complied with, the lessor can lock-in the lease, that is, keep the lease in effect and continue to enforce its provisions. Relief is provided to the locked-in tenant by requiring that the lease permit the tenant to assign or sublet (or both), subject only to reasonable restrictions.

Certain agreements that are often called leases, but which have unique characteristics, are exempt from the application of the remedies legislation. For example, an agreement for exploration for or removal of natural resources is more in the nature of a profit a prendre than a lease and is exempt. There does not appear to be a strong reason to remove the exemption and subject those transactions to the recommendations below.


454. Id. § 1951.2.

455. Id. § 1951.2(a)(2).

456. Id. § 1951.2(a).

457. Id. § 1951.3.

458. Id. §§ 1952.4 (natural resource removal) and 1952.6 (public entity bond projects).

B. Effect of Civil Code Section 1951.4 on Bargaining Over Leasehold Transfer Restriction

One of the concerns expressed over allowing an "Express Sole Discretion Consent Standard" or an "Absolute Prohibition" type of clause is the lessor's bargaining power. Section 1951.4 gives the tenant a built-in edge with leasehold transfer restrictions. The lock-in remedy is a valuable option for the lessor, and he or she can have it only if the lessor subjects himself or herself to the reasonableness standard. Neither the "Express Sole Discretion Consent Standard" nor the "Absolute Prohibition" clause would qualify for the lock-in remedy.

C. Specific Applications of Civil Code 1951.4

The lock-in is available under section 1951.4(b) only "if the lease permits" the tenant to do any of the following:

(1) Sublet, assign, or both;

(2) Sublet, assign, or both, subject to "standards or conditions," and the lessor does "not require compliance with" any "unreasonable" standard or condition;

(3) Sublet, assign, or both, "with the consent of the lessor," and "the lease provides" that consent "shall not unreasonably be withheld."

Suppose a lease does not restrict the tenant's right to assign or sublet. The tenant is automatically allowed to assign or sublet, without restriction and without obtaining the lessor's consent. Thus, if nothing is said one way or the other about leasehold transfers in the lease, the tenant is permitted to assign or sublet. Does the phrase "if the lease permits" in the introductory language of section 1951.4(b) indicate that the permission must be stated in the lease? Logically, express language of permission should not be required, since the tenant receives the intended freedom to transfer whether an express clause is present or not. It can be argued that the "lease permits" if it does not prohibit. However, it would be helpful to clarify the language.

Suppose a lease contains a "Silent Consent Standard" clause which requires the lessor's consent but does not expressly state a stan-

460. See supra notes 24-25 and accompanying text.
461. Id.
462. CAL. CIV. CODE § 1951.4(b) (West 1985).
463. Id. (emphasis added).
464. Id. (emphasis added).
465. See supra note 19 and accompanying text.
standard governing consent. Application of the *Kendall* decision\(^{466}\) will impose a reasonableness standard on the lessor, even though one is not expressed in the lease. Subsection (3) of 1951.4(b) is satisfied only if "the lease provides" that consent shall not be unreasonably withheld.\(^{467}\) Under the *Kendall* rule, the lessor cannot unreasonably withhold consent even if the lease does not so provide.\(^{468}\) The tenant receives the benefit of the required transfer freedom whether the reasonableness standard is express or implied. Since the purpose of the statute is satisfied in either case, the lessor should have the benefit of the lock-in remedy in either case.

Suppose a lease contains specific requirements or conditions that must be met for a permissible transfer—for example, the "Express Specific Requirements"\(^{469}\) type clause. Subsection (2) of 1951.4(b) mandates that the lessor "not require compliance" with any "unreasonable" standard or condition. The tenant should have the burden of proving that the particular requirement is unreasonable at the time and in the manner it is applied. This would be consistent with cases involving the reasonableness standard generally.\(^{470}\) It would be consistent with the placement of the burden of proving reasonably avoidable rent loss on the tenant by section 1951.2. It would also be a realistic recognition of the fact that it is the tenant's fault, a breach of the lease, that sets the whole process in motion.

Suppose a lease contains specific requirements that are reasonable at the time they are included in the lease, but later circumstances make application of one or more of the requirements unreasonable. The fact that a standard or condition becomes unreasonable after execution of the lease should not prevent the lessor from using the lock-in remedy if he or she does not require compliance with the unreasonable requirement. This position is expressed in the California Law Revision Commission comment on section 1951.4.\(^{471}\) The language of subsection (b)(2) to 1951.4 can be construed to adopt this position. It requires that the lessor "not require compliance with" any unreasonable standard or condition.\(^{472}\)

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\(^{467}\) *CAL. CIV. CODE* § 1951.4.

\(^{468}\) *Kendall*, 40 Cal. 3d at 496-97, 709 P.2d at 842, 220 Cal. Rptr. at 823.

\(^{469}\) *See supra* notes 24-25 and accompanying text.

\(^{470}\) *See, e.g.*, Funk v. Funk, 102 Idaho 521, 633 P.2d 586 (1981); *RESTATEMENT* *supra* note 91, § 15.2, comment g; *4 MILLER & STARR, supra* note 404, at 416-17 (1977) & 439 n.17 (1987 Supp.).


\(^{472}\) *CAL. CIV. CODE* § 1951.4(b)(2) (emphasis added).
However, the language could more clearly express that position.

Suppose that one clause or part of a clause allows the tenant to transfer subject only to reasonable limitations if, but only if, the lessor is exercising the lock-in remedy in section 1951.4. Suppose further that another clause or part of a clause contains an expressly agreed provision that either absolutely prohibits transfer or gives the lessor the sole discretion to consent or object to transfer in all other circumstances. A clause presented in a lease practice book published by the California Continuing Education of the Bar appears to be setting up this type of combination.473 One of the remedy provisions states:

After Tenant's default and for as long as Landlord does not terminate Tenant's right to possession of the premises, if Tenant obtains Landlord's consent Tenant shall have the right to assign or sublet its interest in this lease . . . . Landlord's consent to a proposed assignment or subletting shall not be unreasonably withheld.474

The comment to the clause mentions that it is unclear whether this clause in combination with an "Absolute Prohibition" will work to preserve the lock-in remedy, but opines that "such an arrangement probably is permitted."475

Does this type of combination, which allows transfer under the reasonableness standard only if and when the lock-in is exercised, comply with section 1951.4? The statute is unclear on this point. On the one hand, it can be argued that the purpose of the statute is satisfied by the combination. The tenant is given the freedom to transfer when he or she requires it, at the time of the lock-in. However, allowing such a provision eliminates any benefit the section would give a tenant in bargaining for a reasonableness standard governing all transfers.

Suppose a lease contains a "Possession Recovery" clause.476 It gives the lessor the option to recover possession of the property if the tenant attempts to transfer. If the tenant has breached the lease, the exercise of such a right would terminate the tenant's right to possession and result in termination of the lease.477 Thus, the actual exercise of such a provision lets the tenant out from under the lock-in remedy. The unexercised existence of such a clause in the lease does not prejudice the tenant's

473. LEASE PRACTICE, supra note 403, § 3.110.
474. Id. § 3.117, at 164.
476. See supra notes 24-25 and accompanying text.
477. CAL. CIV. CODE § 1951.2(a).
relief under section 1951.4, so it should not prejudice the lessor's remedy under that section.

Suppose a lease contains a "Profit Shift" clause.\footnote{See supra notes 24-25 and accompanying text.} It allows the lessor to receive part or all of the profit generated by the tenant's leasehold transfer. The tenant's relief provided in section 1951.4 is designed to minimize the tenant's losses after a breach and abandonment. It is not designed to assure that the tenant will profit from appreciated value of the leasehold. The existence or exercise of such a clause should not prevent the lessor from exercising the lock-in remedy.

XVI. RESIDENTIAL LEASES

This study is limited to non-residential leases. However, certain general observations can be made concerning residential tenancies.

A. Uncertainty

The rules applicable to assignment and sublease restrictions in residential tenancies in California are even less certain than those applicable to non-residential leases. The Kendall decision implied a requirement of reasonableness into a "Silent Consent Standard" type clause in a commercial lease. Thus, a reasonableness standard will be imposed when a clause requires the lessor's consent but does not expressly state a governing standard. The court expressly refrained from deciding whether its opinion should be extended to residential tenancies.\footnote{Kendall v. Ernest Pestana, Inc., 40 Cal. 3d 488, 492 n.1, 709 P.2d 837, 839 n.1, 220 Cal. Rptr. 818, 820 n.1 (1985).} It is interesting to note that of the four statutes the court referred to as imposing a reasonableness standard on lessors, three apply to residential tenancies only and the fourth applies to residential and other types of leases.\footnote{Id. at 499 n.13, 709 P.2d at 844 n.13, 220 Cal. Rptr. at 825 n.13.} The Kendall court relied heavily on the Wellenkamp loan security case in reaching its conclusion, and that case involved residential property.\footnote{Id. at 498, 709 P.2d at 843, 220 Cal. Rptr. at 824 (citing Wellenkamp v. Bank of Am., 21 Cal. 3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978)).} However, the characteristics of a residential loan and a residential tenancy are typically quite different from the commercial context. For example, a loan generally involves a long-term relationship and a residential tenancy a short-term one. Thus, there is a considerable difference in the duration and impact of a transfer restriction.
There is dictum in Schweiso v. Williams,\(^{482}\) an earlier court of appeal decision, that the court saw no significant difference between a residential and a commercial lease when dealing with obligations of good faith and commercial reasonableness. However, the court limited its adoption of a reasonableness standard to commercial leases.\(^{483}\) So far, no reported California decision has dealt specifically with lease transferability standards in a residential lease. There is no clear-cut pattern in cases of other jurisdictions since most of them involve commercial leases.

**B. Consumer Protection**

Generally, there is stronger concern for "consumer" protection when dealing with a tenancy for housing than there is when dealing with a commercial lease for business operations.\(^{484}\) It has been argued that the common-law and majority rule operates unfairly on residential tenants when there is a housing shortage, and that implication of a sole discretion standard into the "Silent Consent Standard" clause does not meet the reasonable expectations of a residential tenant.\(^{485}\) Residential tenants generally do not hire a lawyer to advise and negotiate concerning the terms of the residential tenancy. The amount of rent is the major concern, and it is reasonable to assume that there is usually little bargaining over the other terms of the tenancy. A residential tenant is typically unconcerned about transfer restrictions at the time of entering into a lease, and thus does not actively bargain over them.\(^{486}\) If the residential rental occurs at a time and place of unit shortages, there is little practical bargaining power.

When a clause requires the lessor's consent but fails to express the standard governing that consent, there are two basic choices for a standard: reasonableness or sole discretion. In the absence of express language to the contrary, it seems likely that most residential tenants would expect a reasonableness standard. Since the lessor generally has drafting control, it is a minimal burden to require a lessor desiring a sole discretion consent standard to expressly state it. If a lessor is required to use express provisions to avoid a reasonableness standard, language of sole discretion or absolute prohibition will probably become commonplace. A tenant who reads the agreement will have notice of the broad restric-


\(^{483}\) Id.

\(^{484}\) See CAL. CIV. CODE § 1671 (West 1985) (liquidated damages) and §§ 1941-1942.5 (West 1985 & Supp. 1988) (habitability and retaliation).

\(^{485}\) Note, supra note 392, at 522.

\(^{486}\) See ROHAN, supra note 11, § 5.01, at 5-10.1.
tion, but will likely have little incentive or power to insist on a reasonableness standard.

C. Short Term

Residential tenancies are typically short term or on a month-to-month basis. If the tenancy is for a fixed term, it is seldom for more than one year. When longer terms are involved, they are usually for a single family residence (free standing or condominium). A local rent control ordinance that prohibits the lessor from terminating a tenancy except for "just cause" can obviously convert a short-term tenancy into a long one. The impact of a rent control ordinance is considered separately below. Transferability of the leasehold is an important economic factor to most commercial tenants, and one that should be carefully considered at the time of entering into a commercial lease. However, in a short-term residential tenancy, it is unlikely that a significant "bonus value" (difference between the agreed rent and the market rental value) will build up. Thus, it is unlikely that a short-term residential tenant will be concerned about the ability to reap the benefit of this bonus value by receiving consideration from a third party assignee or subtenant. Also, a lessor in this situation is not likely to be concerned about getting the bonus value upon a transfer because the rent can be raised to the market in the short term whether there is a transfer or not. For example, a "Profit Sharing" or "Possession Recovery" type of a transfer clause would not likely be worth the time it takes to draft and enforce it.

The short-term nature of a residential tenancy reduces the problems faced by a tenant who wants to move, and thus reduces the need to transfer. If a month-to-month tenant wishes to get out of the agreement, a short time notice (typically 30 days) will do the job. A residential tenant who enters into a fixed short-term tenancy (e.g., a one year lease) and who later decides to move will generally have a relatively short term remaining. If the tenant elects to get out by breaching the lease and abandoning the premises, the tenant will have a relatively short time left on the term for exposure to damages under California Civil Code section 1951.2, and that section provides for an offset of "reasonably" avoidable rent losses. If the lessor keeps the lease in effect by using the "lock-in" remedy under California Civil Code section 1951.4, the lessor is subject to a mandatory reasonableness standard.

Since the lessor is able to recover possession after a relatively short

487. CAL. CIV. CODE § 1951.2 (West 1985).
488. CAL. CIV. CODE § 1951.4.
time due to expiration of a fixed term or termination of a periodic tenancy (absent rent control limitations), there may be less need for absolute control over transfer in the interim. However, when an unlawful detainer action is involved to recover possession, a mandatory reasonableness standard could cause a lessor additional problems when faced with an unconsented "Arrieta" occupant.\footnote{489. Arrieta v. Mahon, 31 Cal. 3d 381, 644 P.2d 1249, 182 Cal. Rptr. 770 (1982); see also CAL. CIV. PROC. CODE §§ 715.020(d) (West 1987) and 1174.3 (West Supp. 1988).}

When a short-term tenancy is involved, the duration of the transfer restraint is limited and has less practical impact than in a long-term lease. Also, resolving a dispute over reasonableness by litigation is generally impractical in a short-term tenancy.

D. Type of Property

The degree of tolerable lessor control over transferability may depend upon the type of residential property subject to the tenancy. One's attitude toward transfer restrictions in a residential lease can shift dramatically depending on the nature of the transaction. Suppose you have a nice single family residence which has served as your family nest since you personally designed and built it. It is filled with unique furnishings collected over the years. You have been temporarily transferred or you are planning an extended trip and need to rent your home, furnished, to provide income for loan payments, taxes, insurance and maintenance. You select your tenant according to your own personal standards, preferences and instincts. Should you be required to have a "commercially reasonable objection" to prevent a transfer by this tenant? In some situations, the lessor, as well as the tenant, may be considered to be in need of consumer protection.

On the other hand, suppose that a major apartment development and management company owns hundreds of virtually identical apartment units throughout the state, with professional on-site management and security. Do you mind imposing a reasonableness standard on that lessor?

The Restatement recognizes the distinction between these two situations when applying a reasonableness standard. It points out that "[a] reason may be reasonable in relation to residential property that is the personal home of the landlord that would not be reasonable as to other residential property."\footnote{490. RESTATEMENT, supra note 91, § 15.2 comment g and illustration 8 at 105-06.}

If the validity and scope of a transfer restriction depends upon the
type of residential property involved, it is difficult to make clear distinctions that can be easily applied. There are a variety of situations where legislation has made a distinction between one-to-four unit residential transactions and other residential transactions.\footnote{491} This would cover the hypotheticals posed above, and it might be a reasonable, although less than perfect, compromise distinction.

\section{E. Mobilehomes}

The expense and difficulty of moving a mobilehome put mobilehome site tenancies in a distinct category. The lessor's ability to restrict transfer of the tenancy is strictly limited when title to the mobilehome is transferred. The limitations are contained in a separate article of the comprehensive "Mobilehome Residency Law," particularly in California Civil Code sections 798.73-798.74 (sale of mobilehome), 798.78 (death transfer and later sale), and 798.79 (foreclosure transfer and later sale).\footnote{492} It seems that these limitations should be preserved due to the unique nature of the mobilehome tenancies.

\section{F. Continuing Liability}

A tenant who assigns or sublets to a third party remains liable to the lessor for breaches of the tenancy obligations in the absence of a release, and a lessor's consent to the transfer is not a release. If the tenant can terminate the tenancy without breach, the typical residential tenant is better off terminating the tenancy rather than risking continuing exposure to liability related to premises no longer controlled by the tenant. Thus, a "freedom to transfer" may be an illusory benefit for most tenants, and a trap for some who transfer to a person who turns out to be irresponsible.

The degree of protection provided to the lessor by this continuing liability depends on the continued availability and solvency of the original tenant.

\section{G. Rent Control}

A rent control ordinance that strictly limits the lessor's ability to
terminate a tenancy, or ability to decline to renew it, dramatically changes the potential term of a residential lease. When a local jurisdiction adopts rent control, it is likely to include some form of “just cause” limitations on the lessor’s power to end the tenancy (e.g., rent default, extensive rehabilitations, move-in by lessor or family, etc.). These limitations restrict the lessor’s power to terminate the tenancy, but typically leave the tenant free to terminate it.

If a lessor were to be subjected simultaneously to a “just cause” limit on termination, and a mandatory reasonableness standard on tenant transfers, the result would be a rather unique tenancy. A typical monthly periodic tenancy would become an indefinitely long-term tenancy (theoretically perpetual), with occupants chosen by successive tenants. The tenant would have the unilateral right to terminate on thirty days notice without cause.

A tenant enjoys the benefits of a bonus value (here, the difference between the controlled rental and a free market rental) while occupying the premises. This serves the basic purpose of the controlled rentals, and it does not seem necessary to go further and limit the lessor’s ability to restrict transfers by the tenant.

One type of ordinance allows the lessor to raise the rent to the market rate when the tenancy terminates and the unit is relet. Suppose that a lessor could not prevent transfer, and a tenant could transfer the unterminated tenancy at the same controlled rental. The original tenant, who no longer occupies the unit, could receive profit in the amount of the bonus value from the third party. The new transferee occupant, by paying an “assignment fee” or sublease rent to the original tenant, would pay more than the controlled rental. The lessor would lose the ability to catch the rent up to the free market rental.

Under another type of ordinance, the rent remains controlled even when the tenancy terminates and the unit is relet. The lessor cannot require a higher rent from the new occupant whether the former tenancy is terminated or transferred. In theory, the new occupant does not have to “buy” the bonus value from the present tenant because the new occupant will be protected by the rent ceiling under a new tenancy. In practice, if there is a shortage of rent controlled units available, an existing tenant may be able to “sell” his or her position if the lessor cannot restrict transfers.

Obviously, there are ways a rent control ordinance can be designed to deter a windfall profit to the vacating tenant at the expense of the new occupant and the owner. However, the point is that free transferability
by the tenant is not necessary to accomplish the public purpose of rent control, and in some instances it might be counterproductive.

H. Basic Issues

This study contains several conclusions, summarized in Section Q, concerning the validity and interpretation of transfer restrictions in non-residential leases. Underlying the conclusions are two basic issues that need to be resolved with respect to residential tenancies.

First, absent express language in the agreement to the contrary, should a lessor who objects to a transfer be held to a reasonableness consent standard? In other words, if the lessor wishes to have a sole discretion standard apply, should that be required to be express in the agreement? If there is no language expressing a different standard, it seems that a reasonableness standard conforms to the likely expectations of a residential tenant. A requirement to expressly disclose a sole discretion standard to a residential tenant is a minimal and reasonable burden.

Second, should the lessor be able to contract away the reasonableness standard in a residential tenancy? In other words, should there be a mandatory reasonableness standard or should the express language of the transfer restriction govern? Here there is a more difficult balancing of policies.

The general approach of the conclusions regarding restrictions in commercial leases is to require disclosure by express agreement, and to allow enforcement of expressly agreed strict restrictions on transfer according to their terms. The following policy issues will have to be resolved with regard to residential leases:

1. Is there a compelling policy reason to depart from the commercial lease approach when a residential tenancy is involved?

2. If a different approach is adopted (for example, a mandatory reasonableness standard):
   (a) Should there be a distinction based on the duration of the tenancy?
   (b) Should there be a distinction based on the type of residential property involved?
   (c) Should there be special provisions for tenancies subject to rent control?

XVII. SUMMARY OF CONCLUSIONS

A. Relating to Commercial Lease Transfer Restrictions

The following conclusions are based on the assumption that,
although they are not necessarily equal in bargaining power, the parties are not involved in a contract that would be invalidated in whole or part under the adhesion doctrine in California.

1. The freedom of the parties to negotiate and contract concerning restrictions on leasehold transfers should be preserved unless there is a compelling public policy reason to interfere.

2. Disclosure of restrictions by express provisions should be encouraged in order to provide clear expectations for the parties.

3. A tenant may freely transfer unless the lease imposes a restriction.

4. Restrictions on leasehold transfers are permitted but strictly construed. Ambiguities are construed in favor of transferability.

5. A "Silent Consent Standard" clause is one that requires the lessor's consent to a leasehold transfer by a tenant, but that does not contain an express standard governing the lessor's consent. The clause does not expressly state that the lessor is subject to a reasonableness standard nor does it expressly state that the lessor has the freedom of a sole discretion standard.

The traditional common-law and majority view holds that the lessor is free to use subjective sole discretion in withholding consent. There are several recent cases from other states that imply into this type of clause a reasonableness standard to govern the lessor. These cases still represent a minority view but might be considered to indicate a trend. However, there are also some recent cases that decline to adopt the minority view. The Restatement (Second) of Property implies a reasonableness standard into this type of clause. The California Supreme Court, in Kendall v. Ernest Pestana, Inc., also adopted the minority view and implied a reasonableness standard into this type of clause.

The implication of a reasonableness standard into the "Silent Consent Standard" clause is justified by public policy. However, careful consideration should be given to the possibility of unfairness resulting from the retroactive application of this rule.

6. An "Express Reasonableness Standard" clause is one that requires the lessor's consent to a leasehold transfer by the tenant, and that by express agreement of the parties imposes a standard of reasonableness.

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493. See generally Restatement, supra note 91, § 15.2.
495. Restatement, supra note 91, § 15.2.
on the lessor.\textsuperscript{497}

The common-law and majority view, the minority view, and the Restatement (Second) of Property consider this type of clause valid.

If the reasonableness standard is complied with, this clause does not violate the covenant of good faith and fair dealing and it does not violate the rule against restraints on alienation.

7. An "Express Sole Discretion Consent Standard" clause is one that requires the lessor's consent to a leasehold transfer by the tenant, and that by \textit{express} agreement of the parties gives the lessor the sole discretion to refuse consent.\textsuperscript{498} An "Absolute Prohibition" type clause is one in which \textit{express} agreement of the parties absolutely prohibits leasehold transfers by the tenant.\textsuperscript{499}

It should be noted that the "Sole Discretion Standard" and "Absolute Prohibition" type clauses do not comply with California Civil Code section 1951.4, so the lessor would not be able to use the lock-in remedy provided in that section.

The common-law and majority view consider these types of clauses valid. There is no trend of holdings in out-of-state cases rejecting this view. The clauses are valid according to the Restatement (Second) of Property if "freely negotiated."\textsuperscript{500} Although there is some language in \textit{Kendall} criticizing the common-law and majority view in general, the holding of that case does not prevent the use of such clauses.\textsuperscript{501}

Public policies do not justify prohibiting the freedom to contract for these types of clauses. The Restatement position presents a fair balance between policy and freedom of contract. However, the phrase "freely negotiated" should be clarified.

It is unlikely that a tenant in a freely negotiated long-term lease would agree to this type of restriction for the full term. Thus, negotiations usually take care to avoid such a long-term sole discretion or absolute prohibition restriction. However, there may be concern that such restrictions on a lease term approaching fee simple characteristics could cause substantial adverse consequences. If this is a realistic concern, it could be solved by a time limit after which a mandatory reasonableness standard would govern the lessor. A time limit would be a more direct solution than an absolute prohibition of such clauses in all leases, regardless of term. The particular time chosen for the limit would, however, be

\textsuperscript{497} \textit{Restatement}, supra note 91, § 15.2 comment h.
\textsuperscript{498} \textit{Id.} at comment i.
\textsuperscript{499} \textit{Id.} at comment d.
\textsuperscript{500} \textit{Id.} at § 15.2(1).
\textsuperscript{501} \textit{Kendall}, 40 Cal. 3d at 506, 709 P.2d at 849, 220 Cal. Rptr. at 830.
largely arbitrary.\textsuperscript{502}

8. The recent litigation over this area of the law has been generated in large measure by lessors' attempts to "sweeten," rather than preserve, the deal made in the lease. The lessor's demand comes as an apparent surprise at the time of the proposed transfer. Consideration should be given to requiring an express lease clause to support a lessor's demand for participation in bonus value profit by increase in rent or otherwise. If the express provision is present, it has been negotiated and provided for at the time the lease is entered into. The express provision converts the demand from a surprise into one of the reasonable expectations of the parties. However, a prohibition against a lessor's demand for money in exchange for consent might create more problems than it solves: it could deter legitimate compromises; and it could create difficult litigation over motivations.\textsuperscript{503}

9. Specific requirements or conditions for a leasehold transfer by the tenant, expressly agreed to by the parties in the lease, should be free from attack as unreasonable, unless and until the lessor exercises the lock-in remedy pursuant to California Civil Code section 1951.4.

10. A lessor's right to elect to recover possession of the premises when a tenant proposes a leasehold transfer, expressly agreed to by the parties in the lease, should not be considered an unreasonable restraint on alienation or a violation of the covenant of good faith and fair dealing.

11. A lessor's right to receive part or all of the profit generated by a leasehold transfer by a tenant, expressly agreed to by the parties in the lease, should not be considered an unreasonable restraint on alienation or a violation of the covenant of good faith and fair dealing.

\textbf{B. Relating to the Lock-in Remedy in Civil Code Section 1951.4}

California Civil Code section 1951.4 allows the lessor to keep the lease in effect and enforce its terms (i.e., "lock-in" the lease) after the tenant has breached the lease and abandoned the premises.\textsuperscript{504} However, this remedy is available only "if the lease permits" the tenant to make a leasehold transfer subject only to reasonable limitations. The following conclusions relate to that code section.

1. If a lease does not restrict transfer, the tenant is automatically free to assign or sublet without the lessor's consent. It should not be

\textsuperscript{502} See \textit{supra} notes 24-25 and accompanying text for a discussion of these types of clauses.

\textsuperscript{503} See \textit{supra} notes 438-50 and accompanying text.

\textsuperscript{504} \textsc{Cal. CIV. Code} § 1951.4(b) (West 1985).
necessary to expressly grant the right to assign or sublet in order to comply with section 1951.4.

2. If a lessor's consent is subject to an implied reasonableness standard (e.g., a "Silent Consent Standard" clause), it should be considered in compliance with the requirements of section 1951.4. It should not be necessary to have the reasonableness standard expressed in the lease.

3. For purposes of compliance with section 1951.4, specific requirements or conditions for a leasehold transfer by the tenant, expressly agreed to by the parties in the lease, should be presumed to be reasonable. An example is the "Express Specific Requirements" type of clause.\(^{505}\) If there is a later dispute over reasonableness, the tenant should have the burden of proving that a particular standard or condition is unreasonable at the time and in the manner it is applied.

4. It is possible that a particular requirement or condition, although reasonable at the time of entering the lease, becomes unreasonable due to changed circumstances. As long as the lessor does not require compliance with the unreasonable standard or condition, the existence of an unreasonable requirement or condition in the lease should not prevent the lessor from using the remedy in section 1951.4.

5. A lease might provide that the tenant can transfer subject only to reasonable restrictions if, but only if, the lessor is exercising the remedy provided in section 1951.4. In all other respects, the lease provides for a sole discretion standard or an absolute prohibition against transfer. It is not clear whether this combination is permissible under the present statute. There are competing considerations in resolving the issue, but it should be resolved and clarified.

6. The remedy in section 1951.4 should not be denied to a lessor just because of the presence in the lease of an expressly agreed provision giving the lessor the right to elect to recover possession of the premises when a tenant proposes a leasehold transfer. Note, however, that the exercise of this right would terminate the lease and deny the lessor the lock-in remedy.

7. The remedy in section 1951.4 should not be denied to a lessor just because of the presence in the lease or the exercise of an expressly agreed provision giving the lessor the right to receive part or all of the profit generated by a leasehold transfer by a tenant.

\(^{505}\) See generally CAL. CIV. CODE § 1951.4(b)(2)-(3).
PART 2
LEASEHOLD TRANSFER RESTRICTIONS

LESSOR REMEDIES FOR BREACH OF
ASSIGNMENT AND SUBLEASE
RESTRICTIONS

I. Scope of Part

This Part examines the remedies available to the lessor when a tenant wrongfully violates a transfer restriction in a commercial lease of real property.

Assume that a lessor and tenant enter into a commercial lease of real property. A clause in the lease restricts the tenant’s ability to transfer to a third party without the lessor’s consent. Later, the tenant transfers or proposes to transfer all or part of the leasehold to a third party. The transfer will be in the form of either an assignment to an assignee, or a sublease to a subtenant. The lessor properly refuses consent to a proposed assignment or sublease. The propriety of the refusal assumes that the restriction clause is valid and that the lessor complies with the applicable consent standard. The tenant and the third party complete the assignment or sublease without the lessor’s consent or over the lessor’s objections (or it has been done without requesting the lessor’s consent).

What are the lessor’s remedies in California? Should the remedies be clarified or modified?

II. California Cases

There is a pertinent series of California cases extending back to the 1800s. The cases are consistent in their description of the effects of an unconsented transfer. The chronological development of the series is discussed briefly below.

In the 1893 case of Randol v. Tatum, the California Supreme Court stated that “an assignment in violation of the covenant was not absolutely void” and that the “lessor did not have the option of declaring the assignment void,” but the lessor could elect “to avoid the lease and

506. For a discussion of the types of restriction clauses, see supra notes 24-25 and accompanying text.
507. See supra notes 32-53 and accompanying text for a discussion of clause validity and consent standards.
508. These same issues are involved when the transfer restriction is contained in a sublease from the tenant/sublessor to a subtenant, and the tenant/sublessor seeks remedies against the subtenant.
509. 98 Cal. 390, 33 P. 433 (1893).
end the term.” 510 The case involved a lessor’s action against the sureties on a rent bond. 511 The sureties responded that rent had been properly tendered by an assignee and thus, there was no default. 512 The lessor argued that the assignment was without his consent, in violation of the lease, and thus, a tender by the assignee was improper. 513 Also, he seemed to argue that the assignee could have no leasehold rights except by a lease violation, and thus the sureties could not rely on the assignee’s offer of performance. 514 However, since the lessor did not terminate the lease, the assignee was the legal owner of the leasehold and the proper person to pay the rent. 515

In the 1897 case of Garcia v. Gunn, 516 the California Supreme Court stated: “It seems to be the law that . . . the lessor has only the option to forfeit the lease for the breach of the condition, and that the assignment is not void but passes the term, and the only remedy is for breach of the covenant.” 517 This was a claim and delivery action for goatskins brought by an assignee of a lease of Guadalupe Island. 518 The suit was against parties who had taken the skins from wild goats on the island. 519 The defendants unsuccessfully argued that since the assignment had been without the lessor’s consent, the assignee was not entitled to possession of the island at the time the skins were taken. 520

In the 1909 case of Potts Drug Co. v. Benedict, 521 the California Supreme Court stated that an assignment is not void if the lessor’s consent has not been obtained. 522 In Potts, the leased premises were totally destroyed by fire after the assignment was made but before the assignees took possession. 523 The tenant sued the assignee for the balance due on the sale of the leasehold estate. 524 The assignee unsuccessfully argued that the leasehold interest had not passed at the time of the fire, due to the lack of the lessor’s consent. 525

510. Id. at 396-97, 33 P. at 435.
511. Id. at 393, 33 P. at 433-34.
512. Id., 33 P. at 434.
513. Id. at 393-95, 33 P. at 433-35.
514. Id. at 398, 33 P. at 436.
515. Id.
516. 119 Cal. 315, 51 P. 684 (1897).
517. Id. at 318, 51 P. at 685.
518. Id. at 316-17, 51 P. at 684-85.
519. Id. at 317, 51 P. at 685.
520. Id. at 318, 51 P. at 685.
521. 156 Cal. 322, 104 P. 432 (1909).
522. Id. at 327, 104 P. at 434.
523. Id. at 326, 104 P. at 434.
524. Id. at 324, 104 P. at 433.
525. Id. at 326-27, 104 P. at 434-35.
In the 1928 case of *Buchanan v. Banta*[^526], the California Supreme Court stated that when there is an unauthorized breach of the covenant not to assign, “the lessor has only the option to forfeit the lease for such breach; the assignment is not void, but voidable only at the option of the lessor, which option he must exercise according to law.”[^527] In this case, the lessor brought an unlawful detainer action against the defendants, claiming that they owed rent under a month-to-month tenancy after a lease surrender.[^528] The defendants successfully argued that they had the status of assignees of the lease and were therefore entitled to credit for prepaid rent under the lease.[^529]

The court in *Buchanan* referred to the 1927 case of *Miller v. Reidy*,[^530] decided by the California Court of Appeal. *Miller* involved an unconsented transfer. The third party transferee ignored the lessor’s demand that he vacate.[^531] The lessor accepted rent from the transferee, but attempted to reserve his rights.[^532] Particularly, he put a statement on rent receipts stating that the rent was received without prejudice to the lessor’s rights under the lease.[^533] The *Buchanan* court quoted *Miller* with approval:

> This was a clear attempt to eat the cake and still keep it. His actions belie his words. Waiver is a question of intention. For the lessors month after month to accept rents specified in the lease, and at the same time declare that there was a forfeiture, results in an irreconcilable inconsistency.... If an unauthorized assignment had been made the lessors had the right to declare the term at an end, or they could have waived the breach and let the lease continue. Nowhere within that agreement nor in the law is there a stipulation or provision that they might do both.[^534]

In *Chapman v. Great Western Gypsum Co.*,[^535] decided in 1932, the California Supreme Court stated:

> The assignment of a lease in violation of a covenant against

[^526]: 204 Cal. 73, 266 P. 547 (1928).
[^527]: *Id.* at 76-77, 266 P. at 548 (citations omitted).
[^528]: *Id.* at 74, 266 P. at 547.
[^529]: *Id.* at 74-75, 266 P. at 547-48.
[^531]: *Id.* at 759-60, 260 P. at 359.
[^532]: *Id.* at 760, 260 P. at 359.
[^533]: *Id.*
[^534]: *Buchanan*, 204 Cal. at 77-78, 266 P. at 548-49 (quoting *Miller v. Reidy*, 85 Cal. App. 757, 762, 260 P. 358, 360 (1927) (citations omitted)).
[^535]: 216 Cal. 420, 14 P.2d 758 (1932).
assignment without the consent of the lessor is nevertheless a binding assignment which passes the leasehold estate. . . . Such an assignment in violation of the covenant is, however, subject to the option in the lessor to forfeit the lease. The only remedy for the breach of such a covenant would be the exercise by the lessor of his option to forfeit the lease.\footnote{536}

In \textit{Chapman}, the tenant, without the lessor's consent, granted a lender a leasehold mortgage which was recorded.\footnote{537} Later, the tenant assigned the lease to an assignee with the lessor's consent.\footnote{538} The assignee, with knowledge of the leasehold mortgage, exercised an option to purchase contained in the lease.\footnote{539} The lessor conveyed the leasehold to the assignee, and there were subsequent reconveyances.\footnote{540} The mortgagee brought an action to establish that the lien on its mortgage was still attached to the title when the assignee exercised the option to purchase.\footnote{541} One of the arguments raised against the mortgagee was that the lien could not attach because the mortgage violated the clause prohibiting assignment without the lessor's consent. The court held that the mortgage did not violate this clause, and even if it did, it was valid in the absence of a lease forfeiture by the lessor.\footnote{542} In the 1944 case of \textit{People v. Klopstock},\footnote{543} the California Supreme Court stated that a series of assignments without the lessor's consent:

\begin{quote}
were merely \textit{voidable}, not void; there was no ipso facto termination of the lease by reason of the lessee's failure to obtain the lessor's written consent to assignment. Since the lessor did not elect to exercise its option to \textit{avoid} the original assignment in the manner prescribed by law, its notice . . . that it did not recognize the validity of the assignment gave no legal force to its demand therein that such assignee remove all property owned by it from the leased premises . . . . While the course of action pursued by the lessor . . . was sufficient to apprise the assignee that it \textit{might be} dispossessed . . . the lessor's option to \textit{void} the objectionable transfer depended upon its declaration of \textit{a forfeiture upon proper notice} as provided by law. But the lessor did not take advantage of the exclusive remedy available to
\end{quote}

\footnote{536. \textit{Id.} at 427, 14 P.2d at 761.}
\footnote{537. \textit{Id.} at 422-23, 14 P.2d at 759.}
\footnote{538. \textit{Id.} at 423, 14 P.2d at 759.}
\footnote{539. \textit{Id.} at 423-24, 14 P.2d at 759.}
\footnote{540. \textit{Id.} at 423, 14 P.2d at 759.}
\footnote{541. \textit{Id.} at 422, 14 P.2d at 758.}
\footnote{542. \textit{Id.} at 427, 14 P.2d at 761.}
\footnote{543. 24 Cal. 2d 897, 151 P.2d 641 (1944).}
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...it for termination of the lease, and accordingly [the subsequent assignee] succeeded to all the rights of the lessee. Klopstock involved the assignee's successful claim of entitlement to compensation in an eminent domain action.

The court in Klopstock referred to the 1942 case of Northwestern Pacific R.R. Co. v. Consumers Rock & Cement Co., decided by the California Court of Appeal, involving a like lease and a like initial unconsented assignment. Northwestern Pacific involved an unlawful detainer action by the lessor. The trial court denied possession to the lessor, but ordered the defendant assignee to pay the reasonable rental value of the premises, which was in excess of the rent provided in the lease. This award of rental value was reversed on appeal. Since the lease and the assignment remained in effect, the agreed rent still governed. The lessor refused consent to the assignment, refused tender of rent, and notified the assignee that it refused to recognize the validity of the assignment. The Klopstock court quoted, with approval, Northwestern Pacific:

If the lessor desired to stand upon the covenant against assignment, he could have given notice of his election to declare a forfeiture of the lease and could have sued for breach of the covenant. He could also have had his remedy in unlawful detainer if possession had been thereafter withheld following proper notice. But we find no authority indicating that the lessor had the option of merely giving notice of the invalidity of the assignment without declaring a forfeiture . . . .

In the 1964 case of Sexton v. Nelson, the California Court of Appeal stated:

A lease is not terminated ipso facto upon its transfer in violation of a provision therein declaring its nontransferability . . . . The breach of a provision against assignment confers upon the lessor, at his election, the right to effect a forfeiture of the lease in the manner authorized by law. If the lessor does not elect to declare a forfeiture because of such a breach, the assignment in question is valid. If he does elect to declare a forfeiture he must

544. Id. at 901-02, 151 P.2d at 643 (emphasis in original).
546. Id. at 722, 123 P.2d at 872.
547. Id. at 723, 123 P.2d at 872-73.
548. Id. at 722-23, 123 P.2d at 872.
give notice of his intention in the premises.\textsuperscript{551} The lessor brought an action seeking to have a lease declared terminated by reason of violation of a transfer restriction, among other reasons.\textsuperscript{552} There was no evidence that the lessor had attempted to declare a forfeiture. Even if the lessor had attempted to do so, the court held that a transfer of the tenant corporation’s stock did not violate the transfer restriction.\textsuperscript{553} In the 1965 case of \textit{Weisman v. Clark},\textsuperscript{554} the California Court of Appeal stated:

An assignment in violation of the covenant is not void and does not void the lease but passes the term, and the only remedy for such a violation is an action for breach of covenant. Such a restriction against assignment is the personal covenant for the benefit of the lessor unless he elects to take advantage of the breach and thus the assignment remains valid until he does so.\textsuperscript{555}

The court also said that the lessor “had the option to decide whether or not he wanted to declare a forfeiture or proceed with the lease.”\textsuperscript{556} The tenant had formed a corporation and had assigned the lease to the corporation in exchange for a portion of the stock. Later, the tenant and other stockholders sold their stock to defendant. A short time later, the restaurant being operated on the premises closed and the corporation was adjudged bankrupt. The tenant sued for the balance due on the stock sale. The defendant unsuccessfully claimed that there was a failure of consideration because the lessor had not consented to the transaction.\textsuperscript{557}

The \textit{Weisman} court also commented on waiver by virtue of the lessor’s conduct. “There is no waiver on the part of the lessor due to an acceptance of rent without actual knowledge of the assignment or sublease. Such knowledge must be actual, not constructive.”\textsuperscript{558}

In the 1966 case of \textit{Karbelnig v. Brothwell},\textsuperscript{559} the California Court of Appeal dealt with an issue of waiver and stated: “If the lessor accepts payments of rent from the assignee, even under a stipulation reserving the right to declare a forfeiture, the right is waived.”\textsuperscript{560} However, the

\begin{footnotesize}
\textsuperscript{551} Id. at 258, 39 Cal. Rptr. at 413 (citations omitted).
\textsuperscript{552} Id. at 252-53, 39 Cal. Rptr. at 409-10.
\textsuperscript{553} Id. at 258, 39 Cal. Rptr. at 413.
\textsuperscript{554} 232 Cal. App. 2d 764, 43 Cal. Rptr. 108 (1965).
\textsuperscript{555} Id. at 768, 43 Cal. Rptr. at 110 (citations omitted).
\textsuperscript{556} Id. at 768, 43 Cal. Rptr. at 110.
\textsuperscript{557} Id. at 766, 43 Cal. Rptr. at 109.
\textsuperscript{558} Id. at 769, 43 Cal. Rptr. at 111 (citations omitted).
\textsuperscript{559} 244 Cal. App. 2d 333, 53 Cal. Rptr. 335 (1966).
\textsuperscript{560} Id. at 341, 53 Cal. Rptr. at 340.
\end{footnotesize}
court held that an express non-waiver clause allows the lessor to accept rent while deciding whether to forfeit the lease.\textsuperscript{561}

\section*{III. Lease Termination Remedy}

The basic principles developed in the California cases mentioned above can be summarized as follows:\textsuperscript{562}

1. A prohibited transfer is voidable, not void. Thus, the interest passes from the tenant to the third party, subject to the right of the lessor to take remedial action.

2. A prohibited transfer does not automatically terminate the lease.

3. The lessor can elect to terminate the lease and recover possession of the property.\textsuperscript{563}

4. If the lessor fails to terminate the lease, the transfer remains effective.

5. A lessor may waive the right to terminate the lease by conduct, for example by accepting rent with actual knowledge of the transfer.\textsuperscript{564} A "non-waiver" clause may protect the lessor from this type of implied waiver.\textsuperscript{565}

The major California cases developing these principles involve assignments, not subleases. There are, however, cases that indicate that a sublease will be treated in the same manner.\textsuperscript{566} There does not appear to be any substantial reason why the same rules concerning the validity of the transfer, the lessor's election to forfeit the lease or let the transfer stand, and waiver by conduct should not also apply to a sublease.

\textsuperscript{561} Id. at 342-43, 53 Cal. Rptr. at 341.


\textsuperscript{563} See CAL. CIV. PROC. CODE §§ 1161(4), 1162, 1164 (West 1982) and § 1174 (West Supp. 1988). A prohibited assignment or sublease provides statutory grounds for an unlawful detainer action by the lessor to terminate the lease and recover possession from the tenant, an assignee, or a subtenant.

\textsuperscript{564} Weisman, 232 Cal. App. 2d at 769, 43 Cal. Rptr. at 111; Miller, 85 Cal. App. at 762, 260 P. at 360.


\textsuperscript{566} Guerin v. Blair, 33 Cal. 2d 744, 746-47, 204 P.2d 884, 885 (1949) (personal property lease); Licht v. Gallatin, 84 Cal. App. 240, 245, 257 P. 914, 916 (1927) (although court treated transaction as sublease, it might have been partial assignment); Gray v. Maier & Zobelein Brewery, 2 Cal. App. 653, 658, 84 P. 280, 282 (1906); see also 49 AM. JUR. 2D Landlord and Tenant § 494 (1970); M. Friedman, Friedman on Leases § 7.304d (2d ed. 1983).
Although there are significant differences between an assignment and a sublease, these differences do not affect the basic alternatives of forfeiting the lease or leaving the lease and the change in effect. This similarity in treatment for remedy purposes is consistent with the similarity in treatment for purposes of determining the validity and consent standard of the transfer restriction.

However, if the lessor sues the third party for breaches of the lease covenants, the differences between an assignment and a sublease can have an effect. There is no privity of contract or estate between the lessor and a subtenant (absent an assumption by the subtenant), but there is privity of estate between the lessor and an assignee (and also privity of contract if there is an assumption by the assignee.) This is discussed below in the section on damage remedies.

IV. Damage Remedies

A. In Connection With Lease Termination

When the lessor terminates the lease because of the tenant’s breach, California Civil Code section 1951.2 provides that the lessor may recover the worth at the time of award of the following items:

1. Rent Before Termination: “unpaid rent which had been earned at the time of termination”,

2. Deficiency Damages Between Termination and Award: “the amount by which the unpaid rent which would have been earned after termination until the time of award exceeds the amount of such rental loss that the lessee proves could have been reasonably avoided”;

3. Deficiency Damages After Award: “the amount by which the unpaid rent for the balance of the term after the time of award exceeds the amount of such rental loss that the lessee proves could be reasonably avoided”;

4. Miscellaneous Damages: “[a]ny other amount neces-

567. For a discussion of the differences, see supra notes 11-23 and accompanying text.
569. See supra notes 11-23 and accompanying text.
570. CAL. CIV. CODE § 1951.2(a)(1) (West 1985). Subsection (b) calls for the addition of interest to provide the “worth at the time of award.”
571. Id. § 1951.2(a)(2). Subsection (b) calls for interest to provide the “worth at the time of award.”
572. Id. § 1951.2(a)(3). Subsection (b) calls for a discount to provide the “worth at the time of award.”
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sary to compensate the lessor for all the detriment proximately caused by the lessee's failure to perform his obligations under the lease or which in the ordinary course of things would be likely to result therefrom.\textsuperscript{573}

This Author has not found any case directly applying section 1951.2 in connection with a lease termination following a wrongful transfer. However, there is no apparent reason why it would not apply. Lease termination and damages are consistent remedies.\textsuperscript{574}

If the lessor brings an unlawful detainer action to terminate the lease and recover possession, an additional action to recover damages may be necessary. The items of money recovery allowed in an unlawful detainer action are quite limited in order to preserve its summary nature.\textsuperscript{575} The lessor can bring a separate action for damages not recoverable in the unlawful detainer action.\textsuperscript{576}

B. Absent Lease Termination

Suppose that the lessor elects not to terminate the lease, or engages in conduct that results in a waiver of the right to terminate the lease. The wrongful assignment or sublease remains in effect. Is the lessor entitled to recover damages, if any, caused by the assignment or sublease? These damages might result from such facts as a loss of percentage rentals, or the transferee's change in use causing increased insurance premiums,\textsuperscript{577} fire damage,\textsuperscript{578} or hazardous substance liability.\textsuperscript{579} There might be a violation of a use restriction clause as well as a transfer restriction clause. Generally, a lessor is entitled to leave a lease in effect and recover damages for breach of a covenant.\textsuperscript{580} There seems to be no reason to make a distinction when a transfer restriction clause is involved.

The California cases discussed above state that the assignment or

\textsuperscript{573} Id. § 1951.2(a)(4).
\textsuperscript{574} Restatement, supra note 91 § 13.1. Dictum in Northwestern Pacific R.R. Co. v. Consumers Rock & Cement Co., 50 Cal. App. 2d 721, 123 P.2d 872 (1942), discussed supra at notes 545-49 and accompanying text, suggests that the lessor “could have given notice of his election to declare a forfeiture of the lease and could have sued for breach of the covenant.” Id. at 723, 123 P.2d at 873.
\textsuperscript{577} See Rouiaine v. Simpson, 84 N.Y.S. 875 (1903).
\textsuperscript{578} See Lepla v. Rogers, 1 Q.B. 31 (1893).
\textsuperscript{580} Restatement, supra note 91, § 13.1(2).
sublease is valid unless the lessor elects to terminate the lease. Language in some of the cases implies that the only way for the lessor to enforce a transfer restriction clause is to terminate the lease. For example, the court in Buchanan stated that when the transfer restriction covenant is breached, “the lessor has only the option to forfeit the lease for such breach.”581 In the Chapman case, the court stated: “The only remedy for the breach of such a covenant [a covenant not to assign without the lessor’s consent] would be the exercise by the lessor of his option to forfeit the lease.”582 However, those cases did not involve claims for damages without lease termination. The use of the terms “only option” or “only remedy” were used in connection with the question whether the unconscended transfer could be treated as void absent a lease termination. Thus, the damage issue was not directly addressed.

A treatise on California law supports the right to a damage action for breach of covenant even in the absence of a lease forfeiture.583 It states: “If the lessor elects not to declare a forfeiture, his only remedy is for breach of covenant against the lessee, which does not affect the validity of the assignment.”584 Unfortunately, the case cited as authority did not involve a lessor’s action for damages for breach of the transfer restriction covenant.585 The treatise also states: “The breach of a covenant against assignment also gives the lessor the option to sue for damages for breach, or in unlawful detainer if possession is withheld after notice to vacate.”586 Again, the case cited as authority did not involve a lessor’s action for damages for breach of the transfer restriction.587

I have not found any California case expressly allowing or expressly denying damages to the lessor who fails to terminate the lease. However, there is a case that denied damages based on reasonable rental value.588 There, the lessor sued for possession and reasonable rental value damages in excess of the agreed rent.589 Since the lease was not terminated, the lessor was not entitled to possession, and could not collect rental value in

581. Buchanan v. Banta, 204 Cal. 73, 76, 266 P. 547, 548 (1928).
583. 42 CAL. JUR. 3d, supra note 404, § 199.
584. Id. at 232.
586. 42 CAL. JUR. 3d, supra note 404, at 232.
589. Id. at 722, 123 P.2d at 872.
excess of the rent provided in the lease. This case did not involve an action for damages caused by breach of the transfer restriction covenant itself. An action for damages based on the transferee’s reduced production of percentage rentals is distinguishable. Such an action would directly involve the transfer restriction breach. There is support for damages without termination of the lease in out-of-state cases and texts.

A clause restricting transfer of the leasehold is typically worded as a covenant by the tenant. A lease is considered to be a contract as well as a conveyance in California. The Civil Code provides for damages for breach of a contract covenant as follows:

For the breach of an obligation arising from contract, the measure of damages, except where otherwise expressly provided by this Code, is the amount which will compensate the party aggrieved for all the detriment proximately caused thereby, or which, in the ordinary course of things, would be likely to result therefrom.

It seems that the lessor should be entitled to recover damages caused by a breach of the covenant restricting transfer, unless the lessor has waived the breach, or has engaged in conduct which estops the lessor from asserting a breach.

A court of appeal has stated: “Waiver is the intentional relinquishment of a known right after knowledge of the facts.” If we view the lessor’s failure to terminate the lease as a waiver of the breach, the lessor would not be able to enforce a damage remedy. However, if we view it as a waiver of a particular remedy for the breach, the lessor should be able to enforce a different remedy—the right to damages. Termination of the lease and collection of damages are two distinct remedies. The lessor might waive both remedies. However, waiver of one does not necessarily mandate the loss of the other.

Is there a compelling reason to treat the lessor’s waiver of the right

590. Id. at 723, 123 P.2d at 872-73.
593. CAL. CIV. CODE § 3300 (West 1977).
to terminate the lease as a mandatory waiver of the right to damages, regardless of the lessor's contrary intent? This result would have the benefit of putting an end to the transfer dispute. On the other hand, the lessor would be forced to choose between the harsh remedy of forfeiture or no remedy at all. The lessor may be willing to forego termination of the lease if he remains protected by the right to recover damages for the breach.

A decision to allow the lessor to recover damages even if the lessor elects not to terminate will not eliminate factual ambiguities. Absent express language, it may be unclear from the facts whether the lessor intends to waive one or both of the remedies. For example, the lessor's acceptance of rent with knowledge of the transfer is a waiver of the right to terminate the lease absent a non-waiver clause. Will this also result in an implied waiver of the right to damages? Absent other facts, the acceptance of rent should not be treated as a waiver of the right to damages. Since the lease is not terminated, the lessor is entitled to the rent. He or she should not have to forgo that entitlement in order to preserve the remedy for damages.

It is curious that there are no California cases expressly dealing with these damage issues. Perhaps this is the "sleeping dog" problem that seldom arises. Perhaps the prospect of serious damages from the transfer motivates lessors to elect to terminate. If that prospect is not present, perhaps lessors prefer to ignore the situation rather than end up with an expensive quest for nominal damages.

C. Liability of Third Party

The tenant made the transfer restriction covenant to the lessor, and is liable for damages resulting from the breach. Also, the tenant remains liable for other breaches of the lease that occur after either an assignment or a sublease. This is based on privity of contract between the lessor and tenant which continues absent a release of the tenant. Is the third party also liable to the lessor for breach of the transfer restriction covenant?

Generally, absent an assumption agreement, a subtenant is not directly liable to the lessor for breaches of the prime lease. There is no privity of estate or contract between them. However, a subtenant can be held liable for actual or punitive damages for wrongfully withholding

596. Id.
597. See, e.g., Food Pantry, 58 Haw. 606, 575 P.2d 869.
598. See supra notes 11-23 and accompanying text.
599. Id.
An assignee is directly liable to the lessor for breaches of the lease occurring after the assignment. There is privity of estate between the lessor and assignee during the time the assignee holds the leasehold estate. However, unless there is an assumption agreement, the assignee is not liable for a breach that occurred before he acquired the leasehold. The act of transfer, by which the assignee acquired the leasehold, constitutes the breach. This is true although the damages may be suffered later. It is not clear whether the breach will be treated as occurring before or after the assignee has acquired the leasehold. It can be argued that it is the tenant's wrongful act of transferring that constitutes the breach, and the assignee should not be liable. On the other hand, it can also be argued that a transfer is necessary for a breach to occur, and the assignee must acquire the leasehold before there is a transfer. Thus, it is the assignee's acquisition of the leasehold which completes the breach and the tenant and assignee are co-actors in the breach.

A related problem occurs if the assignee wrongfully reassigns in violation of a lease covenant. The assignee is not liable for breaches occurring after he or she has parted with the leasehold estate, absent an assumption. A technical argument could be made that the assignee has parted with the estate before the transfer is perfected. However, it does not seem realistic to adopt a theory that would absolve the assignee from liability for a wrongful transfer where he or she is the active transferee. Even though the third party may avoid liability to the lessor for damages, the third party still risks the possibility of the lease being terminated by the lessor.

V. THE MISSING REMEDY—"DISABLING" RESTRAINT

The California cases discussed above make it clear that the lessor cannot on the one hand keep the lease in effect, and on the other hand treat the unconsented transfer as void. It is unlikely that a lessor would
draft this as his or her exclusive remedy even if it were available. However, it would be a desirable alternative remedy for the lessor. It would allow the lessor to preserve favorable lease terms while blocking the disapproved transfer.

A remedy that treats an unconsented transfer as void is called a disabling restraint on alienation.\(^7\) Also, the use of an injunction to enforce a promise not to transfer without the lessor's consent has a similar disabling effect.\(^8\) The disabling restriction has the obvious result of blocking the transfer. It may also have less obvious results which can trap the unwary. For example, the third party in unconsented possession may not have a sufficient insurable interest to recover on his insurance policy for fire damage.\(^9\)

A remedy that treats an unconsented transfer as voidable, but effective unless the lessor elects to terminate the lease, is called a forfeiture restraint on alienation.\(^10\) California treats the restraint as a forfeiture restraint, not as a disabling restraint. This is consistent with the traditional view that a "disabling restraint is more objectionable from a public policy standpoint because it imposes a complete freeze on the movement of ownership."\(^11\)

If the jurisdiction allows disabling restraints, it is technically possible to draft and enforce a transfer restriction in a manner that would allow the lessor to block the transfer without terminating the lease.\(^12\) Whether or not a disabling restraint should be allowed as an alternate remedy is a policy decision.

Restraints on alienation, although permitted, are a disliked interference with commerce.\(^13\) The lessor can terminate the lease and recover damages, or leave the lease in effect and recover damages.\(^14\) It can be argued that the lessor is adequately protected without providing for a freeze on the movement of leasehold ownership. On the other hand, it

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\(^{607}\) Restatement, supra note 91, § 15.2 comment c; 6 Property, supra note 307, § 26.7, at 417.

\(^{608}\) 6 Property, supra note 307, § 26.51, at 490.

\(^{609}\) See Splish Splash Waterslides, Inc., v. Cherokee Ins. Co., 167 Ga. App. 589, 307 S.E.2d 107 (1983). A Georgia statute provided that a lease of less than five years was a use right which could not be transferred without the lessor's consent.

\(^{610}\) Restatement, supra note 91, § 15.2 comment b; 6 Property, supra note 307, § 26.8, at 418.

\(^{611}\) Restatement, supra note 91, § 15.2 comment c; 6 Property, supra note 307, § 26.9, at 419.

\(^{612}\) M. Friedman, supra note 566, § 7.304a at 262; 2 Powell, supra note 11, 246(1) at 372.103; 49 Am. Jur. 2d., supra note 566, §§ 408, 494.

\(^{613}\) See supra notes 54-90 and accompanying text.

\(^{614}\) See supra notes 562-605 and accompanying text.
might be argued that an historic perception of evil resulting from a disabling restraint does not justify denial of a logical remedy to block a prohibited transfer. The remedy allows the lessor to retain the benefits of the existing lease while avoiding an unconsented transfer.

In addition to a policy of dislike of restraints on alienation, a basic policy of contract remedies is involved in the decision. The present California approach is consistent with the view that a contracting party has the choice between performance or payment of compensation for failure to perform. This view was concisely stated in Chief Justice Bird’s concurring and dissenting opinion in *Seaman’s Direct Buying Services, Inc. v. Standard Oil Co.*615

Indeed, the assumption that parties may breach at will, risking only contract damages, is one of the cornerstones of contract law. “[I]t is not the policy of the law to compel adherence to contracts, but only to require each party to choose between performing in accordance with the contract and compensating the other party for injury resulting from a failure to perform. This view contains an important economic insight. In many cases it is uneconomical to induce completion of the contract after it has been breached.” In most commercial contracts, recognition of this economic reality leads the parties to accept the possibility of breach, particularly since their right to recover contract damages provides adequate protection.616

It seems that forfeiture and damages are generally adequate to protect the lessor; however, they may be inadequate in some situations. Perhaps a reasonable compromise would treat the transfer as voidable, but allow the lessor to nullify the transfer while keeping the lease in effect if the lessor can show the inadequacy of the other remedies.

If California law is changed to allow the lessor to dispossess the third party without terminating the lease, certain other statutory clarifications would be required. The lessor would have to be given the right to bring an unlawful detainer action to dispossess the third party while recognizing the paramount right to possession in the tenant.617 Also, the relationship to the basic remedies code provisions would have to be clarified by providing that the third party can be dispossessed without terminating the tenant’s right to possession.618

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616. *Id.* at 778, 686 P.2d at 1173, 206 Cal. Rptr. at 369 (Bird, C.J. concurring in part and dissenting in part) (quoting POSNER, ECONOMIC ANALYSIS OF LAW at 55 (1972)).
617. CAL. CIV. PROC. CODE §§ 1161-1161a (West 1982).
VI. DILEMMA OF THE ILLUSORY "LOCK-IN" REMEDY

California has adopted a comprehensive set of remedies for tenant breaches.619 The basic plan of the legislation, contained in California Civil Code section 1951.2, is to have an immediate termination of the lease and an immediate cause of action for damages. Under this basic plan, the lease is terminated in either of the following situations: (1) where the tenant breaches the lease and abandons the premises; or (2) where the tenant breaches the lease and the lessor terminates the tenant's right to possession.620

The tenant can unilaterally terminate the lease by committing a breach and abandoning the property. The lessor has been given the opportunity to prevent the tenant from triggering termination. The lessor can use the lock-in remedy contained in California Civil Code section 1951.4.621 If the lease specifically provides for the remedy, and the section is complied with, the lessor can lock-in the lease. This means that the lessor can keep the lease in effect and enforce its provisions. Relief is provided to the locked-in tenant by requiring that the lease permit the tenant to assign or sublet, or both, subject only to reasonable restrictions.

Consider the following sequence:

1. The tenant breaches a lease covenant other than the transfer restriction and abandons the premises.
2. The lessor elects to keep the lease in effect and exercises the lock-in remedy under section 1951.4.
3. The tenant makes an unconsented transfer over the reasonable objections of the lessor.

In this situation, the lessor can either terminate the lease and get rid of the undesirable transferee, or leave the lease and the transfer in effect. The lessor cannot keep the lease in effect and block the reasonably objectionable transfer. The lessor, faced with the unreasonable transfer in violation of the lease, must either give up the lock-in remedy of Section 1951.4 or permit the transfer. The only way the lessor can get the transferee out of possession is to terminate the tenant's right to possession. As soon as the lessor does this, the lease is terminated.622

This imposes a serious limitation on the effectiveness of the lock-in remedy. A tenant might breach and abandon with the expectation of terminating the lease. If the lessor tries to block that expectation by ex-

620. Id. § 1951.2(a).
621. Id. § 1951.4.
622. See id. §§ 1951.2(a), 1951.4(b).
ercising the lock-in, the tenant might knowingly make an unreasonable transfer so that the lessor will terminate the lease. This is not without risk to the tactical tenant. The lessor may leave the lease and sue the tenant for damages caused by breach of the covenant.623

A possible solution would be to allow the lessor to keep the lease in effect and nullify the transfer. However, this would involve the policy considerations discussed above.624

VII. SUMMARY OF CONCLUSIONS

A. Lease Termination

1. A prohibited transfer in the form of an assignment or sublease is voidable, not void. The interest passes from the tenant to the third party, subject to the right of the lessor to take remedial action.

2. A prohibited transfer does not automatically terminate the lease.

3. The lessor can elect to terminate the lease and recover possession of the property.

4. If the lessor fails to terminate the lease, the transfer remains effective.

5. A lessor’s waiver of the right to terminate the lease may be express or implied from conduct.

B. Damages

1. If the lessor elects to terminate the lease, the lessor should be able to recover from the tenant the damages suffered, if any, in accordance with California Civil Code section 1951.2.

2. If the lessor elects not to terminate the lease, or waives the right to terminate the lease, the lessor should be able to recover from the tenant the damages suffered, if any, in accordance with the usual rules for breach of contract.

3. It should be possible for the lessor to waive the right to terminate the lease without waiving the right to damages.

4. The subtenant who receives the wrongful sublease from the tenant is not liable to the lessor for the tenant’s breach of the transfer restriction in the prime lease.

5. It is unclear whether the assignee, who receives the wrongful as-

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623. See supra notes 577-97 and accompanying text.
624. See supra notes 619-24 and accompanying text for a discussion of policy considerations.
assignment from the tenant is liable to the lessor for the tenant's breach of
the transfer restriction. There are competing arguments. This should be
clarified.

6. It is unclear whether the non-assuming assignee who wrongfully
reassigns is liable to the lessor for breach of the transfer restriction.
There are competing arguments. This should be clarified.

C. **Disabling Restraint**

1. The lessor is not allowed to keep the lease in effect and treat the
transfer as void. There are competing arguments concerning the allow-
ance of this remedy.

2. Consideration should be given to allowing the lessor to block or
nullify the transfer, without terminating the lease, if the lessor establishes
that other remedies are inadequate.

3. If the law is changed to allow the lessor to nullify the transfer
and dispossess the transferee, the statutes dealing with unlawful detainer
and basic lease breach remedies should be conformed with.

D. **Lock-in Remedy Dilemma**

1. The requirement that the lessor terminate the lease in order to
avoid a wrongful transfer places a serious limitation on the effectiveness
of the lock-in remedy in California Civil Code section 1951.4.

2. The limitation could be avoided by allowing the lessor to nullify
the transfer and dispossess the transferee, without terminating the lease.
However, allowing this remedy would involve the competing considera-
tion related to the disabling restraint type remedy.

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**PART 3.**

**TENANT REMEDIES FOR WRONGFUL
ENFORCEMENT OF
ASSIGNMENT AND SUBLEASE
RESTRICTIONS**

I. **Scope of Part**

This Part examines the remedies available to a tenant when, pursu-
ant to a transfer restriction in a commercial lease of real property, a les-
sor wrongfully refuses consent to an assignment or sublease by a tenant.

Assume that a lessor and tenant enter into a commercial lease of
real property. A clause in the lease restricts the tenant's ability to trans-
fer to a third party without the lessor’s consent. The lessor is subject to an express or implied reasonableness consent standard. Later, the tenant proposes to transfer all or part of the leasehold to a third party. The transfer will be in the form of either an assignment to an assignee, or a sublease to a subtenant. The lessor wrongfully refuses to consent to the transfer. The wrongfulness of the refusal is based on the assumption that the lessor is subject to a reasonableness consent standard, and withholds consent unreasonably. As an alternative, the wrongful enforcement of a transfer restriction could involve the lessor’s objection to a proposed transfer that is not within the scope of the restriction. In this variation, the lessor does not have the right to require consent to the proposed transaction.

What are the tenant’s remedies in California? Should the remedies be clarified or modified?

II. COVENANT VS. CONDITION

A. Distinction and Effect

This section assumes a factual situation where the lessor is subject to a reasonableness consent standard and that he or she has unreasonably refused to consent. Occasionally, an express consent standard is clearly worded as a covenant by the lessor that he or she will be reasonable in withholding consent, or that he or she will not unreasonably refuse consent. For example, the clause requiring the lessor’s consent for a leasehold transfer might say: “Lessor promises that he will not unreasonably withhold consent.” More commonly, however, the consent clause contains a phrase that “consent is not to be unreasonably withheld” or that “consent will not be unreasonably withheld” or that “consent shall not be unreasonably withheld.” Absent express covenant language, the language imposing a reasonableness standard is subject to two different views. One view considers the language to be a covenant by the lessor.

625. For a discussion of the types of restriction clauses, see supra notes 24-25 and accompanying text.
626. For a discussion of consent standards, see supra notes 32-53 and accompanying text.
627. Due to the policy of strict construction, a transaction will generally escape the restriction unless the clause expressly takes it into consideration. For a discussion of strict construction, see supra notes 56-60 and accompanying text.
628. The same issues are involved when the transfer restriction is contained in a sublease from the tenant/sublessor to a subtenant, and the subtenant seeks remedies against the tenant/sublessor.
The other view considers the language to be a qualification or condition of the tenant's duty to get the lessor's consent.630

There is a dramatic difference between the two views when the tenant seeks a remedy. If the reasonableness standard is a covenant by the lessor, an unreasonable refusal to consent is a breach of contract. The tenant then has the normal breach of contract remedies, including an action for damages. If, however, the reasonableness standard merely qualifies the requirement to get the lessor's consent, an unreasonable refusal merely eliminates the need for consent. The tenant can then proceed to transfer without the lessor's consent.

In theory, the tenant may seem to have solid remedies in either case. In practice, the remedy for a reasonableness qualification or condition may be akin to the tenant having contractual permission to levitate without artificial assistance. The practical problems with this remedy are discussed below in Subpart IV.631

Negotiating positions of the lessor and tenant can be strongly affected by the choice of a reasonableness covenant or condition. A wrongful withholding of consent in violation of a covenant can lead to an expensive breach of contract. It is easier for the lessor to say "no" if the tenant is unable to point out the contractual liability for damages that will be suffered. However, if the tenant is able to show potential tort liability,632 the lessor will realize there is an expensive risk attached even to a reasonableness condition.

The California courts have not taken a definitive position on the issue of a covenant versus a condition. There is dictum by a court of appeal in the 1928 case of Kendis v. Cohn633 that supports the view that reasonableness is a qualification of the tenant's obligation to obtain consent, not a covenant by the lessor.634 The matter has not been an issue of consequence in subsequent decisions. Rather, subsequent to Kendis, there has been an increasing emphasis on a lease as a contract and on the covenant of good faith and fair dealing in every contract.635 These devel-

631. See infra notes 652-79 and accompanying text.
632. See infra notes 680-752 and accompanying text.
634. Id. at 64-66, 265 P. at 854.
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opments are consistent with treating the reasonableness standard as a covenant.

The view that the reasonableness standard is merely a qualification or condition seems to place a premium on semantic gamesmanship. It is at variance with the modern emphasis on good faith performance and reasonable expectations. It has been criticized as subjugating intent to "technical syntax, nicety of expression or semantics" and as being "contrary to the modern concept of contract law." The Restatement apparently recognizes this problem, and adopts the view that the provision for a reasonableness standard is a covenant. Under that view, the tenant is "entitled to all the remedies available for a breach of a promise." Apparently, therefore, the majority view treats the express reasonableness standard as a covenant. Naturally, the lessor wishes to reduce exposure to damages for failure to comply with a reasonableness standard. Interpretation of the provision as a qualification or condition, rather than as a covenant, seems to put a premium on obscurity. It would be more appropriate to require that a limitation on the tenant's remedies be express. Such a requirement will provide notice and an opportunity to bargain.

B. Implied Reasonableness Standard

The reasonableness consent standard can be imposed upon the lessor in two ways. It can either be expressly provided for in the lease, or it can be implied. The Restatement makes a curious distinction: if the lease expressly provides for the reasonableness standard, it is treated as a covenant, and breach of contract remedies are available; if the reasonableness standard as a covenant. 638 Naturally, the lessor wishes to reduce exposure to damages for failure to comply with a reasonableness standard. Interpretation of the provision as a qualification or condition, rather than as a covenant, seems to put a premium on obscurity. It would be more appropriate to require that a limitation on the tenant's remedies be express. 639 Such a requirement will provide notice and an opportunity to bargain.


637. RESTATEMENT, supra note 91, § 15.2 comment h.

638. Fahrenwald v. La Bonte, 103 Idaho 751, 754, 653 P.2d 806, 809 (1982); Annotation, Construction and Effect, supra note 37. There is a statement to the contrary in a 1970 law review note. See Note, supra note 392, at 521. However, it is likely that smart money today would bet on the covenant view.

639. There are limitations on the ability to contract away liability for wrongful acts, particularly if they are tortious. See, e.g., CAL. CIV. CODE § 1668 (West 1985); Tunkl v. Regents of University of California, 60 Cal. 2d 92, 383 P.2d 441, 32 Cal. Rptr. 33 (1963). This is particularly true when a residential tenancy is involved. See, e.g., CAL. CIV. CODE § 153 (West 1985); Henrioulle v. Marin Ventures, Inc., 20 Cal. 3d 512, 573 P.2d 465, 143 Cal. Rptr. 247 (1978).

bleness standard is implied, damages are not available.\textsuperscript{641} The soundness of this result has been questioned.\textsuperscript{642}

The Restatement's distinction is probably based on the belief that if the standard is implied, the lessor does not reasonably anticipate liability for damages. If the lessor does not have reason to believe that he or she will be subjected to a court-imposed reasonableness standard, this belief makes sense. The surprise liability problem could arise due to a retroactive imposition of a reasonableness requirement on a clause that is silent about the consent standard.\textsuperscript{643} It could also arise if a court were to invalidate a clause expressly giving the lessor sole discretion and mandate a reasonableness standard. On the other hand, if the lessor has reason to expect a reasonableness standard, he or she should expect breach of contract ramifications for unreasonableness.

In California, the implied reasonableness standard is the product, at least in substantial part, of the covenant of good faith and fair dealing.\textsuperscript{644} The covenant of good faith and fair dealing is based on the reasonable expectations of the parties. The reasonableness obligation is imposed because of a covenant not to injure the reasonable expectations of the tenant. It would be incongruous if the tenant did not have contract remedies for the lessor's unreasonable refusal to consent, as long as the lessor has reason to know that he or she is subject to a reasonableness standard.

\section*{III. Self-Help}

Suppose the tenant has requested consent to a proposed transfer. The lessor is subject to a reasonableness consent standard and has unreasonably refused consent. The tenant may legally go ahead with the transfer, without judicial intervention. However, this is not likely to be a practical remedy.

The tenant faces termination of the lease and liability for damages to the lessor if he or she is incorrect about the lessor's unreasonableness. There is also potential liability to the third party transferee. In addition, a knowledgeable third party is unlikely to step into the risk of litigation and possible loss of possession if reasonable alternative sites are available.

The proposed transferee is faced with a lessor who says consent is

\addcontentsline{toc}{section}{References}

\textsuperscript{641} Restatement, \textit{supra} note 91, \textsection 15.2 comment h.
\textsuperscript{642} Fahrenwald, 103 Idaho at 754-55 n.3, 653 P.2d at 809-10 n.3. The court left resolution of the issue to another day because the issue was not before it.
\textsuperscript{643} For a discussion of retroactive application of a reasonableness standard, see \textit{supra} notes 379-437 and accompanying text.
\textsuperscript{644} Kendall, 40 Cal. 3d at 500, 709 P.2d at 844, 220 Cal. Rptr. at 825.
required and has been reasonably refused. The tenant says that the lessor is unreasonable and consent is not required. The propriety of the refusal can be litigated and the reasonableness issue reduced to a judgment. However, a knowledgeable third party will prefer a clean deal, and will not look forward to the thrill of prolonged and expensive litigation. There is a risk that the lessor might prevail and the transferee will have business disruption and other problems associated with a relocation. Also, there is the possibility that a new site will be more expensive or more difficult to find at the time of relocation. Even if the proposed transferee is reasonably certain of the result, and receives an indemnity agreement from the tenant, the transferee will likely need some inducement to proceed.

The tenant should not attempt to use the self-help remedy without first asking the lessor for consent. In *Thrifty Oil Co. v. Batarse,* the California Court of Appeal held that a subtenant and third parties could not prevail in an unlawful detainer action by the sublessor because there was a failure to seek consent. The court commented that the request for consent "is not a mere formality, as it affords the lessor the opportunity to protect his interests and also minimizes the risks that a . . . [transferee] will place himself in jeopardy." It also is a hallmark of 'common courtesy,' which is the cornerstone of 'good faith and fair dealing.' The court expressly left open the issue of the necessity of a request for consent where it would be a futile act. The court also left open the possibility of relief from forfeiture to prevent hardship in certain cases. The need to rely on either of these two possibilities indicates a significant lapse in planning by the tenant.

IV. CONTRACT REMEDIES

A lease is a contract. A lessor's unreasonable rejection of a transfer is a violation of a reasonable consent covenant. This results in a breach of the lease contract. The tenant is entitled to the normal remedies for breach of contract.

646. Id. at 775, 220 Cal. Rptr. at 289.
647. Id.
648. Id. at 778, 220 Cal. Rptr at 290.
650. See supra notes 629-44 and accompanying text regarding the covenant versus condition distinction.
A. Excuse or Compel Consent

The tenant who has requested consent and been refused is involved in an "actual controversy" necessary to seek declaratory relief. The tenant is entitled to declaratory relief to establish that the lessor’s refusal to consent is wrongful and that the requirement is excused. The proposed transferee may also be entitled to bring an action for declaratory relief.

Additionally, the tenant should be able to obtain specific performance to compel consent. The code provisions dealing with specific performance do not contain any impediments to such an action. Damages must be inadequate in order to obtain specific performance, but real property has historically been treated as unique. While the statutory presumption that damages are inadequate would not apply because the action is not for breach of an agreement to transfer real property, that presumption shows the special treatment accorded real property. A recent California case has pointed out that although the tenant's leasehold is an estate in real property the leasehold estate itself is not real property. This historically accurate curiosity should not prevent practical minds from recognizing the close relationship between a leasehold and real property.

B. Excuse Performance and Terminate Lease

Can the tenant use the lessor's breach of covenant as a basis for excusing the tenant’s performance, and for termination of the lease? This presents the classic confrontation between the lease as a conveyance and as a contract.

The New Jersey case of Ringwood Associates, Ltd. v. Jack's of Route 23, Inc. contains an excellent discussion of this issue. Traditional

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652. CAL. CIV. PROC. CODE § 1060 (West 1982).
655. Hedgecock v. Mendel, 146 Wash. 404, 263 P. 593 (1928); M. FRIEDMAN, supra note 566, § 7.304b; Annotation, Construction and Effect, supra note 37, at 684 n.18, 696.
657. Oksner, CALIFORNIA REAL PROPERTY REMEDIES PRACTICE, Specific Performance, § 5.5, (Cal. CEB 1982).
662. Id. at 303-11, 379 A.2d at 513-17.
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property law doctrine, applicable to the lease as a conveyance, treats covenants by the lessor and the tenant as independent. Thus, the lessor's breach did not justify the tenant's termination unless there was an actual or constructive eviction. This property rule limited the tenant to a damage remedy. Contract law recognizes mutuality of covenants, and a substantial breach of a material covenant by one party can excuse performance of the other party.

The court in Ringwood discussed the trend toward extending contract remedies to a tenant. Although the trend is particularly apparent in residential tenancies, the court recognized that it was also appropriate in commercial leases. The parties contemplate a contractual relationship, and the right to terminate for a substantial breach of a material dependent covenant is an important remedy in that relationship. The Ringwood decision contains an important discussion of the inadequacy of other remedies available to a commercial tenant. It is difficult for the tenant to find a third party willing to participate in the transfer while faced with the lessor's rejection. Damages are difficult to calculate. The court concisely summed up the situation:

When a party to a lease agreement has breached his obligation to render a certain performance [to reasonably consent] which is a substantial benefit for which the other party has bargained and given consideration, it would be inequitable to require the other party to continue his performance under the lease contract and hope for an adequate judicial remedy in the future.

The approach taken in Ringwood is fair, logical, and consistent with the trend to emphasize the contractual aspects of a lease. However, there is a jurisdictional split on the issue. The more recent cases reflect the contract approach and allow termination. The Restatement recognizes that the mutually dependent covenants doctrine applies to leases when the performance of a promise by the lessor has a significant impact on the benefits anticipated by the tenant. It also specifically recognizes termination of the lease as a remedy for breach of a covenant to not

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663. Id. at 306-09, 379 A.2d at 514-16.
664. Id. at 310-11, 379 A.2d at 516.
665. See supra notes 645-48 and accompanying text for discussion of "Self-help."
666. Ringwood, 153 N.J. Super. at 310, 379 A.2d at 516.
667. M. Friedman, supra note 566, § 7.304b; Annotation, Construction and Effect, supra note 37 at 701, 702, 704.
669. Restatement, supra note 91, § 7.1(1) and comment c.
unreasonably withhold consent.\textsuperscript{670}

There is no California case that specifically resolves the issue of lease termination as a remedy for wrongfully withholding consent to a leasehold transfer. However, California has clearly adopted the contract doctrine of mutually dependent covenants for residential\textsuperscript{671} and commercial\textsuperscript{672} tenancies. It therefore would be inconsistent to deny mutuality with respect to the reasonable consent covenant. There appears to be no substantial reason to deny the tenant the right to terminate upon establishing a substantial breach of a material covenant.

The right to the contract remedy of termination depends on treating the reasonable consent standard as a covenant rather than a condition.\textsuperscript{673}

C. Damages

California Civil Code section 3300 provides:

For the breach of an obligation arising from contract, the measure of damages, except where otherwise expressly provided by this Code, is the amount which will compensate the party aggrieved for all the detriment proximately caused thereby, or which, in the ordinary course of things, would be likely to result therefrom.\textsuperscript{674}

This is the basic California statutory provision for breach of contract damages. The reasonable consent covenant is an obligation arising from contract, so the tenant should be entitled to damages upon its breach.\textsuperscript{675} There may be problems calculating damages, but this should not affect the basic entitlement unless damages are too speculative.\textsuperscript{676} Again, the right to contract damages depends on treating the reasonable consent standard as a covenant rather than a condition.\textsuperscript{677}

\textsuperscript{670} Id. § 15.2 comment h.
\textsuperscript{671} Green v. Superior Court, 10 Cal. 3d 616, 635, 517 P.2d 1168, 1181, 111 Cal. Rptr. 704, 716-17 (1974).
\textsuperscript{673} See supra notes 629-44 and accompanying text for a discussion of "Covenant vs. Condition."
\textsuperscript{674} CAL. CIV. CODE § 3300 (West 1977).
\textsuperscript{675} Fahrenwald v. La Bonte, 103 Idaho 751, 653 P. 2d 806 (1982); Annotation, Construction and Effect, supra note 37, at 697-99; M. FRIEDMAN, supra note 61, § 7.304b; RESTATEMENT supra note 91, § 7.1(2).
\textsuperscript{677} See supra notes 629-44 and accompanying text for a discussion of "Covenant vs. Condition."
D. Unlawful Detainer Defense

The issues permitted in an unlawful detainer action are limited to preserve the summary nature of the remedy. However, when a lessor seeks to terminate the lease and recover possession based on an alleged wrongful transfer by the tenant, the wrongful withholding of consent is obviously in issue. A transfer without consent is not a breach if that consent is wrongfully withheld. It is important for the tenant to actually request the consent in order to protect his or her position.

V. Tort Remedies

The tenant may also be able to establish the lessor's liability on a tort theory. This includes the possibility of recovering punitive as well as compensatory damages.

A. Economic Interference

California recognizes the related torts of interference with contract and interference with prospective economic advantage. It is not necessary that an enforceable contract exist between the parties. Thus, it would not be a defense if the tenant and the prospective transferee had only entered into a conditional contract or no contract at all. The plaintiff must show that the defendant intended to cause the result of interfering with the transaction. This should not be difficult for the tenant to accomplish. The essence of the transaction is the proposed transfer to the third party, and the lessor wrongfully refuses to allow the transfer.

In Richardson v. La Rancherita, the California Court of Appeal upheld a tenant's judgment against a lessor based on interference with contract. The corporate tenant and third party originally proposed an assignment of the leasehold as part of the sale of a restaurant business operated on the premises, and the lessor refused to consent unless the lease was renegotiated to provide for a higher rent and future escalation.

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678. See generally CALIFORNIA RESIDENTIAL LANDLORD-TENANT PRACTICE, § 7.6 (C. Scott, G. Graham, J. Sherlin eds., Cal. CEB 1986).


680. 5 WITKIN, SUMMARY OF CALIFORNIA LAW, TORTS, §§ V, D, E (9th ed. 1988).


682. Seaman's, 36 Cal. 3d at 765-66, 686 P.2d at 1164-65, 206 Cal. Rptr. at 360-61.


684. Id. The successful plaintiffs were a corporate successor tenant (by way of a consented assignment) and its shareholders.
The parties restructured the transaction as a sale of the corporate tenant's stock by the shareholders to the third party. The lessor insisted that its consent was still necessary. This insistence caused a delay of about thirty days in closing the stock sale.

The corporate tenant and its shareholders filed an action for declaratory relief and for damages due to intentional interference with contract. The transfer restriction clause in the lease prohibited assignment or sublease without the lessor's consent. Sale of stock by the shareholders of the corporate tenant was neither an assignment nor a sublease, so the lessor was without power to reject the transaction. A judgment for damages caused by the delay in closing was affirmed.

*Sade Shoe Co. v. Oschin & Snyder* involved a transfer restriction clause which specifically covered a sale of voting shares of a corporate tenant. The lessor refused consent to a sale of the corporate stock. When the deal failed, the prospective purchaser sued the lessor for damages, including punitive damages, on the tort theory of interference with contract. The trial court sustained the lessor's demurrer without leave to amend. It found that the lessor's refusal of consent was justified and there was no tort liability. The court of appeal reversed. The decision appears to make the curious suggestion that a refusal of consent that is permissible under the terms of the lease might still result in tort liability.

The court in *Hamilton v. Dixon* commented that it was "somewhat bemused" by this apparent inconsistency in *Sade*. In *Hamilton*, the California Court of Appeal affirmed a judgment that the lessor's refusal to consent to a sublease did not create liability to the tenant for tortious interference with contract. This case was disapproved by the
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California Supreme Court in *Kendall v. Ernest Pestana, Inc.* However, the disapproval was based on the issue of which consent standard was appropriate to apply. The court did not specifically discuss the propriety of the tort action.

The recent case of *Kreisher v. Mobil Oil Corp.* involved a tort cause of action for interference with prospective economic advantage, and a jury verdict for over two million dollars in punitive damages. The trial court entered judgment against lessor Mobil Oil, following a jury verdict, for $214,000 compensatory damages and $2,002,500 punitive damages. The tenant, a Mobil station franchisee, based his causes of action on the lessor's failure to comply with a reasonableness standard when the lessor refused to consent to a transfer of the tenant's leasehold and gasoline service station franchise. The lease and franchise agreements both contained a "silent consent standard" clause. That is, the clause required Mobil's consent to transfer, but it did not specify the standard governing consent. One third party offered the tenant $28,000 for the transfer and another offered $31,000.

The relationship between the parties was based on two related documents: a franchise agreement and a station lease. The relationship continued through a series of three year term contracts going back to 1971.

The sequence of events leading to litigation is discussed in detail above. The tenant then filed an action against the lessor for compensatory and punitive damages based on eight causes of action. The three causes of action which ultimately went to the jury and led to the judgment were: breach of contract and the implied covenant of good faith and fair dealing; intentional interference with prospective economic advantage; and, intentional infliction of emotional distress.

The refusal to consent was at the heart of all the causes of action.

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705. *Id.* at 395, 243 Cal. Rptr. at 666.
706. *Id.* at 393-94, 243 Cal. Rptr. at 665.
707. *Id.* at 395, 243 Cal. Rptr. at 666.
708. See supra text accompanying notes 147-57 for a discussion of the "silent consent standard."
709. *Id.* at 392-93, 243 Cal. Rptr. at 664.
710. *Id.* at 392, 243 Cal. Rptr. at 664.
711. See supra notes 705-09 and accompanying text.
713. *Id.* at 393-94, 243 Cal. Rptr. at 665.
leading to the judgment. On appeal, the court pointed out that contract execution, consent refusal and jury verdict all occurred before the Kendall decision was filed on December 5, 1985. That case subjected lessors to a reasonableness standard, implied into a "silent consent standard" clause. The Kreisher decision reviewed the principles involved in retroactivity, including foreseeability, reliance, public policy and fairness. It concluded that the lessor was not required to conform to standards that took effect after the significant events had occurred.

The court reversed the judgment because the lower court based its decision on the lessor's refusal to give consent. It did not question the propriety of an interference tort cause of action based on a wrongful refusal to consent. It merely held that the consent was not wrongful under the circumstances presented.

When considering the potential of punitive damages in cases of this nature, it is interesting to note that the highest price offered to the tenant for a transfer in Kreisher was $31,000. The punitive damage award was $2,002,500. It is not possible to determine from the opinion the full extent of the facts that produced this sizeable award, or to determine the facts of the cause of action for infliction of emotional distress which might have contributed to it.

I have not found any California appellate decision questioning the availability of tort actions for economic interference based on a wrongful refusal of the lessor to consent to a transfer by the tenant. There does not seem to be any significant policy reason that would deny such a remedy to the tenant, as long as the cause of action can be factually established.

B. Bad Faith Breach of Contract

The reasonableness consent standard is closely related to the implied covenant of good faith and fair dealing which is implied in leases. In Seaman's Direct Buying Service, Inc. v. Standard Oil Co., the California Supreme Court discussed the issue of "whether, and under what circumstances, a breach of an implied covenant of good faith and fair dealing in a commercial contract may give rise to an action in tort."

A tort action for breach of that contract covenant has been recog-
nized when there is a special relationship between the contracting parties. This special relationship has been characterized by elements of public interest, adhesion, and fiduciary responsibility.\textsuperscript{720} This relationship has been found primarily between an insurer and insured.\textsuperscript{721} Seaman's recognized that there are probably similar characteristics in other relationships which deserve similar treatment.\textsuperscript{722}

For example, a relationship between an employer and employee might have similar characteristics.\textsuperscript{723} Subsequent to Seaman's, a court of appeal, in Wallis v. Superior Court,\textsuperscript{724} held a tort cause of action had been stated for bad faith breach of an employment related contract. The court discussed other characteristics of contracts that may also generate tort liability. They are: (1) inherently unequal bargaining power; (2) a non-profit motive for entering the contract, such as peace of mind or security; (3) inherently inadequate contract damages because they do not make the superior party account for its actions and they do not make the inferior party whole; (4) special vulnerability because of the type of potential harm and the need to place trust in the other party's performance; and (5) the defendant's awareness of the vulnerability.\textsuperscript{725}

The relationship between a bank and its depositor was involved in Commercial Cotton Co., Inc. v. United California Bank.\textsuperscript{726} In an action for tortious breach of the covenant of good faith and fair dealing, the court found sufficient similarities between banking and insurance company relationships with their customers to uphold a punitive damage award.\textsuperscript{727}

When the relationship does not involve the special elements of a basic dependence, it will not generally be sufficient to generate tort liability for breach of contract. Multiplex Insurance Agency, Inc. v. California Life Insurance Co.,\textsuperscript{728} distinguished Wallis and Commercial Cotton in an action by an insurance agency against an insurance company for refusal to pay commissions.\textsuperscript{729} The court reversed a judgment for punitive damages and pointed out that the parties were both commercial enterprises.


\textsuperscript{721} Id. at 768, 686 P.2d at 1166, 206 Cal. Rptr. at 362.

\textsuperscript{722} 36 Cal. 3d at 768-69, 686 P.2d at 1166, 206 Cal. Rptr. at 362.

\textsuperscript{723} Tameny v. Atlantic Richfield Co., 27 Cal. 3d 167, 179 n.12, 610 P.2d 1330, 1337 n.12, 164 Cal. Rptr. 839, 846 n.12 (1980).


\textsuperscript{725} Id. at 1118, 207 Cal. Rptr. at 129.


\textsuperscript{727} Id. at 516, 209 Cal. Rptr. at 544.

\textsuperscript{728} 189 Cal. App. 3d 925, 235 Cal. Rptr. 12 (1987).

\textsuperscript{729} Id. at 931-32, 235 Cal. Rptr. at 20-21.
the contract was entered into for profit, there was no disparity in bargaining power, and contract damages were adequate.\footnote{730}{Id. at 938, 940, 235 Cal. Rptr. at 20-21.}

The usual commercial lease transaction does not seem to involve the special relationship which leads to a tort action for breach of the covenant of good faith and fair dealing. Although this Part does not specifically address residential tenancies, it seems that a modern urban dweller seeking basic shelter would be a likely candidate for special relationship protection.\footnote{731}{Id. at 795, 556 P.2d at 682.}

When considering extension of tort remedies beyond situations where the special relationship exists, the California Supreme Court pointed out that these were “largely uncharted and potentially dangerous waters”\footnote{732}{Id. at 791, 556 P.2d at 680.} and suggested that “it is wise to proceed with caution.”\footnote{733}{Id. at 795, 556 P.2d at 681.} The court went on to recognize that even without a special relationship tort remedies may be available against a party who denies that a contract exists in order to avoid liability.\footnote{734}{Id. at 794, 556 P.2d at 681.} The denial must be in bad faith and without probable cause.\footnote{735}{Id. at 795, 556 P.2d at 682.}

In the typical case where a lessor wrongfully refuses to consent to a transfer, the lessor does not deny the existence of the contract. However, the court in \textit{Seaman’s} relied in part on \textit{Adams v. Crater Well Drilling, Inc.},\footnote{736}{276 Or. 789, 556 P.2d 679 (1976).} a case decided by the Oregon Supreme Court. \textit{Adams} involved a contract to drill a water well for a price that varied depending on the soil encountered while drilling.\footnote{737}{Id. at 795, 556 P.2d at 680.} The driller exacted an overcharge by threatening to sue the property owner.\footnote{738}{Id. at 791, 556 P.2d at 680.} The owner was allegedly fearful of the stress that litigation would cause his critically ill wife.\footnote{739}{Id. at 791, 556 P.2d at 680.} The court upheld a punitive damage award against the driller.\footnote{740}{Id. at 795, 556 P.2d at 681.} He was a tortious wrongdoer because he coerced payment of the money by threat of a suit, and he knew he had no rightful claim to the money.\footnote{741}{Id. at 794, 556 P.2d at 681.}

\textit{Seaman’s} court referred to \textit{Adams} and stated:

There is little difference, in principle, between a contracting party obtaining excess payment in such manner, and a con-
tracting party seeking to avoid all liability on a meritorious claim by adopting a "stonewall" position ("see you in court") without probable cause and with no belief in the existence of a defense. Such conduct goes beyond the mere breach of contract. It offends accepted notions of business ethics.\textsuperscript{742}

Suppose a lessor seeks to exact an increase in rent or other premium as the price of consent knowing that he or she is not entitled to withhold. Suppose further that he or she threatens to bring an unlawful detainer action to forfeit the lease and recover possession unless his or her demands are met. It seems likely that the members of the court in \textit{Seaman's} would allow a tort action.\textsuperscript{743}

In \textit{Cohen v. Ratinoff},\textsuperscript{744} the tenant included a cause of action for bad faith breach of contract based on the lessor's wrongful refusal to consent, and sought punitive damages.\textsuperscript{745} The court reversed a judgment in favor of the lessor on the pleadings.\textsuperscript{746} However, this case focused on the issue of applying the reasonableness standard to the lessor's refusal to consent. There was no significant discussion of the appropriateness of a tort cause of action. The \textit{Seaman's} case had not yet been decided. In the \textit{Kendall} case, the Supreme Court recognized the effect of the \textit{Cohen} decision and commented: "While we express no view on the merits of the claim for punitive damages in \textit{Cohen}, we note that not every breach of the covenant of good faith and fair dealing in a commercial contract gives rise to an action in tort."\textsuperscript{747}

It is beyond the scope of this Article to deal with the propriety of providing tort remedies, including punitive damages, for breach of contract. This is a major and complex issue. The admonition by the \textit{Seaman's} court to proceed cautiously is good advice. However, certain general observations can be made with respect to the wrongful denial of consent to transfer. There does not appear to be a sufficient "special relationship" between the parties to a commercial lease to justify a tort action for breach of contract, although that relationship might be present in some residential tenancies. There might be tort liability without a spe-

\begin{itemize}
\item \textsuperscript{742} \textit{Seaman's}, 36 Cal. 3d at 769-70, 686 P.2d at 1167, 206 Cal. Rptr. at 363.
\item \textsuperscript{743} The case was heard before Justices Bird, Broussard, Grodin, Kaus, Mosk, and Reynoso. Although Chief Justice Bird filed a separate concurring and dissenting opinion, there is nothing in that opinion to indicate that she would be less likely to find a tort cause of action. Justices Broussard and Mosk are the only ones of the six still on the court.
\item \textsuperscript{744} 147 Cal. App. 3d 321, 195 Cal. Rptr. 84 (1983). See supra notes 140-43 and notes 331-39 and accompanying text for a discussion of \textit{Cohen}.
\item \textsuperscript{745} \textit{Cohen}, 147 Cal. App. 3d at 326, 195 Cal. Rptr. at 86.
\item \textsuperscript{746} Id. at 331, 195 Cal. Rptr. at 89.
\item \textsuperscript{747} \textit{Kendall}, 40 Cal. 3d at 497 n.11, 709 P.2d at 842 n.11, 220 Cal. Rptr. at 823 n.11.
\end{itemize}
cial relationship if, in order to exact a better deal than the lease provides, the lessor: wrongfully withholds consent to transfer; threatens action to terminate the lease; has no probable cause to withhold consent; and, is without belief in the right to withhold consent. There is, however, no California case expressly adopting any of these positions.

C. Other Torts

Occasionally, an overzealous lessor or agent will avoid the niceties of due process procedures and use wrongful self-help methods to dispossess a tenant and the unconsented transferee. Self-help methods of recovering possession are wrongful even if the tenant is in breach. When there is a wrongful refusal of consent, the self-help dispossession is a separate wrong. The situation can produce a variety of torts, such as trespass, assault, battery, and conversion. The truly zealous lessor may also invite an action for infliction of emotional distress.

D. Punitive Damages

The fact that a wrongful refusal to consent to a transfer may lead to a tort cause of action does not necessarily mean that punitive damages are likely. Punitive damages are reserved for odious conduct characterized by "oppression, fraud or malice." The following instructions for jurors give an excellent summary of the required foul deed:

If you find that plaintiff suffered damage as a . . . result of the conduct of the defendant on which you base a finding of liability, you may then consider whether you should award punitive damages against defendant . . ., for the sake of example and by way of punishment. You may in your discretion award such damages, if, but only if, you find by clear and convincing evidence that said defendant was guilty of [oppression] [fraud]

748. See Kassan v. Stout, 9 Cal. 3d 39, 507 P.2d 87, 106 Cal. Rptr. 783 (1973). In Kassan, after learning that the lessees had sold their leasehold interest in violation of a lease provision, the lessor posted a notice stating his intention to reclaim the premises. Immediately thereafter the lessor entered the premises and evicted the lessees. The court found no abandonment by the lessees, and held that the lessor's remedy lay with the statutory 3-day notice provision and the judicial system.


[or] [malice] in the conduct on which you base your finding of liability.

[“Malice” means conduct which is [intended by the defendant to cause injury to the plaintiff] [or] [despicable conduct which is carried on by the defendant with a willful and conscious disregard for the [rights] [or] [safety] of others.] [A person acts with conscious disregard of the rights or safety of others when [he] [she] is aware of the probable dangerous consequences of [his] [her] conduct and willfully and deliberately fails to avoid those consequences].

[“Oppression” means despicable conduct that subjects a person to cruel and unjust hardship in conscious disregard of that person’s rights.]

[“Despicable conduct” is conduct which is so [vile,] [base,] [contemptible,] [miserable,] [wretched,] [or] [loathsome] that it would be looked down upon and despised by ordinary decent people.]

[“Fraud” means an intentional misrepresentation, deceit, or concealment of a material fact known to the defendant with the intention on the part of the defendant of thereby depriving a person of property or legal rights or otherwise causing injury.]

The law provides no fixed standards as to the amount of such punitive damages, but leaves the amount to the jury’s sound discretion, exercised without passion or prejudice.

In arriving at any award of punitive damages, you are to consider the following:

(1) The reprehensibility of the conduct of the defendant.
(2) The amount of punitive damages which will have a deterrent effect on the defendant in the light of defendant’s financial condition.

[(3) The amount of actual damages.]752

VI. STATUTORY REMEDIES

There are statutory remedies available if the lessor wrongfully dispossesses the tenant and transferee. A forcible entry and detainer action can be brought to recover possession and damages.753 Treble punitive damages are possible in such an action when the lessor is guilty of

"malice."\textsuperscript{754}

In addition to actual damages, punitive damages of up to $100.00 per day are available to a residential tenant when the lessor seeks to dispossess the parties by interfering with access or utilities.\textsuperscript{755}

VII. SUMMARY OF CONCLUSIONS

A. Covenant vs. Condition

1. Absent express language of covenant; there are two views concerning the effect of an express reasonableness consent standard. One treats the standard as a covenant by the lessor. Under this view, the tenant has contract remedies for breach of covenant if the lessor unreasonably withholds consent. The other view treats the standard as a qualification or condition of the tenant's obligation to obtain the lessor's consent. Under this latter view, the tenant is excused from obtaining consent that is unreasonably withheld, but the tenant is not entitled to damages for breach of contract or other contract remedies.

2. It is more fair, practical and realistic to treat the express reasonableness standard as a covenant.

3. An implied reasonableness consent standard is subject to the same two views that it is either a covenant or a condition.

4. It is more fair, practical and realistic to treat the implied reasonableness standard as a covenant, as long as the lessor has reason to know that he or she is subject to a reasonableness standard.

B. Self-help

1. The tenant can proceed with the transfer if the tenant has requested consent and the lessor has wrongfully denied it.

2. This remedy has serious practical limitations.

C. Contract Remedies

1. The tenant can bring an action to declare that the lessor's consent is not required, or to compel the lessor to consent.

2. There are differing views concerning the tenant's right to terminate the lease and be excused from further performance. One view, emphasizing the lease as a conveyance, treats the covenants as independent and denies the right to terminate. The other view, emphasizing the lease


\textsuperscript{755} \textsc{Cal. Civ. Code} § 789.3 (West 1982); see also \textsc{Kinney v. Vacari}, 27 \textsc{Cal. 3d} 348, 612 P.2d 877, 165 \textsc{Cal. Rptr.} 787 (1980); Hale v. Morgan, 22 \textsc{Cal. 3d} 388, 584 P.2d 512, 149 \textsc{Cal. Rptr.} 375 (1978).
as a contract, treats material covenants as mutually dependent and allows termination. The better view would allow the tenant to terminate the lease if there is a substantial breach of a material covenant.

3. The tenant’s right to the contract remedy of termination depends on treating the reasonable consent standard as a covenant.

4. The tenant is entitled to contract damages for breach of covenant.

5. The tenant’s right to the contract remedy of damages depends on treating the reasonable consent standard as a covenant.

6. The tenant is entitled to use the lessor’s wrongful refusal to consent as a defense against an unlawful detainer action based on an unconsented transfer.

D. Tort Remedies

1. The tenant may be able to establish tort causes of action against the lessor for interference with contract or interference with prospective economic advantage when the lessor’s wrongful refusal to consent delays or disrupts the transfer transaction.

2. The lack of an enforceable contract between the tenant and the prospective transferee does not prevent recovery for economic interference.

3. There does not appear to be a sufficient “special relationship” between the parties to a commercial lease to justify a tort action for breach of contract, although that relationship might be present in some residential tenancies.

4. There might be tort liability without a special relationship if, in order to exact a better deal than the lease provides, the lessor: wrongfully withholds consent to transfer; threatens action to terminate the lease; and is without probable cause to withhold consent and without belief in the right to withhold consent.

5. Several tort actions can be involved if the lessor wrongfully dispossesses the tenant and third party. For example, there may be circumstances of trespass, assault and battery, conversion and infliction of emotional distress.

6. Punitive damages are only recoverable if the lessor is guilty of oppression, fraud or malice.

E. Statutory Remedies

1. The tenant has statutory remedies available if the lessor wrongfully dispossesses the tenant or transferee by direct or indirect means.
PART 4.
IN VOLUNTARY LEASEHOLD TRANSFERS:
EFFECT OF RESTRICTIONS AGAINST
ASSIGNMENT AND SUBLEASING

I. SCOPE OF PART

This Part deals with the application of a restriction against leasehold transfers, contained in a commercial lease of real property, to involuntary transfers. For convenience, the word "transfer" is used to refer to either an assignment or a sublease.\footnote{An assignment is a transfer of the entire leasehold, whereas a sublease is a transfer of only an interest in the leasehold. The distinctions between an assignment and a sublease, although significant, are not important for the purposes of this study. For a discussion of the distinctions, see supra text accompanying notes 11-23.}

Certain transfers originate in a voluntary act of the tenant, but end up as a transfer based on operation of the law rather than the specific intent of the tenant to transfer. The following are examples: a tenant makes a will and later dies; a tenant executes a mortgage and later defaults leading to foreclosure; or, a tenant files a voluntary petition in bankruptcy leading to a transfer to the trustee in bankruptcy. These transfers by operation of law are treated as involuntary transfers in this Article.

Assume that a lessor and tenant enter into a commercial lease of real property. The lease contains a clause restricting transfers of the leasehold by the tenant. Later, an involuntary transfer occurs. Typically, the involuntary transfer will occur because of the death or financial obligations of the tenant. The lessor seeks a remedy, usually termination of the lease, for non-compliance with the transfer restriction. A dispute between the lessor and the transferee ensues.

Does the transfer restriction clause entitle the lessor to terminate the lease (or seek other remedies) based on an involuntary transfer?

II. TYPES OF INVOLUNTARY TRANSFERS

The death of a tenant does not ordinarily terminate a lease.\footnote{CAL. CIV. CODE § 1934 (West 1985).} Thus, the leasehold, as part of the deceased tenant's estate, will be distributed to beneficiaries of a will or intestate heirs, or be sold during administration. The transfer by operation of law, pursuant to a will, the intestate
succession statutes, or probate administration statutes is treated as an involuntary transfer.\footnote{758}{See infra notes 760-94 and accompanying text.}

Financial obligations of the tenant can cause a variety of involuntary transfers of the tenant's leasehold, or temporary loss of control over the leasehold. For example, there may be an execution sale to satisfy judgment creditors, a foreclosure or trustee's sale under a delinquent mortgage or deed of trust on leasehold security, an appointment of a receiver to control the property (control without transfer) while litigation is pending, or a transfer to or by a trustee in bankruptcy in connection with bankruptcy proceeding.\footnote{759}{See infra notes 795-820 and accompanying text.}

III. APPLICABLE RULES

A. In General

Restrictions against leasehold transfers, although permissible, are strictly construed in favor of transferability. Strict construction is a product of the policy against restraints on alienation.\footnote{760}{See infra notes 795-820 and accompanying text.} Since the lessor may terminate the lease if a prohibited transfer occurs,\footnote{761}{See supra notes 301-57 and accompanying text.} the policy against forfeitures also leads to strict construction against the restriction.\footnote{762}{See supra notes 562-69 and accompanying text.} For example, one California statute provides: "A condition involving a forfeiture must be strictly interpreted against the party for whose benefit it is created."\footnote{763}{See Stratford Co. v. Continental Mortgage Co., 74 Cal. App. 551, 555, 241 P. 429 (1925).}

Restrictions against involuntary transfers are permissible, but the rule of strict construction requires that the restriction expressly cover the involuntary transfer involved. As a result, a general restriction against assignments or subleases will be interpreted to cover only voluntary transfers.\footnote{764}{See Farnum v. Hefner, 79 Cal. 575, 21 P. 955 (1889); see also RESTATEMENT, supra note 91, § 15.2 comment c; 2 POWELL, supra note 11, at 372.100-372.103; 49 AM. JUR. 2D, supra note 566, § 414; Annotation, Transfer in Bankruptcy, or Otherwise in Interest of Creditors or Lien Holders, as Violating Covenant in Lease Against Assignment, 46 A.L.R. 847, 847 (1927).} The involuntary transfer restriction must be specific.\footnote{765}{For an example of an express specific clause, see LEASE PRACTICE, supra note 403, § 3.114.}

This is an old rule which was followed in England at an early date.\footnote{766}{See note (A) to Dumpor's Case, 4 Coke 119B, 76 Eng. Rep. 1110, 1111 (K.B. 1587).} However, a tenant cannot take advantage of this rule by attempting to
disguise a voluntary transfer as an involuntary one in order to evade the clause.\textsuperscript{767}

\textbf{B. Death Transfers}

Transfers caused by the death of the tenant are not covered by a general transfer restriction.\textsuperscript{768} There is some authority for a difference in treatment for a death transfer by intestate succession and one by will.\textsuperscript{769} It is generally agreed that an intestate transfer upon the death of the tenant is not covered by a general restriction against leasehold transfers. Some cases have held that a death transfer by will is covered by the general restriction because the will reflects the tenant's intent. It seems that the approach taken by the cases which do not distinguish between the two types of death transfers is more consistent, and in keeping with probable expectations. California appears to treat a will transfer as beyond the scope of a general transfer restriction.\textsuperscript{770} Language in a lease, which includes a general transfer restriction, binding upon the heirs, successors, executors and administrators of the tenant is usually insufficient to restrict a transfer upon death.

Although a death transfer is a transfer by operation of law, it is risky for the lessor to rely only upon a clause restricting transfer "by operation of law." \textit{Stratford Co. v. Continental Mortgage Co.}\textsuperscript{771} is a good example of the strictness of construction. In \textit{Stratford}, a lease clause gave the lessor the option to terminate if "any person, other than the lessee named herein, shall secure possession of the interest of the lessee hereunder, under execution, or by reason of any receivership or proceeding in bankruptcy, or other operation of law, or otherwise . . . ."\textsuperscript{772} The tenant died intestate and the administratrix sold and assigned the leasehold.\textsuperscript{773} The lessor attempted to terminate the lease through an unlawful detainer action.\textsuperscript{774} Although someone other than the tenant secured possession, and there was a transfer by operation of law, the court found that the language was limited to solvency events and did not apply to an involuntary

\textsuperscript{767} \textit{Farnum}, 79 Cal. at 581, 21 P. at 957; see also 49 AM. JUR. 2d, supra note 566, § 415.

\textsuperscript{768} California Packing Corp. v. Lopez, 207 Cal. 600, 279 P. 664 (1929); see also 2 \textit{POLLER, supra note 11}, § 246[1], at 372.102-372.103; 4 \textit{WITKIN, SUMMARY OF CALIFORNIA LAW, Real Property} § 644 (9th ed., 1987).

\textsuperscript{769} See 49 AM. JUR. 2d, supra note 566, § 420.


\textsuperscript{772} \textit{Id.} at 553, 241 P. at 430 (emphasis added).

\textsuperscript{773} \textit{Id.}

\textsuperscript{774} \textit{Id.} at 552, 241 P. at 429-30.
death transfer.\textsuperscript{775}

Burns v. McGraw\textsuperscript{776} is another example of the risks of relying on the general phrase “by operation of law.” In that case, a clause prohibited assignment without the lessor’s consent, and specifically provided that the lease was not assignable “by operation of law.” Another clause provided that certain solvency events such as appointment of a receiver, assignment for benefit of creditors and bankruptcy would constitute a breach of the lease.\textsuperscript{777} The tenant died leaving the leasehold to a beneficiary.\textsuperscript{779} The court determined that the beneficiary could take the leasehold without the lessor’s consent.\textsuperscript{780} The court pointed out that “the lessor desiring ... protection against the intrusion of strangers, has only to insert in the lease ‘very special’ language reserving the right to terminate the lease upon a tenant’s death, or requiring consent to a bequest of the lease.”\textsuperscript{781}

In the more recent Miller v. San Francisco Newspaper Agency\textsuperscript{782} case, newspaper dealership agreements simply provided that they were “not assignable nor transferable in whole or in part by Dealer, voluntarily, by operation of law or otherwise.”\textsuperscript{783} The court held that the phrase “by operation of law” was sufficient to prevent transfer by will to a beneficiary.\textsuperscript{784} The court distinguished the situation where the phrase is contained in the context of language referring to the tenant’s “potential financial demise,” and thus is limited to solvency events.\textsuperscript{785} Even though this case involved dealership agreements rather than leases, the court did not treat them as personal service contracts, so the more liberal construction of the restriction cannot be explained on that basis.\textsuperscript{786}

Horning v. Ladd\textsuperscript{787} also involved a simple clause which did not refer to solvency events, but the court reached the opposite result from Miller. In Horning, an installment sale contract provided that the contract could

\textsuperscript{775} Id. at 554, 241 P. at 430.
\textsuperscript{777} Id. at 483, 171 P.2d at 149.
\textsuperscript{778} Id. at 483-84, 171 P.2d at 149.
\textsuperscript{779} Id. at 484, 171 P.2d at 149.
\textsuperscript{780} Id. at 485, 171 P.2d at 150.
\textsuperscript{781} Id. at 488, 171 P.2d at 152.
\textsuperscript{782} 164 Cal. App. 3d 315, 210 Cal. Rptr. 159 (1985).
\textsuperscript{783} Id. at 317, 210 Cal. Rptr. at 160.
\textsuperscript{784} Id.
\textsuperscript{785} Id. at 318, 210 Cal. Rptr. at 161.
\textsuperscript{786} A Maryland court has held that a clause which prohibited transfers by operation of law was broad enough to cover a merger by which the tenant corporation was extinguished and the leasehold transferred to the surviving corporation by force of statute. Citizens Bank & Trust Co. v. Barlow Corp., 295 Md. 472, 456 A.2d 1283 (1983).
not be assigned by the buyer "nor by operation of law." The court held that the clause did not prevent the buyer's interest from passing upon death.

The issue of clause coverage arose in an unusual manner in Joost v. Castel. The tenant died and the representatives of his estate claimed that lease clauses caused the termination of the lease in the event of death. A clause entitled "Assignment and Subletting" restricted assignment or sublease without the lessor's consent, and specifically prohibited assignment or sublease by "operation of law or otherwise." The court held that this clause "clearly applied to voluntary acts" and not the death of the tenant. Another clause entitled "Nontransferable Involuntarily" provided that in the event of bankruptcy, or certain other solvency events, the lessor had the option to terminate the lease. Since this clause only applied to solvency type events, not death, and since it was optional whether the lessor terminated or not, the court held that this clause did not result in termination.

C. Financial Obligation Transfers

An execution sale is not covered by a general restriction against leasehold transfers. In Farnum v. Hefner, the clause provided that the tenant would not "underlet any portion of said premises nor assign this lease without the written permission" of the lessor. The court referred to the clause as the "ordinary kind" and held that it applied to voluntary, not involuntary, assignments. The court pointed out that the lessor can subject involuntary transfers to the restriction by express language. There are, however, recent specific statutory provisions dealing with execution sales of leaseholds to enforce money judgments.

California Code of Civil Procedure section 695.035 is divided into two major parts. Part (a) provides that the leasehold can be transferred to satisfy a money judgment if the tenant has the right to voluntarily

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788. Id. at 808, 321 P.2d at 797.
789. Id. at 811, 321 P.2d at 798.
791. Id. at 140, 91 P.2d at 173.
792. Id.
793. Id. at 140-41, 91 P.2d at 174.
794. Id. at 140, 91 P.2d at 173-74.
795. Farnum v. Hefner, 79 Cal. 575, 580, 21 P. 955, 957 (1889); see also Powell, supra note 11, at 372.01.
796. 79 Cal. 575, 21 P. 955 (1889).
797. Id. at 577, 21 P. at 956.
798. Id. at 580, 21 P. at 957.
799. Id. at 581, 21 P. at 957.
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sublet or assign either without restriction, or subject to conditions or standards that are met by the transferee. If the lease requires the lessor's consent to an assignment or sublease, the lessor's consent is necessary and the lessor is subject to the same consent standard that would apply to a voluntary transfer. For example, if there is an express or implied reasonable consent standard, the lessor would have to show a commercially reasonable objection to the transfer. If, however, the clause expressly gives the lessor the right to use sole discretion, he or she would not have to show a reasonable objection to the involuntary transfer. Part (b) nullifies a provision restricting involuntary transfers to the extent that it would prevent the application of part (a). This statute does not change the rule that holds an involuntary transfer is not subject to a general transfer restriction. It merely prevents a clause that would restrict execution sales more severely than it restricts voluntary transfers.

The appointment of a receiver to take control of the premises is not covered by a general restriction against leasehold transfers. This result can be justified either on the basis that it is involuntary, or on the additional basis that a receivership does not typically involve a transfer of any interest in the leasehold. However, a specific restriction against receiverships should generally be enforced. The recent Superior Motels case involved the issue of whether an express anti-receivership provision in a lease was an invalid restraint on alienation. The disputed lease clause provided that the appointment of a receiver to take possession of the tenant's assets would constitute a breach of the lease. The clause was attacked as an unreasonable restraint on alienation in violation of California Civil Code section 711. That section provides: "Conditions restraining alienation, when repugnant to the interest created, are void." The court said that the section only prohibits restraints that are unreasonable, those not necessary to protect, or prevent impairment of, a security. The court cited Kendall and two secured loan transaction cases as authority for this proposition. The court

800. CAL. CIV. PROC. CODE § 695.035 (West 1987).
801. Part I discusses the appropriate consent standard to apply. See supra notes 32-49.
802. 49 AM. JUR. 2D, supra note 566, § 417.
803. See Urban Properties Corp. v. Benson, 116 F.2d 321 (9th Cir. 1940).
805. Id. at 1042, 241 Cal. Rptr. at 489.
806. CAL. CIV. CODE § 711 (West 1982).
went on to say that it cannot resolve the validity of the clause in the abstract and there was no evidence regarding the necessity of the provision to protect security interests.\textsuperscript{810} The question of whether there is a need to comply with a reasonableness standard is the subject of part 1, subpart VI of this article.\textsuperscript{811}

A foreclosure or trustee’s sale under a mortgage or deed of trust on leasehold security is not covered by a general restriction, even though the security instrument originated in the voluntary act of the tenant.\textsuperscript{812} There is some question whether the tenant’s execution of the deed of trust violates a general transfer restriction in California. In the 1932 \textit{Chapman v. Great Western Gypsum} \textsuperscript{813} case, the Supreme Court decision stated that “we do not believe that a covenant against assignment contained in a lease is violated by the giving of a mortgage on the lease.”\textsuperscript{814} This result can be explained either by strict construction or by the fact that execution of a deed of trust creates a lien and does not transfer the leasehold. The recent \textit{Airport Plaza, Inc. v. Blanchard} \textsuperscript{815} decision by a court of appeal mentions \textit{Chapman}, but states that a clause which restricts “assignment or ‘transfer’ of the lease, ‘in whole or in part, or [lessee’s] interest’ . . . is broad enough to cover transfers to secure a loan.”\textsuperscript{816} The court in \textit{Airport Plaza} found that the lessor’s objection to hypothecation of the leasehold was reasonable.

A voluntary assignment for the benefit of creditors has been held to be covered by a general restriction against transfer.\textsuperscript{817} Although it is usually the result of financial difficulties, it is a voluntary act without operation of law. However, California Civil Code section 1954.1 temporarily limits the lessor’s right to terminate when there is a general assignment for the benefit of creditors.\textsuperscript{818} That section allows the assignee to occupy and to operate the business on the premises for up to 90 days after the assignment, notwithstanding any lease provision. The assignee is required to pay rent provided for in the lease.

A bankruptcy proceeding is not covered by a general restriction against leasehold transfers, and this construction is generally followed
whether the bankruptcy petition is involuntary or voluntary.\textsuperscript{819} The transfer results from operation of law rather than the tenant's specific intent to transfer. Even if the lease contains a transfer restriction specifically aimed at bankruptcy proceedings, the Federal Bankruptcy Act has detailed limitations on and procedures for enforcement of leasehold transfer restrictions.\textsuperscript{820}

IV. SUMMARY OF CONCLUSIONS

1. Restrictions on involuntary transfers of a leasehold are, with some limitations, permitted.
2. The policies of dislike of restraints on alienation and dislike of forfeitures lead to a strict construction against restrictions on involuntary transfers.
3. A general restriction on transfer will be construed to apply to voluntary, not involuntary transfers.
4. A restriction on involuntary transfers must be express and specific.
5. The rules in this area of the law are old and well established.
6. There is some question in the cases concerning the degree of specificity required, however the questions can be avoided by careful drafting to express the intent and expectations of the parties with respect to particular types of transfers.
7. There are existing statutory limitations on the enforceability of solvency type transfer restrictions. For example: (a) it is not permissible to impose a stricter restriction on involuntary transfers by execution sales than is imposed on voluntary transfers; (b) when a general assignment for the benefit of creditors occurs, there is a temporary grace period during which the lessor cannot terminate a lease; (c) the Federal Bankruptcy Act limits enforcement of transfer restrictions when actions under the Act are involved.

\textsuperscript{819} 49 AM. JUR. 2D, \textit{supra} note 566, § 416; Annotation, \textit{supra} note 11, at II; \textit{Restatement, supra} note 91, § 15.2 comment e, illustration 2.

PART 5.
USE RESTRICTIONS IN LEASES:
RELATIONSHIP TO RESTRICTIONS AGAINST ASSIGNMENT AND SUBLEASE

I. SCOPE OF PART

This Part examines the relationship between a restriction on use of the premises and a restriction on transfer of the leasehold, contained in a commercial lease of real property. It focuses on the specific issue of whether the reasonable consent standard, imposed on some transfer restrictions by the California Supreme Court in the Kendall v. Ernest Pestana, Inc. decision, also applies to use restrictions. For convenience, the word “transfer” is used in this study to refer to either an assignment or a sublease.

Assume that a lessor and tenant enter into a commercial lease of real property. The lease contains a use restriction clause. The clause either absolutely prohibits any use of the premises other than the one specified, or it prohibits other uses unless the lessor consents. As an alternative, the clause may either absolutely compel a specific use of the premises, or it may compel the use unless the lessor consents to a change. Later, the tenant proposes to change the use. As another alternative, the tenant and a potential transferee may propose the use change in connection with a proposed assignment or sublease. The lessor refuses to allow the change in use and a dispute ensues.

Is the lessor held to an objective standard of commercial reasonableness when he or she refuses to allow a change in use of the premises?

II. TYPES OF CLAUSES

There are a variety of clauses dealing with use of leased premises. The following are brief descriptions of the most common types.

1. Specific Use Only. The clause prohibits use of the premises for anything other than the specified use or uses. It is desirable to use language such as “only” or “solely” to make it clear that the use is lim-

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822. See supra notes 175-254 and accompanying text for a discussion of Kendall and its ramifications.
823. An assignment is a transfer of the entire leasehold, whereas a sublease is a transfer of only an interest in the leasehold. The distinctions between an assignment and a sublease, although significant, are not important for the purposes of this study. For a discussion of the distinctions, see supra notes 11-23 and accompanying text of the principal study.
824. See LEASE PRACTICE, supra note 403, § 3.58 at 104-05.
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...itted to the specific use. Otherwise, there is a danger that the clause will be interpreted to mean that the specified use is permitted, but that other uses are also permitted. 825

2. Specific Use Mandatory. The clause affirmatively requires the premises to be used for the specified use or uses. 826 This type of clause usually compels the operation of a certain type of business, and it may get into details of the business such as hours of operation, quality of merchandise, etc. If a clause does not specifically compel operations, it will generally not be construed to require the tenant to actually use the premises, and the tenant may cease using the premises altogether. 827

3. Specific Use Prohibited. This type of clause prohibits specific use or uses of the premises. 828

4. Specific Use Protected. This clause prohibits the lessor from using or permitting the use of the lessor's other property for specific businesses. 829

The first three types of clauses restrict the tenant's use of the premises. The fourth type of clause protects the tenant's use of the premises, generally against competition. 830 This Part considers the first three types of clauses. 831

Clauses that restrict the tenant's use of the premises fall into two general categories. The "consent" type provides that the lessor's prior consent is required to any variation from the specific use restrictions. 832 The "absolute" type merely sets forth the restriction as an absolute requirement, and there is no mention of the lessor's consent to any variation. 833

825. 4 MILLER & STARR, supra note 404, § 27:73, at 351; 7 ROHAN, supra note 11, § 6.02, at 6-6.

826. See LEASE PRACTICE, supra note 403, § 3.60.


828. It may also prohibit certain general types of activities. See ROHAN, supra note 11, § 6.05(7), at 6-19; LEASE PRACTICE, supra note 403, § 3.59, at 105-06.

829. ROHAN, supra note 11, § 6.05 (12), (13), at 6-19 to 6-20.

830. For a general discussion of lease competition clauses, see ROHAN, supra note 11, § 6.04, at 6-10 to 6-14.

831. For a recent application of the covenant of good faith and fair dealing to the fourth type of clause, see Edmond's of Fresno v. MacDonald Group, Ltd., 171 Cal. App. 3d 598, 217 Cal. Rptr. 375 (1985).

832. See LEASE PRACTICE, supra note 403, § 3.58.

833. ROHAN, supra note 11.
III. PURPOSES

Use restriction clauses serve a variety of purposes. In a percentage rent lease, the rent is based on the revenues produced on or from the premises. Generally, there is a minimum base rent, and the likelihood and amount of percentage rent varies with the circumstance. The agreed percentage set forth in the lease is typically based on the tenant's particular type of business. There is a wide variation among rates, based on the type of business, and a change of use of the premises can significantly affect percentage rental income. For example, a tenant might change the use from a large general merchandise retail sales store to a warehouse used to store goods sold elsewhere.

The lessor may want to preserve the drawing power of a certain type of use in a shopping center. For example, a general merchandise retail sales store, or a grocery store, would be expected to attract a larger volume of people than a warehouse or a racquetball facility. That drawing power brings people to the center and generates profits for other tenants who are paying percentage rentals. The drawing power also helps to maintain the overall economic health of the center and facilitates renting space in the center.

The variety and balance of tenants are other important considerations to a shopping center lessor. Control over the mix can have an important effect on the degree of economic success of the center. Also, the lessor wants to avoid violating any exclusive rights or non-competition protection given to other tenants. The protection given one tenant depends on the lessor's control over other tenants. In addition to mix, the lessor may want to maintain a certain image for a center or a building. This image may involve more than just a control over the general type of business. It can involve factors such as name recognition, quality of goods and services, ethnic character of goods and services and others.

A different use may increase the burden on the building, the common areas or the requirements for lessor services. For example, the new use may require use of heavy equipment that causes noise and vibrations which disturb other tenants. The change in use may require the operation of a forklift, which causes extreme bearing weight on small areas and accelerates deterioration of pavement and floors. There may be a substantial increase in use of parking areas, elevators and other common areas and facilities. There may be an increased demand for services fur-

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835. See Lippman, 44 Cal. 2d at 139-40, 280 P.2d at 777.
nished by the lessor, such as electricity, water and trash pick-up. Insurance costs and availability may change with a change in use. The new use may involve alterations to the building such as partition walls and signs.

Continuation of a specific use may be necessary to preserve a non-conforming use authorization under zoning or building codes. The costs and risks of liability for hazardous substances will vary dramatically depending on the particular use. In some cases, control over use may be necessary to prevent the tenant from putting the owner into violation of a deed restriction.

The lessor may own adjoining parcels and the particular use of the leased parcel might complement the lessor's business on the other parcel. The property may have been in the lessor's family and used for certain purposes for generations, and he or she wants to keep it so. There may be certain tax benefits derived by the lessor in maintaining a particular use. A lessor may just personally like a certain use, or personally fear change.

This is not intended as a catalogue of possible purposes of a use restriction clause. It should, however, show that there are many reasons supporting such a clause.

IV. RELATIONSHIP TO TRANSFER RESTRICTIONS

A. In General

There is a basic similarity between restrictions on leasehold transfers and restrictions on premises uses. Absent restriction, the tenant has freedom to transfer or change the use, but the lessor can validly impose a restriction on transfers or changes in use. The freedom to change use, absent an express restriction, is limited to lawful purposes and uses that are "not materially different from that for which the premises are ordinarily used or for which they were constructed or adapted." However, an occasional unauthorized or unlawful use might lead only to remedies of damages and injunction, not a forfeiture. Restrictions on

836. See supra notes 2-10 and notes 54-90 and accompanying text. 837. ROHAN, supra note 11, § 6.02, at 6-6. 838. See supra notes 2-10 and notes 54-90 and accompanying text. 839. ROHAN, supra note 11, § 6.02, at 6-6; RESTATEMENT, supra note 91, § 15.1 comment e. 840. 4 MILLER & STARR, supra note 404, § 27:25, at 265, § 27:23, at 350. 841. See, for example, Keating v. Preston, 42 Cal. App. 2d 110, 108 P.2d 479 (1940), where the tenant holding a lease for a restaurant in a hotel occasionally accommodated the desire of customers to wager. This was before California made it exceptionally easy to legally satisfy this desire.
transfer and on use are construed in favor of the tenant.\textsuperscript{842}

\textbf{B. Reasonableness Requirement}

There is a close relationship between transfer restrictions and use restrictions when the proposed transfer involves a change in use of the premises by the transferee. The transferee is subject to the use restrictions in the lease.\textsuperscript{843} If the lessor is subject to a reasonableness standard in giving or withholding consent to a transfer, a proposed change in use involves factors to be considered in the reasonableness test. Some of these factors were specifically mentioned by the court in the \textit{Kendall} decision. They include: legality and suitability of the use; the need for alterations; and the nature of the occupancy; the tenant mix in a shopping center.\textsuperscript{844} Thus, a lessor who wishes to restrict transfer should look carefully to the drafting of a use clause.\textsuperscript{845} Absent a restriction on use, a lessor will have a difficult time meeting the reasonableness standard when he or she objects to a transfer on the basis that the transferee will change the use of the premises.\textsuperscript{846} If the tenant can change the use, the lessor has no legally enforceable expectation that the use will remain the same.

Subsequent to \textit{Kendall}, a court addressed the issue of reasonableness in the context of a transfer involving a change of use that would eliminate percentage rentals. \textit{John Hogan Enterprises, Inc. v. Kellogg}\textsuperscript{847} involved a percentage rent lease with a clause that limited use to a women's ready-to-wear shop.\textsuperscript{848} The tenant had been operating at a stable profit for several years and producing percentage rentals above the minimum rent.\textsuperscript{849} The tenant entered escrow to assign the lease to a third party who proposed to operate an antique store as a hobby.\textsuperscript{850} There would not be sufficient revenue to produce percentage rentals, so only the minimum rent would be paid by the third party for the remaining nine years.

\textsuperscript{842} For a discussion of transfer restrictions, see \textit{supra} notes 54-60 and accompanying text. Regarding use restrictions, see 4 \textsc{Miller \\& Starr}, \textit{supra} note 404, § 27.73, at 351; \textsc{Rohan}, \textit{supra} note 11, § 6.02, at 6-6.

\textsuperscript{843} \textsc{Restatement}, \textit{supra} note 91, § 15.1, comment e; 49 \textsc{Am. Jur. 2d}, \textit{supra} note 566, §§ 450, 508.


\textsuperscript{845} This is particularly true in a percentage rent lease. See \textit{infra} notes 29-31 and accompanying text.

\textsuperscript{846} See, \textit{e.g.}, Roundup Tavern, Inc. v. Pardini, 68 Wash. 2d 513, 413 P.2d 820 (1966).

\textsuperscript{847} 187 Cal. App. 3d 589, 231 Cal. Rptr. 711 (1986).

\textsuperscript{848} \textit{Id.} at 591, 231 Cal. Rptr. at 712.

\textsuperscript{849} \textit{Id.} at 592, 231 Cal. Rptr. at 712.

\textsuperscript{850} \textit{Id.}
of the term. The third party agreed to pay the tenant $150,000.00 for the assignment. That amount was "equivalent to the difference over the remaining nine years of the lease between the minimum rent and the actual rents the Lessor had historically received." The court held that the lessor was subject to a reasonableness consent standard. It then made an irrefutable comment in holding, as a matter of law, that the lessor met the reasonableness standard. The court stated that a lessor's refusal "to consent to highway robbery cannot be deemed commercially unjustified." The court made an important distinction. While a lessor's refusal to consent in order to increase his or her return above that provided in the lease is generally considered unreasonable, it is reasonable to object to a transfer that would place the lessor in a worse financial position than he or she bargained for and could expect to continue under a percentage lease.

The Hogan court did not appear to directly deal with the use clause. The clause limited use to a women's ready-to-wear shop. The third party intended to use the premises as an antique shop. Probably the court considered the proposed change of use issue as included in, and overpowered by, the loss of rent issue. There does not seem to be any basis to speculate that the court would have allowed the change in use if there had not been a drop in rent.

Another potential relationship between transfer and use restrictions might exist. In the Kendall case, a clause prohibited the tenant from transferring the leasehold without the lessor's consent. The clause did not specifically state whether the lessor's consent was governed by a "sole discretion" standard or a "reasonableness" standard. The court imposed a reasonableness standard. The view has been expressed that perhaps the Kendall case might foretell the imposition of a reasonableness standard on a clause restricting use of the premises. This is discussed in Section V below.

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851. Id.
852. Id.
853. Id. at 592 n.2, 231 Cal. Rptr. at 712 n.2.
854. Id. at 593, 231 Cal. Rptr. at 713.
855. Id. at 594, 231 Cal. Rptr. at 713.
856. Id., 231 Cal. Rptr. at 714.
857. Id. at 593, 231 Cal. Rptr. at 712.
858. Kendall, 40 Cal. 3d at 496, 709 P.2d at 891, 220 Cal. Rptr. at 823-24; see supra notes 196-204 and accompanying text.
C. Public Policies

The imposition of a reasonableness consent standard on leasehold transfer restrictions by the court in Kendall flowed from two distinct public policies: (1) the policy of property law against restraints on alienation; and (2) the policy of contract law in favor of good faith and fair dealing.  

1. Restraints on alienation

The policy against restraints on alienation, applicable to transfer restrictions, is not applicable to use restrictions. This is true even though the use restriction impedes transfer. Even restraints on use of fee estates have been allowed for almost any purpose, whether the restraints be imposed as covenants, or as conditions which provide for forfeiture upon violation. In Mountain Brow Lodge No. 82, Independent Order of Odd Fellows v. Toscano, the court pointed out that use restrictions "have been upheld by the California courts on numerous occasions even though they hamper, and often completely impede, alienation. That case involved a gratuitous conveyance of a fee simple defeasible to a fraternal lodge. The deed contained a restriction on "sale or transfer" by the lodge, and a restriction requiring "the use and benefit" for the lodge only. After the grantors died, the lodge brought an action to quiet title against the restrictions. The restraint on alienation was declared void. However, the court upheld the restriction on use, which it interpreted as limited to lodge, fraternal and other purposes for which the fraternal lodge was formed. This obviously limited the ability of the lodge to transfer the property. Similarly, a restriction that limited use of property to the erection and maintenance of a dam in a conveyance of a


865. Id. at 26, 64 Cal. Rptr. at 818.

866. Id. at 24, 64 Cal. Rptr. at 817.

867. Id., 64 Cal. Rptr. at 817.

868. Id. at 23, 64 Cal. Rptr. at 817.

869. Id. at 24, 64 Cal. Rptr. at 817.

870. Id. at 25, 64 Cal. Rptr. at 818.
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fee simple defeasible has been upheld in California. Although this is only a use restriction, there is a limited market for a dam.

It is generally accepted outside California that use restrictions are allowed even if they impede transfer, and that the policy against restraints on alienation is not applicable to a use restriction. Most of the cases distinguishing restrictions on use from restrictions on alienation, and upholding the use restrictions, involve a restriction on a fee interest. Since a restriction on use of a fee estate is allowed, a restriction on a smaller estate, the leasehold, is obviously allowed. Comparing a grantor with a lessor, the lessor has a much more substantial interest in the restricted property. Traditionally, the policy against restraints on alienation has been more liberal in allowing restraints on leaseholds than on fees.

2. Good faith and fair dealing

The covenant of good faith and fair dealing is the other basis for the imposition of a reasonableness consent standard on certain transfer restrictions. It seems that both restrictions on transfer and restrictions on use are subject to the obligation of good faith and fair dealing. However, this does not necessarily mean that good faith and fair dealing mandates a commercially reasonable standard for restrictions on use. This is discussed in section V(C) below.

V. VALIDITY AND CONSENT STANDARD

A. In General

Generally, as discussed in subsection IV(C)(1) above, restrictions on use are valid. An illegal purpose may, however, invalidate the restriction. Assuming that the use restriction is valid, does the implied covenant of good faith and fair dealing require that the lessor allow a change in use unless he or she has a commercially reasonable objection?

B. Purpose Invalidity

The purpose sought to be accomplished by the use restriction may cause it to be unenforceable because of constitutional or statutory violations. An early California decision, Los Angeles Investment Co. v.

872. Mountain Brow Lodge No. 82, 257 Cal. App. 2d at 26-27, 64 Cal. Rptr. at 819.
873. See supra notes 301-22 and accompanying text.
874. See Kendall, 40 Cal. 3d at 500, 709 P.2d at 844, 220 Cal. Rptr. at 825-26.
Gary discussed the distinction between a transfer restriction and a use restriction, and upheld a deed restriction against use of the property by anyone but Caucasians. Today, a restriction on use that has a purpose of racial exclusion is recognized as repugnant to the constitution and unenforceable.

California Civil Code section 53 provides in part that "every restriction or prohibition as to the use or occupation of real property because of the user's or occupier's sex, race, color, religion, ancestry, national origin, or blindness or other physical disability is void." Taormina Theosophical Community, Inc. v. Silver involved a community developed for retired members of the Theosophical Society. Although the Society was not technically considered a religion, the court held that the broad protections against discrimination in Civil Code section 53 invalidated a restriction limiting use of the property to members only.

Exclusive business use protections and non-competition use restrictions, although generally permissible, may at times be so broad as to run afoul of federal or state legislation protecting free trade and competition.

C. Good Faith and Fair Dealing

1. In general

The covenant of good faith and fair dealing is implied in every contract in California, and a lease is considered to be a contract as well as a conveyance. Good faith and fair dealing permeates the contractual relationship, so there is little reason to doubt its application to a use restriction clause. That does not, however, necessarily compel a conclusion that the lessor must show a commercially reasonable objection in order to prevent a change in use by the tenant.

875. 181 Cal. 680, 186 P. 596 (1919).
879. Id. at 968, 190 Cal. Rptr. at 40.
880. Id. at 976, 190 Cal. Rptr. at 45.
883. Kendall, 40 Cal. 3d at 498, 500, 709 P.2d at 843, 844, 220 Cal. Rptr. at 824; see also CAL. CIV. CODE § 1925 (West 1985).
The obligation of good faith and fair dealing is discussed at length in Part 1, section XII(B).\(^{884}\) Basically, it prevents one party from doing something that deprives the other of benefits contemplated under the contract. It protects the reasonable expectations of the contracting parties against interference by one to the disadvantage of the other. The covenant of good faith and fair dealing does not prevent the parties from bargaining and expressly providing for restrictions.

The wording of the use restriction clause can make a significant difference in expressing the reasonable expectations of the parties. As discussed in Section B, above, the various types of use restriction clauses fall into two general types, the "absolute" type and the "consent" type.

2. Absolute type restriction

The absolute type restriction sets forth the specific use requirements and limitations as unqualified obligations. There is no mention of the possibility of variations with the lessor’s consent. For example, a clause might provide that “the tenant shall use the premises only for a retail bookstore, and not for any other purpose whatsoever.” It is hard to see how a tenant could later convince a court that this language led him or her to expect that he or she could change the use unless the lessor had a commercially reasonable objection. The tooth fairy may exist, but most people look to dental insurance for real expectations. A prominent leasing attorney has commented that:

[if the lessor] simply states that the sole purpose will be as specified in the lease, then arguably there can be no change without an actual amendment of the lease. To argue otherwise would be to say that the tenant could change any lease provision by simply requiring the landlord to be “reasonable.” Why not, for example, change the rent?\(^{885}\)

The obligation of good faith and fair dealing thus does not open every contractual provision to judicial renegotiation.

It should not be necessary for the lessor to justify his or her insistence that the express terms of the absolute type restriction clause be complied with. Two code sections support this conclusion. California Civil Code section 1930 states: "When a thing is let for a particular purpose the hirer must not use it for any other purpose; and if he does, he is liable to the letter for all damages resulting from such use, or the letter

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884. See supra notes 358-72 and accompanying text.
may treat the contract as thereby rescinded.\textsuperscript{886} The related section 1931(1) provides: "The letter of a thing may terminate the hiring and reclaim the thing before the end of the term agreed upon: 1. When the hirer uses or permits a use of the thing hired in a manner contrary to the agreement of the parties."\textsuperscript{887}

3. Consent type restriction

The consent type use clause sets forth the restrictions and then states that variations are not permitted without the lessor's prior consent. Here, the possibility of a change in use is introduced into the language. The issue now becomes the proper standard to apply to the lessor's consent. Can the lessor withhold consent in his sole discretion, or must he or she have an objective and commercially reasonable reason to do so?

If the clause expressly states that the lessor's consent is subject only to a sole discretion standard, or that the lessor's consent is not subject to a reasonableness standard, that express provision should be honored. The obligation of good faith and fair dealing does not support an expectation of a reasonableness standard in the face of express contrary language.\textsuperscript{888} On the other hand, if the clause expressly imposes a reasonableness standard, for example, a provision that "consent will not be unreasonably withheld," reasonableness is a contractual expectation.

If the standard governing consent is expressed in the clause, that standard becomes part of the agreement concerning use of the premises. Thus, either the express sole discretion or the express reasonableness consent standard is consistent with California Civil Code sections 1930 and 1931(1) quoted above.

The only difficulty in determining expectations occurs when a use clause requires the lessor's consent, but says nothing about the standard to be applied—the "Silent Consent Standard." This was the situation faced by the court in Kendall, except that the restriction there was on transfer, not use.\textsuperscript{889} The court used both the policy against restraints on alienation and the covenant of good faith and fair dealing to produce the reasonable consent standard for a transfer restraint.\textsuperscript{890} Since the policy against restraints on alienation does not apply to restrictions on use, will good faith and fair dealing alone produce a reasonable consent standard

\textsuperscript{886} CAL. CIV. CODE § 1930 (West 1985).
\textsuperscript{887} Id. § 1931(1).
\textsuperscript{888} See supra notes 358-72 and accompanying text for related discussion regarding transfer restrictions.
\textsuperscript{889} Kendall, 40 Cal. 3d at 494 n.5, 709 P.2d at 840 n.5, 220 Cal. Rptr. at 821 n.5.
\textsuperscript{890} Id. at 506-07, 709 P.2d at 849, 220 Cal. Rptr. at 830.
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for a use restriction? The answer depends on the reasonable expectations of the parties. Absent an express clause one way or the other, do the parties contemplate that the lessor is to have sole discretion or to have commercially reasonable limitations?

A California practice text gives an example of a silent consent standard clause that requires consent, but does not express a standard. It then comments without qualification that "[u]nder this typical basic use clause the landlord can be arbitrary and unreasonable in refusing to consent to a change in use, and the tenant has no recourse." This statement is appropriate when referring to an absolute type clause where consent is not mentioned, or to a consent type clause which has an express sole discretion standard; however, it seems risky advice when referring to a silent consent standard clause, especially after Kendall. The text cites two authorities: California Civil Code section 1930, quoted above, and Isom v. Rex Crude Oil Co. If a clause expressly requires that a lessor not unreasonably withhold consent to a change in use, the lessor could not unreasonably withhold consent and then take advantage of section 1930 to seek damages or rescission. If a reasonable consent standard is imposed on the lessor by implication, rather than by express provision, the lessor is in no better position to unreasonably withhold consent and seek relief under section 1930.

Does section 1930 prevent an implied reasonableness standard when the lessor's consent is required but no standard is expressed? The section states in part: "When a thing is let for a particular purpose the hirer must not use it for any other purpose." This language appears to strictly limit the tenant. However, when the lessor agrees to a consent type use restriction, he or she is leasing the premises either for the particular stated purpose or for an alternative purpose to which he or she consented. The statute does not appear to preclude an implied reasonableness standard for the alternative purpose. As a practical matter, this statute has not been addressed by the legislature since the year 1905, and the issue of an appropriate consent standard was probably not considered at that time.

The mentioned California practice text also cited the Isom case to support the lessor's ability to unreasonably withhold consent under a silent consent standard clause. The case is risky authority for that prop-

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891. LEASE PRACTICE, supra note 403, § 3.58, at 104.
892. 147 Cal. 659, 82 P. 317 (1905).
893. CAL. CIV. CODE § 1930.
894. LEASE PRACTICE, supra note 403, § 3.58, at 104.
osition for three reasons. First, it does not appear in the decision that a silent consent standard clause was involved. Second, it appears that a significant factor leading to the decision was the fact that the absentee owner was tricked about the intended use of the property.\textsuperscript{895} Before the property was leased, and unknown to the owner, the eventual tenant had gone onto the land and determined its potential for oil drilling and extraction. He then sent the lessor a letter requesting a lease for a tenement house. Third, the use that caused the lessor to complain involved a permanent removal of a valuable substance from the land.\textsuperscript{896}

It could be argued that since a silent consent standard clause does not expressly provide a reasonableness standard, it is an unambiguous reservation of absolute discretion in the lessor. This argument was specifically rejected by the court in \textit{Kendall}.\textsuperscript{897}

The silent consent standard use restriction seemingly requires interpretation to determine the intent and expectations of the parties. The covenant of good faith and fair dealing requires that the lessor not thwart the tenant's expectations. The issue of whether sole discretion or reasonableness as an intended and expected standard can be left to a case by case determination is a question of fact. In the alternative, a standard can be implied based on the most likely expectation, and that standard would control absent language to the contrary in the clause. For example, as in \textit{Kendall}, a reasonableness standard could be implied or presumed. The parties would still be free to negotiate and expressly provide for a sole discretion standard which would displace the implied reasonableness standard.

The implying of a commercial reasonableness standard for a clause mentioning consent, as was done in \textit{Kendall}, should not be done indiscriminately. There is a danger in turning the word "consent" into a litigable issue of reasonableness wherever it is encountered in a lease. Sometimes consent may be used as a careless shorthand to indicate the obvious proposition that the parties can modify their agreement and change the deal if they are both willing. For example, consider a clause that states: "This lease may not be amended without the written consent of the parties." Surely this should not mean that if one party wants to later change the agreement, the other party must submit to potential litigation over a commercially reasonable modification. The danger of turning courts into forums for an exercise in "let's make a deal" must be recognized.

\textsuperscript{895} \textit{Isom}, 147 Cal. at 660, 82 P. at 317-18.
\textsuperscript{896} \textit{Id.} at 659-60, 82 P. at 317-18.
\textsuperscript{897} \textit{Kendall}, 40 Cal. 3d at 502-03, 709 P.2d at 846-47, 220 Cal. Rptr. at 827-28.
D. "Satisfaction" Condition

There are contract rules relating to "satisfaction" as a condition precedent to one's duty to perform. Suppose that party A does not have to perform the contract unless A is "satisfied" with party B's performance or with some other factor. What standard governs A's satisfaction? There are similarities between these cases and the consent issue. However, there is a major distinction between the two.

The common approaches taken to satisfaction conditions can be summarized as follows: 898

1. The parties are free to expressly provide for a sole discretion standard governing satisfaction.

2. Absent an express standard, if the satisfaction involves fancy, taste or judgment, the sole discretion standard applies.

3. Absent an express standard, if the satisfaction involves mechanical fitness or utility, the reasonableness standard applies.

4. When the sole discretion standard applies, the party need not be reasonable in expressing dissatisfaction. However, the party is still bound by a duty of good faith. In other words, if the party is truly satisfied, he cannot lie and deny that satisfaction.

While similar in many respects, there is a major distinction between the cases involving satisfaction as a condition to perform a contract, and a potential case involving the lessor's consent as a requirement to modification of the contract provision restricting use. If A's promise to perform the contract is conditioned upon A's satisfaction, is A's promise consideration for the promise or performance of B, or is A's promise illusory? Satisfaction condition cases typically involve this issue of contract formation. As a result, courts in these cases focus on imposing some base level minimum obligation on A to avoid an illusory promise. When the sole discretion standard is applied to a party's satisfaction, this is particularly a problem. As a result of the need to impose some obligation on A, courts focus on a minimum duty to act in good faith, if not reasonably.

In the case of a use restriction, the contract is formed and the use restriction is part of the terms of the contract. Thus, in evaluating the lessor's consent requirement, it is not necessary to find some basic duty of the lessor in order to have a contract. The lessor's consent is more in the nature of a modification of the tenant's contract duty to observe the use restriction. It is in the nature of consent to modification, rather than a

898. For a general discussion, see Witkin, supra note 377, §§ 729-735; Restatement, supra note 91, § 228.
condition to performance. Thus, it is not necessary to seek a base level duty to uphold the contract. A binding contract can still exist even though there is no limitation on a party’s refusal to later change its terms. The issue can be addressed as a question of intent and expectations.

Satisfaction condition cases are thus not directly analogous to consent cases. However, the two situations where a satisfaction standard is implied (numbers 2 and 3 above) seem to conform to reasonable expectations. It might be of assistance to look at the possible application of these rules for adopting a satisfaction standard when none is expressed to the adoption of a consent standard when none is expressed. For example, it might be said that:

1. Absent an express standard, if the consent to a change in use involves subjective factors such as fancy, taste or judgment, the sole discretion standard applies.\textsuperscript{899}

2. Absent an express standard, if the consent to a change in use involves objective factors such as mechanical fitness or utility, the reasonableness standard applies.

If the above approach is applied, since objective business factors are involved in a typical commercial lease, an implied reasonableness standard will generally result.\textsuperscript{900} There are still obvious problems in predicting what will be considered subjective or objective factors in all situations. It is just as obvious that the selection of a particular standard governing consent is best left to bargaining and express provision. However, if that was always done, this section would not be necessary.

VI. RELATIONSHIP TO REMEDIES LEGISLATION

A. Remedies Statutes in General

The major remedies provided to the lessor for a tenant’s breach are contained in California Civil Code sections 1951.2 and 1951.4.\textsuperscript{901} The basic plan of section 1951.2 is to have an immediate termination of the lease and an immediate cause of action for damages, including prospective rental loss damages. The contract rule of mitigation of damages is built in by allowing the tenant to prove post-termination rental loss that could have been reasonably avoided by the lessor. The termination of the

\textsuperscript{899} The court in Kendall states that it was not commercially reasonable to deny consent on the basis of “personal taste, convenience or sensibility.” Kendall, 40 Cal. 3d at 501, 709 P.2d at 845, 220 Cal. Rptr. at 826.

\textsuperscript{900} See supra notes 16-18.

\textsuperscript{901} CAL. CIV. CODE §§ 1951.2, 1951.4 (West 1985).
lease is triggered by either of two situations: (1) the tenant breaches and abandons the premises; or (2) the tenant breaches and the lessor terminates the tenant's right to possession of the premises.\textsuperscript{902}

The tenant can unilaterally terminate the lease, pursuant to section 1951.2, by a breach and abandonment.\textsuperscript{903} The lessor is given the opportunity to prevent this unilateral termination and provide for a "lock-in" remedy by section 1951.4.\textsuperscript{904} If the lease specifically provides for the lock-in remedy, and section 1951.4 is complied with, the lessor can keep the lease in effect and continue to enforce its provisions. Relief is provided to the locked-in tenant by requiring that the lease permit the tenant to assign or sublet (or both), subject only to reasonable restrictions. The relationship of the lock-in remedy to restrictions on leasehold transfer restrictions is covered in part I, Section XV.\textsuperscript{905}

### B. Damages Pursuant to Civil Code Section 1951.2

When the lease is terminated due to the tenant's breach, the lessor is entitled to damages pursuant to section 1951.2. The major component of those damages is "the amount by which the unpaid rent which would have been earned . . . exceeds the amount of such rental loss that the lessee proves could be reasonably avoided."\textsuperscript{906}

Suppose that there will be a deficiency and damages if the lessor relets for the use specified in the terminated lease. Suppose further that the lessor could get more rent by leasing for a different use. How does the use restriction in the terminated lease affect the tenant's offset for reasonably avoidable rental loss?

There are two basic situations arising from what the tenant could have done under the terms of the lease if it had not been terminated for breach: first, the tenant could have changed the use without the lessor's consent, or limited only by a requirement for the lessor's reasonable consent. In this situation, it seems that the tenant is entitled to have a possible reasonable change in use considered as one of the factors in determining the reasonably avoidable rental loss. Second, the tenant could not have changed the use because the terminated lease contained an absolute restriction on use or a sole discretion consent standard. It is

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\textsuperscript{902} Id.

\textsuperscript{903} Id. § 1951.2.

\textsuperscript{904} Id. § 1951.4.

\textsuperscript{905} See supra notes 451-78 and accompanying text.

\textsuperscript{906} CAL. CIV. CODE § 1951.2(a)(2), (3) (West 1985). The amount specified is subject to modification to determine the "worth at the time of the award" in accordance with subsection (b) of 1951.2.
a policy decision whether the mitigation concept embodied in section 1951.2 allows the tenant to establish a reasonable alternate use for damage purposes. However, it seems that the lessor should not be required to give up a bargained benefit in order to reduce the damages to a breaching tenant. If the tenant is allowed to base offsets on modifications of the lease terms, which could not have been made absent a breach, what would limit the modifications to the use clause?

C. Lock-in Pursuant to Civil Code Section 1951.4

Section 1951.4 allows the lessor to keep the lease in effect and enforce its terms against a tenant who has breached and abandoned. This lock-in remedy is available only if the tenant is permitted to either assign or sublet, subject only to reasonable restrictions. Does the lessor's exercise of the lock-in remedy change the effect of a use restriction when the tenant seeks to assign or sublet?

The essence of the lock-in remedy is to keep the lease in effect. Section 1951.4 provides that "the lease continues in effect" and "the lessor may enforce all his rights and remedies under the lease." The use clause is an integral part of the continuing lease, and it remains enforceable against the tenant and transferees according to its terms. If it allows the tenant to change the use without restriction or with the lessor's reasonable consent, the transferee would have the same freedom and limitations. If the clause absolutely prohibits change, or gives the lessor sole discretion to prevent change, both the tenant and transferee have to conform to those restrictions.

VII. SUMMARY OF CONCLUSIONS

A. General Relationships

1. Restrictions on the tenant's use of the premises, contained in a commercial lease of real property, have some characteristics in common with restrictions on the tenant's transfer of the leasehold. Absent express restriction, a change in use (with some limitations) or a transfer of the leasehold is permitted. Restrictions on use or transfer are allowed, but construed in favor of the tenant.

2. Although restrictions are valid in general, those that have an illegal purpose are not enforceable.

3. Use restrictions and transfer restrictions are related when a prospective transferee proposes to change the use of the premises. If the

907. Id. § 1951.4.
908. Id. § 1951.4(a).
lessee is subject to a reasonableness consent standard in connection with the transfer restriction, the proposed use of the premises is a factor that can be taken into consideration in testing the reasonableness of the lessee's objection to the transfer. The transferee is subject to the use restriction in the lease. If there is no use restriction in the lease, it is less likely that the lessor can use the proposed change in use as a basis for reasonable objection.

B. Policies Involved

1. *Kendall v. Ernest Pestana, Inc.* involved a clause that restricted transfer without the lessor's consent but failed to express a standard governing consent. The court used two public policies as the bases for imposing a reasonableness standard on the lessor: the policy against restraints on alienation; and the policy in favor of good faith and fair dealing.

2. The policy of property law against restraints on alienation does not apply to a use restriction.

3. The policy of contract law imposing an obligation of good faith and fair dealing applies to use restrictions, but this does not necessarily mean that a lessor must have a commercially reasonable objection to a change in use.

C. Application of Good Faith and Fair Dealing

1. The obligation of good faith and fair dealing prevents one party from doing something which deprives the other of benefits contemplated under the contract. It protects the reasonable expectations of one party against interference by the other party.

2. Good faith and fair dealing do not prevent clearly expressed restrictions on use of the premises.

3. An absolute type restriction states requirements and limitations as unqualified obligations of the tenant, and does not mention the possibility of a variation with the lessor's consent. This type of clause does not create a reasonable expectation that the lessor must have a reasonable objection to prevent a change in use. Good faith and fair dealing do not require such a standard.

4. A consent type restriction states requirements and limitations and provides that they cannot be changed without the lessor's consent. The provision for consent introduces the possibility of a change in use. This type of clause may contain an express reasonableness standard or an

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express sole discretion standard, or it may not contain any express standard.

5. If the consent type restriction contains an express sole discretion standard for the lessor’s consent, it should be enforceable according to its terms. This type of clause does not create a reasonable expectation that the lessor must have a reasonable objection to prevent a change in use. Good faith and fair dealing do not require such a standard.

6. A consent type restriction that does not contain an express standard raises the issue of the intended and expected standard governing consent: sole discretion or reasonableness. The issue can be left to case by case factual determinations, or it can be resolved by establishing an implied standard to govern in the absence of an express contrary provision. This is the issue that the Kendall case resolved by establishing a reasonable consent standard with respect to a transfer restriction.

7. If a consent standard is implied into a clause that restricts use without the lessor’s consent, but that does not contain an express standard, it seems that a reasonableness standard is most consistent with the reasonable expectations of the tenant. The lessor is free to avoid an implied reasonableness standard by bargaining and expressly providing for an absolute restriction or a sole discretion consent standard.

8. There is a danger in extending a reasonableness standard indiscriminately to every clause in a lease that mentions the possibility of consent to a variation. Sometimes the parties may merely intend the consent phrase to express the proposition that the agreement can be modified if both parties are willing. For example, the application of a reasonableness standard to a clause that provides that the lease may not be amended without written consent of the parties would subject the entire contract to judicial renegotiation.

9. The issues raised in this section can be substantially avoided by careful drafting: avoid consent provisions or expressly state the intended and expected standard when using them.

D. Relationship to Remedies Legislation

1. If the lease is terminated due to the tenant’s breach, pursuant to California Civil Code section 1951.2 the tenant’s ability to consider a change of use in connection with proving an offset against damages for reasonably avoidable rental loss depends on what the tenant could have done under the lease if it had not been terminated for breach. There are two basic situations:

A. The tenant could have changed the use without the lessor’s consent, or is limited only by a requirement for the lessor’s reason-
able consent. In this situation, it seems that the tenant is entitled to have a possible reasonable change in use considered as one of the factors in determining the reasonably avoidable rental loss.

B. The tenant could not have changed the use because the terminated lease contained an absolute restriction on use or a sole discretion consent standard. It is a policy decision whether the mitigation concept embodied in section 1951.2 allows the tenant to establish a reasonable alternate use for damages purposes. However, it seems that the lessor should not be required to give up a bargained benefit in order to reduce the damages to a breaching tenant. If the tenant is allowed to base offsets on modifications of the lease terms, which could not have been made absent a breach, what would limit the modifications to the use clause?

2. If the lessor uses the lock-in remedy provided in California Civil Code section 1951.4 upon a breach and abandonment by the tenant, the right of the tenant or the tenant's transferee to change the use of the premises in connection with a transfer of the leasehold depends upon the terms of the lease. The use restriction in the lease should be enforceable according to its terms.

PART 6.
ENFORCEMENT OF LEASEHOLD TRANSFER RESTRICTION AGAINST TENANT'S SUCCESSOR:
SHOULD DUMPOR'S BE DUMPED?

I. SCOPE OF PART

This Part examines the enforceability of a transfer restriction against a tenant's successor in a commercial lease of real property. It examines the effect of the lessor's consent to a transfer by the tenant, or a waiver of the right to object to a transfer.

Assume that a lessor and tenant enter into a commercial lease of real property. A clause in the lease restricts the tenant's ability to transfer to a third party without the lessor's consent.\(^9\) The tenant subsequently assigns the lease to an assignee, either with the lessor's express consent or with the lessor's waiver by inaction. Later, the assignee proposes to reassign the leasehold.

Does the transfer restriction bind the assignee? Should the rule in California be clarified or modified?

\(^9\) For a discussion of the types of restriction clauses, see supra notes 11-23 and accompanying text.
II. DUMPOR'S CASE AND ITS EFFECT

Over 400 years ago, a case set forth a foolish rule. Almost as if it were necessary to prove that the law has a sense of humor in retaining old rules, the rule was imported from England before it could be extinguished, and it lives on in the United States today. That which was foolish in its origin has not become sensible with time. "When the reason of a rule ceases, so should the rule itself."911 That maxim should have a corollary. When a rule is without a solid reason in the first place, its demise should not be prolonged.

A. The Case

The rule in Dumpor's Case912 arose in the following manner. Oxford College913 leased land to a tenant with the "proviso that the lessee or his assigns should not alien the premises to any person or persons, without the special licence of the lessors."914 Subsequently, the lessor "licensed the lessee to alien or demise the land . . . to any person or persons."915 The tenant assigned to a man who, at his death, willed the leasehold to his son.916 When the son died intestate, his administrator assigned the leasehold to the defendant without the lessor's consent.917 The lessor, based on the unconsented assignment, recovered possession and leased to Dumpor.918 The defendant assignee re-entered and Dumpor brought a trespass action against him.919 Poor Dumpor not only lost, but also suffered the ignominy of a foolish rule being named after him.

According to the case, the ultimate assignee was entitled to possession under the leasehold. The lessor had no power to terminate the lease based on the unconsented transfer. This in turn prevented the lessor from validly leasing to Dumpor.

The rule stated to produce this result was that the first assignment with the lessor's consent

had determined [ended] the condition, so that no alienation which he [the assignee] might afterwards make could break the

911. CAL. CIV. CODE § 3510 (West 1970).
913. By its President and scholars.
914. Dumpor's, 76 Eng. Rep. at 1111, 4 Coke at 119b.
915. Id. at 1111-12, 4 Coke at 119b.
916. Id. at 1112, 4 Coke at 119b.
917. Id. 7
918. Id.
919. Id.
proviso or give cause of entry to the lessors, for the lessors could not dispense with an alienation for one time, and that the same estate should remain subject to the proviso after.\textsuperscript{920}

In other words, once the first consented assignment occurs, the restriction against unconsented assignment is no longer enforceable to prevent successive assignments. This treatment of the power to prevent an assignment is perhaps the origin of the phrase “use it or lose it.”

It is difficult to find a reasonable rationale for the rule. The reasons given are more in the nature of conclusions that need further support. The court in \textit{Dumpor’s Case} said that since the consent to the first assignment was “absolute,” it was not possible for the assignee to be subject to the restriction.\textsuperscript{921} Perhaps it could be argued that the lessor’s consent to an assignment “to any person or persons”\textsuperscript{922} was so unrestricted as to indicate an intent to abandon the restriction. This interpretation would focus on the nature of the consent as a waiver of the restriction, rather than on the nature of the restriction itself. The \textit{Dumpor’s} court did not limit its rule based on the nature of the consent. Subsequent cases have not done so either.

The court stated that a condition against assignment cannot be “apportioned.”\textsuperscript{923} Perhaps this could be limited to refer to a lease to two or more tenants, and support a rule that the lessor cannot consent to a transfer by one tenant but refuse consent to the other cotenants. A case referred to by the court involved such a situation.\textsuperscript{924} However, the \textit{Dumpor’s} court did not limit the rule to a cotenant situation.

The transfer restriction is stated to be an “entire” or single condition, as distinguished from a continuing condition.\textsuperscript{925} This appellation generally indicates an obligation that by its nature or by the intent of the parties is subject to a single performance or a single breach. It is not one that is subject to successive performances or breaches. A covenant to complete a building by a specific date is an example of an “entire” obligation.\textsuperscript{926} A covenant to pay rent is an example of a “continuing” obligation. There is nothing in the nature of a transfer restriction that would mandate treatment as “entire” regardless of the parties’ contrary intent.

\textsuperscript{920} Id. at 1113, 4 Coke at 119b-120a.
\textsuperscript{921} Id., 4 Coke at 120a.
\textsuperscript{922} Id. at 1112, 4 Coke at 119b.
\textsuperscript{923} Id. at 1113, 4 Coke at 120a.
\textsuperscript{924} Trin. 28 Eliz. Rot. 256.
\textsuperscript{925} Dumpor’s, 76 Eng. Rep. at 1113, 4 Coke at 120b. For a discussion of the distinction in the context of a transfer restriction, see Crowell v. City of Riverside, 26 Cal. App. 2d 566, 572-73, 80 P.2d 120, 123 (1938).
\textsuperscript{926} McGlynn v. Moore, 25 Cal. 384, 395 (1864).
Rather, a leasehold is by nature subject to successive assignments. A requirement of consent is capable of the same successive occurrences. The intent of the parties can produce an entire or a continuing obligation. The transfer restriction in the lease from the college in Dumpor's Case expressly applied to the tenant "or his assigns." Since the court treated the restriction as "entire," it must have concluded that the restriction by its nature could not be made "continuous." This lacks common sense and logic. It only supports the belief in mystical origins sometimes encountered in ancient property law.

B. Variations

1. General v. Specific Consent. In Dumpor's Case, the lessor gave a general consent for assignment to anyone. Subsequent statements of the rule have not limited it to such a broad consent. It seems taken for granted that consent to a transfer to a specific assignee will have the same effect of permanent removal of the consent requirement.

2. Consent v. Waiver. The lessor in Dumpor's Case expressly consented to the initial assignment. Subsequent applications of the rule have not distinguished an express consent to an assignment from a waiver of the right to object to a transfer.

3. Condition v. Covenant. The court in Dumpor's Case refers to the transfer restriction as a condition. The word condition is most likely used in the case to indicate an obligation for which termination of the leasehold, and reentry into possession, are provided as remedies. This conclusion is supported by the court's comment that the lessor "entered for the condition broken." A broken covenant on the other hand generally leads to a damages remedy. Later cases have not distinguished between a condition and a covenant for purposes of the rule.

4. Assumption. It does not appear that the assignee in Dumpor's Case contractually assumed the lease, so there was no privity of contract between the lessor and the tenant with respect to provisions in the lease. Later cases have not found privity of contract to be an important factor in application of the rule. The lack of privity of contract does not isolate the assignee from the obligations of the prime lease. There is priv-

927. Dumpor's, 76 Eng. Rep. at 1111, 4 Coke at 119b.
928. Annotation, Landlord's Consent to One Assignment or Sublease as Obviating Necessity of Consent to Subsequent Assignment or Sublease, 31 A.L.R. 153, 154 (1924) [hereinafter Annotation, Landlord's Consent]; M. Friedman, supra note 566, § 7.304e.
929. Annotation, Landlord's Consent, supra note 928, at 153; Restatement, supra note 91, § 16.1 reporter's note 7; M. Friedman, supra note 566, § 7.304e.
931. See Annotation, Landlord's Consent, supra note 928, at 155.
osity of estate and the covenants that run with the estate bind the assignee. 932

5. Lease clause variations. The restriction against transfer without the lessor's consent usually comes with the variations set out below. A strict application of the Dumpor's Case rule makes the restriction unenforceable against an assignee in all of the variations. There is authority, discussed below, 933 that the rule will not be applied when there is an express intent to have the restriction control subsequent transfers. This approach allows the restriction to be enforceable against assignees if there is an express provision that it binds successors, or that consent does not waive the restriction on future transfers. The usual lease clause variations are the following:

a. There is no mention of successors, and there is no non-waiver clause.

b. Successors are expressly mentioned in the restriction clause.

c. Successors are not mentioned in the restriction clause itself, but there is a general clause to the effect that the lease provisions are binding upon successors.

d. There is a non-waiver provision in the restriction clause.

e. There is no non-waiver provision in the restriction clause itself, but there is a general clause to the effect that a waiver does not excuse future performance of the obligation waived or performance of other obligations.

6. Conditional Consent. Sometimes the lessor will provide in the written consent itself that the consent is not a waiver of the restriction on future transfers. A strict application of the Dumpor's Case rule would disregard this non-waiver provision. However, there is authority, discussed below, 934 that the rule will not be applied when the consent is conditioned in this manner.

C. Subleases

The rule in Dumpor's Case does not generally apply to successive subleases by the tenant. 935 In other words, when the lessor consents to the first sublease by a tenant, he or she can still force the tenant to obtain

932. See supra notes 11-23 and accompanying text for a discussion of the relationship between the parties.

933. See infra notes 938-40 and accompanying text.

934. See infra notes 980-94 and accompanying text.

935. German-American Sav. Bank v. Gollmer, 155 Cal. 683, 102 P. 932 (1909); see also Annotation, Landlord's Consent, supra note 928, at 157; M. Friedman, supra note 566, § 7.304e.
consent to a subsequent sublease. This distinction between subleases and assignments in application of the rule has been criticized as without logic. It is difficult to be enthusiastic about justifying distinctions in the application of a rule that in itself lacks a solid reason for its existence. However, it could be justified on the basis that the lessor maintains the same privity of estate and privity of contract relationship with the tenant after a sublease. There has not been a transfer of the whole leasehold. A sublease merely creates a tenancy relationship between the tenant/sublessee and the subtenant. It does not change the relationship or obligations between the tenant and lessor.

D. Expressly Binding on Successors

Some cases have focused on the intent of the lessor and tenant at the time they enter into the lease and transfer restriction. If they intend to have the transfer restriction bind a succession of assignees, that intent is honored. This intent is typically expressed in one or both of the following ways. A “non-waiver” clause can provide that “a consent to one assignment, subletting, occupation, or use by another person shall not be deemed to be a consent to any subsequent assignment, subletting, occupation, or use by another person.” Another way of expressing the continuous nature of the obligation is to state that it binds not only the tenant, but also the successors and assigns.

The lease in Dumpor’s Case did express the intent that the restriction bind assigns, but the court disregarded this in developing its rule. If the lease had not expressed this intent, the decision could have been rationalized on the basis that intent to bind successive parties was not clear.

III. THE COVENANT “RUNNING” APPROACH

A. In General

The doctrine of covenants running with the land (and equitable servitudes) has traditionally been used to deal with the binding effect of a

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936. Restatement, supra note 91, § 16.1 reporter’s note 7.
937. For a discussion of the distinctions between an assignment and sublease, and the privity relationships, see supra notes 11-23 and accompanying text.
940. 49 Am. Jur. 2d, supra note 566, § 408, at 423.
promise on the promisor's successor.\footnote{2 Powell, supra note 11, ¶ 246[2], especially pages 372.123-372.125, 372.114-372.118.} The Restatement adopted this approach for dealing with the burden of lease promises passing to a leasehold transferee.\footnote{Restatement, supra note 91, § 16.1(2).} Is the burden of the tenant's promise to refrain from assignment without the lessor's consent binding on a successor to the tenant promisor absent a contractual relationship between the lessor and the assignee? This is the basic question raised by the facts in Dumpor's \textit{Case}.\footnote{76 Eng. Rep. 1110, 4 Coke 119b (K.B. 1578).}

There is no reason why the answer should not be determined by the doctrine of covenants running with the land. A privity of estate relationship exists between the lessor and the assignee.\footnote{See supra notes 11-23 and accompanying text.} The assignee has received the entire estate of the tenant.\footnote{Id.} The burden of the obligation to refrain from unconented transfers of the leasehold estate certainly touches and concerns that estate. In other words, it is related to the leasehold in a most direct way. The assignee of the leasehold could reasonably be held to notice of the provisions in the lease that created and sustains that leasehold.

The principal factual issue is whether the lessor and original tenant intended that the burden of the transfer restriction bind successive parties.\footnote{See Crowell v. City of Riverside, 26 Cal. App. 2d 566, 80 P.2d 120 (1938).} An express statement or phrase to that effect should be honored. In certain situations, it is necessary for the intent to bind assigns to be express.\footnote{See, e.g., CAL. CIV. CODE § 1464 and 1468 (West 1982).} However, there is no intrinsic reason why that intent cannot be implied with regard to the transfer restriction. If the intent is not expressed, the most likely intent should govern. This is just a way of looking at, and following, the reasonable expectations of the parties.

Suppose that the clause states that "the tenant shall not assign or sublet without the lessor's prior written consent, which consent shall not be unreasonably withheld." There is no express language binding assignees. The clause restricts transfer without the lessor's consent. Is it likely that the parties intended and reasonably expect that it only bind the original tenant, and that subsequent parties are free to transfer without any limitation? Or, is it likely that the parties intend and reasonably expect that any and all transfers be subject to review and consent by the lessor? It is asking much of a credulous person to expect that a one-shot restriction is intended.
The lessor's motives for wishing to evaluate and control transfers are no less significant after the first assignment. There is nothing in the language of the clause, above, to contradict the logic of an implied intent that the covenant be continuous. A reference to "the tenant" (or "the lessee") does not indicate a covenant that is personal to the original tenant. After an assignment takes place, "the tenant" is the assignee. For example, a covenant that "the tenant" shall pay rent is binding upon an assignee without express language of "successors and assigns."

In the unusual situation where the parties intend the restriction to govern only the first transfer, they can expressly state that limitation. A lessor and tenant can agree, and expressly provide, that the transfer restriction is personal to, and only binds, the original tenant.

B. Tenant Motivation

It might appear that tenants would welcome the limit on the effectiveness of a leasehold transfer restriction. The freedom to re-assign without the lessor's consent certainly makes the transaction more attractive to the proposed initial assignee. That attractiveness should make it easier for the tenant to make a deal with the third party. However, tenants, as well as lessors, have a reason to adopt a more rational and practical approach to the survival of the restriction. The lessor who knows that there is just one chance at controlling a transfer is more likely to deny consent in order to preserve that control. This increases the difficulty a tenant will have in making a successful assignment.

The tenant's liability to the lessor continues even after the assignment and re-assignments are made, but the assignee's liability to the lessor ceases upon re-assignment. Thus, breaches of the lease after re-assignment, such as non-payment of rent, can be enforced against the original tenant, but not the first assignee. The tenant has no control over the selection of a re-assignee, and the assignee has little motive to be selective. The tenant should hope that the lessor has, and exercises, the right to assure a reliable re-assignee.

948. See supra notes 26-31 and accompanying text.
949. See supra notes 11-23 and accompanying text.
950. Id.
951. If, however, the assignee contractually assumes the obligations of the lease, this creates a contractual privity with the lessor which continues after re-assignment.
IV. MODERN STATUS

A. England

There was a grumbling acceptance of the rule in Dumpor's Case by the English judiciary. Lord Chancellor Eldon observed:

Though Dumpor's [C]ase always struck me as extraordinary, it is the law of the land today. When a man demises to A, . . . with an agreement that if he, his executors, administrators or assigns, assign without licence, the lessor shall be at liberty to re-enter, it would have been perfectly reasonably [sic] originally to say, a licence granted was not a dispensation with the condition; the assignee being by the very terms of the original contract restrained as much as the original lessee.952

Sir James Mansfield commented: "[T]he profession have always wondered at Dumpor's Case, but it has been law so many centuries, that we cannot now reverse it."953 This lack of enthusiasm is reflected in legislation in England that abolished the rule in the middle of the 19th century.954

B. United States

The rule in Dumpor's Case has been followed in many states, but it has been soundly criticized and rejected in others.955 The rule has a "history of frequent and protracted criticism in the very decisions upholding the rule as well as in legal writings."956 It has been referred to as a stumbling block in the way of the profession, and as an artificial rule without sound reason.957 A 1924 Wyoming decision gave an excellent review of the rule and determined that it was not supported by logic, reason, or common sense.958 The court referred to the rule as a "venerable error" and an example of the "pertinacity" of the errors of the law, and rejected it.959

954. 22 & 23 Vict., chap. 35, §§ 1-3 (1859); 23 & 24 Vict., ch. 38, § 6 (1860).
955. M. FRIEDMAN, supra note 566, § 7.304e; 51C C.J.S., Landlord and Tenant § 33, at 77 (1968); 49 AM. JUR. 2D, supra note 566, § 408, at 423; C. MOYNIHAN, supra note 11, at 93; 2 POWELL, supra note 11, ¶ 246[1], at 372.106-372.107 n.60.
956. RESTATEMENT, supra note 91, § 16.1 reporter's note 7.
959. Id. at 283, 225 P. at 596.
The Restatement disapproves of the rule in *Dumpor's Case* and it provides that "the assignee who comes into privity of estate with the landlord is bound by the prohibition against assignment without the landlord's consent."\(^{960}\)

It seems that any following of the rule today in the United States is due to precedential inertia, rather than to a belief that it logically solves any problem. It is like a partially submerged log in a river. It can be found, but the unwary suffer damage.

C. California

The cases in California indicate that the rule in *Dumpor's Case* is discredited, and probably no longer followed, at least where there is an express intent that successors be bound. However, the California Supreme Court has not expressly rejected the rule, and some of the courts of appeal have not been as emphatic as one would wish.

*Kendis v. Cohn*,\(^{961}\) decided in 1928, contains the most complete judicial discussion of the rule in California. The court referred to the fact that restrictions on leasehold assignments are regarded as fair and reasonable, and that the restrictions allow the lessor to limit the right of another to select his or her tenant.\(^{962}\) The court pointed out that the *Dumpor's Case* rule contravenes these rules and prevents the lessor from selecting his or her own tenants and protecting his or her reversion.\(^{963}\) It rejected *Dumpor's Case* in situations where the intent that it be binding on assignees is express.\(^{964}\) Also, the *Kendis* court recognized that it is well settled in other jurisdictions that the rule does not apply to a sublease.\(^{965}\) The California Supreme Court denied a hearing in the case.\(^{966}\)

Early California cases have been cited for the proposition that California follows *Dumpor's Case* and treats the obligation as personal to the original tenant.\(^{967}\) In *Chipman v. Emeric*,\(^{968}\) the court held that the restriction against assignment without consent was abrogated by the first assignment.\(^{969}\) However, the lease clause did not expressly state that it

960. Restatement, supra note 91, § 16.1 comment g.
961. 90 Cal. App. 41, 265 P. 844 (1928).
962. Id. at 54, 265 P. at 849.
963. Id.
964. Id. at 58, 60, 265 P. at 850-51.
965. Id. at 54, 265 P. at 849.
966. Id. at 41, 265 P. at 844.
968. 5 Cal. 49 (1855).
969. Id. at 51.
was intended to bind assignees. Since the court did not specifically mention Dumpor's Case, the Chipman decision could be interpreted to mean that a restraint against alienation will not be enforceable against a successor unless clear intent is expressed.\textsuperscript{970} McGlynn v. Moore\textsuperscript{971} contains, in dicta, a statement that covenants against assignment are not continuing covenants.\textsuperscript{972} The case involved a covenant to construct a building within a certain time limit, which the court properly held to be single and capable of but one performance and breach.\textsuperscript{973} In Randol v. Tatum,\textsuperscript{974} the Dumpor's Case issue was raised but was not dispositive. The lessor, by conduct, waived the right to enforce the restriction.\textsuperscript{975}

Two treatises on California law cite the Baker v. J. Maier & Zobelein Brewery\textsuperscript{976} case for the proposition that a transfer restriction is personal and does not run with the land.\textsuperscript{977} However, there is no holding to that effect in Baker.

In German-American Savings Bank v. Gollmer,\textsuperscript{978} the court stated: "The assignee of a leasehold estate takes it subject to all the obligations imposed by the lease, except that, where there is a condition against assignment without consent (which is necessarily single in its nature), such condition is wholly discharged by the consent or waiver."\textsuperscript{979} The court did not explain why the covenant must by nature be single. The statement is dictum because the clause itself was not drafted in a manner that would show an intent to bind successors.

A conditional consent apparently saved the restriction from lapsing in Rothrock v. Sanborn.\textsuperscript{980} The lessor’s written consent to the initial assignment expressly provided that the consent requirement was not waived and that the lease could not be assigned again without consent.\textsuperscript{981} The court enforced the transfer restriction against the assignee, and did not even mention the rule in Dumpor's Case.\textsuperscript{982}

\textsuperscript{970} Kendis v. Cohn, 90 Cal. App. 41, 54, 265 P. 844, 849 (1928).
\textsuperscript{971} 25 Cal. 384 (1864).
\textsuperscript{972} \textit{Id.} at 396.
\textsuperscript{973} Id.
\textsuperscript{974} 98 Cal. 390, 33 P. 433 (1893).
\textsuperscript{975} \textit{Id.} at 396-97, 33 P. at 435.
\textsuperscript{976} 140 Cal. 530, 74 P. 22 (1903).
\textsuperscript{977} 42 \textit{CAL. JUR. 3D}, \textit{supra} note 404, § 195; 4 Miller & Starr, \textit{supra} note 404, § 27:92, at 415-16.
\textsuperscript{978} 155 Cal. 683, 102 P. 932 (1909).
\textsuperscript{979} \textit{Id.} at 688, 102 P. at 934.
\textsuperscript{980} 178 Cal. 693, 174 P. 314 (1918).
\textsuperscript{981} \textit{Id.} at 694, 174 P. at 315.
\textsuperscript{982} \textit{Id.}
In *Miller v. Reidy*, the lease provided that "the lessee shall not assign . . . without the written consent of the lessor." A separate clause provided that all the lease provisions were binding on "the successor or assigns of the lessee." The lessor consented to an assignment by the tenant to a first assignee and a reassignment to a second assignee. The lessor sought to terminate the lease for breach based on an uncon- 

It seems that this linguistic alchemy would require that the clause
expressly state that it binds the tenant, the tenant's assignees, the assignee's reassignee, etc. The court commented that the restriction could be made binding upon subsequent assignees "by appropriate language in the lease itself or by a qualified consent to each assignment." Probably the lawyer who drafted the lease thought that the lease contained appropriate language to assure continuing covenants.

The language in *Miller* regarding the *Dumpor's Case* issue is dictum. The lessor had waived any right to terminate by accepting rent with knowledge of the protested transfer. The lessor's petition for hearing was denied by the California Supreme Court based on the waiver by conduct. The court commented: "We are not to be understood as approving or disapproving what is said elsewhere in the opinion concerning the covenant against assignment contained in the lease." *Taylor v. Odell* also involved a waiver by the lessor's conduct, but the court volunteered dictum that "a restriction against assignment is a personal covenant made for the benefit of the lessor and does not run with the

984. Id. at 759, 761, 260 P. at 359, 360.
985. Id. at 759, 761, 260 P. at 360.
986. Id. at 760, 260 P. at 359-60.
987. The court referred to a notice from the lessor protesting the "subletting" in this last transaction. However, the court treated it as an assignment. Id.
988. Id. at 761, 260 P. at 360.
989. Id.
990. Id.
991. Id. at 763, 260 P. at 361.
992. Id.
The criticism of the rule by the *Kendis* court was discussed and approved in *Crowell v. City of Riverside.* *Crowell* makes a clear distinction between a single restriction obligation and a continuous one. If the clause does not state the restriction to be binding on the tenant’s assigns, it is single and does not bind the assignee. If the clause states that it binds the tenant and his assigns, it is continuous and enforceable against the assignee. However, the case involved a sublease rather than an assignment. The court recognized the distinction “assumed” to exist between restrictions on successive assignments and on successive subleases, but did not decide whether that distinction was the law in California.

In the 1980s, two cases mentioned the rule in *Dumpor’s Case,* but neither of them directly involved multiple assignments of a leasehold. *Laguna Royale Owners Association v. Darger* basically involved a “time-sharing” enterprise by a unit owner in a condominium project. Each of the unit “owners” received a Subassignment and Occupancy Agreement which contained restrictions against assignment and subleasing by the unit holder. The condominium association brought an action to enforce the clause against a successor to the original unit holder. The successor argued that their interest was in essence a fee and that restraints against fee transfers were void. The court commented: “It would appear that defendants’ argument more appropriately ought to be that once consent was given . . . [to the first transfer], the rule in *Dumpor’s Case* . . . became applicable and that thereafter no consent to any further assignment was required.” There was no further discussion of the rule.

In *Boston Properties v. Pirelli Tire Corp.*, the lease contained a restriction against assignment or subleasing without the lessor’s consent,

994. Id. at 120-21, 122 P.2d at 923 (citing Laird v. McPhee, 90 Cal. App. 136, 265 P. 501 (1928)).
996. Id. at 572, 80 P.2d at 123.
997. Id. at 573, 80 P.2d at 123.
998. Id. at 576, 80 P.2d at 125.
1000. Id. at 675, 174 Cal. Rptr. at 139.
1001. Id. at 673, 174 Cal. Rptr. at 138.
1002. Id.
1003. Id. at 678, 174 Cal. Rptr. at 141.
1004. Id. at 680, 174 Cal. Rptr. at 142.
1005. Id. at 680-81 n.7, 174 Cal. Rptr. at 142-43 n.7.
and the clause contained an express non-waiver provision to the effect that consent given would not excuse getting it for further transactions.\textsuperscript{1007} The original tenant sublet to a subtenant with the consent of the lessor.\textsuperscript{1008} The subtenant later sub-sublet to a sub-subtenant.\textsuperscript{1009} The second sublease was without the lessor’s consent.\textsuperscript{1010} The lessor brought an unlawful detainer action against the original tenant, with whom it continued to have privity of estate and privity of contract, seeking termination of the lease and recovery of possession.\textsuperscript{1011} The leasehold was not transferred to an assignee and there was no issue of the binding nature of the covenant against a successor to the tenant.

The court in \textit{Boston Properties} held that the restriction against subleasing without consent continued in effect and bound the original tenant, the original tenant could not give the subtenant any greater rights or freedom than it had, and the subtenant was subordinate to the terms of the master lease.\textsuperscript{1012} The sub-sublease without the lessor’s consent, and without any effort to obtain consent, and with the original tenant’s knowledge and consent, was a breach of the master lease and the lessor was entitled to terminate the lease.\textsuperscript{1013} The court commented that \textit{Kendis v. Cohn} “makes clear that the rule in \textit{Dumpor’s} case is not the law in California.”\textsuperscript{1014} This was dictum since the court was dealing with subleases, not assignments.

To summarize, in California there is language in early cases indicating, but not directly holding, that California follows \textit{Dumpor’s Case} with respect to successive assignments. There is language in later California cases criticizing, and at least one holding by a court of appeal rejecting, the rule. There is no California Supreme Court decision expressly involving the issue and either adopting or rejecting the rule. The decisions distinguish between a restriction that is expressly made binding on assignees, and one that is not express. The former has been treated as a continuing covenant which binds successors. The latter has been treated as a single and personal covenant which binds only the original tenant. California appears to follow the consensus that \textit{Dumpor’s Case} does not apply to subleases.

\textsuperscript{1007.} Id. at 990 n.1, 185 Cal. Rptr. at 59 n.1.
\textsuperscript{1008.} Actually, it was a successor to the original lessor. This was not a material factor in the case.
\textsuperscript{1009.} \textit{Boston Properties}, 134 Cal. App. 3d at 990, 185 Cal. Rptr. at 59.
\textsuperscript{1010.} Id.
\textsuperscript{1011.} Id. at 991, 185 Cal. Rptr. at 59.
\textsuperscript{1012.} Id. at 992, 185 Cal. Rptr. at 60.
\textsuperscript{1013.} Id. at 992-94, 185 Cal. Rptr. at 60-62.
\textsuperscript{1014.} Id. at 993, 185 Cal. Rptr. at 61.
V. DRAFTING SOLUTIONS

Various drafting solutions have been suggested to avoid application of the rule in *Dumpor's Case*.\textsuperscript{1015} The effectiveness of most of these solutions depends on at least some modification of the rule. The solutions are based on the parties expressing intent that the obligation continue to bind successors. The rule is based on the perceived nature of the obligation, not the intent of the parties.\textsuperscript{1016}

The following are suggestions that have been made:

1. An express clause in the lease making the transfer restriction binding on assignees should be given effect.\textsuperscript{1017} This is clearly contrary to the holding in *Dumpor's Case*. It may be necessary to expressly state that it binds not only "assigns," but also all re-assignees.\textsuperscript{1018} Since this suggestion is based on expressing the intent of the parties, it should not make any difference whether this intent is expressed in a specific provision in the transfer restriction clause or in a general clause applicable to all lease obligations.

2. An express clause in the lease stating that a consent to, or waiver of, one assignment is not a waiver of the consent requirement for future assignments should be given effect.\textsuperscript{1019} Since this suggestion is based on expressing the intent of the parties, it should not make any difference whether this intent is expressed in a specific provision in the transfer restriction clause or in a general clause applicable to a waiver of any lease obligation.

3. An express statement in the writing granting the lessor's consent to the effect that consent is to the particular assignment, and is not a waiver of the duty to get consent for subsequent assignments, should be given effect.\textsuperscript{1020}

There is a drafting solution that would not require a modification of *Dumpor's Case*: the lessor could require, as a condition of consent, that each assignee execute an independent agreement not to make a further transfer without the lessor's consent.

It is unfortunate to have a rule that is illogical and impractical, and

\textsuperscript{1015} M. FRIEDMAN, supra note 566, § 7.304e.

\textsuperscript{1016} See supra notes 912-27 and accompanying text.

\textsuperscript{1017} 42 CAL. JUR. 3D, supra note 404, § 195; 4 MILLER & STARR, supra note 404, § 27:92, at 915-16.

\textsuperscript{1018} For a discussion of Miller v. Reidy, 85 Cal. App. 757, 761, 260 P. 358, 360 (1927), see supra notes 983-92 and accompanying text.

\textsuperscript{1019} M. FRIEDMAN, supra note 566, § 7.304e.

\textsuperscript{1020} RESTATEMENT, supra note 91, § 16.1 reporter's note 7; see Rothrock v. Sanborn, 178 Cal. 693, 174 P. 314 (1918); see also Annotation, Landlord's Consent, supra note 928, at 155.
that requires specific drafting to avoid. This unnecessarily perpetuates a trap. It makes more sense to take an approach that is consistent with the intent and reasonable expectations of the parties.1021

VI. SUMMARY OF CONCLUSIONS

1. The rule in Dumpor's Case, taken from an English case in 1578, states that once the lessor consents to an assignment of the leasehold by the original tenant, the obligation to obtain the lessor's consent to an assignment is not enforceable against assignees.

2. The rule has been interpreted to apply:
   a. even if the lease expressly provides that the transfer restriction is intended to bind assignees;
   b. whether the lessor's consent was general (assignment permitted to any party) or specific (assignment permitted to specific party);
   c. whether the initial assignment is permitted by express consent or by a waiver implied from conduct;
   d. whether the transfer restriction is worded as a condition or a covenant; and
   e. whether or not the initial assignee contractually assumed the lease.

3. Subleases have generally been considered exempt from the rule. That is, consent is required for subsequent subleases.

4. The rule has been criticized and repealed in England. Although the rule has been uniformly criticized in the United States, some states continue to follow it. It has been rejected by the Restatement.

5. It appears that California does not follow the rule. However, there is dicta to the contrary in early cases, and there is no clear holding by the California Supreme Court rejecting the rule.

6. There are drafting solutions for avoiding the rule, but most solutions require a modification of the rule.

7. The rule is illogical and serves no useful purpose. It serves only as a trap for the unwary.

8. A leasehold transfer restriction may be intended to be binding only on the original tenant (i.e., single or personal). On the other hand, the restriction may be intended to apply to all successors from the tenant and to all subsequent transfers (i.e., continuous). Intent should control.

1021. See supra notes 938-51 and accompanying text.
There is nothing in the nature of the obligation that would prevent its treatment as a continuous obligation.

9. Intent that the obligation be continuous may be expressed by language to the effect that it is binding on successors. Although "assigns" or "successors" are the words typically used to express this intent, no specific word or words should be required. Either a provision in the transfer restriction clause, or a separate general clause applicable to all lease obligations, should be sufficient.

10. The intent of a continuous obligation may also be expressed by language to the effect that a consent or waiver does not excuse the requirement to obtain consent in the future. Either a provision in the transfer restriction clause, or a separate general clause applicable to all lease obligations should be sufficient.

11. It is most probable that, absent language to the contrary, the obligation is intended to be continuous and that the parties reasonably expect it to be continuous. Thus, the easiest and most logical approach would be to presume that the restriction is continuous, absent express intent to the contrary.