DePaul Law Review

Volume 5
Issue 2 *Spring-Summer 1956*

Article 7

Effect on a Percentage Lease of a Tenant's Conducting the Same Business on Other Property

DePaul College of Law

vision should cover many cases now being decided under section 15 (2) of the Sales Act as sales by description under the implied warranty of merchantability.

CONCLUSION

As has been noted, a sale by description has been understood to include almost *any* sale, whether the goods were present or not. This is a most liberal view. Other courts have ignored the problem that the phrase "by description" *should* raise, or perhaps it has not been brought to their attention. Still other courts have considered inspection by the buyer to be the key to the problem, in spite of the contradiction between "by description" and "by inspection." Difficulty of thorough inspection, latent defects, and the like have moved these courts to stretch the meaning of sale by description so that a warranty might be found. In the sale of foodstuffs which cause injury it would seem that almost any result is possible. For example, in Illinois, where there is apparently a tendency toward strictness in the interpretation of "by descripion," warranties in the sale of carbonated beverages have been implied without a contract much less a sale by description, in spite of the fact that the statute does not differentiate between sales of foodstuffs or hard goods.

The whole problem is a technical one, the handling of which has varied from fact situation to fact situation. This is due, perhaps, to conflicting desires to extend, on the one hand, the utmost in protection to the consumer public at large; and, on the other, to comply with the law as it is written.

EFFECT ON A PERCENTAGE LEASE OF A TENANT'S CONDUCTING THE SAME BUSINESS ON OTHER PROPERTY

A percentage lease is one wherein the tenant is required to pay as rental a specified percentage of the gross income from business conducted upon the premises. To the ordinary covenants of a lease are added certain clauses governing the manner in which business may be conducted, how the percentage is estimated, and how it is to be paid to the landlord.[1]

Litigation in the percentage lease field most often centers around the determination of gross income. The most common situation is the subject matter of this note—the tenant, either innocently or willfully, deprives the landlord of his expected return on the lease by transferring some or all of the business to another location. The amount of business to which the percentage clause is to attach is accordingly decreased, to the detriment of the landlord and to the benefit of the tenant.

[1] McMichael, Leases, p. 21 (4th ed., 1947).

The landlord may receive legal relief upon two different approaches to the determination of the problem.

1. Does an express provision of the lease apply to the transferred business? If the portion of the business which is transferred is operated by the tenant as part of the business which is still subject to the percentage lease, then the court may hold that it too is covered by the percentage lease rate.
2. If it is not covered by an express provision of the lease, and most often it is not, will the court protect the landlord by implying a promise by the tenant to use reasonable efforts to effectuate business upon the premises? Since this is a question of the presumed intention of the parties, the answer is contingent upon an examination of the facts of each case.

I

The first line of attack by the landlord to include the transferred business under the express provisions of the lease was also that first considered by the courts. The Supreme Court of Washington, in 1928, in the case of *Cissna Loan Co. v. Baron*,[2] where a tenant with a department store under a percentage lease rented an adjacent building, knocked down the wall, and then moved the ladies-ready-to-wear and the millinery department into the adjacent building, held that the tenant was "conducting one business only . . . and is bound to pay as rent for respondent's building the agreed percentage of the gross sales. . . ."[3] The next decision to subject the transferred sales to the percentage lease clause was *Gamble-Skogmo, Inc. v. McNair Realty Co.*,[4] a case in the federal courts which held that sales of farm implements made in a building across the alley and on a separate lot were to be included under the percentage rate since there was only one department store and one manager, with all advertising being carried on from that one store. The New York Court of Appeals, in *Mutual Life Insurance Co. v. Tailored Woman, Inc.*,[5] decided in 1955, followed the general principles laid down in the earlier cases but reached a different result on analogous facts. Here, a tenant operated the first three floors of a department store under a promise in a lease to pay a percentage rental on all sales made "on, in, and from the demised premises." Tenant, after entering into a second lease at a flat rate for the fifth floor, changed the elevator structure of the building and moved the fur department up to that floor. Advertising, window displays, the storage of the furs, and the continued use of the main store personnel continued as under the percentage lease. Tenant paid commissions to those sales people on the lower floors who sent customers to the fifth floor department. The court held that, while those sales which were made because of the direction of the

[2] 149 Wash. 386, 270 P. 1022 (1928). [3] Ibid., at 390, 1024.

[4] 98 F. Supp. 440 (D.C. Mont., 1951), Aff'd 193 F. 2d 876 (C.A. 9th, 1952).

[5] 309 N.Y. 248, 128 N.E. 2d 401 (1955).

salespeople on the lower floors were subject to the percentage rental, all other sales made on the fifth floor were not subject to it. A strong dissent argued: (1) that all sales were subject to the express provisions of the lease, and (2) that they were covered by an implicit obligation of good faith conduct by the tenant in every lease.

A generalization that the transferred business which is still operated as one main business will be subject to the percentage clause can be made only with caution for several reasons:

1. The transfer of a minor department has been held not to be covered by the percentage clause.[6]

2. It has been held that the applicability of the percentage clause was a question of fact for the jury although the circumstances indicated that the tenant was conducting one business.[7]

3. One court permitted a tenant to pay only a part of the profits to the landlord.[8]

II

The question then arises whether the court will imply a promise upon the part of the tenant to make a reasonable effort to conduct business upon the leased premises. The courts have a tendency in this situation to quote and rely upon the maxim of Judge Cardozo that: "A promise may be lacking, and yet the whole writing may be 'instinct with an obligation,' imperfectly expressed."[9]

The courts have stressed certain facts to arrive at the intention of the parties. They are the following:

1. If the lease states a substantial minimum[10] plus the percentage clause, the

[6] "A contrary construction would be anomalous in that it would result in the exaction of rent from one not a tenant in favor of another not the landlord and defy the common meaning of the word 'rent'" Dunham & Co. v. 26 East State Street Realty Co., 134 N.J. Eq. 237, 249, 35 A. 2d 40, 47 (1943).

[7] Tenant of a lumber company under a percentage lease clause made sales through agents away from the premises and made some deliveries through another yard but handled all orders through the leased premises and collected payment there. Thomin v. Norwood Sash & Door Mfg. Co., 74 Ohio App. 505, 59 N.E. 2d 605 (1944).

[8] Under a lease of a parking lot which gave the landlord a percentage of the gross receipts "derived in any manner, directly or indirectly, from or by the use or occupancy" of the premises, the tenant entered into a flat rate lease of the adjoining premises and moved overflow cars from the first lot to the second lot and at night issued second lot tickets to cars entering on the first lot. Lawrence Barker, Inc. v. Briggs, 39 Cal. 2d 654, 248 P. 2d 897 (1952).

[9] Wood v. Lucy, Lady Duff-Gordon, 222 N.Y. 88, 91, 118 N.E. 214, 214 (1917).

[10] McMichael categorizes percentage leases into the following types:

"1. Lease calling for a definitely stated percentage of gross sales as rental with no minimum or maximum stated.

"2. Lease with a definitely indicated rental, to which is added a stated percentage of gross sales over and above a given amount.

"3. Lease calling for a stated percentage of gross sales as rental with a guaranteed minimum.

[Footnote 10 continued on following page]

courts will not imply a promise.[11] A recent decision from the Illinois Appellate court of the first district, in answer to the argument that inequities would result, was "The short answer to this is that such was his contract."[12]

2. If it is a renewal lease with a percentage feature, the court will imply a promise upon the part of the tenant to use reasonable efforts to entitle the landlord to an amount which is equivalent to that which he had been receiving under the former flat rental rate although the lease states a substantial minimum.[13]

3. If the lease states no minimum, the court will not permit the tenant to deprive the landlord of his rental by a wrongful diversion of business to other property but will imply a promise to use reasonable efforts to do business upon the leased premises.[14]

The topic of percentage lease law is a relatively new but important field. The legal history of the diversion of business by a tenant under a percentage lease dates from the *Cissna Loan Co.* case in 1928 and covers a discoverable total of seventeen decisions in the appellate courts of the United States. Since the foundations have been laid, the lawyer should be able to surmise the decision of law on a stated set of facts. But the landlord who is eager for profits and not for lawsuits should heed the precept "*Wise landlords pick their tenants.*"[15]

"4. Lease with rental based on percentage of gross sales with both minimum and maximum guarantees provided.

"5. Lease providing that the landlord shall receive as rental a percentage of all profits arising from occupancy."—McMichael, Leases, p. 21 (4th ed., 1947).

[11] "No case has come to our attention which holds as a matter of law that under a percentage lease with a guaranteed substantial minimum rental, covenants are to be implied of the kind which appellee seeks to have implied in the lease under consideration." Percoff v. Solomon, 259 Ala. 482, 490, 67 So. 2d 31, 39 (1953). Accord: Cousins Inv. Co. v. Hastings Clothing Co., 45 Cal. App. 2d 141, 113 P. 2d 878 (1941); Masciotra v. Harlow, 105 Cal. App. 2d 376, 233 P. 2d 586 (1951); Fox v. Fox Valley Trotting Club, 4 Ill. App. 2d 94, 123 N.E. 2d 595 (1954); William Berland Realty Co. v. Hahne & Co., 26 N.J. Super. 477, 98 A. 2d 124 (1953), aff'd in part and rev'd in part on other grounds in 29 N.J. Super. 316, 102 A. 2d 686 (1954); Jenkins v. Rose's 5, 10 and 25¢ Stores, Inc., 213 N.C. 606, 197 S.E. 174 (1938); Palm v. Mortgage Invest. Co., 229 S.W. 2d 869 (Tex. Civ. App., 1950); Joseph E. Seagram & Sons v. Bynum, 191 F. 2d 5 (1951). But see Parrish v. Robertson, 195 Va. 794, 80 S.E. 2d 407 (1954).

[12] Fox v. Fox Valley Trotting Club, 4 Ill. App. 2d 94, 101, 123 N.E. 2d 595, 598 (1954).

[13] Selber Bros. v. Newstadt's Shoe Stores, 203 La. 316, 14 So. 2d 10 (1943).

[14] Where lease stated that tenant was to pay a stipulated percentage of sales from a gasoline station, the court ruled against a tenant who attempted to deprive the landlord of his rental by constructing pumps on an adjacent lot to which the percentage clause was inapplicable. "Here the defendant willfully and deliberately and purely with the intention of injuring the Plaintiff built himself a station right next door. . . . The law will treat the income from the new place as belonging to the old, especially since the evidence clearly shows that there was no change in volume." Seggebruch v. Stosor, 309 Ill. App. 385, 389, 33 N.E. 2d 159, 160 (1941); Goldberg v. Levy, 11 N.Y.S. 2d 315 (1939).

[15] McMichael, Leases, p. 31 (4th ed., 1947).