#50 5/16/66

Memorandum 66-24

Subject: Study 50 - Leases

We have previously distributed to you Memoranda 66-7 and 66-15 and a First Supplement to Memorandum 66-15 relating to leases. This memorandum will gather together the matters presented by the previous memoranda so that this memorandum need by the only one considered on this subject.

Distributed with this memorandum is the tentative recommendation that the Commission approved and sent out for comments. Also accompanying this memorandum are two copies of a revised recommendation designed to meet the criticisms that were made of the original tentative recommendation. The original tentative recommendation is on white paper (with a gold cover); the revised version is on yellow paper (with a gold cover). [The revised version on yellow is substantially the same as that distributed (on green paper) with Memorandum 66-15. The further revisions we suggested in the First Supplement to Memorandum 66-15 have been incorporated into it, and we have made a few other minor changes. If any of you wish to check the revised version on yellow against the previous version on green, a table appears at the back of this memorandum which spots each change made from the previous version.] We have also sent you a staff study on the problems incident to the termination of leases.

The Commission's tentative recommendation on this subject was distributed to more than 300 persons who requested copies as a result of a notice we had published in the State Bar Journal and in various legal newspapers. Attached to this memorandum are the following comments that have been received as a result of this distribution:

Exhibit I (pink) -- State Bar

Exhibit II (gold) - Professor Verrall

Exhibit III (pink) - United States Leasing Corporation

Exhibit IV (yellow) - John F. Taylor

Exhibit V (white) - J. H. Petry

Exhibit VI (green) - Fireman's Fund Insurance Co.

Exhibit VII (buff) - Albert J. Forn

Exhibit VIII (blue) - George Herrington

Exhibit IX (pink) - Los Angeles County Counsel

Exhibit X (gold) - Orange County Counsel

The tentative recommendation seems to have received a mixed reaction. Mr. Forn states, "I was pleased to see that the recommendaticns resolve a number of problems that I have encountered in my practice." The Fireman's Fund Real Estate Department writes, "I agree with and approve of the recommended legislation . . . ." On the other hand, Professor Verrall states, "My conclusions are the comments should be withdrawn and the legislation reconsidered."

In this memorandum, we will consider first those comments that deal with the scope of our recommendation; we will then consider those comments going to the basic policies underlying our recommendation; next we will deal with those comments dealing with specific problems; and finally we will include some notes on the revised recommendation--indicating sources for language and mentioning remaining problems.

APPLICATION OF THE COMMISSION'S PROPOSALS TO CHATTEL LEASES

The Northern Section of the State Bar Committee (Exh. I, Min. 11/8/65 ¶ 5,) the United States Leasing Corporation (Exh. III), and John F. Taylor (of Dinkelspiel & Dinkelspiel)(Exh. IV) all raise questions concerning the application of the recommendation to chattel leases.

As John F. Taylor points out, there is extensive statutory regulation of the chattel leasing area already. Moreover, contracts for the lease of chattels are not encumbered with common law conveyancing theory based on the concept of a lease as an estate in land and rent as a feudal service incident to an estate in land.

In Oakland Cal. Towel Co. v. Roland, 93 Cal. App.2d 713 (1949), the court applied usual contract doctrines to a breach of a lease of personal property and permitted the recovery of damages by the lessor for the loss of prospective profits.

Inasmuch as the problems that have been identified in connection with leases have all related to leases of real property, we think that there is no need for our recommendation to deal with the rights arising out of chattel leases at all. We recommend, therefore, that the tentative recommendation be revised to deal only with real property.

The revised tentative recommendation (on yellow) reflects this suggestion. The proposed statute has been relocated in the portion of the Civil Code dealing with leases of real property, and all reference to leases of personal property has been deleted.

POLICY UNDERLYING RECOMMENDATION

As a background for the following discussion, you should read the staff study that has been distributed for the May 27-28 meeting.

The basic policy decision that underlies the recommendation is that a lease is fundamentally a contract by which the lessor promises a continuing permission for the lessee to use and occupy the leased property in return for which the lessee promises to pay a consideration usually called rent. This, in substance, is what Section 1925 of the Civil Code says. The Commission's recommendation is intended to implement the declaration of

Section 1925 by making clear that upon an abandonment of leased property by the lessee or upon his eviction for good cause, the lessor may resort to the ordinary contract remedies for the protection of his rights. The contractual doctrines of anticipatory breach and mitigation of damages are applicable, and damages are recoverable for prospective loss of the benefit of the bargain.

Most of our correspondents seem to approve of the policy. The Southern Section of the State Bar approved all of the stated principles underlying the recommendation except that relating to the presumption arising from a reletting of the property. Exh. I, So. Sec. Min. The United States Leasing Corporation states, "[W]e commend your basic approach to a revision of law through the application of general contract principles of damages, as opposed to real property concepts . . . ." Ex. III, p.1. The Fireman's Fund, Real Estate Department, wrote, "I agree with and approve of the recommended legislation . . . ." Exh. VI. Albert J. Forn stated, "I was pleased to see that the recommendations resolve a number of problems that I have encountered in my practice." Exh. VII.

The Northern Section of the State Bar Committee generally approves the statute ("this statute as far as it goes is a good start but requires further drafting"), but expressed some reservations ("Will there not be a tendency to breach leases, in some instances, gambling on expert testimony to avoid damages."). Exh. I, Nor. Sec. Min. 11/8/65, p. 1, Nor. Sec. Min. 11/22/65, p. 5. George Herrington's letter to Senator Cobey is very critical in a general way, but the only letter he addressed to us raises a problem we think we can solve. Exh. VIII. He raises no other specific objections, and it is possible that his broadside attack is merely to enhance the possibility that his specific problem will be taken care of.

Professor Verrall's letter (Exh. II) is critical of both the basic policy and the means we have chosen to implement it. Some of his disagreement

flows from a different opinion of the existing law than we have. Our differences on the law and the basic policy involved will be discussed here, for it is necessary to decide the underlying policy first so that the statute can be prepared to reflect that policy.

Professor Verrall's position is that a wholesale abandonment of the common law concept that a lease is a conveyance of an estate in land and that the lessee's rental obligation is an incident of that estate is unwarranted. See Exh. II, p.5, ¶.9.

On page 4 of Exhibit II, Professor Verrall questions requiring application of the contractual doctrine of mitigation of damages to leases. "There is no proof that lessors have used this course abusively." he asserts that requiring mitigation (or, rather, limiting damages to those that are not avoidable) may give rise to new hardships and abuses. Somewhat inconsistently, however, he suggests at the top of page 8 (Exh. II) that a lessor be limited to (1) rescission, (2) reletting the property and periodically recovering deficiencies resulting from required reletting or (3) damages measured by the loss of the bargain (which denies avoidable damages). And at the bottom of page 8 (Exh. II), he suggests that lessors will abusively refuse to mitigate damages under the new statute.

Professor Verrall also questions the wisdom of granting a defaulting lessee the right to recover prepayments. On page 7 (Exh. II), he asserts that this will undermine the protective devices that are now available to a lessor. On page 6, ¶ 11, and on page 10, ¶ 7, he asserts that the statutes providing for relief from forfeitures are now applicable to lessees. We know of no case that sustains this assertion, however.

Our view that a lease should be viewed more as a contract is not unique. In The California Lease--Contract or Conveyance?, 4 Stan. L. Rev. 244 (1952), it states:

> The modern lease more closely resembles a contract for the purchase of space and services than it does the purchase of an interest in land.

In 31 Cal. L. Rev. at 338-339 (1943), there appears:

> With regard to the legal obligations of lessor and lessee it has been stated that the task of modern courts is "to divorce the law of leases from its medieval setting of real property law and adapt it to present day conditions and necessities by means of contract principles. . ." The California Supreme Court in Medico-Dental Etc. Co. v. Horton & Converse did just that when it joined the small minority of jurisdictions which frankly treat a lease like an ordinary bilateral contract . . . . [But it later retreated, see the Stanford Law Review article cited immediately above.]
>
> The presence of special rules which are applied to determine the effect of breaches of covenant by one party to a lease on the duties of the other is explained by the Restatement of Contracts as existing "partly for historical reasons and partly because the grantor of a lease . . . has performed the major part of his side of the transaction." In the light of changing conditions surrounding the uses to which land is put, the former reason is not very persuasive; the latter no longer based upon fact. It is true that a lease is regarded primarily as a conveyance of an interest in land and that the law of real property grew up before the doctrine of mutually dependent promises had developed. However the historical approach seems unsound, particularly since the feudal tenancy, with its emphasis on farm land from which the rent was said to "issue" has given way to a large extent to the "business lease" containing covenants of both parties relating to the use of the buildings on the land, which frequently is the chief consideration. This economic change which has led to the modern lease-contract not only invalidates the argument against interdependency of covenants based upon traditional notions, but also explains why execution of the lease cannot properly be held to constitute substantial performance on the part of the lessor.

In Professor Corbin's treatise on contracts, the problem is discussed in a variety of contexts. In discussing "constructive eviction," Professor Corbin states:

> The word "constructive" shows that it is not the law of property that the court is applying, but the law of mutual dependency in contracts; it is believed that the time has come to recognize this fact openly and to apply the flexible rules of contract law in determining whether a breach by either party is so material as to discharge the other from further duty. [3A Corbin, Contracts § 686, p. 243 (1960).]

Although legitimate criticism can be made concerning some of our specific proposals, we believe that the overall recommendation that a lease should be regarded as a bilateral contract to the extent that it can be so regarded is amply justified by hardships and forfeitures reflected in the appellate cases.

Kulawitz v. Pacific Woodenware & Paper Co., 25 Cal.2d 664 (1944), is a good example. The lessee auctioned off the goods in his store, retired from business, and stopped paying rent. After the lessor was unable to relet the premises, he let adjoining premises for a business that would have competed with the lessee had the lessee still been in business. For this breach of his covenant, the lessor was held to forfeit all right to rent from the lessee for the remainder of the lease term.

In Warming v. Shapiro, 118 Cal. App.2d 72 (1953), the lessee lost $12,000 because the lessor had surficient foresight to label the prepayment of that sum as both a bonus and a prepayment of rent, while in Boral v. Caldwell, 223 Cal. App.2d 157 (1963), the defaulting lessee was able to recover the advance payment of $2,000 (which was also to be credited to the last two months' rent) because the lessor once referred to the payment as a "security deposit."

In A-1 Garage v. Lange Investment Co., 6 Cal. App.2d 593 (1935), the lessee not only lost the $10,000 that was paid to the lessor upon the execution of the lease, he had to pay a judgment of $2,975.02 in addition to

compensate the lessor for accrued rentals at the time of the termination of the lease. The case is older now, and perhaps it shouldn't cause much concern because of its age. But its statement of the applicable law is still being cited and relied on in such cases as Warming v. Shapiro.

The other cases mentioned in the tentative recommendation, in the staff study, and in the law review articles cited are further illustrations of the assertion here made. But those detailed immediately above are sufficient to make the point.

We still recommend that the general thrust of the recommendation should be to make contractual principles applicable to leases. We see no reason to continue the fiction that a lessee has an interest in the leased property after he has abandoned it or after he has been evicted from it. We should recognize that the contract is at an end for purposes of performance even though it continues for purposes of determining damages.

Actually, the idea that a lessor may evict a lessee yet preserve the lessor-lessee relationship was unknown to the common law. At common law, exercise of the landlord's right of reentry terminated the lesser estate and all rights and duties incident thereto. The idea that a right of reentry can be exercised without terminating the servient estate has evolved from attempts to harmonize common law and contractual concepts. The idea is unrealistic, and the hardships it has created are recognized by all of the writers who have published in this field.

The revised tentative recommendation reflects our adherence to this view. It merely spells out this view in considerably more detail than appeared in the original tentative recommendation.

COMMENTS ON PRELIMINARY DISCUSSION

Professor Verrall (Exhibit II) criticized the preliminary discussion

appearing in the tentative recommendation. The other writers did not. We will mention Professor Verrall's specific criticisms below and point out how we attempt to meet them. The numbers on the points discussed are Professor Verrall's.

1. Professor Verrall criticizes our characterization of the Supreme Court's decisions as "vacillating" between property and contract theories. In the revised recommendation, we have deleted this language.

2. Professor Verrall questions our assertion that the doctrine of anticipatory breach has not been applied in lease cases. We think that the cases cited in the tentative recommendation so hold. We do not see how one can escape from this conclusion when the Supreme Court states unequivocally that the lessor has but three remedies, none of which is an immediate suit for the prospective losses that have been caused by the lessee's default. See the discussion of the damages remedy in lease cases in the staff study on pages 18-32.

Professor Corbin concludes that the California cases reject the notion that the lessee's repudiation of his lease and his refusal to pay further rent is an anticipatory breach for which damages for the loss of the future rentals can be recovered. Corbin, Contracts § 986 note 54 (1951). The Court of Appeals for the Eighth Circuit reached the same conclusion in Hawkinson v. Johnston, 122 F.2d 724, 137 A.L.R. 420 note 3 (1941).

We could amplify the discussion in the tentative recommendation, but we think that the proposition that the doctrine of anticipatory breach is not applied in lease cases (except where a mining lease is involved) is both correct and sustained by the cases cited.

Professor Verrall also objects to the form of our statement concerning the lessor's right to retake possession, relet after notification to the lessee, and recover damages from the lessee in the amount of any deficiency

at the end of the term. § B. 2, I First, p.3; § B. 6, p.5. The tentative recommendation states that the third course available to the lessor is, after notifying the lessee, to "relet the property for the benefit of the lessee and recover damages in the amount of the excess of the rentals called for in the original lease over the rentals obtained by reletting." Professor Verrall asserts that this form of statement must assume that Welcome v. Hess is overruled, that language of the Supreme Court stressing that this course of action is for damages must be disregarded, and that chance language in some DCA opinions alone should be recognized.

The statement on page 3 to which Professor Verrall objects was not taken from a DCA opinion, it is based on the Supreme Court's language in Kulawitz v. Pacific etc. Paper Co., 26 Cal.2d 664, 671 (1944), which has become the definitive statement of the lessor's rights upon abandonment. The Supreme Court there defined the third course open to the lessor as follows: "or (3) to retake possession for the lessee's account and relet the premises, holding the lessee for the difference between the lease rentals and what it was able in good faith to procure by reletting." (Emphasis added.) The statement in the tentative recommendation is no different in substance. See the discussion on pages 26-30 of the staff study. We believe that Professor Verrall's position must assume that Treff v. Gulko and Phillips-Hollman, Inc. v. Peerless Stages (discussed in the study) are the whole law on the subject despite the inconsistent later pronouncements by the Supreme Court. See page 30 of the staff study. In view of the uncertainty concerning the correct theory, all one can do is parrot the language of the Supreme Court, and this is what the tentative recommendation does.

3. Professor Verrall criticizes the form of the statement defining anticipatory breach at the top of page 2. The form of statement follows

the discussion appearing in 4 CORBIN, CONTRACTS 831-832. We do not know wherein it is not careful or wherein it is inaccurate. In the revised version, we have remedied the implication that a lessor has but two remedies.

4. Professor Verrall asserts that the cases cited in the second paragraph on page 2 do not support the proposition stated that anticipatory breach has not been applied to leases. See the discussion above under # 2.

5. True. Acceptance of surrender is equivalent to rescission. The discussion in the tentative recommendation is accurate.

6. This point is discussed above under # 2.

7. We have modified the discussion in the revised recommendation to make clear that Costello's holding related to termination of a lease for breach and that the loss of the right to further rentals flows from the termination, not the eviction. As modified, the discussion seems to meet Professor Verrall's objection.

8. The Barker and Burke cases are accurately cited for the proposition stated. See the discussion in the staff study at pp. 45-47; see also pp. 33-37.

9. This is a policy objection discussed above. The common law theory of rent is based on the feudal system and the concept of tenure. We cannot see where it has any place in the modern world.

10. We have modified the discussion in the revised recommendation to indicate more clearly the relevance of our reference to liquidated damages.

11. We know of no case holding that "advanced rentals and bonus payments in lease cases where in fact forfeitures come within Section 3275." The cases cited in the preliminary discussion of the basic policy involved demonstrate that forfeitures are enforced. Other writers concur. See the discussion in the staff study at pp. 39-42.

12. Professor Verrall questions our statement that Civil Code Section 3308 does not relieve a lessee from forfeitures. That the enactment of Section 3308 in 1937 has not had any effect on the law applicable to advance payments by lessees is assumed in the recent case of Boral v. Caldwell, 223 Cal. App.2d 157 (1963). In Warming v. Shapiro, 118 Cal. App.2d 72 (1953), an advance payment of rental was held nonrecoverable regardless of the amount of damage suffered by the lessor, but the case does not indicate whether a 3308 clause was in the lease. It is obvious from the decision, however, that Section 3308 cannot relieve a lessee from such a forfeiture when the parties have not included a 3308 provision in the lease.

13 and 14 refer to specific statutory recommendations and will be discussed in connection therewith.

COMMENTS ON PROPOSALS IN TENTATIVE RECOMMENDATION

Some of the comments received are directed toward specific sections. Others suggest additional provisions which may be included. We will discuss the criticisms of the proposed sections under this heading, reserving suggested additions for later discussion. We will also indicate how we attempt to meet the criticisms raised in the revised recommendation.

Section 1936

The State Bar (No. Sec.), J. H. Petry, and the Fireman's Fund all suggest that "abandonment" should be defined. Mr. Petry's letter points out that a lessor sometimes had difficulty determining whether vacation of the premises plus nonpayment of rent amounts to an abandonment. He suggests that a two months' delinquency in rental payments plus vacation of the leased property should amount to an abandonment.

The need for definition stems from the fact that some lessees do not want the lessor to be able to terminate the lease merely because the

property is vacant, and the lessors want to know with certainty when the lessee's interest ends so that they do not risk forcible entry damages when they retake the property.

We recommend the definition of both "repudiation" and "abandonment" and we have defined both terms in the revised recommendation. See Sections 1951, 1951.5.

Professor Verrall objects to the statement in the comment that the courts have not considered abandonment to be a breach. The comment appears in revised form in the first paragraph of the comment to Section 1952.5.

Professor Verrall objects to the policy underlying this section. He suggests, as an alternative to Section 1936, a section permitting the lessor upon a total breach to (1) cancel the remainder of the lease contract, (2) continue the lessor-lessee relationship with an obligation to minimize the lessee's liabilities (and account to the lessee for profits?)

or (3) terminate the relationship and recover damages for the loss of the remainder of the lessee's contractual obligation.

In effect, this alternative proposal would be similar to the proposed legislation. It would have the advantage of spelling out the lessor's remedies at a little greater length and thus making them more definite. Under our proposed legislation, we have always assumed that the lessor has the right to rescind for substantial breach. We did not think that anything we proposed inhibited that right. Rescission, of course, involves restoration of values received under the contract. See CIVIL CODE § 1691. So far as continuance of the relationship is concerned, we have recognized that under some circumstances specific performance may be an available remedy (which, of course, involves continuance of the relationship). Termination of the relationship and damages is the basic remedy provided under our proposed statute.

The Commission should compare this proposed alternative with the remedies generally provided a party to an ordinary continuing contract upon an anticipatory breach by the other party.

First, the injured party may rescind. 5 WILLISTON, CONTRACTS (Rev. ed.) § 1337, p. 3753; 4 CORBIN, CONTRACTS (1951) § 979 (Corbin speaks here of restitutionary relief because he does not regard unilateral rescission as a true rescission, see § 982); Restatement, Contracts §§ 318, 326, 347-349 (the Restatement uses Corbin's nomenclature, see §§ 406-409).

Second, the injured party may treat the contract as terminated for purposes of performance and sue immediately for his present and future damages. But, he may not proceed with performance of the contract and expect to recover damages for such performance. "He will not be given damages for any part of

his loss that he could have avoided by refraining from continued performance or by making reasonable effort." 4 CORBIN, CONTRACTS (1951) §§ 954, 983.

Third, the injured party may sue for specific performance of the contract if the case is one that is suitable for the granting of such a remedy. 5A CORBIN, CONTRACTS (1964) § 1141.

The repudiating party has the right to withdraw his repudiation before the injured party has changed his position materially in reliance on the repudiation and before there has been an actual nonperformance of a duty created by the contract. 4 CORBIN, CONTRACTS (1951) § 980; CIVIL CODE § 1440. Corbin indicates that there is some uncertainty concerning the right of retraction when there has been an actual breach of a minor duty imposed by the contract as well as a repudiation; but he suggests that the rule should be that the repudiating party should have the right to retract the repudiation before the injured party has materially changed his position and to thus convert the total breach into a partial breach. 4 CORBIN, CONTRACTS (1951) § 980, p. 936.

Where an anticipatory breach of an installment contract occurs, there is some uncertainty as to when the statute of limitations begins. If the breach is wholly anticipatory--i.e., if there has been no failure to perform under the contract--there seems to be little question but that the statute of limitations begins to run at the time performance is called for, not at the time of the repudiation. 4 CORBIN, CONTRACTS (1951) § 989, p. 967; Restatement, Contracts § 322. But where there has actually been some failure of performance already due coupled with a repudiation of the obligation to perform the remainder, it is uncertain whether the statute of limitations runs on all of the past and future damages from the date of the first failure to perform or whether the statute merely runs on each installment as it falls

due under the contract. The partial breach (failure to pay the installment) plus the repudiation amounts to a total breach for which but one action may be maintained. If a lease is likened to an employment contract, there should be but one action for the wrongful repudiation (discharge) and the statute should run from the time of the failure to perform the obligations of the lease. See discussion in 4 CORBIN, CONTRACTS (1964 Supp.) § 987 note 62.

The other major consequence of an anticipatory breach is that it operates to excuse further performance by the injured party. 4 CORBIN, CONTRACTS (1951) § 977. Had this rule been applied in the Kulawitz case, the lessor's letting of adjacent premises for a business that would have competed with the lessee's (if the lessee were still in business) would not have discharged the lessor's claim for damages against the lessee for his abandonment of the lease.

We recommend that these rules be spelled out in the statute. The revised recommendation does so. Section 1952 provides that a lease is terminated by a lessor's exercise of the right of reentry. Section 1952.5 provides that a repudiation is a breach and excuses counter-performance. Section 1953 permits the retraction of a repudiation before the other party has changed position. Section 1953.5 provides the usual contractual remedies--rescission, termination and damages, and specific performance. Section 1954 specifies the time when the statute of limitations begins. (Section 1954 also meets a criticism of the Northern Section of the State Bar Committee. No. Sec. Min. 11/8/65, ¶ 8.)

The Northern Section of the State Bar Committee and Albert J. Forn both suggest that the statute should spell out the lessee's rights as well as the rights of the lessor. Accordingly, we have worded these sections in the revised recommendation so that they apply both ways. As indicated in the staff study, the revised sections probably state existing law insofar as a lessee's rights are concerned. See pp. 47-50.

Sections 3320 and 3322

Professor Verrall points out that there is a defect in the language of Sections 3320 and 3322 in that subdivisions (a) of these sections literally provide for a double recovery. The Northern Section of the State Bar Committee also objects to much of the drafting in Sections 3320 and 3322. Professor Verrall suggests that the details of subdivisions (a)-(d) of Section 3322 are actually included in subdivision (e).

We propose to meet these objections by deleting Section 3322 and revising Section 3320. See the notes on the revised recommendation at the back of this memorandum.

Section 3321

Professor Verrall suggests that this provision may be abused. A lessor may leave the property vacant deliberately or may relet it at a low rental. It seems to us unlikely that a lessor would deliberately take a lower rate of rent in order to preserve a defaulting lessee's liability instead of taking the "bird in the hand" of a reasonable rate of rent. And even if a lessor did so, the lessee would be better off than under existing law.

The Southern Section of the State Bar Committee approved the entire recommendation except the principle embodied in Section 3321. The objection was based on the varying conditions under which the property might be relet. Professor Verrall makes essentially the same point on page 10.

In the revised recommendation, the section is numbered 3323, and it has been revised to reflect the fact that it can be used under the revised statute when the lessee is suing for damages as well as when the lessor is suing for damages.

Section 3323

Professor Verrall suggests that the comment be revised to eliminate the implication that the section deals only with abandonment cases or that all liquidated damages provisions have been held void. The revised comment appears with Section 3324 in the revised recommendation.

Section 3324

Professor Verrall raises the question whether the section should cover leases where provision is made that the lessor shall recover attorney's fees if the lessee sues.

He suggests that rescission of a lease may end the right to attorney's fees. This would be true only if the rescission were effective. If the lessee sued for breach of the covenant of quiet enjoyment, he would still be entitled to attorney's fees under this section if the lessor's rescission were ineffective--and the lessee would be entitled to substantive relief only if the rescission were ineffective.

He also asks if Civil Code Section 794 is repealed by implication. Section 794 of the Civil Code provides that upon the termination or abandonment of an oil and gas lease, the lessee must, on demand, execute a quitclaim deed. Failure to do so makes the lessee liable to the lessor for any damages caused by such failure and, in addition, for reasonable attorney's fees. We see no inconsistency between that section and Section 3324, so we do not see how it could be repealed by implication.

The Northern Section suggests the amendment of (a)(2) to read:

> (2) If the lease provides that one party may recover fees then the other party to the lease may also recover attorney's fees incurred in obtaining relief for the breach of the lease should he prevail.

In the revised recommendation, this section appears as Section 3325.

Section 3325

Professor Verrall states that he assumes "Section 3325 would not deny the lessee the more extensive relief [from forfeiture] he now enjoys." As indicated in the discussion at the beginning of the memorandum, our views concerning the extent of the lessee's right to be relieved from forfeiture differ considerably from Professor Verrall's.

Nothing in Section 3325 appears to inhibit whatever rights a lessee may have under Code of Civil Procedure Section 1179. Section 1179 permits a court, in cases of hardship, to restore a tenant to his rights under a lease where such rights were ended by unlawful detainer judgment under Section 1174. Section 3328 (3327 in the revised version) provides specifically that rights under Section 1179 are unaffected.

Professor Verrall states that the comment's use of the Caplan and Freedman cases cannot be supported. All that we can say is that we disagree, for the comment merely states what those cases held.

Professor Verrall suggests that Section 3325 may be inconsistent with the section which recognizes liquidated damages provisions. In the revised version (Section 3326), we have attempted to clarify this by a cross-reference.

Section 3326

This section appears in the revised recommendation as subdivision (b) of Section 3322. Professor Verrall objects to the comment regarding reletting "for the account of the lessee." The revised version of the comment is more

precise; but we have a basic disagreement with Professor Verrall over the existing state of the law. See #2 of Comments on Preliminary Discussion, supra.

Section 3327

The State Bar objects to the reference to the damages "specified in this article." It asserts that this requires a greater showing than now is required in equity. Since this article provides the measure of the lessor's damages for breach of a lease, we cannot see how the section's reference can be improper. The Northern Section comments: "In effect this makes this act for all ostensible purposes automatic and exclusive in all cases." And this is true to the extent that this act prescribes the exclusive measure of the lessor's damages for total breach of a lease. We cannot conceive of a case where the lessor should be entitled to recover more than "all the detriment proximately caused by the lessee's breach . . . or which in the ordinary course of things would be likely to result therefrom."

The Northern Section suggests that res judicata problems should be explored. Nothing in Section 3327 authorizes more than one action for a particular breach.

The Northern Section also points out that incidental damages are allowed in specific performance actions. We do not believe that Section 3327 will have any effect on the power of an equity court in that regard.

The Northern Section suggests modification of the section to read:

> Nothing in this article affects the right to obtain specific or preventive relief if otherwise appropriate.

If the scheme of the revised recommendation is accepted, it is unnecessary to consider these criticisms. The right to seek specific relief is provided in Section 1953.5. This section is thus unnecessary, and we left it out of the revised recommendation.

Section 3328

In the revised recommendation, this section appears as 3327. The Northern Section of the State Bar Committee suggested a revision to prevent a lessor from seeking damages in a second action which were denied in the previous action. The revised section attempts to meet this criticism.

Code of Civil Procedure Section 1174

Professor Verrall's comment on this section again asserts his view that the lessee's covenant to pay rent should be regarded as independent of the lessor's obligation to let him use the property.

We still believe that this doctrine of the independence of the covenant to pay rent is at the root of most of the problems in this area of the law. The basic concept that a lessee should have to pay rent for a property he has been evicted from seems unjust. If the lessee has breached the lease so that eviction and termination of the lease is justified, then the lessee should be liable for the damages he has caused--but not for the rental of a property he can no longer use.

SUGGESTED ADDITIONAL PROVISIONS

Lease-purchase plans for public improvements

Mr. George Herrington's letter suggests that the Commission's proposal would interfere with the construction of public improvements under the lease-purchase plan of financing. Letters from Orange County and Los Angeles County are to the same effect.

The legal background of his letter should be understood. The principal case is Dean v. Kuchel, 35 Cal.2d 444 (1950). The Constitution of California, in Article XVI, Section 1, provides that the Legislature may not incur an indebtedness in excess of $300,000 except by an act that has been approved by the people in a general election. In 1949, the Legislature passed a statute authorizing the Director of Finance to lease state property for a term not exceeding 40 years on condition that the lessee construct a building thereon and lease the property back to the state, the state acquiring title to the building at the end of the term.

Pursuant to this statute, the State leased a tract of land to a contractor for a term of 35 years and for a rental of $1.00. The contractor agreed to construct a building in accordance with state plans and specifications on the property within 325 days. Upon completion of the building, the property was leased back to the state for $3,325 per month ($2500 for rental, $825 for taxes and insurance) for a term of 25 years. Upon termination of the 25-year building lease, the 35-year "ground lease" automatically terminated. In any event, regardless of performance by the state, title to the building vested in the state at the end of the 35-year ground lease.

This scheme was held valid despite the constitutional debt limitation.

Because of the nature of a lessee's rental obligation, this arrangement obviously created a binding obligation on the part of the state to pay $3325 per month for 25 years. The "lessor" had nothing to do for this money after completion of the building. The binding nature of the rental obligation could be used as collateral for construction loans by the contractor. Thus, a $500,000 building could be built without a state-wide election.

Mr. Herrington's letter expresses fear that our proposed statute will upset this arrangement by abolishing the concept that the lessor may decline to relet property upon a lessee's default and collect the full rental as it comes due. Without an enforceable installment obligation (called "rent"), lenders would not be as willing to advance money, interest rates would probably rise, and the financing of public improvements would be made more difficult.

There appear to us to be two ways to get at Mr. Herrington's problem. One is to add a provision making the statute inapplicable to lease-back arrangements. This, however, appears to us to be undesirable because it would leave the applicable law somewhat obscure. Another way to get at the problem is to provide specifically that leases providing for the construction of improvements and their transfer at the end of the term are specifically enforceable.

We recommend the addition of Section 3387.5, as contained in the revised recommendation, to meet Mr. Herrington's objection.

Personal property

J. H. Petry proposes the addition of a provision permitting a lessor to dispose of personal property left behind by abandoning tenants. See his letter, Exhibit V (white). We added Section 1954.5 to the revised recommendation in response to this proposal.

Small claims jurisdiction

Mr. J. H. Petry (Exhibit V) suggests that small claims court jurisdiction be broadened to include unlawful detainer actions. He argues that unlawful detainer proceedings are now too expensive in the small case.

This argument seems based on a false premise. Code of Civil Procedure Section 117 provides that a municipal court sitting as a small claims court

has jurisdiction in unlawful detainer proceedings. It is true that this provision was held unconstitutional in Mendoza v. Small Claims Court, 49 Cal.2d 668 (1958), but that decision was met by a 1959 amendment. Witkin gives the history of the section as follows:

> By amendments in 1955 and 1957 the Legislature attempted to give a municipal judge sitting as the small claims court jurisdiction over "proceedings in unlawful detainer after default in rent for residential property where the term of the tenancy is not greater than month to month, and where the whole amount claimed is one hundred fifty dollars ($150) or less." . . . This provision was held unconstitutional in Mendoza v. Small Claims Court (1958) 49 C.2d 668, 321 P.2d 9, on the following analysis: (1) Due process requires a hearing with the right to counsel, which is not allowed in the small claims court. (2) Ordinarily the plaintiff by electing to sue there waives the right, and the defendant may appeal to the superior court, with an automatic stay, and have a trial de novo with representation by counsel . . . . (3) But in unlawful detainer proceedings stay pending appeal is discretionary with the trial judge . . . , and the result under the amendment would be that the tenant's right of possession could be taken from him initially without the kind of hearing required by the due process clause.
>
> Responding to the implied suggestion in the Mendoza case the Legislature in 1959 adopted the following addition to C.C.P. 117j . . . : "If, in an unlawful detainer proceeding . . . judgment is for plaintiff, proceedings on the judgment are automatically stayed, without the filing of a bond by defendant, until the expiration of the time for appeal, and, if an appeal is perfected, until the appeal is decided." [Witkin, California Procedure 1965 Supplement 104. Emphasis is Witkin's.]

In effect, then, the proposal is to give justice court judges unlawful detainer jurisdiction in small claims, for municipal judges sitting in small claims now have unlawful detainer jurisdiction. A sizeable percentage of justice court judges are nonlawyers. Justice courts have jurisdiction in unlawful detainer when not sitting in small claims. C.C.P. § 112. Should we propose to extend the jurisdiction of the small claims court?

Retroactivity

The Northern Section of the State Bar Committee strongly urges that a section be added limiting the effect of the legislation to leases executed

after its effective date. Exh. I, Nor. Sec. Min. 11/22/65, ¶ 2. The Southern Section, however, comments:

> . . . the advisability of having two sets of laws covering this field over an indefinite period of years should be given serious consideration.

We added Section 13 to the revised recommendation to carry out the Northern Section's suggestion. This avoids any constitutional question involving impairment of the obligation of contracts.

ADDITIONAL NOTES ON REVISED RECOMMENDATION (YELLOW)

For those of you who read the revised recommendation (green) that was sent out with Memorandum 66-15 and do not wish to proof read the revised recommendation (yellow) to discover what additional revisions have been made, we are providing the following table to indicate precisely where the additional revisions are (changes in section numbers are not indicated):

Location in Revised Recommendation (green) distributed with Memorandum 66-15	Location in Revised Recommendation (yellow) distributed with this memorandum
Page 9, ¶ 7, line 3	Same
Page 12, § 1951	Same page, subdivision (d) added
Page 13	Page 13, last ¶ added
---------	New page 14 added (see notes following table)
Page 14, subdivision (a)	Page 15, subdivision (a) revised
Page 14, subdivision (d)	Page 15, subdivision (d) revised
Page 14, last line	Page 15, "the possession of" added in last line
---------	Page 16 added
Page 15, Comment, third and fourth lines	Page 17, Comment, third and fourth lines

Page 16, § 1952, third line	Page 18, § 1953, third line
Page 18, fourth line from bottom	Page 20, fourth line from bottom
Page 21, subdivision (a), third line	Page 22, subdivision (a) third and fourth lines
Page 28, following "Rest., Cont. § 336"	Page 30, same location, paragraphing added
Page 29, lines 1 and 2	Page 31, lines 1 and 2
Page 33, § 3326, lines 1, 3, 9, and 11	Page 35, § 3326, passim
Page 35, § 3327, last line	Page 37, last line
Page 35, last two lines	Page 37, last two lines

Some of the revised recommendation has been discussed in the previous portions of this memorandum. The following material points out certain matters to be noted in regard to the drafting and identifies some remaining policy problems.

Section 1951

Subdivisions (a) and (b) are based on the Restatement of Contracts, Section 318. For comparison, it provides:

> 318. In the case (1) of a bilateral contract that has not become unilateral by full performance on one side, and (2) of a unilateral contract where the agreed exchange for the promise or for its performance has not been given, any of the following acts, done without justification by a promisor in a contract before he has committed a breach under the rules stated in §§ 314-315, constitutes an anticipatory repudiation which is a total breach of contract:
>
> (a) a positive statement to the promisee or other person having a right under the contract, indicating that the promisor will not or cannot substantially perform his contractual duties;
>
> (b) transferring or contracting to transfer to a third person an interest in specific land, goods, or in any other thing essential for the substantial performance of his contractual duties;
>
> (c) any voluntary affirmative act which renders substantial performance of his contractual duties impossible, or apparently impossible.

Section 1951.5

We have defined abandonment as repudiation plus vacating the property because this is the concept that is needed in Sections 1952(c) and 3326. Subdivision (b) appeared in the revised recommendation (green) distributed previously as Section 1953.5 as a device to help Mr. Petry's lessor.

Section 1952

Stating the manner in which a lease is terminated is needed to give real meaning to Section 1953.5 and to put down the idea that the lessee may be evicted while the lease continues.

Section 1952.5

This section is designed to overcome Oliver v. Loydon, which held that a repudiation unaccompanied by an abandonment or nonperformance was not a breach, and Kulawitz v. Pacific Woodenware & Paper Co., which held that a covenant not to rent to competing businesses was an independent covenant from the lessor's viewpoint but was a dependent covenant from the lessee's viewpoint--a result referred to in the Stanford Law Review as "one-way dependency" and as "Kulawitz' vacillating 'implied dependency' with its possible one-way results."

Section 1953

Section 1953 is based on the Restatement of Contracts, Section 319:

> 319. The effect of a repudiation is nullified
> (a) where statements constituting such a repudiation are withdrawn by information to that effect given by the repudiator to the injured party before he has brought an action on the breach or has otherwise materially changed his position in reliance on them; or

(b) where facts other than statements constitute such repudiation and these facts have, as the injured party knows, ceased to exist before action brought or such change of position as is stated in clause (a).

Section 280 of the Restatement is similar. In Subsection (1), Section 280 states that a repudiation excuses counterperformance of a dependent promise; and in Subsection (2), Section 280 states:

(2) The party making a statement within the rule stated in Subsection (1) has power to nullify the effect of the statement by a retraction, as long as the other party has not materially changed his position.

Section 1953.5

This section is discussed in connection with Section 1936 of the originally recommended statute, supra. The policy questions presented by Professor Verrall's suggestion (Exhibit II, page 8 at top) is whether a lessor should have an absolute right to specific performance in all cases (with or without an obligation to sublet) or whether he should have a qualified right as provided in this section.

Section 1954

This section is based on Section 322 of the Restatement of Contracts:

322. If no action on an anticipatory breach is brought before the time fixed by the contract for the beginning of performance by the party who has committed such a breach, the period of the Statute of Limitations begins to run only from the time so fixed by the contract.

Section 1954.5

In connection with Section 1954.5, you should compare Civil Code Sections 1862, 1864-1872, and 2080-2080.9.

Section 3320

Section 3320 is substantially the same as the version that appeared in the tentative recommendation. The following differences appear:

(1) The reference to abandonment or repudiation in the preliminary language has been deleted as unnecessary in light of the definition of "repudiation" in Section 1951 and the provision in Section 1952.5 that a repudiation is a breach.

(2) In subdivision (a), the words "The worth of the excess" have been taken from existing Section 3308 and substituted for "The excess" which appears in the tentative recommendation. The term, "the value of the rentals," has been deleted and "the rent and charges equivalent to rent"--also taken from Section 3308--has been substituted. These revisions were made in response to the State Bar's complaint that it could not understand the previous terminology (see Nor. Sec. Min. 11/8/65, ¶ 6, p. 4) and in response to Professor Verrall's suggestion that "rental" by itself is too narrow a term (see p. 9 of letter). The use of the term "the portion of the term following such termination" instead of "the remainder of the term" is also in response to the State Bar criticism.

(3) The language in the tentative recommendation as to the time of calculating the damages has been deleted in response to State Bar criticism. See Nor. Sec. Min. 11/22/65, ¶ 7, points Third and Fifth. A valid point is made in this criticism that, as a general rule, interest is not

allowed on unliquidated debts. Thus, although it might be proper to allow interest on overdue liquidated rental installments, it might be improper to allow interest on overdue unliquidated rental installments. We concluded that the problem is not peculiar to landlord-tenant law, and we should permit the courts to apply the generally applicable rules.

(4) Subdivision (b) has been substituted for a cross-reference to an incidental damages section. The incidental damages section has been deleted. This revision is in response to Professor Verrall's comment pointing out that there was a defect in wording which authorized double recovery and that, as a practical matter, all of the subdivisions of the incidental damages section were covered substantively by the final subdivision of that section. Subdivision (b) appeared in the tentative recommendation as the final subdivision of Section 3322, the incidental damages section. The State Bar (Nor. Sec.) also objected to the drafting of Section 3322 as it appeared in the tentative recommendation. This redraft avoids these objections. The substance of the comment to the incidental damages section has been placed in the comment to Section 3320.

Section 3321

We have added a new Section 3321. It is in response to the State Bar's suggestion that the statute deal with the lessee's rights upon wrongful termination by the lessor. Nor. Sec. Min. 11/22/65 ¶ 1.

Section 3322

Subdivision (b) was previously approved. It appeared in the tentative recommendation as Section 3326.

Subdivision (a) has been added because the form of the redraft makes it necessary to state specifically the lessor's duty to mitigate damages. The previous draft accomplished its purpose by limiting the damages the

lessor could recover upon an abandonment. The revision offers the lessor three alternative remedies upon an abandonment (see § 1953.5) but does not affirmatively prohibit him from resting on his lease and suing for all of the remaining rentals. Hence, we found it necessary to state specifically that a party may not recover for any detriment caused by a breach (which includes an abandonment) that could be avoided through the exercise of reasonable diligence. The rule stated in subdivision (a) has a counterpart in Section 3326, which permits an abandoning lessee to recover from the lessor everything paid to the lessor in excess of the actual damages occasioned by the abandonment.

Subdivision (a) is based on the Restatement of Contracts, Section 336, subdivision (1):

> 336. (1) Damages are not recoverable for harm that the plaintiff should have foreseen and could have avoided by reasonable effort without undue risk, expense, or humiliation.

Section 3323

Section 3323 is based on Section 3321 as contained in the tentative recommendation. It has been revised, however, to reflect the fact that it can be used under this draft when the lessee is suing for damages as well as when the lessor is suing for damages.

Note that Professor Verrall suggested that this provision might be subject to abuse and that the State Bar, Southern Section, objected to the provision because of the varying terms and conditions under which the property might be relet.

Section 3324

This section was previously approved as part of the tentative recommendation (it was numbered 3323 in the tentative recommendation). The last paragraph has been added to the comment because the statute now deals with lessee's rights as well as lessor's.

Section 3325

Section 3325 was approved as Section 3324 of the tentative recommendation. Note the objections to the section discussed previously in this memorandum. The State Bar's (No. Sec.'s) redraft of subdivision (a)(2) will not fit unless it is made a separate subdivision (b).

Section 3326

Section 3326 was approved as Section 3325 of the tentative recommendation. A reference to Section 3324 was added to meet an objection of Professor Verrall. We think this change is nonsubstantive.

Section 3327

This section was approved as part of the tentative recommendation.

It has been revised to prevent recovery on a claim for damages where the claim was previously denied.

Section 3308

The repeal of Section 3308 was previously approved.

Section 3387.5

This section is new, and it is designed to meet the lease-purchase problem raised by George Herrington, Los Angeles County, and Orange County.

C.C.P. § 1174

The amendment of this section was previously approved. Note the objection of Professor Verrall. P. 11 of Exhibit II. The policy underlying the amendment is also supported by Section 1952 which provides that any form of eviction terminates the lease, not merely an eviction under Code of Civil Procedure Section 1174.

Commissioner Stanton has also raised a question concerning Code of Civil Procedure Section 1174 that should be decided by the Commission before a final recommendation on this subject is made.

Section 1174 provides (as the Commission proposes to amend it) that a judgment for unlawful detainer after default in the performance of the obliga-

tions of a lease must declare the forfeiture of the lease. But, if the three-day notice sent by the lessor (as a condition of bringing the action) did not state the election of the lessor to declare the forfeiture of the lease, the court is empowered to delay execution upon the judgment for five days during which time the lessee has the right to cure his default. And, if the lease is for a term of more than one year, it does not contain a provision forfeiting the lessee's interest upon default, and the three-day notice does not contain a declaration of forfeiture, the court is required to delay execution for five days during which time the lessee has the right to cure his default.

Thus, a lessor is entitled to immediate execution in any case where he declares a forfeiture of the lessee's interest in the three-day notice. Failure to so declare may result in a five-day delay in execution in any case, and in the case of certain long term leases that do not contain forfeiture clauses, such failure results in an automatic five-day delay in execution.

In any case, however, Section 1179 of the Code of Civil Procedure empowers the court to relieve a tenant "in case of hardship" from forfeiture of his interest if the tenant applies for such relief within 30 days after the forfeiture is declared and fully cures his default in performance under the lease.

Although the language is archaic--"termination" should be used instead of "forfeiture"--we made no change in the substantive parts of these sections other than to eliminate the portion that permits a lessee to be evicted without termination of his interest. But, inasmuch as it will make little difference substantively under Section 1952 whether the lessor declares a forfeiture or termination or whether he doesn't--in either event the lease must terminate if the lessee vacates pursuant to the notice or is evicted--should Section 1174 continue to distinguish between cases where the lessor declares a forfeiture and where he does not. The only substantive effect of the declaration will be that the lessee cannot obtain the five-day stay of execution.

If no substantive change is desired--that is, if the lessor should be entitled to get immediate execution of the unlawful detainer judgment when he wants it--should the relevant sections be revised to require a more meaningful declaration of the lessor's intent on the three-day notice? If this were done, the statutes would provide in substance that if the lessor declared that immediate surrender of the premises (at the end of the three-day period) is demanded, he could obtain immediate execution. But without such a declaration, the court could order a five-day delay.

Thus, the questions for the Commission to decide are:

Should a lessor have a right to immediate execution of an unlawful detainer judgment where he declares his intent to exercise such right?

If so, should the Code of Civil Procedure be revised to require the lessor to declare his election in more meaningful language?

Respectfully submitted,

Joseph B. Harvey
Assistant Executive Secretary

Memo 66-24 EXHIBIT I

THE STATE BAR OF CALIFORNIA
601 McAllister Street
San Francisco 94102

John H. DeMoully, Esq.
Law Revision Commission
Stanford University, California

December 9, 1965

Dear Mr. DeMoully:

At the request of Seth M. Hufstedler, Chairman, Committee on Administration of Justice of the State Bar, we are forwarding 15 copies of minutes to date of the two sections of the committee, on the Commission's Tentative Recommendation Relating to the Rights and Duties Attendant Upon Abandonment or Termination of a Lease (July 23, 1965).

President Sutro has approved the direct transmission of the Committee's minutes to the Commission, but upon the understanding that the views expressed are those of the Sections of the Committee, and are not necessarily those of the Board of Governors.

Mr. Hufstedler also wishes the reservation made that no General Meeting of the Committee of Administration of Justice has taken place during the study; hence, the Committee as such has not had an opportunity to express final views.

Your request to Mr. Hayes was for a report, if possible, by December, 1965.

As you have indicated changes may be made in the Tentative Recommendation, the Committee would appreciate being supplied with your revised text.

Yours very truly,

G. H. Elmore

G. H. Elmore

GHE:ew

cc: Board Liaison, Mr. Sutro, Mr. Hayes
Mr. Hufstedler, Mr. Gray and Committee Members

(So. Sec. 10/11/65)

AGENDA No. 11 - Lessor's Damages and Rights Upon Abandonment or Breach of Lease (New CC 320 et seq.) - Law Revision Commission.

ACTION TAKEN:

1. Upon consideration of the principles set forth at pages 8 and 9 of the California Law Revision Commission's tentative recommendation relating to the rights and duties attendant upon abandonment and termination of a lease, dated July 23, 1965, a motion was passed unanimously:

(a) approving the first principle enunciated;
(b) approving the second principle, but noting that it would be better stated if the wording "such as expenses necessarily incurred" were deleted;
(c) approving the third principle, such approval limited to the first sentence thereof;
(d) approving the fourth through seventh principles, and noting that no comment appeared to be necessary on principles 8 and 9 (matters of mechanics only).

2. A motion was passed unanimously recommending:

(a) that any proposed legislation in this field state expressly whether it is applicable to leases executed prior to its effective date;
(b) that if retroactive application of such legislation is contemplated, a thorough analysis of the constitutionality of such a provision be undertaken;
(c) that if retroactive application of such legislation is not contemplated, the advisability of having two sets of laws covering this field over an indefinite period of years should be given serious consideration.

Mr. Wall reported orally.

DISCUSSION:

In the course of discussing the third principle, the Section was opposed because of the varied circumstances that might arise, to the recommendation that the rental provided in a new lease (a re-letting after termination by reason of the lessee's abandonment or other breach) should be presumed to be the fair rental value of the property, as well as to the stated conclusion arising from such a presumption.

The Section in its consideration of this agenda item made no attempt to review how accurately the stated principles of the recommendation have been carried out by the proposed code sections, but limited its consideration to the principles themselves in view of the fact that this is a tentative recommendation only.

(Nor Sec. Min. 11/8/65)

AGENDA NO. 11. Lessor's Damages and Rights Upon Abandonment or Breach of Lease (New C.C. 3320 et seq.).

Mr. Kallgren reported orally after distributing copies of his written report to the members present.

After discussion, it was the sense of the Section (no formal vote was taken) that some statute is in order to better clarify the rights of both the lessor and lessee on breach by the other, and that this statute as far as it goes is a good start but requires further drafting.

During discussion, certain questions were raised, as follows:

1. Does this proposal apply to leases executed prior to its effective date?

Serious doubts were expressed by members as to the constitutionality of retroactive application. This may involve a deprivation of vested property rights. By way of an example, certain things may not be waived by the parties under the proposal. An existing lease may be abrogated or rendered ineffective because its key provisions constitute waivers prohibited under the new law.

(Agenda No. 11 continued

Aside from constitutional considerations, the majority of the Section believe the parties should be governed by the law existing at the time of their agreement. Leases are negotiated in the light of and special provisions are adopted because of the then existing law. This proposal would subject existing contracts to an entirely different law contrary to the intent of the parties.

2. In Sec. 1936 do "abandonment" or "repudiation" require further definition?

"Abandonment" of the lease itself may be distinguished from abandonment of the "leased property". In present form it may refer to a vacation of the premises regardless of whether the lessee continues to pay rent. For a definition of "abandonment" used in easement cases, see City of Los Angeles v. Abbot, 129 Cal. App.144,148.

3. This proposal in present form is concerned only with the landlord's remedies on the tenant's wrongful breach of the lease. Sec. 1936 states that "repudiation" by the lessor as well as the lessee of obligations of the lease is "a breach of the lease". So what are the remedies of the lessee?

The distinction between "contract" and "real property" approaches is not spelled out. The remedies here are statutory. This gives no help to the injured lessee. The proposal in present form leaves the entire law too one-sided in favor of the lessor. (Note: Time did not permit discussion concerning what recourse the tenant should have on wrongful breach by the landlord but it was noted that the present statutory scheme is inadequate [see for example CC 1942 which is silent as to damages if tenant is forced to vacate the premises because of the landlord's failure to keep the premises fit for occupancy].)

4. In Sec. 1936 does the phrase "at or before the time for performance" include a repudiation during or after time for performance?

5. It should be noted that under Sec. 3320 this proposed act will apply to any rental whether of real or "personal" property. From its face this could apply to the rental of a car or other chattels. The policy of extending this proposal beyond the landlord-tenant situation should have further review. The "comments" do not cover this. Perhaps "lease" for purposes of this act should be defined.

6. Sec. 3320 is uncertain and vague. Some examples are:

What is meant by "value of the rentals"? Isn't the measure of damages based upon the unpaid rents or charges due under the lease? C.C. 3308 talks about "rent and charges equivalent to rent". What more does "value" involve? The term "value" unless further defined raises speculative considerations.

The first and last sentences in sub-paragraph (a) conflict. The first sentence refers to damages as an "excess" of rentals due or to become due under the lease and "reasonable rental value". In the last sentence the landlord is allowed the "full" rental installments "then due". What is meant by "discounting rental installments not then due"? Is this where the "excess" formula of damages applies?

It is not clear what interest the lessor is entitled to as to rents coming due after the breach. Is he limited to interest on the judgment in such cases?

7. The implication of Sections 3320 and 3322 is that the landlord has an absolute duty to re-let or to try to re-let the premises. This gives rise to certain problems which apparently the proposal would leave to litigation. Situations involving changing neighborhoods, urban renewal or re-development, and condemnation are commonplace. It may cost more to re-let than would be realized on having the place occupied for the remaining period under the lease. Or say it would be an almost futile gesture on the part of the lessor to try to re-let. In such instances it would be unfair to the lessee to charge him with the costs and expenses incurred by the lessor in attempting to lease or in leasing the premises. Such "incidentals" can be far in excess of the remaining rental installments due under the lease.

Does "reasonable time" in Sec. 3322 (a) include the lessor's inability to re-let the premises over the remainder of the rental period? What about the absentee lessor who doesn't learn of "abandonment" until too late to re-let? If not, what is the "fair rental value" in such cases? This becomes very speculative in cases where a new rental for the same purposes (say a business) has become improbable because of a threatened freeway or re-development.

The foregoing point up that it is fairer to both parties in many situations to hold the lessee to his "bargain", i.e. permit the lessor to leave the premises vacant and hold the lessee for the full rents and charges due or to become due under the lease.

8. It is not clear under the proposal when the statute of limitations begins to run against the landlord or when suit may be commenced. The proposal apparently assumes the court will apply reasoning of anticipatory breach but problems can be visualized, i.e. remedies provided here are statutory and do not necessarily evolve from the law of contracts. If limitations run from time of breach will there be a tolling until an absentee landlord gets notice of his tenant's quitting the lease? Can the landlord sit back and wait for the rent to accrue, suing for the rentals on each due date? This act appears exclusive. See No. 12 below.

9. How does this affect the periodic tenancy? May the month to month tenant avoid the 30 days written notice? Should "incidental damages" incurred in re-letting apply here or in other short term leases (under 6 months)? Is the "excess" formula appropriate in such cases?

10. As to Sec. 3321 this should be checked to see that there is no conflict with or conforming amendment required in the New Evidence Code.

11. In Sec. 3322 (a) what constitutes a "retraction"? Does the lessee have a reasonable time to "retract"? Again this proposal permits increased litigation over its terms. In this sense, the present law has a certain degree of certainty which when dealing with property is more desirable than attempting to arrive at so-called equitable results. For example, the property can be tied up indefinitely in a lawsuit to no-one's advantage.

What will be the effect of this proposal on the administration of estates where there is a contest? Distribution can be held up indefinitely.

12. In Sec. 3327 how do you prove that "damages" under this act would be inadequate? This requires a greater showing of "inadequacy of damages" than now required in equity. In effect this makes this act for all ostensible purposes automatic and exclusive in all cases.

13. While Sec. 3328 provides that a lessor cannot recover twice for the same items where he first brings an "unlawful detainer" action, it is not clear that he may not seek damages in his unlawful detainer action and, having been denied them, relitigate the same items in an action under this new title. A member suggested that this possibility could be precluded by amending the last line of 3328 to add the words "prayed for or" before the word "awarded".

Res judicata problems should also be explored under Sec. 3327. Incidental damages are allowed in specific performance suits.

14. A severability clause should be included.

Note: This matter will be continued for further comments, if any, by Messrs. Myers, Benas, Bonapart, Zinke and Elmore.

(Nor. Sec. Min. 11/22/65)

AGENDA NO. 11. Lessor's Damages and Rights Upon Abandonment or Breach of Lease (New C.C. 3320 et seq.).

Continued from the meeting of 11/8/65.

Further comments are as follows:

1. The Section strongly urges that any proposal include provisions on the tenant's rights in the event of a wrongful termination by the lessor. If the present proposal purports to be comprehensive, it is incomplete until there is a mutuality of remedies for the lessee and lessor alike.

2. The effective date should be spelled out and the Section recommends that it only apply to leases executed on or after the effective date of the act. This recommendation is made as a matter of legislative policy as well as because of constitutional doubts.

3. In Sec. 3322(a) the phrase, "allowed by the lessor to the lessee to retract the repudiation or cure the breach or" should be deleted. Implicit is a duty on the lessor to give the lessee reasonable time to cure his breach.

4. Sec. 3324(a)(2) appears ambiguous. It is believed it should be more definitely stated, such as:

> "; or if the lease provides that one party may recover fees then the other party to the lease may also recover attorney's fees incurred in obtaining relief for the breach of the lease should he prevail." (Note: Such amendment would require a conforming change in the opening sentence of paragraph (a).)

5. The phrase, "the damages specified in this article are inadequate and specific or preventive relief is" should be deleted from Sec. 3327. The omitted words could be confusing and are unnecessary.

6. It is suggested that the words "sought or" be inserted, instead of "prayed for or", before "awarded" in the last line of Sec. 3328(b). See comment 13. in Northern Section Minutes of 11/8/65.

7. The Northern Section does not believe that Sec. 3320 (a "key" section) is satisfactorily worded at present and suggests it be re-worked. New concepts in landlord-tenant relations are being attempted. It seems important that members of the Bar, as well as members of the public participating in lease transactions have a specific knowledge of remedies and liabilities, and in more than general terms.

It is noted that unpaid rent to the time of judgment is a traditional concept; likewise, the right of the landlord to sue for rent as it becomes due, in several actions.

With this background, Sec. 3320 seems extremely fragmentary in stating the "damage" rule.

These points were discussed:

First, what is meant by "remainder of term." Is it from time of breach? From time of judgment? The last sentence appears to imply that the "remainder" is computed from the date of judgment- an impossible date. Or is it the date of testimony? If so, a period may elapse between such date and the date of "decision" such as jury verdict or filing of findings and conclusions in a non-jury case. The words "as of the time when the lessor's damages are determined" create difficulty in the above connection.

Second, "Value of rentals" due or to become due as the beginning figure in the computation appears uncertain. The Section suggests that "amount" should be substituted for "value". However, after discussion, it was not certain whether this was the Commission's intent. If "amount" is not apt, how is "value" to be determined. Is it contemplated that "expert" testimony will be required, with increased cost to both parties?

Third, what rental installments are to be "discounted" in point of time, i. e., unpaid as of commencement of suit or as of time of

trial or as of time of decision or judgment or as of time of "breach"? Again, the question is raised as to what is meant by "discounted". Is it intended a rate of return shall be allowed or is it a general direction that an "expert" is to make some undefined form of "discount" in arriving at a figure.

Fourth, what is the result of delay in bringing a claim to suit and trial on the part of the landlord?

If the "remainder of the term" commences as of time of trial, decision or judgment, could not the lessor leave the premises vacant after the breach, and then get full rent and interest (without offset for mitigation) for as long as 4 years? How will this operate in a short term lease, when the trial may be after the lease term has run.

Fifth, when does interest past due on "rental installments" commence torun? From the date when due under the lease terms? If this is an unliquidated amount such as "value" how is interest to be computed? Compare above comments as to amount. Or, are "rental installments" different from "rentals" so that interest is only intended on the dollar amount stipulated rental in the lease? The Section also notes that often a lease is a percentage rental lease. How is interest to be allowed?

Sixth. Particularly in a long term lease, how is the "reasonable rental value" to be calculated, except in the limited case provided for by Sec. 3321 (premises actually leased).

Seventh. The duty to relet appears only inferentially, i. e., that the reasonable rental value is to be deducted. However, this may be a matter of Bar education, rather than a defect in wording.

Eighth. The "key" wording of deducting reasonable rental value appears to raise policy problems. Presumably, the value can be determined by expert testimony. But there are many variables, particularly in long-term leases, such as change in neighborhood, redevelopment projects, condemnation of the same or nearby property. Will there not be a tendence to breach leases, in some instances, gambling on expert testimony to avoid damages. It is recognized, however, that these questions are inherent in the underlying concept of the Act.

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UNIVERSITY OF CALIFORNIA, LOS ANGELES

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SCHOOL OF LAW
LOS ANGELES, CALIFORNIA 90024

January 27, 1966

California Law Revision Commission
Crothers Hall, Stanford University
Stanford, California, 94305

Re: Proposed Legislation
on Landlord-Tenant

Dear Sirs:

My answer to your letter of January 5 is rather extensive. The late receipt of the Tentative Recommendation of July 23, 1965, has not allowed time to reduce the answer to a more manageable size.

My answer follows in three parts: A. Conclusions. B. Comments on Background Statement. C. Comments on Proposed Legislation Section by Section.

Sincerely yours,

H.E. Verrall

Harold E. Verrall

HEV:mmj

A. Conclusions

You ask for my assessment of the merits of the tentative recommendations concerning the problems presented when a lessee abandons and repudiates a lease transaction. My conclusions are the comments should be withdrawn and the legislation reconsidered. The comments if submitted would treat the Legislature like a busy lawyer would treat an adversary in preliminary proceedings. The treatment seems a blunderbus treatment. The comments do not accurately state California law so as to show the character and extent of existing evils. They are replete with emotion-charged words and ideas and seem more like statements by a lobbyist with an axe to grind than by a disinterested commission enlightening the Legislature. And I am not yet convinced that the proposed legislation would cure existing evils without creating equally serious hardships to those resulting from current California law. Also I am of the opinion that some mistakes occur in the language of the proposed legislation, perhaps an inconsistency between Sections 3320 and 3322. Mistakes often occur. They are to be expected. Reference might be made to Civil Code Section 140.5 and Probate Code Section 201.5. The Commissions effort to avoid stating a classification test twice in identical words, lead to a statement of two tests resulting in one classification, in some situations, when the wealth was in its original form and a different classification when in a transmuted form.

The Commission started with the problem of lessor protection when the lessee abandoned and repudiated the lease. That problem necessarily included protection of the lessee in such situation from abusive action by the lessor. The proposed legislation goes far beyond the original problem and raises many problems which should not be lightly treated. Certainly proposed section 1936 relates to abandonment but section 3320 relates to damages upon termination for all types of substantial breach as well as termination by abandonment or other repudiation. Any case of a breach by a lessee of sufficient materiality to permit a termination of the lease, is covered. As the types of property and types of situation involved in lease transactions (real, personal, business, residential single-units, multiple-units, luxury, etc.) are multiple one would almost have to be a God to determine the effect of the legislation on lease practices.

And even in the area of the problem and the operation of proposed Section 1936, there are numerous questions to be answered. For instance: What effect will the legislation have on tort liability? A general starting point is that responsibility for maintenance of property in safe condition rests on the possessor. Thus now it rests on the lessee even if he abandons until the lessor again is in possession.

B. Comments on Background Statements in order of appearance:

1. Section 1925 was not a legislative directive to treat leases as contracts and to forget that they were also conveyances. Property as well as contract relationships are involved. The great popularity of stressing the contractual aspects of the lessor-lessee relationship common twenty-five years ago, is no longer evident in cases and writings. There is still recognition that the great and growing change in the lessor-lessee relationships, makes mechanical application of the doctrines developed prior to this century harsh and impossible, makes changes in the doctrine necessary, and requires increased recognition that the contractual acts of the parties must be separate from property interests in some areas, such as breach. Section 1925 came from the Field Code of 100 years ago when bailment and lease were beginning to be subjected to contractual modification. Foreseen was the need to change doctrines of the past. The courts had much to consider beyond the recognition of the contractual aspects of modern bailments and leases. The contracts tied in with property interests may affect tort liability, may affect rights and obligations of sublessees or assignees, or may affect the rights of transferees of the owner, etc., as well as rights on frustration and on breach, etc. The fact that they do not apply a so-called contract principle in one case and do apply one in another case, does not mean the courts should be charged with vacillation.

2. Starting on page 1 and continuing on the next few pages two ideas are interwoven. It is stated that in lease law the doctrine of anticipatory repudiation is not recognized and that the doctrine of no recovery of avoidable damages is not recognized. As the basic proposed legislation relates to real and to personal property leases the validity of the ideas must be supported by bailment as well as land lease cases.

First; Is the doctrine of Anticipatory Repudiation recognized in lease cases?

This problem was raised in Gold Min. & Water Co. v. Swinerton, 23 P.2d 19, 121 P.2d 840 (1943) and notices that there is some doubt about it in real property cases. In a mining lease case there is now no doubt. But as the court noticed the doctrine has some support in prior California cases and in cases from sister states. There seems little reason to doubt that a lessor has remedies other than doing nothing on abandonment by the lessee with actions for rents on due dates, or in accepting a surrender and discharging the lessee (like a promisee would do if he rescinded a contract). There is a third course open to him, resuming control and reletting bringing home to the lessee that this is being done to protect him from full liability for rentals and not to discharge him from such liability. The doubts are over the true nature of this course, whether it leaves the lessor-lessee relation and in effect makes the lessor an agent of the lessee for reletting or whether it ends the relation and in effect makes the

lessor minimize the damages by reletting. The Commission Recommendations and Supporting Statement indicates that the former of the two positions is the only conclusion to reach from the cases. (See p. 3, p. 4, p. 7, p. 12, p. 25.) The whole course of the law, with the exception of some chance statements, principally dicta, such as in Dorcich v. Time Oil Company, 103 Cal.App.2d 677, 230 P.2d 10 (1951), has been toward recognition of the lessor's rights to a third course of allowing him the benefit of his bargain while he acts to end the relationship of lessor-lessee. The remedy, barring a lease provision under C.C. § 3308, was one in which the damage element was speculative leading to a delay in the commencement of the action.

If the lessor is to continue the relationship on reletting, which is the Commissions position on present California law (page 3), then it would be necessary to say the lessor is acting as agent of the lessee to relet and the lease provisions on rental due dates are no longer binding and unforceable. To reach such conclusions would mean Welcome v. Hess, 90 Cal. 507, 27 Pac. 369 (1891), is overruled, and that the language of the Supreme Court cases, some holding and some dicta, stressing the third course as an action for damages and not for rentals in five or six cases should be disregarded and some chance language in four or five District Court of Appeal opinions alone should be recognized. The maturing of the action for damages at the end of the term also was a conclusion based on New York cases which recognized that the lessor-lessee relation ended when the lessor acted. California cases have recognized the lessor-lessee relation can be continued on a reletting where a lease provision so provides or where a new agreement that the lessor can so act to relet is found. For cases on lease provisions see Original Study, page 40 (Mimeo 25) et seq. For cases on new agreements, see Original Study page 39 (Mimeo 24).

In personal property cases, the courts have discussed the doctrine of anticipatory repudiation, but again as in the real property cases, there is some uncertainty. See Hertz Driv-Ur-Self v. Schenley Dist., 119 C.A.2d 754, 260 P.2d 93 (1953); Oakland Cal. Towel Co. v. Roland, 93 C.A.2d 713, 209 P.2d 854 (1949).

Certainly a case for legislation ending the doubts mentioned in Gold Min. & Water Co. v. Swinerton, 23 C.2d 19, 142 P.2d 22 (1943), can be made out but I cannot accept that it has been made out.

Second: Is the doctrine that damages which can be avoided are not recoverable, applicable in lease cases? California has recognized that a lessor is under no obligation to act to minimize damages when a lessee abandons and repudiates the lease. Original Study p. 18 (Mimeo 8). The recognition of this is normally in dicta but there are also direct holdings. But there is no proof that lessors have used this course abusively. Abstract justice would support legislation making the doctrine applicable in lease cases. The job

of the draftsman of such legislation is most difficult if new hardships and abuses are not to arise. See Original Study p. 18 (Mimeo 9).

3. More care is voiced in California cases in defining the doctrine than is found in sentence 1 on page 2. See Guerrieri v. Severini, 51 Cal.2d 12, 330 P.2d 635 (1958). The last sentence of the paragraph could be supported by the Costello Case cited page 30 of the Recommendations but it is just a dictum. The Supreme Court has repeatedly denied that the lessor has only two courses. This is clearly revealed in the summary of Supreme Court cases appended to the original study. Admittedly many lessors attempting to protect themselves without intending to release their lessees, fall into a trap of Surrender by operation of law.

4. The first sentence of the second paragraph on page 2, is clearly not supported by the cases cited.

5. Point "Second" on page 3 in lease law is no different than rescession in contracts cases. If a promisee rescinds he discharges the promisor from further obligation.

6. Point "Finally" - the third course open to the lessor assumes that the relation of lessor-lessee is to continue. In comment 2 supra, this is discussed and the assumption is questioned.

7. Page 4 says when a lessor acts to dispossess a defaulting lessee by use of unlawful detainer proceedings he may lose the right to the rest of the rentals. The Costello Case is not an unlawful detainer case but contains a dictum. Your later consideration of C.C.P. Section 1174 and the Costello Case is slightly at variance with the inferences from this page. See page 30 of the recommendations.

8. The citations of Lawrence Barker, Inc. and the Burke Case, page 4, add nothing to the recommendations supporting statement. They are cases involving court recognition of lease provisions concerning lessor rights on breach by the lessee.

9. The paragraph on rent, page 5, voices the idea that the concept of rent developed at the common law, is outworn and at times denies a lessor an effective remedy against a defaulting lessee. The fault with the statement is that it is premised on "Course Three" being a course which preserves the lessor-lessee relation. There is no need to change the common law concept of rent to protect a lessor - there is only a need to make clear that he can terminate the relationship on abandonment by the lessee and at the same time get damages in the value of his bargain.

10. Starting on page 5 is a complaint that lessees may be subjected to forfeitures when they breach the lease transaction, something that contract law would not tolerate. What lease provisions for liquidated damages has to do with this, is remote. As an attempt to guard against lessee forfeiture it would seem of secondary importance. Acceleration provisions would seem to increase the chances of

lessee forfeiture. The statement that they are invalid generally then seems to help prevent forfeiture by the lessee. Ricker v. Rombaugh, of course, was an extreme provision and there is no reason to assume all such provisions are void.

11. The loss of prepaid rentals and bonus payments is next considered to evidence a bias against lessees on the part of the courts. The contracts treatment of advanced payments is stated to be different and not of forfeiture character. The Freedman Case, cited page 6, was a case where relief against forfeiture as provided by Civil Code Section 3275 was involved in a contracts case. The Caplan Case also allowed a recovery but two justices thought the matter should not justly be treated as one of course. There is no question but that advanced rentals and bonus payments in lease cases where in fact forfeitures come within Section 3275. And there is no question but that many times they are not forfeitures at all but are merely inadequate protective devices on the part of the lessor. I personally cannot find court bias and cannot accept the generalities voiced concerning Freedman and Caplan.

12. The comment on Section 3308 concludes that it does not relieve a lessee from forfeiture. Page 7. The classification of all advance payments lost to a lessee on breach, as forfeitures, is too broad a statement (page 6) and the conclusion that some are not considered in determining damages under Section 3308, cannot be supported.

13. The statement on page 7 concerning unlawful detainer continues the assumption that only by continuing the relationship of lessor-lessee after breach or by a 3308 lease provision, can a lessor get the benefit of his bargain. It should be noticed that in unlawful detainer only detention damages are involved and the courts have said only damages specifically provided by statutes can be considered. The statement falls far short of stating reasons for changing C.C.P. Section 1174. Possessory rights of lessors can be found in cases where termination of the relation is not desired and should not be forced. But at least if it is to be forced that course should be justified first.

14. Principle 3 on page 8, is a partial repetition of 2 with some procedural matters added. Apparently the burden of proof is on the lessor to make out his case under 2 but if a new lease is involved the burden of proof is on the lessee to show it unreasonable.

C. Comments on the proposed legislation.

1. Section 1936, page 11.

The supporting comment that the courts have not considered abandonment a breach is not true. They have held that the lessee by his unilateral act cannot force a determination on the lessor and that

the lessor by his acts inconsistent with a continuation of the relationship can end it and by so doing release the lessee from the obligations of the lease - similar to rescission in contracts. Also the last paragraph of the supporting comment is not true.

Apparently the idea is that the lessee by abandoning necessarily ends the lease transaction with a minor qualification provided by proposed Section 3322(a) that the lease can be revived by retraction as requested by the lessor (or before the lessor changes his position, perhaps). This idea is further qualified by proposed section 3327 on equitable relief. The policy behind Section 1936 then may not be so strong as to prevent a lessor and a lessee from contracting for a continuation of the lease on the event of an abandonment or other breach.

In considering the effect of the proposed legislation the type of property involved must be considered: (a) personalty of all types, (b) industrial or commercial property of great value, (c) such property of lesser value generally let for shorter periods of time, (d) luxury residential property of the high-rise type, (e) luxury residential single-unit property, (f) cheap residential property in many-unit developments, and (g) cheap residential property of single, duplex, etc., character.

In type (g) and frequently in type (f) and (e) cases litigation following abandonment is not practical. As a practical matter many lessors would accept the loss of a bargain under Section 1936 rather than litigate damages. This would probably be true in many cases of leases of types (g) (f) and (e). Custom has been to get protection by way of first and last months' rentals in advance and with all rentals payable at the beginning of the rental periods. This now is being undermined by Section 3325 permitting the defaulting lessee with no more than a small-claims fee to force litigation on his lessor, already in a position of hardship.

If Section 1936 forces a lessor of these types to sue for the breach or if Section 3325 permits the defaulting tenant to force litigation on the lessor, then the legislation is increasing his position of hardship and giving an irresponsible lessee a "whip handle." If the proposed legislation is enacted I would see immediate cases in which lessors of types (g) (f) and (e) would include (1) contractual provisions permitting continuation of the lease with the lessor obligated to make reasonable attempts to relet as agent for the lessee, (2) contractual provisions making first and last month rentals liquidated damages, and (3) contractual provisions providing a period for reletting if the lessor acts on basis that lease is terminated and a provision for retraction if lessor elects to continue the letting. Rights to contract inconsistent with Section 1936 have to be determined and any possible conflict of the meaning of Sections 3325 and 3323 would have to be determined.

An alternative to a Section 1936 would be a section permitting a lessor on abandonment or other total breach by the lessee to (1) accept a termination of the relationship releasing the lessee from further liabilities under the lease, (2) refuses to terminate the relationship with an obligation to assign or sublet to minimize lessee's liabilities with piecemeal recovery of deficiencies, or (3) terminate the relationship with damages such as currently defined in Section 3308 together with its election requirements. Such a section with some protective sections to cover special circumstances would have more predictable results than the current proposals.

2. Section 3320, page 14.

Apparently the idea is to determine, at the time of abandonment or other total breach, lease rental values and reasonable rental values on the open market, and to give the excess of the former over the latter as basic damages and then to add under (b) incidental damages as provided in Section 3322.

During a period of negotiation for a retraction and for a period which might be rather extended because of the type of property involved and a depressed market, reletting may not be accomplished by a lessor a long time after his lessee abandons. The reserved rentals for such periods are denominated incidental damages by Section 3322. Such periods are included in a computation of basic damages under Section 3320. Assume a letting at $300 a month; an abandonment followed by a reasonable three months period of negotiation for retraction and for reletting; a determination that reasonable rental value was the same as reletting at $200 a month; and the judgment was at the end of the three month period. Section 3320 says compute at full value 3 months lease rentals ($900) subtract reasonable rental value at full value claim to judgment ($600) and add incidental damages according to Section 3322 and here under (a) these are $900. I leave out discounted periods as not material to the illustration. I can read some inadequacy of language in either 3320 or 3322. Clearly double recovery is not intended.

The lessor forced into a litigation would probably continue letters and calls for retraction (Section 3322(a)) and then commence action allowing it to proceed on a slow course to judgment. The longer judgment is delayed the higher the lease rental value. The reasonable rental value for remainder of term after breach would remain unaffected by delay although it would be considered full up to judgment and a discounted value thereafter. In the case of lessors having hundreds of units to rent and always with vacancies, reletting of the particular unit might well be of no pressing concern. Section 3321 would not come into operation and the lessee could not force a reletting on the lessor. Or such a lessor might lease the particular unit at a very low rental. He has vacancies and this might not be injurious at all to him. Now under Section 3321 the defaulting lessee has the difficult task of convincing the fact finder that the rent on reletting is not reasonable. This comment on what a lessor of some types of property might do, is merely

to draw attention to the fact that attempts at detailed legislation in an area of great diversification is at best difficult.

There are many cases where the lessor's return is beyond the reserved "rentals." These would be included in Section 3322 (e) in some but not all cases. Some leases can have as their purpose the building of land and rental value of the land and this can be outside the bargain between the lessor and the lessee. There are many cases in which the proposed damages sections will not make Section 1936 really meaningful and truly protective of the lessor without burden on the lessee. By way of illustration: I know of lettings at 10 to 20 percent under area markets because the particular tenants have reputations for careful use of residential property. The true value of that lease could not be proved under Sections 1936, 3320 and 3322.

From the point of view of administration of Section 3320, some questions should be asked. The comment shows that "rental" is to be construed to include at least some payments (such as tax) and some acts in addition to money payments of rent, apparently all acts and payments bargained for in return for land or chattel use. As the "comment" will not be available to the bench or the bar and clearly not available to lessors, it may be asked whether some term not so closely associated with technical rents should be used.

Bargained-for returns for use of leased property may be difficult of proof but not to the extent that the case can be brought within Section 3327. The types of personalty today being leased and the variant situations involved mean lease returns vary widely. The many different real property lease situations show the same variations in returns. Some of these cases just cannot be covered by Sections 1936 and 3320, with fairness to lessors or perhaps with fairness to lessees. To practically rule out the lessor's right to insist on a continuation of the lessor-lessee relation against a defaulting lessee, may put the parties to proof which makes the breach remedy really no remedy at all. It was practical considerations similar to these suggestions that led to a return of far less comprehensive legislation to the New York Law Revision Commission in 1960 and to no action by the legislature on much restricted legislation submitted by that commission in 1961.

3. Section 3321, page 17.

Attention was directed in the comment on Section 1935, to the many types of lease within the coverage of the proposed legislation. Section 3321 may give some lessors a practical advantage because the proving that a rental is reasonable or the proving that it is not reasonable, is difficult. Section 3321 gives the lessor who relets a benefit in that the rentals on reletting are presumptively the reasonable value and places a very practical burden on the lessee. Lessors of multi-unit residential property and perhaps others, with normal vacancies, can lease or refrain from leasing and when they lease can lease at full, near full, or at a rate much lower than current market rentals, as the occasion benefits them. On a good

market but not such a good one as to care for all their vacancies, a near full or a low rental may be contracted. The burden of proof to show unreasonable is on the lessee.

Section 3321 says the presumption is the rentals on reletting are presumed to be the reasonable rental value of the term covered by the new lease. Suppose the lessee abandons and the lessor relets for part of the remainder of the original period or he lets for a period far beyond the remainder of the original period. Now rentals are in part determined by the duration of the lease. What may be a reasonable rental under the new lease may be different from the reasonable rental value of the remainder of the original period. This being true does Section 3321, as the comment indicates it does, establish the reasonable rental value under the basic damage section 3320? The operation of Section 3321 might be even more questionable if the new lease involved graduated base rentals and graduated percentage of business returns in computing the full rentals.

4. Section 3322, page 19.

At least three of the first four subdivisions, and I believe all four, are included within the coverage of subparagraph (e).

5. Section 3323, page 21.

No comments other than notice the coverage of Sections 3320 to 3322 is greater than abandonment cases. Reading the comment may lead legislators to the belief that liquidated damage provisions have all been held void and that the proposed section affects only abandonment cases. Either inference would be erroneous.

6. Section 3324, page 22.

I can see leases in which the lessor waives attorney's fees in cases of breach but includes a provision for such fees should the lessee sue.

The section applies in cases of breach of a lease. Involved in such a breach may be breach of covenants for quiet enjoyment, repairs, restricted use, rentals, etc. Attorney's fees under these covenants apparently would be lost if lessor elected to end lease. I am not sure this was in mind when the proposal was drafted.

Would the Section repeal by implication part of Section 794 of the Civil Code?

7. Section 3325, page 23.

In case of lessee substantial breach or lessee abandonment, the lessor can avoid forfeiture by seeking the benefits of Section 3327. In case of lessor acts to terminate lease for substantial breach, lessee now has protection of Civil Code Section 3275 and C.C.P. section 1179. I assume proposed Section 3325 would not deny lessee the more extensive relief he now enjoys. This must be con-

sidered because the proposed legislation applies in termination cases other than those involving abandonment. Proposed section 3328 is a partial answer.

Repetition of the complaint over the statement of existing law in the Background Statement, is not necessary here. The Comment's use of Freedman and of Caplan cannot be supported.

A common lease provision is to make advanced payments liquidated damages on lessee breach. This in effect is a waiver of the right to their recovery. Section 3323 permits reasonable liquidated damage provisions. Should a possible problem of conflict be raised by a provision the Comment states "probably unnecessary"?

8. Section 3326, page 25.

The Comment states if the lessor leases "on his own account," the rationale of the California cases indicates the lessee is entitled to the profits. I can find no basis for this conclusion in the holding or reasoning of any case. The remainder of the first sentence of the Comment--if the lessor leases on the lessee's account, infers that the lease obligation continues. That of course is true in some cases but not in all cases as is pointed out in the discussion of the Background Statement.

9. Section 3327, page 26.

No comment.

10. Section 3328, page 27.

No comment.

11. Section 3308 repeal, page 28.

See comment on Proposed Section 1936 with alternative legislation possible.

12. Section 1174 modifications, page 29.

It must be kept in mind that the proposed legislation covers cases other than those of abandonment and repudiation of the lessees. Leases in abandonment and repudiation situations can be kept alive under lease provisions making the lessor agent to manage the property or under new agreements to that effect and under proposed Section 3327. If instead of abandoning the lessee breaches and indicates repudiation but refuses to leave, the lessor's need to proceed under C.C.P. 1174 as modified would require a judgment "declaring the forfeiture of such lease." Section 3328 says Section 3327 or other provisions in the article are not intended to affect unlawful detainer proceedings. The effect then of the modification will be to force the lessor to take some other action than unlawful detainer--time consuming and expensive. The result will be to put him in a position of hardship.

I cannot follow the argument that "the deleted language is no longer necessary." There are many cases in which a lessor may need protection by use of Unlawful Detainer without termination of the lease.

UNITED STATES LEASING CORPORATION
633 BATTERY STREET • SAN FRANCISCO, CALIFORNIA • EXBROOK 7-1787

August 24, 1965

California Law Revision Commission
School of Law
Stanford University
Stanford, California

Re: Lease Remedies

Gentlemen:

We have read your Study and Tentative Recommendations relative to lease remedies and would like to offer our comments for your consideration.

Our interest in your study is not academic but practical in view of the proposed legislation's inclusion of leases of personal property. United States Leasing Corporation is the largest and oldest independent equipment leasing firm in the country. It is headquartered in San Francisco with an extensive sales force operating in all fifty states, and has four foreign affiliates. We quite obviously, therefore, share a very real interest in legislation such as this.

Chattel leasing is not a well developed field of the law, but is commanding increasing attention, particularly in the areas of taxation and creditors' rights. Any attempt to deal with the questions of remedies and enforcement of leases through legislative proposals must necessarily include full consideration of the problems peculiar to equipment leasing.

Although in general principle we commend your basic approach to a revision of law through the application of general contract principles of damages, as opposed to real property concepts, we suggest that the considerations reflected in the "Tentative Recommendations" of July 23, 1965, are not sufficiently responsive to the problems of the equipment lessor.

Our mutual interest in the subject at hand perhaps will be better served by general reference here to areas which in our mind deserve further study than by detailed analysis, however, we shall welcome the opportunity to respond to any interest you may have in further discussing these questions.

First, a thorough study should be made of the desirability of enacting identical provisions for both real and personal property leases. The transitory and totally depreciating nature of personal property materially distinguishes it from real property as do the questions involved in its evaluation. Relating this to your paragraphs 2 and 3 (page 8 of the Proposals), no specific consideration appears to be given to the more common alternative (to reletting) of sale of repossessed property by the lessor. How, if at all, shall sale proceeds realized be apportioned between lessor and lessee in mitigation? Within the context of paragraph 4 would a stipulated loss value provision keyed to the time of default be regarded as an enforceable liquidated damage provision?

With respect generally to the consideration of forfeitures (paragraph 5), which we appreciate equity abhors, consider the fact that more frequently in the case of real estate the landowner seeks to lease land in which he has made an investment without a specific lessee in mind. On the other hand, commercial and industrial equipment leasing invariably involves a purchase, and therefore financial commitment by the lessor, predicated upon the specifications of a specific lessee. When the latter defaults the lessor is left with property which he acquired not because of a predetermination that it would be generally attractive to others (as in the case of equipment or auto rental concerns which purchase for general inventory), but because a specific lessee has required the item and has agreed to lease it for a specified period, typically including a major portion of the articles' useful economic life. A default in this latter situation requires a remedy more closely akin to full realization of the contracted-for price.

Lastly, remedies of the lessor cannot be considered without due regard to conflicting interests of other creditors of the financially defunct lessee. For instance, a major area of concern today to the equipment lessor is the applicability of the Uniform Commercial Code to its transactions. Specifically, Section 1201(37) defines when a lease shall create a "security interest" for the purpose of the now effective Code. The test, however, is uncertain. In considering remedies of the chattel lessor, the problem of coordinating new legislation with existing remedies provided for in the Commercial Code certainly deserves attention. Thus, the basic question is presented, what is a lease under the proposed legislation? Are leases with options to purchase for nominal consideration to be included?

A very real step forward would be accomplished through legislation providing for recordation, and therefore public notice, of the lessor's interest in leased property in the hands of the

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lessee, irrespective of whether the instrument is later judged to be a true lease or not. Civil Code Section 3440 pertaining to sale and leasebacks requires such recording to avoid a presumption of fraud, and it would just as logically be appropriate for the protection of lessor and other potential creditors of the lessee in a straight lease situation where the lessor purchases the leased property directly from the vendor.

These several points do not by any means exhaust the problems which must be considered in contemplating legislation affecting the rights of parties to a lease, whether of real or personal property. However, we do hope that they will provoke further thought by the Commission and those studying the problem on its behalf. We would welcome an opportunity to discuss at your convenience any aspect of your deliberations about which we might be knowledgeable.

Very truly yours,

Brandt Nicholson

Brandt Nicholson
Secretary & General Counsel

BN d

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SAN MATEO COUNTY OFFICE
234 MARSHALL STREET
REDWOOD CITY
CALIFORNIA
EMERSON 6-9561

August 25, 1965

California Law Revision Commission
School of Law
Stanford University
Stanford, California

Re: Tentative recommendations relating to the rights and duties attendant upon abandonment or termination of a lease.

Gentlemen:

This is in response to your invitation for comments relative to the captioned study and resulting recommendations. We are most interested in the real property aspects of the work but this letter concerns only its implications in the field of chattel leasing.

It is evident that although the recommendations deal with both real and chattel leases, the study focused mainly, if not exclusively, on real property transactions. We believe that the recommendations, if enacted, could cause considerable difficulty when applied to chattel leases.

The Commission, in making its final recommendations, should consider the several factors that distinguish a chattel lease from a realty lease. Some of them are these: In many chattel leases the lessor purchases the equipment to the specifications of the lessee and obtains from the lessee a promise to pay the full purchase price plus a finance charge, as rent, over the term of the lease; the economic life of the equipment is often substantially depreciated at the end of the promised term; in many chattel leases there is an option at the end of the initial term to acquire title, or to renew indefinitely, for a relatively nominal consideration; the contractual remedy upon default by the lessee, usually invoked, is repossession and sale of the equipment and the assertion of a deficiency obligation; and, perhaps most important, there already exist regulatory statutes applicable to chattel lease remedies,

The most serious problems that occur to us if the tentative recommendations were adopted would result from their inconsistencies with existing legislation such as the Rees-Levering Motor Vehicle Sales Act (Civ. C., sec. 2981 et seq.), the Unruh Act (Civ. C., sec. 1802 et seq.), and Division 9 of the Uniform Commercial Code.

The latter legislation, applicable to "secured transactions," sets forth in some detail the available remedies to a secured party upon the default of a debtor. There seems little doubt that many leases of personal property constitute "secured transactions" within the meaning of the Commercial Code. (UCC, secs. 1201(37), 9102(1), (2).) Under the proposed legislation a chattel transaction could be a "lease" as well as a "secured transaction" under Division 9 of the Commercial Code.

One example of potential conflict is between proposed Section 3326 of the Civil Code, which permits the lessor to keep any "profit made on the reletting," and section 9504(2) of the Commercial Code, which requires the secured party ("lessor") to account to the debtor ("lessee") for any surplus following disposition of the collateral.

Other areas where the Commercial Code at least overlaps, if not contradicts, the proposed legislation, are in the provisions governing disposition of collateral following default (sec. 9504), the right to retain the collateral in satisfaction of the obligation (sec. 9505), the right of the debtor to redeem the collateral (sec. 9506), and the debtor's rights for failure of the secured party to comply with the default provisions (sec. 9507).

The remedies of a lessor of chattels subject to the strict regulations of the Rees-Levering Motor Vehicle Sales Act and the Unruh Act are much more circumscribed than under the proposed legislation. (See Civ. C., secs. 1811.1 et seq.; 2982 et seq.)

We do not mean to suggest that an easy solution would be to exclude from the proposed legislation transactions that are subject to Division 9 of the Commercial Code or the other regulatory Acts. It is very difficult to determine, at this stage in the development of the Commercial Code, which kinds of leasing transactions are covered. Moreover, it may well be that even a "true" lease which is not a Division 9 "secured transaction" might be more akin to a chattel secured transaction rather than a real estate transaction; hence, chattel security rules ought to apply. But we do not necessarily believe that all chattel lease transactions should be excluded from your proposed legislation.

In any event, we urge the Commission to extend the study into the area of chattel leasing transactions prior to presenting its final recommendations.

Respectfully yours,

DINKELSPIEL & DINKELSPIEL

By John F. Taylor

JFT/ed

J. H. PETRY
ATTORNEY AT LAW
374 COURT STREET
SAN BERNARDINO, CALIFORNIA 92401
AREA CODE 714
TURNER 9-9545

January 31, 1966

California Law Revision Commission
Room 30, Crothers Hall
Stanford University
Stanford, California 94305

Dear Sirs:

At my request you sent to me the following:

1. Study to Determine Whether the Law Respecting the Rights of a Lessor of Property When it is Abandoned by the Lessee should be Revised.

2. Tentative Recommendation relating to the Rights and Duties Attendant Upon Abandonment or Termination of a Lease.

I have not had time to read these carefully so have merely glanced through them to determine whether they cover some problems which I think need legislative enactment. I didn't find anything on the points I have in mind so I strongly urge that your recommendations include a draft of legislation to assist the Landlord under the following circumstances:

(a) Under the present law, whether a Lessee or Tenant has abandoned the premises is determined by the trier of fact with no guide other than previous decisions and circumstances of the case under consideration. The Landlord should have some assurance that if certain facts exist, the court will rule that there has been a surrender or abandonment. Legislation should provide that if the Lessee or Tenant is delinquent for 60 days in the payment of rent and has not been found on the premises after reasonable effort by the Landlord, the court will presume that the Lessee or Tenant abandoned or surrendered the premises and lease, if any. A Landlord should not be required to spend money, time and effort trying to locate the tenant. If the Tenant intends to be absent from the premises for an unusual length of time, he should notify the Landlord or, at least, he should keep the rent current.

(b) A property owner frequently has the problem of deciding what to do with personal property that is left on his premises by a previous occupant, whether a previous owner or only a tenant. He assumes considerable risk by making any disposition of such personal property. Again, he should not be put to expense, time or effort to determine who owns the personal property or where the owner is located. Legislation should provide that the Landlord may store the property for 30 days and if unclaimed after that, may make any disposition he wishes of it. The 30-day period, of course, would have to be worked in with the suggestion in (a) above. However, this provision should not be limited strictly to the Landlord-Tenant relationship because there are some cases where a person buys real property and finds personal property is left on it and if he disposes of it, he takes a chance that some third party may assert ownership and claim damages.

(c) Unlawful detainer actions are costly if a Landlord must retain an attorney. I think the objections of the California Supreme Court as set out in the Mendoza case could be overcome by proper phraseology of a new statute and that there should be legislation to give unlawful detainer jurisdiction to a Small Claims Court. Apparently the Supreme Court was concerned with a stay of execution, and surely that could be taken care of by appropriate legislation.

Yours very truly,

J. H. Petry

JHP:HLP

FIREMAN'S FUND INSURANCE COMPANY
3333 CALIFORNIA STREET
SAN FRANCISCO, CALIFORNIA

September 24, 1965

State of California
California Law Revision Commission
Room 30, Crothers Hall
Stanford University
Stanford, California 94305

Gentlemen:

"Abandonment or Termination of Lease"

I have read with interest the tentative recommendations of the California Law Revision Commission relating to rights and duties attendant upon abandonment or termination of a lease.

I agree with and approve of the recommended legislation, with one exception. The use of the term "abandonment" concerns me. We have found it necessary in many instances to vacate property. In doing so we continue to pay rent and meet all other commitments in the lease. It has always been our position that vacation of the premises is not abandonment, but I have found no authority that this is an acknowledged legal concept.

It strikes me that without a distinction being made between vacation and abandonment, one who vacates with full intention to recognize his commitments under the lease could possibly be held to have abandoned the leased property, thereby subjecting himself to a suit for damages and precluding his obtaining relief over the remaining term of the lease by subletting or buying out the remainder of his liability at a reduction in total cost. Mightn't the term "repudiation" be sufficient and "abandonment" not used?

Very truly yours,

Gordon W. Hackett,
Real Estate Department

GWH:em

ES	
[illegible]	
JC	
AL	

ALBERT J. FORN
ATTORNEY AT LAW
SUITE 1058 ROOSEVELT BUILDING
727 WEST SEVENTH STREET
LOS ANGELES 17, CALIFORNIA
MADISON 2-4577 · MADISON 2-4795

October 11, 1965

California Law Revision Commission
School of Law
Stanford University
Stanford, California

Gentlemen:

Thank you for the copy of the Tentative Recommendation relating to the law on termination of leases. I was pleased to see that the recommendations resolve a number of problems that I have encountered in my practice.

However it seems to me that one specific fact situation has been overlooked, that is the case where the landlord tries to "bleed" a building by drastically curtailing the normal services. To illustrate: lets say that we have an office building to which tenants are attracted because of its prestige value, and because of its excellent management. A new owner takes over the building, he fires two elevator operators and two maintenance men. Thereafter the bathrooms are no longer kept up and begin to stink, the halls are not policed during the business day and become habitually littered with cigar butts, cigarette wrappers and so on. Patrons find that they have to wait two or three minutes for an elevator. Cockroaches overrun the offices; and the tenants find that they are no longer in a prestige building and that their clientele is slipping away.

Under present law in California there seems to be no adequate protection for the tenant whose lease still has several years to run when faced with this situation. The covenant to pay rent is supposedly an independent covenant and the tenant may not offset his claim of damages against the rent. Nor can the tenant claim an eviction in most instances. In addition it is extremely difficult for the tenant to prove the extent of his damages.

It seems to me that your recommendations overlooked the problem of this type of defaulting landlord, and I believe that your recommendations should cover such a situation. I have read that in New York the law permits a percentage of the tenants in this situation to petition the court to appoint a receiver. I don't know how this works out in practice, but it shows that the problem is not an uncommon one.

Very truly yours,

ALBERT J. FORN

AJF:lw

ORRICK, DAHLQUIST, HERRINGTON & SUTCLIFFE
COUNSELORS AND ATTORNEYS AT LAW
405 MONTGOMERY STREET
SAN FRANCISCO, CALIFORNIA 94104

W. H. ORRICK
OF COUNSEL

TELEPHONE 392-1120
AREA CODE 415
CABLE "ORRICK"

January 4, 1965

The Honorable James A. Cobey
P. O. Box 1229
Merced, California

Dear Jim:

I am enclosing a copy of a letter I have just written to the California Law Revision Commission. I do not understand why the Commission disregarded the report of its own expert who was employed by the Commission to determine the advisability of making changes in the existing law. This report very clearly indicated that no such changes were necessary or desirable and certainly should not be made without a very thorough and careful study of the whole subject matter of leasehold interest. Obviously, the Commission has made no such study. No consideration has been given to complex leases involving office buildings, retail stores, manufacturing establishments or shopping centers or other similar complex situations. No consideration has been given to long-term leases such as 99-year leases. My letter points out only one area in which the legislation is wholly inadequate. Isn't there something that can be done to bring order out of chaos?

Sincerely,

GH/le
enclosure

The nonprofit corporation or the contractor acquires the funds necessary to construct the public improvement through private financing secured by an assignment of the rentals which the public body agrees to pay to the nonprofit corporation or the contractor pursuant to the leaseback of the land and public improvement. Upon payment in full of the indebtedness incurred with respect to the construction of the public improvement, the leaseback terminates and the public body acquires title in fee to the public improvement.

Proposed Civil Code Section 3320 would prevent a lender or contractor from relying only upon the promise of a public body to pay rentals due under a leaseback, and would impose upon such lender or contractor the obligation of looking to the public improvement in order to obtain funds to satisfy the indebtedness, in the event of default by the public body. This would impose a burden upon a lender or contractor which does not presently exist and could either increase the interest rates charged for the money lent, which would increase the cost of the public improvement to the public body, or preclude entirely the use of this type of financing. Presumably lenders, many of whom are located outside of California, would not be as willing to lend money in California where the security was primarily a mortgage on a leasehold interest in a public improvement rather than an enforceable promise by a public body to pay rentals, as the lenders lack the facilities to manage the property and would wish to avoid a situation in which they would be required to do so. It should be realized that where a nonprofit corporation is formed to assist the public body by obtaining financing, such a corporation has no paid staff and no funds with which to manage or attempt to relet the property.

Furthermore, the limiting of the damages recoverable by the nonprofit corporation or contractor when the public body defaults to those rentals in excess of the reasonable rental value for the property would often result in default in the payment of the indebtedness incurred to construct the public improvement, for in many cases the public improvement could not be relet, there being either an extremely limited or no market for improvements such as city halls, county courthouses, public libraries, and corporation yards. An Eastern insurance company purchasing bonds of a nonprofit corporation organized to construct a county jail would certainly have no use for the jail following foreclosure of the mortgage on the leasehold interest. The concept of reasonable rental value is practically meaningless under these circumstances, for the public improvement could be relet, if at all, only after substantial alterations which change the purpose for which it was constructed.

W. DAHLQUIST
GEORGE HERRINGTON
ERIC SUTCLIFFE
NATHAN D. ROWLEY
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ORVILLE A. ROHLF
WALTER C. OLSON
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C. RICHARD WALKER
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ANDREW DOWNEY ORRICK
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RICHARD C. SALLADIN

ORRICK, DAHLQUIST, HERRINGTON & SUTCLIFFE
COUNSELORS AND ATTORNEYS AT LAW
SAN FRANCISCO, CALIFORNIA 94104

December 30, 1965

California Law Revision Commission
Room 30, Crothers Hall
Stanford University
Stanford, California 94305

Attention: Mr. John H. DeMoully, Executive Secretary

Re: Tentative Recommendation Relating to the Rights and Duties Attendant Upon Abandonment or Termination of a Lease

Gentlemen:

We have reviewed your tentative recommendation dated July 23, 1965 relating to the rights and duties attendant upon abandonment or termination of a lease and wish to make the following comments.

The enactment of the legislation contained in the tentative recommendation would seriously limit the financing of needed public improvements by public bodies in California by means of a lease and leaseback arrangement between the public body and either a contractor or a nonprofit corporation formed to assist the public body finance the improvement. This method of financing the acquisition of public improvements has been utilized by the State of California and by counties and cities within the State and has been approved by the California courts. Dean v. Kuchel, 35 C.2d 444 (1950), County of Los Angeles v. Byram, 36 C.2d 694 (1951), City of Montclair v. Donaldson, 205 C.A.2d 201 (1962), McClain v. County of Alameda, 209 C.A.2d 73 (1962), City of La Habra v. Pellerin, 216 C.A.2d 99 (1963), Lagiss v. County of Contra Costa, 223 C.A.2d 77 (1963), County of Los Angeles v. Nesvig, 231 A.C.A. 659 (1965). The public body leases land to the nonprofit corporation or the contractor for a period of years. The nonprofit corporation or the contractor simultaneously leases the land and any improvements to be constructed thereon back to the public body for a lesser period of years, agreeing to construct the public improvement thereon.

The nonprofit corporation or the contractor acquires the funds necessary to construct the public improvement through private financing secured by an assignment of the rentals which the public body agrees to pay to the nonprofit corporation or the contractor pursuant to the leaseback of the land and public improvement. Upon payment in full of the indebtedness incurred with respect to the construction of the public improvement, the leaseback terminates and the public body acquires title in fee to the public improvement.

Proposed Civil Code Section 3320 would prevent a lender or contractor from relying only upon the promise of a public body to pay rentals due under a leaseback, and would impose upon such lender or contractor the obligation of looking to the public improvement in order to obtain funds to satisfy the indebtedness, in the event of default by the public body. This would impose a burden upon a lender or contractor which does not presently exist and could either increase the interest rates charged for the money lent, which would increase the cost of the public improvement to the public body, or preclude entirely the use of this type of financing. Presumably lenders, many of whom are located outside of California, would not be as willing to lend money in California where the security was primarily a mortgage on a leasehold interest in a public improvement rather than an enforceable promise by a public body to pay rentals, as the lenders lack the facilities to manage the property and would wish to avoid a situation in which they would be required to do so. It should be realized that where a nonprofit corporation is formed to assist the public body by obtaining financing, such a corporation has no paid staff and no funds with which to manage or attempt to relet the property.

Furthermore, the limiting of the damages recoverable by the nonprofit corporation or contractor when the public body defaults to those rentals in excess of the reasonable rental value for the property would often result in default in the payment of the indebtedness incurred to construct the public improvement, for in many cases the public improvement could not be relet, there being either an extremely limited or no market for improvements such as city halls, county courthouses, public libraries, and corporation yards. An Eastern insurance company purchasing bonds of a nonprofit corporation organized to construct a county jail would certainly have no use for the jail following foreclosure of the mortgage on the leasehold interest. The concept of reasonable rental value is practically meaningless under these circumstances, for the public improvement could be relet, if at all, only after substantial alterations which change the purpose for which it was constructed.

HAROLD W. KENNEDY
COUNTY COUNSEL

MADISON 5-3811

OFFICE OF THE COUNTY COUNSEL

648 HALL OF ADMINISTRATION
LOS ANGELES 12, CALIFORNIA

4 February 1966

VIA AIR MAIL

California Law Revision Commission
School of Law
Stanford University
Stanford, California 94305

Re: Proposed Civil Code Section 3320

Dear Sirs:

On 28 January 1966 we received from you the material requested, and were informed by Mr. DeMoully that you would appreciate receiving our comments in time for your meeting of 10 February 1966.

As you have been informed by Attorney George Herrington of San Francisco, the statute as proposed would quite possibly have an adverse effect upon the ground lease-construction leaseback program currently being carried out by the County of Los Angeles and other local agencies in Southern California. Ground lease construction of the value of approximately $14 million has already been contracted for by the County of Los Angeles, bids are now being called for an additional $5 million in such construction, and additional projects are currently being considered by the County.

The County of Los Angeles is thus vitally interested in the proposed statute, and generally concurs in the views expressed by Mr. Herrington. However, because of the shortness of our notice of this matter, and its importance to us, we request additional time for consideration and submission of a more extensive statement of our position.

Very truly yours,

HAROLD W. KENNEDY,
County Counsel

By Joel R. Bennett

Joel R. Bennett,
Assistant County Counsel

JRB:bma

ADRIAN KUYPER
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OFFICES OF
THE COUNTY COUNSEL
County Of Orange

COUNTY ADMINISTRATION BUILDING • P. O. BOX 1663 • SANTA ANA, CALIFORNIA 92702 • 834-3

February 9, 1966

California Law Revision Commission
School of Law
Stanford University
Stanford, California

Gentlemen:

This office has been informed of your tentative recommendation relating to the rights and duties attendant upon abandonment or termination of lease, and we have been furnished a copy of a letter addressed to your Commission by George Herrington of the firm of Orrick, Dahlquist, Herrington & Sutcliffe.

The County of Orange and many of the cities within this County have financed public improvements by means of a lease and leaseback arrangement. We share the concern of Mr. Herrington regarding proposed Civil Code Section 1320. Its enactment would seriously impede the financing of public improvements in this County and throughout the State of California. We are of the opinion that, at least in this type of instance, lessors should be entitled to rely solely on the promise to pay rent under a leaseback without having the duty to look to the public improvement.

This office desires to be kept informed of any action of the Law Revision Commission in this field.

Very truly yours,

ADRIAN KUYPER, COUNTY COUNSEL

By _____
Clayton H. Parker
Chief Assistant

CHP:cj

STATE OF CALIFORNIA

CALIFORNIA LAW REVISION COMMISSION

TENTATIVE RECOMMENDATION

relating to

THE RIGHTS AND DUTIES ATTENDANT UPON ABANDONMENT OR TERMINATION OF A LEASE

July 23, 1965

California Law Revision Commission
School of Law
Stanford University
Stanford, California

TENTATIVE RECOMMENDATION OF THE CALIFORNIA LAW REVISION COMMISSION

relating to

THE RIGHTS AND DUTIES ATTENDANT UPON

ABANDONMENT OR TERMINATION OF A LEASE

BACKGROUND

Section 1925 of the Civil Code provides, in effect, that a lease is a contract. Historically, however, a lease was regarded as a conveyance of an interest in land. 2 POWELL, REAL PROPERTY ¶ 221 (1950). The California courts, unwilling to believe completely that the statement in Section 1925 really means what it says, have vacillated between the two concepts. The courts state that a lease is both a contract and a conveyance. Medico-Dental Bldg. Co. v. Horton & Converse, 21 Cal.2d 411, 132 P.2d 457 (1942); Beckett v. City of Paris Dry Goods Co., 14 Cal.2d 633, 96 P.2d 122 (1939). And while at times the courts apply principles of contract law in determining the rights and duties attendant upon abandonment or termination of a lease (see, e.g., Medico-Dental Bldg. Co. v. Horton & Converse, supra), the courts seem to be guided principally by common law property concepts in determining these rights and duties (see, e.g., Kulawitz v. Pacific etc. Paper Co., 25 Cal.2d 664, 155 P.2d 24 (1944); Welcome v. Hess, 99 Cal. 507, 25 Pac. 369 (1891)). See, generally, The California Lease--Contract or Conveyance? 4 STAN. L. REV. 244 (1952).

As a result of this development, the present law does not afford adequate relief to either lessors or lessees when the leasehold is abandoned or the lease is otherwise terminated because of the lessee's breach. Under existing law, a lessor frequently is precluded from recovering damages for all of the detriment caused by the defaulting lessee, and a defaulting lessee may be subjected to forfeitures that are not countenanced under the law relating to contracts generally. See 26 CALIF. L. REV. 385 (1938).

For example, under the law applicable to most contracts, repudiation constitutes a total breach for which an action can be maintained even though the time for full performance has not yet elapsed. Gold Mining & Water Co. v. Swinerton, 23 Cal.2d 19, 142 P.2d 22 (1943); Remy v. Olds, 88 Cal. 537, 26 Pac. 255 (1891). And, under the law applicable to most contracts, a material breach by the promisor gives rise to a duty on the part of the promisee to mitigate damages, i.e., the promisee cannot recover damages for any detriment that is reasonably avoidable. See discussion in Bomberger v. McKelvey, 35 Cal.2d 607, 613-615, 220 P.2d 729 (1950). In contrast, when a lessee repudiates or breaches a lease, the courts frequently require a lessor to choose between forfeiting his right to damages for future injury and enhancing the damages by continuing performance.

Except where a mining lease is involved (see Gold Mining & Water Co. v. Swinerton, supra), the doctrine of anticipatory breach has not been applied to leases. Oliver v. Loydon, 163 Cal. 124, 124 Pac. 731 (1912); Welcome v. Hess, 90 Cal.507, 27 Pac. 369 (1891); In re Bell, 85 Cal. 119, 24 Pac. 633 (1890). Under existing law, when a lessee abandons the leased property and repudiates the remaining obligations of the lease, his actions constitute merely an offer to surrender the remainder of the term. Welcome v. Hess,

90 Cal. 507, 513, 27 Pac. 369 (1891). Confronted with such an offer, the lessor has three courses of action among which he may choose. Kulawitz v. Pacific etc. Paper Co., 25 Cal.2d 664, 671, 155 P.2d 24 (1944). First, he may decline the lessee's offer to surrender and sue for the unpaid rent as it becomes due for the remainder of the term. If the lessor selects this course of action, he has no duty to mitigate damages by reletting the property; he can recover the full amount of the rent while permitting the property to remain vacant. See De Hart v. Allen, 26 Cal.2d 829, 832, 161 P.2d 453 (1945). Second, he may accept the lessee's offer to surrender and thus extinguish the lease. This course of action not only terminates the lessee's interest in the property, it also terminates the lessee's obligation to pay any further rent, and the lessor is not entitled to any damages for the loss of his bargain represented by the original lease. Welcome v. Hess, 90 Cal. 507, 27 Pac. 369 (1891). The cases make clear, too, that any action taken by the lessor that is inconsistent with the lessee's continued ownership of an estate in the leased property will be deemed an acceptance of the lessee's offer to surrender, whether the lessor intended such an acceptance or not. Dorcich v. Time Oil Co., 103 Cal. App.2d 677, 230 P.2d 10 (1951). Finally, if the lessor notifies the lessee of his intention to do so, the lessor may relet the property for the benefit of the lessee and recover damages in the amount of the excess of the rentals called for in the original lease over the rentals obtained by reletting. The lessor cannot sue immediately to recover these damages; the cause of action does not accrue until the end of the term, and the lessor must wait until that time and then sue for all of the rental deficiencies. Treff v. Gulko, 214 Cal. 591, 7 P.2d 697 (1932). The courts have held that prior notification

to the lessee is essential to this course of action and that without such notification the lessor's reletting of the property will terminate the original lease and the lessee's rental obligation. Dorcich v. Time Oil Co., 103 Cal. App.2d 677, 230 P.2d 10 (1951). Apparently, then, this third course of action is unavailable to a lessor who is unable to give proper notice to the defaulting lessee. Such a lessor must choose between permitting the property to remain vacant (thus preserving the lessee's rental obligation) and terminating the lessee's remaining obligation by resuming possession or by reletting the property.

A similar range of choices confronts the lessor whose lessee commits a sufficiently substantial breach of the lease to warrant termination thereof. He may treat the breach as a partial breach, decline to terminate the lease, and sue for the damages caused by the particular breach. In such a case, the lessor must continue to deal with a lessee who has proven to be unsatisfactory. The lessor may also terminate the lease and force the lessee to relinquish the property, resorting to an action for unlawful detainer to recover the possession of the property if necessary. In such a case, the lessor's right to the remaining rentals due under the lease ceases upon the termination of the lease. Costello v. Martin Bros., 74 Cal. App. 782, 241 Pac. 588 (1925). Under some circumstances, the lessor may decline to terminate the lease but still evict the lessee and relet the property for the account of the lessee. Lawrence Barker, Inc. v. Briggs, 39 Cal.2d 654, 248 P.2d 897 (1952); Burke v. Norton, 42 Cal. App. 705, 184 Pac. 45 (1919). See CODE CIV. PROC. § 1174. In such a case, any profit made on the reletting probably belongs to the lessee, not the lessor, inasmuch as the lessee's interest in the property theoretically continues. Moreover, the lessor must be careful in utilizing

this remedy or he will find that he has forfeited his right to the remaining rentals from his original lessee despite his lack of intent to do so. See, e.g., Neuhaus v. Norgard, 140 Cal. App. 735, 35 P.2d 1039 (1934); A. H. Busch Co. v. Straus, 103 Cal. App. 647, 284 Pac. 966 (1930).

Bound by common law property concepts, the courts have considered the lessee's obligation to pay rent as dependent on the continued existence of the term. When the term is ended, whether voluntarily by abandonment and repossession by the lessor or involuntarily under the compulsion of an unlawful detainer proceeding, the rental obligation dependent thereon also ends. In the usual case where the lessor has no reason to expect the lessee to remain available and solvent until the end of the term, continued adherence to these property concepts thus denies the lessor any effective remedy for the loss caused by a defaulting lessee.

Adherence to ancient common law property concepts in the interpretation of leases has caused hardship to lessees as well as to lessors. Under the existing law, lessees may be subjected to forfeitures that would not be permitted under any other kind of contract. The courts have been quick to hold that

provisions in leases for liquidated damages are void. Jack v. Sinsheimer, 125 Cal. 563, 58 Pac. 130 (1899). Similarly, provisions for the acceleration of the unpaid rental installments have been held invalid. Ricker v. Rombough, 120 Cal. App.2d Supp. 912, 261 P.2d 328 (1953). But, if the lessee makes an advance payment to the lessor as an advance payment of rental or "in consideration for the execution of the lease," the lessor is entitled to keep the payment regardless of his actual damages when the lease is terminated by reason of the lessee's breach. A-1 Garage v. Lange Investment Co., 6 Cal. App. 2d 593, 44 P.2d 681 (1935); Curtis v. Arnold, 43 Cal.App. 97, 184 Pac. 510 (1919); Ramish v. Workman, 33 Cal. App. 19, 164 Pac. 26 (1917). See 26 CAL. L. REV. 385, 388 (1938).

In contrast, where the buyer repudiates a contract for the sale of real property, any advance payments made to the seller in excess of his actual damages are recoverable by the buyer. Freedman v. The Rector, 37 Cal.2d 16, 230 P.2d 629 (1951). Moreover, even though a contract for the sale of property recites that an initial payment is in "consideration for entering into the agreement," the courts permit the buyer to recover so much of the payment as exceeds the seller's damages if, in the light of the entire transaction, there was in fact no separate consideration supporting the payment. Caplan v. Schroeder, 56 Cal.2d 515, 15 Cal. Rptr. 145, 364 P.2d 321 (1961).

In 1937, Civil Code Section 3308 was enacted in an effort to ameliorate

the deficiencies in the law relating to leases. The effort, however, was only partially successful. Under Section 3308, if a lease so provides, the lessor may bring an action for damages immediately upon termination of the lease by reason of the lessee's abandonment or breach of the lease. The lessor's damages in such an action amount to the excess of the value of the remainder of the term over the then reasonable rental value of the remainder of the term. Section 3308, however, does not apply unless it is made applicable by a provision in the lease; it does not require the lessor to resort to the remedy provided (and thus require mitigation of damages); and it does not relieve a lessee from forfeiture.

Code of Civil Procedure Section 1174 has also been amended in an effort to alleviate the problems faced by a lessor when his lessee refuses to pay rent or otherwise breaches the lease. Section 1174 provides that the lessor may notify the lessee to quit the premises, and that such a notice does not terminate the leasehold interest unless the notice so specifies. This permits a lessor to evict the lessee, relet the property to another, and recover from the lessee at the end of the term for any deficiency in the rentals. But again, the statutory remedy falls short of providing full protection to the rights of both parties. It does not permit the lessor to recover damages immediately for future losses; it does not require the lessor to mitigate damages; and it does not protect the lessee from forfeiture.

RECOMMENDATION

The Law Revision Commission has concluded that the rules applicable to contracts generally would be fairer to both lessors and lessees than are the rules now applied when a lease is abandoned or otherwise terminated by reason of the lessee's breach. Accordingly, the Commission recommends the enactment of legislation designed to effectuate the following principles:

1. When a lease is abandoned or otherwise terminated by reason of the lessee's breach or repudiation of the lease, the lessor should have an immediate right to recover all of the damages caused by the lessee's default--past, present, and future. He should not be required to defer action until the end of the term and run the risk that the defaulting lessee will then be solvent and available.

2. The basic measure of the lessor's damages should be the loss of the bargain represented by the lease. He should be entitled to recover the difference between the remaining rentals provided in the lease and the fair rental value of the property for the remainder of the term. He should also be entitled to recover any incidental damages resulting from the lessee's default, such as expenses necessarily incurred. But, this should be the limit of his right to exact payment from the lessee. If the lessor chooses to let the property remain idle, he should not be permitted to recover from the lessee the entire remaining rental obligation, as he may do under existing law. Here, as under contract law generally, there should be no right to recover for any loss that is reasonably avoidable.

3. If a lessor relets property after termination of a lease by reason of the lessee's abandonment or other breach, the lessor should not forfeit his right to damages. On the contrary, he should be entitled to recover all reasonable expenses incurred in reletting the property in addition to his basic measure of damages. The rental provided in the new lease should be presumed to be the fair rental value of the property. Thus, the lessor should be entitled to recover the difference between the rentals called for in the old lease and the rentals called for in the new lease unless the defaulting lessee persuades the trier of fact that the reasonable rental value of the property is more than the new lease provides.

4. The validity of a reasonable liquidated damages provision in a lease should be recognized. The amount of the lessor's damage at the time of the abandonment or repudiation by the lessee may not be readily ascertainable; and in such a case, a fair liquidated damages provision should be as enforceable as it would be if contained in any other contract.

5. A defaulting lessee should be entitled to relief from a forfeiture regardless of the label attached to it by the provisions of the lease. A contract for the use of property should not be able to exact forfeitures to any greater extent than a contract for the sale of property.

6. When a lessor relets property after the original lease has been terminated, it should be clear that the reletting is for the lessor's own account, not for the lessee's. Of course, such a reletting should reduce the damages to which the lessor is entitled; but if any profit is made upon the reletting, that profit should belong to the lessor, not the defaulting lessee.

7. It should be clear that a lessor's right to damages for the loss of the remainder of the lease term does not impair his right to specific or preventive relief under the lease in any case where such a form of relief is otherwise appropriate. It should be clear also that a lessor's right to recover such damages is independent of his right to bring an action for unlawful detainer to recover the possession of the property, and that the damages recommended herein are recoverable in a separate action in addition to any damages recovered as part of the unlawful detainer action. Of course, the lessor should not be entitled to recover twice for the same items of damage.

8. Section 3308 of the Civil Code should be repealed. Enactment of legislation effectuating the other recommendations of the Commission would make Section 3308 superfluous.

9. Code of Civil Procedure Section 1174 should be amended to provide that the eviction of a lessee for breach of the lease terminates the lessee's interest in the property. Section 1174 now permits the eviction of a lessee without the termination of his interest in order to permit the lessor to preserve his right to damages. Under the statute recommended by the Commission, the lessor's right to damages does not depend upon the continuance of the lessee's estate, so the provisions of Section 1174 that provide for such continuance are no longer necessary.

PROPOSED LEGISLATION

The Commission's recommendations would be effectuated by enactment of the following measure:

An act to add Section 1936 to Chapter 1 of Title 5 of Part 4 of Division 3 of, to add Article 1.5 (commencing with Section 3320) to Chapter 2 of Title 2 of Part 1 of Division 4 of, and to repeal Section 3308 of, the Civil Code, and to amend Section 1174 of the Code of Civil Procedure, relating to leases.

The people of the State of California do enact as follows:

SECTION 1. Section 1936 is added to the Civil Code, to read:

1936. An abandonment by the lessee of the leased property is a breach of the lease and a repudiation of the remaining obligations of the lease. Repudiation of the obligations of the lease by either the lessor or lessee at or before the time for performance is a breach of the lease.

Comment. Except where a mining lease is involved (see Gold Mining & Water Co. v. Swinerton, 23 Cal.2d 19, 142 P.2d 22 (1943)), the California courts have not considered a lessee's abandonment of the leasehold or repudiation of the lease to be a breach of the lease. Oliver v. Loydon, 163 Cal. 124, 124 Pac. 731 (1912); Welcome v. Hess, 90 Cal. 507, 27 Pac. 369 (1891). Section 1936 is designed to overcome the holdings in these cases and to make the contractual doctrines of anticipatory breach and repudiation applicable to leases generally. Cf. 4 CORBIN, CONTRACTS §§ 954, 959-989 (1951). The damages a lessor may recover for such a breach are specified in Sections 3320-3328.

Under Section 1936, a lessor may bring an action against an abandoning or repudiating lessee immediately after the abandonment or repudiation. In such an action, he may recover not only the rentals that are due at the

time of the action but also the future rentals lost by reason of the lessee's default. The lessor cannot recover, however, for any losses he might reasonably avoid. See Sections 3320 and 3326 and the Comments thereto.

These sections thus nullify the existing rule that a lessor whose lessee has abandoned or repudiated the lease must choose between continuing to recognize the lessee's estate in the property or forfeiting all of his future rights under the lease. See Welcome v. Hess, supra.

SEC. 2. Article 1.5 (commencing with Section 3320) is added to Chapter 2 of Title 2 of Part 1 of Division 4 of the Civil Code, to read:

Article 1.5. Damages Upon Termination or Repudiation of Lease

Comment. This article sets forth in some detail the damages a lessor is entitled to recover when the lessee abandons the leased property or repudiates the lease or the lease is otherwise terminated by reason of the lessee's breach. The article also sets forth the lessee's rights to relief from any forfeiture of advance payments made to the lessor. The remainder of the article is designed to clarify the relationship between the right to damages arising under this article and the right to obtain other forms of relief under other provisions of California law.

§ 3320. Lessor's damages upon termination of a lease for breach, abandonment, or repudiation

3320. Subject to Section 3326, if a lease of real or personal property is terminated because of the lessee's breach thereof, or if the lessee abandons the leased property or otherwise repudiates the lease, the measure of the lessor's damages for such breach, abandonment, or repudiation is the sum of the following:

(a) The excess, if any, of the value of the rentals due or to become due under the lease for the remainder of the term over the reasonable rental value of the property for the same period. In determining the lessor's damages under this subdivision, the value of any rentals shall be computed as of the time when the lessor's damages are determined. Rental installments that are then due or overdue shall be taken at full value plus interest, and rental installments that are not then due shall be discounted.

(b) Any incidental damages provided in Section 3322.

Comment. Section 3320 prescribes the basic measure of the damages a lessor is entitled to recover when the lessee abandons the property or the lease is otherwise terminated by reason of the lessee's breach.

Under Section 3320, the lessor's damages are the excess of the unpaid rentals under the lease over the rentals the lessor can reasonably expect to obtain by reletting the property. In this context, "rentals" refers to all obligations the lessee undertakes in exchange for the use of the leased property. For example, if the defaulting lessee had promised to pay the taxes on the leased property and the lessor could not relet the property

under a lease containing such a provision, the loss of the defaulting lessee's assumption of the tax obligation would be included in the damages the lessor is entitled to recover under Section 3320.

The measure of damages described in Section 3320 is essentially that described in Civil Code Section 3308 (superseded by this article) as enacted in 1937. Section 3308's measure of damages is applicable, however, only when the lease so provides and the lessor chooses to invoke that remedy. The measure of damages described in Section 3320 is applicable in all cases. Hence, under this section, a lessor may not decline to relet the property and hold the original lessee for the entire remaining rental obligation as he is entitled to do under existing law. Under this section, as under the law relating to contracts generally, the defaulting lessee is not liable for any consequences that the lessor can reasonably avoid.

Section 3320 has been made subject to Section 3326 in order to make it clear that if the lessor relets the property for a rental in excess of the rental provided in the original lease, the damages the lessor is entitled to recover under Section 3320 must be reduced accordingly.

Under Section 3320, the value of the rentals due to the lessor under the original lease should be computed as of the time the lessor's damages are determined. If the dispute is litigated, the value is to be determined as of the time of the award; if the dispute is settled, the value is to be determined as of the time of settlement. If at the time of such determination some rental installments are then due or overdue, they should be taken at full value plus interest. Those that are not then due should be appropriately discounted to reflect their then value. The value of rentals due to the lessor under any new lease and the reasonable rental value of the property

should similarly be computed as of the time the lessor's damages are determined.

In addition to the basic measure of damages prescribed by Section 3320, the lessor is entitled to recover from the lessee certain incidental damages described in Section 3322. See the Comment to that section. And, if the lease so provides, the lessor may be entitled to recover his attorney's fees in addition. See Section 3324.

§ 3321. Rental upon reletting presumed to be reasonable rental value

3321. If leased real or personal property is relet following the termination of the original lease because of the lessee's breach thereof, or following the abandonment of the leased property or other repudiation of the lease by the lessee, the rental due to the lessor under the new lease is presumed to be the reasonable rental value of the property for the term covered by the new lease. This presumption is a presumption affecting the burden of proof and may be overcome only by proof that the reasonable rental value of the property is higher than the rental due under the new lease.

Comment. Under Section 3320, a lessor is entitled to recover from a defaulting lessee the excess of the value of the rentals which would have been due under the original lease for the remainder of the term over the reasonable rental value of the property for the same period. Section 3321 provides that the "reasonable rental value" of the property is presumptively fixed by the new lease when the lessor relets the property. The lessee may overcome the effect of this presumption by persuading the trier of fact that the reasonable rental value of the property is in fact higher than rental fixed by the new lease. But, if the trier of fact is not persuaded that the reasonable rental value of the property is higher than the new rental agreement, the lessor is entitled to recover under Section 3320 the excess of the rentals provided in the old lease over the rentals provided in the new lease.

Section 3321 limits the lessor's recovery under Section 3320(a) to the excess of the rentals provided in the old lease over the rentals provided in the new lease by prohibiting him from overcoming the presumption established

by this section with proof that the reasonable rental value of the property is lower than the rental fixed by the new lease. If the lessor relets the property at a rental in excess of its rental value, he has succeeded in mitigating the damages caused by the lessee's default and the amount he is entitled to recover from the lessee should be accordingly reduced. Section 3321 does not, however, prohibit the lessor from introducing evidence of a lower rental value in order to prevent the lessee from persuading the trier of fact that the reasonable rental value of the property is higher than is indicated by the new lease.

§ 3322. Lessor's incidental damages

3322. If a lease of real or personal property is terminated because of the lessee's breach thereof, or if the lessee abandons the leased property or otherwise repudiates the lease, the incidental damages to a lessor under this article are:

(a) The amount due to the lessor under the lease for any reasonable time allowed by the lessor to the lessee to retract the repudiation or cure the breach or needed by the lessor to relet the property.

(b) Any reasonable expenses incurred in retaking possession of the property.

(c) Any reasonable expenses incurred in caring for the property which would not have been incurred but for the lessee's breach, abandonment or repudiation.

(d) Any reasonable expenses incurred in reletting the property.

(e) Subject to Section 3324, any other damages necessary to compensate the lessor for all the detriment proximately caused by the lessee's breach, abandonment, or repudiation, or which in the ordinary course of things would be likely to result therefrom.

Comment. Section 3322 is included in this article in order to make it clear that the basic measure of damages described in Section 3320 is not the limit of a lessor's recoverable damages when the lessee abandons the leased property or the lease is otherwise terminated by reason of the lessee's breach.

When leased property is abandoned or the lease is otherwise terminated, it will usually be necessary for the lessor to take possession for a time in order to prepare the property for reletting and to secure a new tenant. A lessor must be entitled to recover the rentals due under the lease for this period if the damages awarded are to put him in as good a position as would performance by the lessee of his contractual obligations. The lessor should also be entitled to recover for his expenses in caring for the property during this time, for these are expenses that he would not have had to bear if the lessee had not abandoned the property or breached the lease.

In some cases, too, a lessor may wish to give a lessee an opportunity to retract his repudiation or cure his breach and resume his obligations under the lease. If the lessor does so and the lessee does not accept the opportunity to cure his default, the lessor should be entitled to recover the full amount of the rentals due under the lease for this period of negotiation as well as his expenses in caring for the property during this period.

In addition, Section 3322 provides that the lessor may recover for his expenses in retaking possession of the property, repairing damage caused by the lessee, and in reletting the property. There may be other damages necessary to compensate the lessor for all of the detriment proximately caused by the lessee, and if so, the lessor may recover them also. Subdivision (c), which is based on Civil Code Section 3300, provides that all of the other damages a person is entitled to recover for the breach of a contract may be recovered by a lessor for the breach of his lease. This would include, of course, damages for the lessee's breach of specific covenants of the lease.

Subdivision (f) is "subject to Section 3324" in order to make clear that the lessor's attorney's fees are not recoverable as incidental damages unless the lease specifically so provides.

§ 3323. Liquidated damages

3323. Notwithstanding Sections 3320, 3321, and 3322, upon any breach of the provisions of a lease of real or personal property, the lessor is entitled to recover liquidated damages if they are provided in the lease and meet the requirements of Sections 1670 and 1671.

Comment. Section 3323 does not create a right to recover liquidated damages, it merely recognizes that such a right may exist if the conditions specified in Civil Code Sections 1670 and 1671 are met. Liquidated damages provisions in leases have been held to be void. Jack v. Sinsheimer, 125 Cal. 563, 58 Pac. 130 (1899). Such holdings were proper so long as the lessor's cause of action upon abandonment of a lease was either for the rent as it came due or for the rental deficiencies as of the end of the lease term. Under such circumstances, there could be little prospective uncertainty over the amount of the lessor's damages. Under this article, however, the lessor's right to damages accrues at the time of the abandonment; and because they must be fixed before the end of the term, they may be difficult to calculate in some cases. This will frequently be the case if the property is leased under a percentage lease. It may be the case if the property is unique and its fair rental value cannot be ascertained with certainty. Accordingly, Section 3323 is included as a reminder that the cases holding that liquidated damages provisions in leases are void are no longer controlling, and in some cases such provisions may be valid.

§ 3324. Attorney's fees

3324. (a) In addition to any other relief to which the lessor or lessee is entitled by reason of the breach of a lease of real or personal property by the other party to the lease, the lessor or lessee may recover reasonable attorney's fees incurred in obtaining such relief if:

(1) The lease provides for the recovery of such fees; or

(2) The lease provides that the other party to the lease may recover attorney's fees incurred in obtaining relief for the breach of the lease.

(b) The right to recover attorney's fees as provided in paragraph (2) of subdivision (a) may not be waived prior to the accrual of such right.

Comment. Leases, like other contracts, sometimes provide that a party forced to resort to the courts for enforcement is entitled to a reasonable attorney's fee. Section 3324 makes it clear that the remaining sections in the article do not impair the lessor's rights under such a provision.

Paragraph (2) of subdivision (a) and subdivision (b) are included in the section to equalize the operation of leases that provide for the recovery of an attorney's fees. Most leases are drawn by one party to the transaction (usually the lessor), and the other seldom has sufficient bargaining power to require the inclusion of a provision for attorney's fees that works in his favor. Under Section 3324, if either party is entitled by a provision in the lease to recover attorney's fees, the other may recover such fees when he is forced to resort to the courts to enforce his rights under the lease. To prevent paragraph (2) of subdivision (a) from being nullified by standard waiver provisions in leases, subdivision (b) prohibits the waiver of a party's right to recover under that paragraph until the right actually accrues.

§ 3325. Lessee's relief from forfeiture

3325. If a lease of real or personal property is terminated because of the breach thereof by the lessee, or if the lessee abandons the leased property or otherwise repudiates the lease, the lessee may recover from the lessor any amount paid to the lessor in consideration for the lease (whether designated rental, bonus, consideration for execution thereof, or by any other term) that is in excess of (a) the portion of the total amount required to be paid to the lessor pursuant to the lease that is fairly allocable to the portion of the term prior to the termination, repudiation, or abandonment of the lease and (b) any damages to which the lessor is entitled by reason of such breach, repudiation, or abandonment. The right of a lessee to recover under this section may not be waived prior to the accrual of such right.

Comment. Section 3325 is designed to make the rules stated in Freedman v. The Rector, 37 Cal.2d 16, 230 P.2d 629 (1951), and Caplan v. Schroeder, 56 Cal.2d 515, 15 Cal. Rptr. 145, 364 P.2d 321 (1961), applicable to cases arising out of the breach of a lease. The Freedman case held that a wilfully defaulting vendee under a contract for the sale of real property may recover the excess of his part payments over the damages caused by his breach. The Caplan case held that a wilfully defaulting vendee could recover such an advance payment even though the contract recited that the advance payment was in consideration for the execution of the contract. The court looked beyond the recital and found that there was in fact no separate consideration for the advance payment aside from the sale of the property itself.

Similarly, Section 3325 will permit a lessee to recover advance payments, regardless of how they are designated in the lease, if the court finds that such payments are in fact in consideration for the lease and are in excess of the damages suffered by the lessor as a result of the lessee's breach.

The last sentence of Section 3325 is probably unnecessary. The Freedman and Caplan cases are based on the provisions of the code prohibiting forfeitures. These rules are applied despite contrary provisions in contracts. Nonetheless, the sentence is included to make it clear that the provisions of this section may not be avoided by the addition to leases of provisions waiving rights under this section.

§ 3326. Lessor's benefits on reletting

3326. When a lease of real or personal property is terminated by reason of the lessee's breach thereof, or when the lessee abandons the leased property or otherwise repudiates the lease, and the lessor relets the property, the lessor is not accountable to the lessee for any profit made on the reletting, but any such profit shall be set off against the damages to which the lessor is otherwise entitled.

Comment. Under existing law, a lessor may relet property after the original lessee has abandoned the lease if he does so either on his own account (in which case the lessee's rental obligation is terminated) or for the account of the lessee. See discussion in Dorcich v. Time Oil Co., 103 Cal. App.2d 677, 685, 230 P.2d 10 (1951). Although no case has yet arisen so holding, the rationale of the California cases indicates that if the lessor receives a higher rental upon the reletting than was required by the original lease, the lessee is entitled to the profit.

Under Section 3326, a lessor who relets property after the original lessee has abandoned it does so for his own account. Any profit received is the lessor's, it does not belong to the defaulting lessee. Profit received on the reletting, however, reduces the damages suffered by the lessor for which the lessee is liable.

The rule stated in Section 3326 is similar to the rule applicable when the buyer under a sales contract repudiates the sale and the seller resells the goods to mitigate damages. See COMM. CODE § 2706(6).

§ 3327. Specific or preventive relief

3327. Nothing in this article affects the right to obtain specific or preventive relief if the damages specified in this article are inadequate and specific or preventive relief is otherwise appropriate.

Comment. This article sets forth the damages to which a lessor is entitled when his lessee abandons the leased property or the lease is otherwise terminated by reason of the lessee's breach. Section 3327 is designed to indicate merely that the lessor's right to damages is not his exclusive remedy. In appropriate cases, specific or preventive relief may be granted where the remedy in damages is inadequate.

§ 3328. Unlawful detainer actions

3328. (a) Nothing in this article affects the provisions of Chapter 4 (commencing with Section 1159) of Title 3 of Part 3 of the of the Code of Civil Procedure, relating to actions for unlawful detainer, forcible entry, and forcible detainer.

(b) The bringing of an action under the provisions of Chapter 4 (commencing with Section 1159) of Title 3 of Part 3 of the Code of Civil Procedure does not affect the right to bring a separate action to recover the damages specified in this article; but there shall be no recovery of damages in the subsequent action for any detriment for which damages were awarded in the previous action.

Comment. Section 3328 is designed to clarify the relationship between this article and the chapter of the Code of Civil Procedure relating to actions for unlawful detainer, forcible entry, and forcible detainer. The actions provided for in the Code of Civil Procedure are designed to provide a summary method of recovering possession of property. Those actions may be used by a lessor whose defaulting lessee refuses to vacate the property after termination of the lease.

Section 3328 provides that the fact that a lessor has recovered possession of the property by an unlawful detainer action does not preclude the bringing of a later action to recover the damages to which he is entitled under this article. Some of the incidental damages to which the lessor is entitled may be recovered in either the unlawful detainer action or in an action to recover the damages specified here. Under Section 3328, such damages may be recovered in either action; but the lessor is entitled to recover but once for any particular detriment.

SEC. 2. Section 3308 of the Civil Code is repealed.

~~3308.--The-parties-to-any-lease-of-real-or-personal-property-may-agree therein-that-if-such-lease-shall-be-terminated-by-the-lessor-by-reason-of-any breach-thereof-by-the-lessee,-the-lessor-shall-thereupon-be-entitled-to-recover from-the-lessee-the-worth-at-the-time-of-such-termination,-of-the-excess,-if any,-of-the-amount-of-rent-and-charges-equivalent-to-rent-reserved-in-the lease--for-the-balance-of-the-stated-term-or-any-shorter-period-of-time-over the-then-reasonable-rental-value-of-the-premises-for-the-same-period.~~

~~The-rights-of-the-lessor-under-such-agreement-shall-be-cumulative-to-all other-rights-or-remedies--now-or-hereafter-given-to-the-lessor-by-law-or-by the-terms-of-the-lease;-provided,-however,-that-the-election-of-the-lessor-to exercise-the-remedy-hereinabove-permitted-shall-be-binding-upon-him-and exclude-recourse-thereafter-to-any-other-remedy-for-rental-or-charges-equivalent to-rental-or-damages-for-breach-of-the-covenant-to-pay-such-rent-or-charges accruing-subsequent-to-the-time-of-such-termination.--The-parties-to-such lease-may-further-agree-therein-that-unless-the--remedy-provided-by-this section-is-exercised-by-the-lessor-within-a-specified-time-the-right-thereto shall-be-barred:~~

Comment. Section 3308 is repealed because the remainder of the statute akes it unnecessary. The remedy that Section 3308 states may be provided in a ease is made the general rule, whether or not provided in the lease, under the rovisions of the remainder of the statute.

SEC. 3. Section 1174 of the Code of Civil Procedure is amended to read:

1174. If upon the trial, the verdict of the jury, or, if the case be tried without a jury, the findings of the court be in favor of the plaintiff and against the defendant, judgment shall be entered for the restitution of the premises; and if the proceedings be for an unlawful detainer after neglect, or failure to perform the conditions or covenants of the lease or agreement under which the property is held, or after default in the payment of rent, the judgment shall also declare the forfeiture of such lease or agreement ~~if the notice required by Section 1161 of the code states the election of the landlord to declare the forfeiture thereof, but if such notice does not so state such election, the lease or agreement shall not be forfeited~~.

The jury or the court, if the proceedings be tried without a jury, shall also assess the damages occasioned to the plaintiff by any forcible entry, or by any forcible or unlawful detainer, alleged in the complaint and proved on the trial, and find the amount of any rent due, if the alleged unlawful detainer be after default in the payment of rent. Judgment against the defendant guilty of the forcible entry, or the forcible or unlawful detainer, may be entered in the discretion of the court either for the amount of the damages and the rent found due, or for three times the amount so found.

When the proceeding is for an unlawful detainer after default in the payment of rent, and the lease or agreement under which the rent is payable has not by its terms expired, and the notice required by Section 1161 has not stated the election of the landlord to declare the forfeiture thereof, the court may, and, if the lease or agreement is in

writing, is for a term of more than one year, and does not contain a forfeiture clause, shall order that execution upon the judgment shall not be issued until the expiration of five days after the entry of the judgment, within which time the tenant, or any subtenant, or any mortgagee of the term, or any other party interested in its continuance, may pay into the court, for the landlord, the amount found due as rent, with interest thereon, and the amount of the damages found by the jury or the court for the unlawful detainer, and the costs of the proceedings, and thereupon the judgment shall be satisfied and the tenant be restored to his estate.

But if payment as here provided be not made within five days, the judgment may be enforced for its full amount, and for the possession of the premises. In all other cases the judgment may be enforced immediately.

Comment. The language deleted from Section 1174 was added to permit a lessor to evict a defaulting lessee and relet the premises without forfeiting his right to look to the lessee for any resulting deficiencies in the accruing rentals. Under the pre-existing law, a lessor whose lessee defaulted in the payment of rent had to choose between suing the lessee from time to time to collect the accruing rentals and completely terminating the lease and the lessee's obligation to pay any more rent. Costello v. Martin Bros., 74 Cal. App. 782, 786, 241 Pac. 588 (1925).

Inasmuch as Civil Code Sections 3320-3328 permit a lessor to terminate a lease without forfeiting his right to damages for the loss of the future rentals due under the lease, the deleted language is no longer necessary.

Revised May 15, 1966

STATE OF CALIFORNIA

CALIFORNIA LAW REVISION COMMISSION

TENTATIVE RECOMMENDATION

relating to

THE RIGHTS AND DUTIES ATTENDANT UPON ABANDONMENT OR TERMINATION OF A LEASE

California Law Revision Commission
30 Crothers Hall
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Revised May 15, 1966

TENTATIVE RECOMMENDATION OF THE CALIFORNIA LAW REVISION COMMISSION

relating to

THE RIGHTS AND DUTIES ATTENDANT UPON

ABANDONMENT OR TERMINATION OF A LEASE

BACKGROUND

Section 1925 of the Civil Code provides, in effect, that a lease is a contract. Historically, however, a lease was regarded as a conveyance of an interest in land. 2 POWELL, REAL PROPERTY ¶ 221 (1950). The California courts state that a lease is both a contract and a conveyance. Medico-Dental Bldg. Co. v. Horton & Converse, 21 Cal.2d 411, 132 P.2d 457 (1942); Beckett v. City of Paris Dry Goods Co., 14 Cal.2d 633, 96 P.2d 122 (1939). But while at times the courts apply principles of contract law in determining the rights and duties attendant upon abandonment or termination of a lease (see, e.g., Medico-Dental Bldg. Co. v. Horton & Converse, supra), the courts seem to be guided principally by common law property concepts in determining these rights and duties (see, e.g., Kulawitz v. Pacific Woodenware & Paper Co., 25 Cal.2d 664, 155 P.2d 24 (1944); Welcome v. Hess, 90 Cal. 507, 25 Pac. 369 (1891)). See, generally, The California Lease--Contract or Conveyance? 4 STAN. L. REV. 244 (1952).

As a result of the clash of contract and conveyance concepts the present law does not afford adequate relief to either lessors or lessees when the leasehold is abandoned or the lease is otherwise terminated because of the lessee's breach. Under existing law, a lessor is sometimes precluded from recovering damages for all of the detriment caused by the defaulting lessee, and a defaulting lessee is sometimes subjected to forfeitures that are not countenanced under the law relating to contracts generally. See 26 CALIF. L. REV. 385 (1938).

For example, under the law applicable to most contracts, repudiation constitutes a total breach for which an action can be maintained even though the time for full performance has not yet elapsed. Gold Mining & Water Co. v. Swinerton, 23 Cal.2d 19, 142 P.2d 22 (1943); Remy v. Olds, 88 Cal. 537, 26 Pac. 255 (1891). And, under the law applicable to most contracts, a material breach by the promisor gives rise to a duty on the part of the promisee to mitigate damages, i.e., the promisee cannot recover damages for any detriment that is reasonably avoidable. See discussion in Bomberger v. McKelvey, 35 Cal.2d 607, 613-615, 220 P.2d 729 (1950). In contrast, when a lessee repudiates or breaches a lease, the courts have held that the lessor must choose among forfeiting his right to damages for future injury, enhancing the damages by continuing performance, and deferring recovery of his damages until the end of the term. Kulawitz v. Pacific Woodenware & Paper Co., 25 Cal.2d 664, 671, 155 P.2d 24, 28 (1944); Treff v. Gulko, 214 Cal. 591, 7 P.2d 697 (1932).

Except where a mining lease is involved (see Gold Mining & Water Co. v. Swinerton, supra), the doctrine of anticipatory breach has not been applied to leases. Oliver v. Loydon, 163 Cal. 124, 124 Pac. 731 (1912); Welcome v. Hess, 90 Cal. 507, 27 Pac. 369 (1891); In re Bell, 85 Cal. 119, 24 Pac. 633 (1890). Under existing law, when a lessee abandons the leased property and repudiates the remaining obligations of the lease, his actions constitute merely an offer to surrender the remainder of the term. Welcome v. Hess, 90 Cal. 507, 513, 27 Pac. 369, 370 (1891). Confronted with such an offer, the lessor has three courses of action among which he may choose. Kulawitz v. Pacific Woodenware & Paper Co., 25 Cal.2d 664, 671, 155 P.2d 24, 28 (1944). First, he may decline the lessee's offer to surrender and sue for the

unpaid rent as it becomes due for the remainder of the term. If the lessor selects this course of action, he has no duty to nitigate damages by reletting the property; he can recover the full amount of the rent while permitting the property to remain vacant. See De Hart v. Allen, 26 Cal.2d 829, 832, 161 P.2d 453, 455 (1945). Second, he may accept the lessee's offer to surrender and thus extinguish the lease. This course of action not only terminates the lessee's interest in the property, it also terminates the lessee's obligation to pay any further rent, and the lessor is not entitled to any damages for the loss of the bargain represented by the original lease. Welcome v. Hess, 90 Cal. 507, 27 Pac. 369 (1891). The cases make clear, too, that any action taken by the lessor that is inconsistent with the lessee's continued ownership of an estate in the leased property will be deemed an acceptance of the lessee's offer to surrender, whether the lessor intended such an acceptance or not. Dorcich v. Time Oil Co., 103 Cal. App.2d 677, 230 P.2d 10 (1951). Finally, if the lessor notifies the lessee of his intention to do so, the lessor may relet the property for the benefit of the lessee and recover damages in the amount of the excess of the rentals called for in the original lease over the rentals obtained by reletting. The lessor cannot sue immediately to recover these damages; the cause of action does not accrue until the end of the term, and the lessor must wait until that time and then sue for all of the rental deficiencies. Treff v. Gulko, 214 Cal. 591, 7 P.2d 697 (1932). The courts have held that prior notification

to the lessee is essential to this course of action and that without such notification the lessor's reletting of the property will terminate the original lease and the lessee's rental obligation. Dorcich v. Time Oil Co., 103 Cal. App.2d 677, 230 P.2d 10 (1951). Apparently, then, this third course of action is unavailable to a lessor who is unable to give proper notice to the defaulting lessee. Such a lessor must choose between permitting the property to remain vacant (thus preserving the lessee's rental obligation) and terminating the lessee's remaining obligation by resuming possession or by reletting the property.

A similar range of choices confronts a lessor when a lessee commits a sufficiently substantial breach of the lease to warrant termination thereof. He may treat the breach as a partial breach, decline to terminate the lease, and sue for the damages caused by the particular breach. In such a case, the lessor must continue to deal with a lessee who has proven to be unsatisfactory. The lessor may also terminate the lease and force the lessee to relinquish the property, resorting to an action for unlawful detainer to recover the possession of the property if necessary. If the lease is terminated, the lessor's right to the remaining rentals due under the lease ceases upon the termination of the lease. Costello v. Martin Bros., 74 Cal. App. 782, 241 Pac. 588 (1925). Under some circumstances, the lessor may decline to terminate the lease but still evict the lessee and relet the property for the account of the lessee. Lawrence Barker, Inc. v. Briggs, 39 Cal.2d 654, 248 P.2d 897 (1952); Burke v. Norton, 42 Cal. App. 705, 184 Pac. 45 (1919). See CODE CIV. PROC. § 1174. But in such a case, it may be that any profit made on the reletting belongs to the lessee, not the lessor, inasmuch as the lessee's interest in the property theoretically continues. Moreover, the lessor must be careful in utilizing

this remedy or he will find that he has forfeited his right to the remaining rentals from the original lessee despite his lack of intent to do so. See, e.g., Neuhaus v. Norgard, 140 Cal. App. 735, 35 P.2d 1039 (1934); A. H. Busch Co. v. Strauss, 103 Cal. App. 647, 284 Pac. 966 (1930).

Bound by common law property concepts, the courts have considered the lessee's obligation to pay rent as dependent on the continued existence of the term. When the term is ended, whether voluntarily by abandonment and repossession by the lessor or involuntarily under the compulsion of an unlawful detainer proceeding, the rental obligation dependent thereon also ends. Because the lessor usually cannot expect the lessee to remain available and solvent until the end of the term, continued adherence to these property concepts frequently denies the lessor any effective remedy for the loss caused by a defaulting lessee.

Adherence to ancient common law property concepts in the interpretation of leases has caused hardship to lessees as well as to lessors. Under the existing law, lessees may be subjected to forfeitures that would not be permitted under any other kind of contract. Although the courts have been quick to hold that

provisions in leases for liquidated damages are void (Jack v. Sinsheimer, 125 Cal. 563, 58 Pac. 130 (1899)), and although provisions for the acceleration of the unpaid rental installments have been held invalid (Ricker v. Rombough, 120 Cal. App.2d Supp. 912, 261 P.2d 328 (1953)), other provisions that are substantively indistinguishable have been held valid. Joffe, Remedies of California Landlord upon Abandonment by Lessee, 35 SO. CAL. L. REV. 34, 44 (1961); note, 26 CAL. L. REV. 385, 388 (1938). Thus, if a lessee's advance payment to the lessor is designated as an advance payment of rental or "in consideration for the execution of the lease," the lessor is entitled to keep the payment regardless of his actual damages when the lease is terminated by reason of the lessee's breach. A-1 Garage v. Lange Investment Co., 6 Cal. App.2d 593, 44 P.2d 681 (1935); Curtis v. Arnold, 43 Cal. App. 97, 184 Pac. 510 (1919); Ramish v. Workman, 33 Cal. App. 19, 164 Pac. 26 (1917).

In contrast, where the buyer repudiates a contract for the sale of real property, any advance payments made to the seller in excess of his actual damages are recoverable by the buyer. Freedman v. The Rector, 37 Cal.2d 16, 230 P.2d 629 (1951). Moreover, even though a contract for the sale of property recites that an initial payment is in "consideration for entering into the agreement," the courts permit the buyer to recover so much of the payment as exceeds the seller's damages if, in the light of the entire transaction, there was in fact no separate consideration supporting the payment. Caplan v. Schroeder, 56 Cal.2d 515, 15 Cal. Rptr. 145, 364 P.2d 321 (1961).

In 1937, Civil Code Section 3308 was enacted in an effort to ameliorate

the deficiencies in the law relating to leases. The effort, however, was only partially successful. Under Section 3308, if a lease so provides, the lessor may bring an action for damages immediately upon termination of the lease by reason of the lessee's abandonment or breach of the lease. The lessor's damages in such an action amount to the excess of the worth of the remainder of the term over the then reasonable rental value of the remainder of the term. Section 3308, however, does not apply unless it is made applicable by a provision in the lease; it does not require the lessor to resort to the remedy provided (and thus require mitigation of damages); and it does not relieve a lessee from forfeiture.

Code of Civil Procedure Section 1174 has also been amended in an effort to alleviate the problems faced by a lessor when the lessee refuses to pay rent or otherwise breaches the lease. Section 1174 provides that the lessor may notify the lessee to quit the premises and that such a notice does not terminate the leasehold interest unless the notice so specifies. This permits a lessor to evict the lessee, relet the property to another, and recover from the lessee at the end of the term for any deficiency in the rentals. But again, the statutory remedy falls short of providing full protection to the rights of both parties. It does not permit the lessor to recover damages immediately for future losses; it does not require the lessor to mitigate damages; and it does not protect the lessee from forfeiture.

RECOMMENDATION

The Law Revision Commission has concluded that the rules applicable to contracts generally would be fairer to both lessors and lessees than are the rules now applied when a lease is abandoned or is terminated by reason of the lessee's breach. Accordingly, the Commission recommends the enactment of legislation designed to effectuate the following principles:

1. Repudiation of a lease, like repudiation of any other contract, should be a breach of the lease and give rise immediately to remedial rights on the part of the aggrieved party. It should be clear that an abandonment of the lease by the lessee is a repudiation of the lease, and to facilitate determination of when an abandonment has occurred, the law should specify that vacating the leased property together with nonpayment of two successive rental installments amounts to a repudiation.

2. When a lease has been repudiated or breached in a material respect, the aggrieved party should have the right to resort to the usual contract remedies that are available upon a breach of any other contract. The aggrieved party should have the right to rescind the lease, terminate the lease for purposes of performance and sue for any damages caused, or sue for specific or preventive relief if the remedy of damages is not adequate. Moreover, it should be clear that a repudiation excuses the aggrieved party from further compliance with his obligations under the lease.

3. The party repudiating his obligations under a lease should have the right, as he does under contracts generally, to retract his repudiation and thus nullify its effect at any time before the aggrieved party has brought action upon the repudiation or otherwise changed in his position in reliance thereon.

4. When a lease has been repudiated or breached in a material respect, the aggrieved party should have an immediate right to recover all of the damages caused by the other's default--both past and prospective. When the lessee abandons the property, the lessor should not be required to defer action until the end of the term and run the risk that the defaulting lessee will then be solvent and available.

5. The basic measure of the damages for breach of a lease should be the loss of the bargain represented by the lease. The aggrieved party should be entitled to recover the difference between the remaining rentals provided in the lease and the fair rental value of the property for the remainder of the term. He should also be entitled to recover any incidental damages resulting from the breach, such as expenses necessarily incurred or lost profits. But, this should be the limit of his right to exact payment from the defaulting party. Thus, if the lessor chooses to let the property remain idle, he should not be permitted to recover from the lessee the entire remaining rental obligation, as he may do under existing law. Here, as under contract law generally, there should be no right to recover for any loss that is reasonably avoidable.

6. If a lessor relets property after termination of a lease by reason of its breach, the rental provided in the new lease should be presumed to be the fair rental value of the property. Thus, if the lessee abandons the lease and the lessor relets the property, the lessor should be entitled to recover the difference between the rentals called for in the old lease and the rentals called for in the new lease unless the defaulting lessee persuades the trier of fact that the reasonable rental value of the property is actually more than the new lease provides.

7. The validity of a reasonable liquidated damages provision in a lease should be recognized. The amount of the prospective damage that may be caused by a particular breach may not be readily ascertainable, and in such a case, a fair liquidated damages provision should be as enforceable as it would be if contained in any other contract.

8. A defaulting lessee should be entitled to relief from a forfeiture regardless of the label attached to it by the provisions of the lease. A

contract for the use of property should not be able to exact forfeitures to any greater extent than a contract for the sale of property.

9. When a lessor relets property after the original lease has been terminated, it should be clear that the reletting is for the lessor's own account, not for the lessee's. Of course, such a reletting should reduce the damages to which the lessor is entitled; but if any profit is made upon the reletting, that profit should belong to the lessor, not the defaulting lessee.

10. It should be clear that a lessor's right to recover damages is independent of his right to bring an action for unlawful detainer to recover the possession of the property, and that the damages recommended herein are recoverable in a separate action in addition to any damages recovered as part of the unlawful detainer action. Of course, the lessor should not be entitled to recover twice for the same items of damage.

11. Section 3308 of the Civil Code should be repealed. Enactment of legislation effectuating the other recommendations of the Commission would make Section 3308 superfluous.

12. Code of Civil Procedure Section 1174 should be amended to provide that the eviction of a lessee for breach of the lease terminates the lessee's interest in the property. Section 1174 now permits the eviction of a lessee without the termination of his interest in order to permit the lessor to preserve his right to damages. Under the statute recommended by the Commission, the lessor's right to damages does not depend upon the continuance of the lessee's estate, so the provisions of Section 1174 that provide for such continuance are no longer necessary.

13. If a lease is part of a lease-purchase agreement, it should be clear that the lessee's obligation under the lease is specifically enforceable and that he may not, by abandoning the lease, leave the lessor with only the right to recover damages measured by the difference between the consideration specified in the lease and the fair rental value of the property. Lease-purchase agreements frequently contemplate that the rental specified will also compensate the lessor for the improvement that he has agreed to transfer to the lessee at the end of the term. It is necessary, therefore, that the parties understand that the lessee's obligation to pay the full amount of the consideration specified in the lease may not be defeated by his own act of abandoning the leased property.

PROPOSED LEGISLATION

The Commission's recommendations would be effectuated by enactment of the following measure:

An act to add Sections 1951, 1951.5, 1952, 1952.5, 1953, 1953.5, 1954, and 1954.5 to Chapter 2 of Title 5 of Part 4 of Division 3 of, to add Article 1.5 (commencing with Section 3320) to Chapter 2 of Title 2 of Part 1 of Division 4 of, to add Section 3387.5 to, and to repeal Section 3308 of, the Civil Code, and to amend Section 1174 of the Code of Civil Procedure, relating to leases.

The people of the State of California do enact as follows:

SECTION 1. Section 1951 is added to Chapter 2 of Title 5 of Part 4 of Division 3 of the Civil Code, to read:

1951. A lease of real property is repudiated by either the lessor or the lessee when he, without justification:

(a) Communicates to the other party by word or act that he either will not or cannot perform his remaining obligations under the lease;

(b) Does any act which renders substantial performance of his obligations under the lease impossible or apparently impossible;

(c) In the case of a lessee, vacates the leased property and fails to pay two successive rental installments; or

(d) In the case of a lessor, evicts the lessee from the leased property.

Comment. Section 1951 is definitional. The substantive effect of a repudiation as defined in Section 1951 is described in the following sections.

Subdivisions (a) and (b) follow the definition of an anticipatory repudiation that appears in the Restatement of Contracts, Section 318. Because it is sometimes difficult for a lessor to determine whether a lessee

actually intends to assert any further interest in the leased property when the lessee merely moves from the premises and fails to pay rent, subdivision (c) provides an arbitrary rule that vacating the leased property together with nonpayment of two successive rental installments amounts to a repudiation.

Subdivision (d) refers to an eviction "without justification." This refers to an eviction that the lessor did not have a right to make under the terms of the lease or under the substantive law governing the rights of lessors and lessees generally. If the lessor had the right to evict the lessee, the lease is terminated by the eviction under the provisions of Section 1952.

SEC. 2. Section 1951.5 is added to said chapter, to read:

1951.5. (a) A lease of real property is abandoned by a lessee when he repudiates the lease and vacates the leased property.

(b) If a lessee abandons a lease of real property, the lessor may enter and take possession thereof without legal process.

Comment. Subdivision (a) of Section 1951.5 is definitional. The substantive effect of an abandonment is described in subdivision (b) and the following sections.

If a lessor mistakenly believes that the lessee has abandoned the leased property and retakes possession thereof without legal process, he may be liable in damages for forcible entry and detainer. Section 1951.5 and Section 1951(c) are designed to protect a lessor from the risk of wrongly deciding that the lessee has abandoned the property. Under these sections, the vacating of the property by the lessee coupled with his nonpayment of two successive rental installments amounts to an abandonment as a matter of law. Thereafter, the lessor may take possession of the property pursuant to subdivision (b) of Section 1951.5 without fear of liability for forcible entry and detainer.

SEC. 3. Section 1952 is added to said chapter, to read:

1952. A lease of real property is terminated prior to the expiration of the term when:

(a) The lessor, with justification, evicts the lessee from the property;

(b) The lessee vacates the property pursuant to a notice served pursuant to Sections 1161 and 1162 of the Code of Civil Procedure or pursuant to any other notice or request to vacate the property; or

(c) The lessee abandons the lease and the lessor retakes possession of the property unless such possession is taken for the sole purpose of preventing injury to or deterioration of the property.

Comment. Section 1952 prescribes certain conditions under which a lease is terminated prior to the end of the term. The list is not exclusive. Section 1933 also sets forth certain conditions under which a lease is terminated. And, of course, if a lease is rescinded pursuant to Sections 1688-1693, the interests of the respective parties come to an end prior to the expiration of the term of the lease.

Subdivisions (a) and (b) change the California law. Under Code of Civil Procedure Section 1174 (as amended in 1931), a lessee could be evicted from the leased property without terminating the lease. Presumably that provision was designed to overcome such cases as Costello v. Martin Bros., 74 Cal. App. 782, 241 Pac. 588 (1925), which held that the eviction of the lessee terminated the lease and ended the lessor's right to recover either the remaining rentals due under the lease or damages for the loss of such rentals. Because Section 1953.5 provides for the recovery of damages despite the termination of the lease and the eviction of the lessee, there is no further need to continue the fiction that the leasehold estate continues when the lessee has no right to the possession of the leased property.

Under subdivision (c), a lease is not automatically terminated by the lessee's abandonment. The lessor may want to require the lessee to perform the remainder of his obligations under the lease and, if so, he may bring an action to obtain a decree of specific performance. See Section 1953.5(c). But if the lease is not specifically enforceable either because damages would provide the lessor with an adequate remedy or because the lessee has an equitable defense (such as laches) to an action for specific performance, the lessor must rely on one of the two remedies based on termination of the lease--damages or rescission--specified in Section 1953.5.

SEC. 4. Section 1952.5 is added to said chapter, to read:

1952.5. Repudiation of a lease of real property is a breach of the lease and excuses further performance of the obligations of the lease by the other party to the lease.

Comment. Except where a mining lease is involved (see Gold Mining & Water Co. v. Swinerton, 23 Cal.2d 19, 142 P.2d 22 (1943)), the California courts have not applied the contractual doctrine of anticipatory repudiation to a lessee's abandonment of the leasehold or repudiation of the lease. See Oliver v. Loydon, 163 Cal. 124, 124 Pac. 731 (1912); Welcome v. Hess, 90 Cal. 507, 27 Pac. 369 (1891). Section 1952.5 is designed to overcome the holdings in these cases and to make the contractual doctrines of anticipatory breach and repudiation applicable to leases generally. Cf. 4 CORBIN, CONTRACTS §§ 954, 959-989 (1951).

In accordance with the law relating to the anticipatory repudiation of contracts generally, Section 1952.5 also provides that a repudiation excuses further performance of the lease by the other party. See RESTATEMENT, CONTRACTS § 280; 4 CORBIN, CONTRACTS § 977, p. 920 (1951). In this regard, Section 1952.5 changes the California law as stated in Kulawitz v. Pacific Woodenware & Paper Co., 25 Cal.2d 664, 155 P.2d 24 (1944), which held that a lessee's vacating of the leased property together with his failure to pay the rent did not excuse the lessor from compliance with a covenant not to permit a competing business to occupy the adjoining premises.

Section 1952.5 merely declares that a repudiation of a lease excuses further performance by the other party. It does not affect any rules that have developed concerning what other kinds of conduct may excuse further performance. Thus, Section 1952.5 will have no effect on the holding in Medico-Dental Building Co. v. Horton & Converse, 21 Cal.2d 411, 132 P.2d 457 (1942), which held that a lessor's breach of a covenant not to permit a competing business to operate in the same building with the lessee excused the lessee from further performance of his obligations under the lease.

SEC. 5. Section 1953 is added to said chapter, to read:

1953. The effect of a repudiation of a lease of real property is nullified if (before the other party has rescinded or terminated the lease, brought an action for damages caused by the repudiation, or otherwise changed his position in reliance on the repudiation) the repudiator:

(a) Indicates clearly to the other party that the repudiator intends and is able to perform his remaining obligations under the lease; and

(b) In a case where the repudiation consisted of acts rendering substantial performance impossible or apparently impossible, changes his position to enable his performance of his remaining obligations under the lease.

Comment. Section 1953 codifies the rule applicable to contracts generally that a party who repudiates a contract may retract his repudiation, and thus nullify its effect, if he does so before the other party to the contract has materially changed his position in reliance on the repudiation. RESTATEMENT, CONTRACTS §§ 280, 319; 4 CORBIN, CONTRACTS § 980 (1951).

SEC. 6. Section 1953.5 is added to said chapter, to read:

1953.5. When a party repudiates a lease of real property or otherwise breaches the lease in a material respect, the other party may:

(a) Rescind the lease in accordance with Chapter 2 (commencing with Section 1688) of Title 5 of Part 2 of Division 3;

(b) Terminate the lease and recover damages in accordance with Article 1.5 (commencing with Section 3320) of Chapter 2 of Title 2 of Part 1 of Division 4; or

(c) Obtain specific or preventive relief in accordance with Title 3 (commencing with Section 3366) of Part 1 of Division 4 to enforce the provisions of the lease if damages would provide inadequate relief and specific or preventive relief is otherwise appropriate.

Comment. Under existing California law, when a lessee abandons the leased property and repudiates the lease, the lessor has three alternative remedies: (1) to consider the lease as still in existence and sue for the unpaid rent as it becomes due for the unexpired portion of the term; (2) to consider the lease as terminated and retake possession for his own account; or (3) to retake possession for the lessee's account and relet the premises, holding the lessee for the difference between the lease rentals and what the lessor is able in good faith to procure by reletting. Kulawitz v. Pacific Woodenware & Paper Co., 25 Cal.2d 664, 671, 155 P.2d 24, 28 (1944).

Similar alternatives are available to a lessor when the lessee commits a sufficiently material breach of the lease to warrant eviction. The lessor may simply decline to evict the lessee and sue for the damages caused by the particular breach. See, e.g., Richards v. Silveira, 97 Cal. App. 166, 275 Pac. 478 (1929). The lessor may terminate the lease, evict the lessee, and

retake possession for his own account. Costello v. Martin Bros., 74 Cal. App. 782, 241 Pac. 588 (1925). And, the lessor may evict the lessee, relet the property for the account of the lessee, and hold the lessee liable for any deficiencies resulting from the reletting. Cf. CODE CIV. PROC. § 1174. See Lawrence Barker, Inc. v. Briggs, 39 Cal.2d 654, 248 P.2d 897 (1952).

Section 1953.5 substitutes for these remedies the remedies specified in the section. Under Section 1953.5, a lessor will not be able to let the property remain vacant and to sue for the unpaid rent as it becomes due, for Section 3322 provides that a party to a lease that has been breached cannot recover for any detriment caused by such breach that could have been avoided through the exercise of reasonable diligence. A lessor will, however, be able to rescind the lease under subdivision (a) or terminate the lease under subdivision (b) and, in either event, recover the possession of the property. Damages for the loss of the remainder of the lease are recoverable even though the lease is terminated. And, in those cases where damages for breach of the lease would not be an adequate remedy, the lessor may obtain specific enforcement of the provisions of the lease.

The remedies specified in Section 1953.5 may also be used by a lessee when the lessor breaches the lease, but in this respect Section 1953.5 merely continues the preexisting law without significant change. Fong v. Rossi, 87 Cal. App.2d 20, 195 P.2d 854 (1948)(lessee entitled to rescind and recover prepaid rent); Beckett v. City of Paris Dry Goods Co., 14 Cal.2d 633, 96 P.2d 122 (1939)(lessee may recover damages for loss of profits and loss of good will); Penilla v. Gerstenkorn, 86 Cal. App. 668, 261 Pac. 488 (1927)(lessee may obtain specific enforcement of agreement to lease).

SEC. 7. Section 1954 is added to said chapter, to read:

1954. The time for the commencement of an action based on the repudiation of a lease begins to run:

(a) If the repudiation occurs before any failure of the repudiator to perform his obligations under the lease, at the time of the repudiator's first failure to perform the obligations of the lease.

(b) If the repudiation occurs at the same time as, or after, a failure of the repudiator to perform his obligations under the lease, at the time of the repudiation.

Comment. Section 1954 clarifies the time the statute of limitations begins to run on a cause of action for repudiation of a lease. The rule stated is based on Section 322 of the Restatement of Contracts. Under the preexisting California law, the statute of limitations did not begin to run until the end of the lease term. See De Hart v. Allen, 26 Cal.2d 829, 161 P.2d 453 (1945).

SEC. 8. Section 1954.5 is added to said chapter, to read:

1954.5.(a) Whenever a lessor of real property finds personal property remaining upon the leased property following the termination of the lease and the lessor knows or has reason to believe that the personal property belongs to the former lessee, the lessor shall give written notice of such finding to the former lessee. Such notice shall be given by mail addressed to the former lessee at his post-office address, if known, and if not known, such notification shall be addressed to the former lessee at the location of the leased property. Personal delivery of such notice may be substituted for delivery by mail.

(b) If notice of the finding is mailed to or personally delivered to the former lessee within 21 days after the termination of the lease, title to the property vests in the lessor upon the expiration of six months from the date of the termination of the lease unless, within such six months, the owner of the property appears, proves his ownership of the property, and tenders payment of all reasonable charges for the storage and preservation of the property. If notice of the finding is not mailed to or personally delivered to the former lessee within 21 days after the termination of the lease, title to the property vests in the lessor upon the expiration of six months from the date of the mailing or delivery of the notice or three years from the date of the termination of the lease, whichever is earlier, unless within such time the owner of the property appears, proves his ownership of the property, and tenders payment of all reasonable charges for the storage (for not to exceed six months) and preservation of the property.

(c) If the lessor refuses to restore the property to an owner who has made reasonable proof of ownership and tendered payment for the

storage and preservation of the property as provided in subdivision (b), the owner may recover the property or its value, together with damages for its detention and a reasonable attorney's fee, by civil action commenced within six months after the date of such refusal.

(d) The lessor may, in lieu of holding the property for the owner pursuant to subdivision (b), sell the property in the manner specified in subdivision (3) of Section 9504 of the Uniform Commercial Code and hold the proceeds of such sale for the owner pursuant to subdivision (b) in the following cases:

(1) When the property is in danger of perishing or of losing the greater part of its value; or

(2) When the lessor's charges for the storage and preservation of the property amount to two-thirds of its value.

Comment. Section 1954.5 is designed to provide a lessor with a simple procedure for disposing of personal property found remaining on the leased property following the termination of the lease. The section relates to property to which the lessor has no claim. If the lessor has a lien claim against the property, Sections 1861 and 1861a of the Civil Code and Sections 9101-9507 of the Uniform Commercial Code govern the parties' rights.

SEC. 9. Article 1.5 (commencing with Section 3320) is added to Chapter 2 of Title 2 of Part 1 of Division 4 of the Civil Code, to read:

Article 1.5. Damages Upon Termination or Repudiation of Lease of Real Property

Comment. This article sets forth in some detail the damages that may be recovered when a lease of real property is terminated by reason of the lessee's or lessor's breach. The article also sets forth the lessee's rights to relief from any forfeiture of advance payments made to the lessor. The remainder of the article is designed to clarify the relationship between the right to damages arising under this article and the right to obtain other forms of relief under other provisions of California law.

§ 3320. Lessor's damages upon termination of lease for breach

3320. Subject to Section 3322, if a lease of real property is terminated because of the lessee's breach thereof, the measure of the lessor's damages for such breach is the sum of the following:

(a) The worth of the excess, if any, of the rent and charges equivalent to rent reserved in the lease for the portion of the term following such termination over the reasonable rental value of the property for the same period.

(b) Subject to Section 3325, any other damages necessary to compensate the lessor for all the detriment proximately caused by the lessee's breach or which in the ordinary course of things would be likely to result therefrom.

Comment. Section 3320 prescribes the measure of the damages a lessor is entitled to recover when the lease is terminated because of the lessee's breach.

Under subdivision (a), the basic measure of the lessor's damages are the excess of the unpaid "rent and charges equivalent to rent" under the lease over the rental the lessor can reasonably expect to obtain by relet ting the property. In this context, "rent and charges equivalent to rent" refers to all obligations the lessee undertakes in exchange for the use of the leased property. For example, if the defaulting lessee had promised to pay the taxes on the leased property and the lessor could not relet the property under a lease containing such a provision, the loss of the defaulting lessee's assumption of the tax obligation would be included in the damages the lessor is entitled to recover under Section 3320.

The measure of damages described in subdivision (a) is essentially that described in Civil Code Section 3308 (superseded by this article) as enacted in 1937. Section 3308's measure of damages is applicable, however, only when the lease so provides and the lessor chooses to invoke that remedy. The measure of damages described in Section 3320 is applicable in all cases.

Subdivision (b) is included in this section in order to make it clear that the basic measure of damages described in Section 3320 is not the limit of a lessor's recoverable damages when the lease is terminated by reason of the lessee's breach.

When a lease is terminated, it will usually be necessary for the lessor to take possession for a time in order to prepare the property for reletting and to secure a new tenant. A lessor should be entitled to recover the rentals due under the lease for this period if the damages awarded are to put him in as good a position as would performance by the lessee of his contractual obligations. The lessor should also be entitled to recover for his expenses in caring for the property during this time, for these are expenses that he would not have had to bear if the lessee had not abandoned the property or breached the lease.

In some cases, too, a lessor may wish to give a lessee an opportunity to retract his repudiation or cure his breach and resume his obligations under the lease. If the lessor does so and the lessee does not accept the opportunity to cure his default, the lessor should be entitled to recover the full amount of the rentals due under the lease for this period of negotiation as well as his expenses in caring for the property during this period.

In addition, the lessor should be entitled to recover for his expenses in retaking possession of the property, repairing damage caused by the lessee, and in reletting the property. There may be other damages necessary to compensate the lessor for all of the detriment proximately caused by the lessee, and if so, the lessor should be entitled to recover them also. Subdivision (b), which is based on Civil Code Section 3300, provides that all of the other damages a person is entitled to recover for the breach of a contract may be recovered by a lessor for the breach of his lease. This would include, of course, damages for the lessee's breach of specific covenants of the lease.

Subdivision (b) is "subject to Section 3325" in order to make clear that the lessor's attorney's fees are not recoverable as incidental damages unless the lease specifically provides for the recovery of such fees by either the lessor or lessee.

Section 3320 has been made subject to Section 3322 in order to make it clear that a lessor may not decline to relet the property and hold the original lessee for the entire remaining rental obligation as he is entitled to do under existing law. Under this section, as under the law relating to contracts generally, the defaulting lessee is not liable for any consequences that the lessor can reasonably avoid. Moreover, if the lessor relets the property for a rental in excess of the rental provided in the original lease, the damages the lessor is entitled to recover under Section 3320 must be reduced accordingly.

§ 3321. Lessee's damages upon termination of lease for breach

3321. Subject to Section 3322, if a lease of real property is terminated because of the lessor's breach thereof, the measure of the lessee's damages for such breach is the sum of the following:

(a) The excess, if any, of the reasonable rental value of the property for the portion of the term following such termination over the worth of the rent and charges equivalent to rent reserved in the lease for the same period.

(b) Subject to Section 3325, any other damages necessary to compensate the lessee for all the detriment proximately caused by the lessee's breach or which in the ordinary course of things would be likely to result therefrom.

Comment. Section 3321 prescribes the basic measure of the damages a lessee is entitled to recover when the lease is terminated because of the lessor's breach. It is consistent with the existing California law. Stillwell Hotel Co. v. Anderson, 4 Cal.2d 463, 469, 50 P.2d 441, 443 (1935) ("The general rule of damages is that the lessee may recover the value of his unexpired term and any other damage which is the natural and proximate result of the eviction.") Where appropriate, a lessee may recover damages for loss of good will, loss of prospective profits, and expenses of removal from the leased property. See, e.g., Beckett v. City of Paris Dry Goods Co., 14 Cal.2d 633, 96 P.2d 122 (1939); Johnson v. Snyder, 99 Cal. App.2d 86, 221 P.2d 164 (1950); Riechhold v. Sommarstrom Invest. Co., 83 Cal. App. 173, 256 Pac. 592 (1927).

Section 3321 is subject to Section 3322 to make clear that the defaulting lessor is not liable for any consequences that the lessee can reasonably avoid. Subdivision (b) is subject to Section 3325 in order to make clear that the lessee's attorney's fees are not recoverable as incidental damages unless the lease specifically provides for the recovery of such fees by either the lessor or lessee.

§ 3322. Avoidable consequences; lessor's profits on reletting

3322. (a) A party to a lease of real property that has been breached by the other party may not recover for any detriment caused by such breach that could have been avoided through the exercise of reasonable diligence without risk of other substantial detriment.

(b) When a lease of real property is terminated because of the lessee's breach thereof and the lessor relets the property, the lessor is not accountable to the lessee for any profit made on the reletting, but any such profit shall be set off against the damages to which the lessor is otherwise entitled.

Comment. Under existing California law, a lessor may decline to retake possession of leased property after it has been abandoned by the lessee and recover the full rental as it comes due from time to time under the lease. See De Hart v. Allen, 26 Cal.2d 829, 832, 161 P.2d 453, 455 (1945). Subdivision (a) of Section 3322 substitutes for this rule the rule applicable to contracts generally that a party to a lease that has been breached by the other party may not recover for any detriment caused by such breach that could have been avoided through the exercise of reasonable diligence. See RESTATEMENT, CONTRACTS § 336.

Under existing law, a lessor may relet property after the original lessee has abandoned the lease if he does so either on his own account (in which case the lessee's rental obligation is terminated) or for the account of the lessee. See discussion in Dorcich v. Time Oil Co., 103 Cal. App.2d 677, 685, 230 P.2d 10 (1951). Although no case has yet arisen so holding, the rationale of the California cases indicates that if the lessor receives a higher rental when reletting for the account of the lessee

than was provided in the original lease, the lessee is entitled to the profit.

Under Section 3322, a lessor who relets property after the original lessee has abandoned it does so for his own account; and under subdivision (b) any profit received is the lessor's, it does not belong to the defaulting lessee. Profit received on the reletting, however, reduces the damages suffered by the lessor for which the lessee is liable.

The rule stated in subdivision (b) is similar to the rule applicable when the buyer under a sales contract repudiates the sale and the seller resells the goods to mitigate damages. See COMM. CODE § 2706(6).

§ 3323. Rental upon reletting presumed to be reasonable rental value

3323. If leased real property is relet following the termination of the original lease because of the breach thereof, the rental due to the lessor under the new lease is presumed to be the reasonable rental value of the property for the term covered by the new lease. This presumption is a presumption affecting the burden of proof.

Comment. Under Sections 3320 and 3321, the damages a lessor or lessee is entitled to recover upon termination of the lease because of a breach are based in part on the difference between the value of the rentals which would have been due under the original lease for the remainder of the term and the reasonable rental value of the property for the same period. Section 3323 provides that the "reasonable rental value" of the property is presumptively fixed by the new lease when the lessor relets the property. The effect of this presumption may be overcome by proof that the reasonable rental value of the property is in fact higher or lower than rental fixed by the new lease. EVIDENCE CODE § 606.

§ 3324. Liquidated damages

3324. Notwithstanding Sections 3320 and 3321, upon any breach of the provisions of a lease of real property, liquidated damages may be recovered if they are provided in the lease and meet the requirements of Sections 1670 and 1671.

Comment. Section 3324 does not create a right to recover liquidated damages, it merely recognizes that such a right may exist if the conditions specified in Civil Code Sections 1670 and 1671 are met. Provisions in leases for liquidated damages upon repudiation of the lease by the lessee have been held to be void. Redmon v. Graham, 211 Cal. 491, 295 Pac. 1031 (1931); Jack v. Sinsheimer, 125 Cal. 563, 58 Pac. 130 (1899). Such holdings were proper so long as the lessor's cause of action upon repudiation of a lease was either for the rent as it came due or for the rental deficiencies as of the end of the lease term. Under such circumstances, there could be little prospective uncertainty over the amount of the lessor's damages. Under Section 1953.5 and this article, however, the lessor's right to damages accrues at the time of the repudiation; and because they must be fixed before the end of the term, they may be difficult to calculate in some cases. This will frequently be the case if the property is leased under a percentage lease. It may be the case if the property is unique and its fair rental value cannot be determined. Accordingly, Section 3324 is included as a reminder that the cases are no longer authoritative that have held liquidated damages provisions in leases to be void, and in some cases such provisions may be valid.

So far as provisions for liquidated damages upon a lessor's breach are concerned, Section 3325 is declarative of the preexisting law under which such provisions were upheld if reasonable. See Seid Pak Sing v. Barker, 197 Cal. 321, 240 Pac. 765 (1925).

§ 3325. Attorney's fees

3325. (a) In addition to any other relief to which a lessor or lessee is entitled by reason of the breach of a lease of real property by the other party to the lease, the lessor or lessee may recover reasonable attorney's fees incurred in obtaining such relief if:

(1) The lease provides for the recovery of such fees; or

(2) The lease provides that the other party to the lease may recover attorney's fees incurred in obtaining relief for the breach of the lease.

(b) The right to recover attorney's fees as provided in paragraph (2) of subdivision (a) may not be waived prior to the accrual of such right.

Comment. Leases, like other contracts, sometimes provide that a party forced to resort to the courts for enforcement is entitled to a reasonable attorney's fee. Section 3325 makes it clear that the remaining sections in the article do not impair the lessor's rights under such a provision.

Subdivision (b) and paragraph (2) of subdivision (a) are included in the section to equalize the operation of leases that provide for the recovery of an attorney's fees. Most leases are drawn by one party to the transaction (usually the lessor), and the other seldom has sufficient bargaining power to require the inclusion of a provision for attorney's fees that works in his favor. Under Section 3325, if either party is entitled by a provision in the lease to recover attorney's fees, the other may recover such fees when he is forced to resort to the courts to enforce his rights under the lease. To prevent paragraph (2) of subdivision (a) from being nullified by standard waiver provisions in leases, subdivision (b) prohibits the waiver of a party's right to recover under that paragraph until the right actually accrues.

§ 3326. Lessee's relief from forfeiture

3326. Subject to the lessor's right to obtain specific enforcement of the lease, if a lease of real property is terminated because of the breach thereof by the lessee or if the lessee abandons the lease, the lessee may recover from the lessor any amount paid to the lessor in consideration for the lease (whether designated rental, bonus, consideration for execution thereof, or by any other term) that is in excess of (a) the portion of the total amount required to be paid to the lessor pursuant to the lease that is fairly allocable to the portion of the term prior to the termination or abandonment of the lease and (b) any damages, including liquidated damages as provided in Section 3324, to which the lessor is entitled by reason of such breach or abandonment. The right of a lessee to recover under this section may not be waived prior to the accrual of such right.

Comment. Section 3326 is designed to make the rules stated in Freedman v. The Rector, 37 Cal.2d 16, 230 P.2d 629 (1951), and Caplan v. Schroeder, 56 Cal.2d 515, 15 Cal. Rptr. 145, 364 P.2d 321 (1961), applicable to cases arising out of the breach of a lease. The Freedman case held that a wilfully defaulting vendee under a contract for the sale of real property may recover the excess of his part payments over the damages caused by his breach. The Caplan case held that a wilfully defaulting vendee could recover such an advance payment even though the contract recited that the advance payment was in consideration for the execution of the contract. The court looked beyond the recital and found that there was in fact no separate consideration for the advance payment aside from the sale of the property itself.

Similarly, Section 3326 will permit a lessee to recover advance payments, regardless of how they are designated in the lease, if the court finds that

such payments are in fact in consideration for the lease and are in excess of the damages suffered by the lessor as a result of the lessee's breach.

The last sentence of Section 3326 is probably unnecessary. The Freedman and Caplan cases are based on the provisions of the code prohibiting forfeitures. These rules are applied despite contrary provisions in contracts. Nonetheless, the sentence is included to make it clear that the provisions of this section may not be avoided by the addition to leases of provisions waiving rights under this section.

Section 3326 will change the California law. Under the existing California law the right of a lessee to recover an advance payment depends on whether the advance payment is designated a security deposit (lessee may recover), liquidated damages (lessee may recover), an advance payment of rental (lessee may not recover), or a bonus or consideration for the execution of the lease (lessee may not recover). Compare Warming v. Shapiro, 118 Cal. App.2d 72, 257 P.2d 74 (1953)($12,000 forfeited because designated as both a bonus and an advance payment of rental) with Thompson v. Swiryn, 95 Cal. App.2d 619, 213 P.2d 740 (1950)(advance payment of $2,800 held recoverable as a security deposit). See discussions in Joffe, Remedies of California Landlord upon Abandonment by Lessee, 35 SO. CAL. L. REV. 34, 44 (1961) and Note, 26 CAL. L. REV. 385 (1938). See also Section 3324 and the Comment to that section.

§ 3327. Unlawful detainer actions

3327. (a) Nothing in this article affects the provisions of Chapter 4 (commencing with Section 1159) of Title 3 of Part 3 of the Code of Civil Procedure, relating to actions for unlawful detainer, forcible entry, and forcible detainer.

(b) The bringing of an action under the provisions of Chapter 4 (commencing with Section 1159) of Title 3 of Part 3 of the Code of Civil Procedure does not affect the right to bring a separate action to recover the damages specified in this article; but there shall be no recovery of damages in the subsequent action for any detriment for which a claim for damages was made and determined on the merits in the previous action.

Comment. Section 3327 is designed to clarify the relationship between this article and the chapter of the Code of Civil Procedure relating to actions for unlawful detainer, forcible entry, and forcible detainer. The actions provided for in the Code of Civil Procedure are designed to provide a summary method of recovering possession of property. Those actions may be used by a lessor whose defaulting lessee refuses to vacate the property after termination of the lease.

Section 3327 provides that the fact that a lessor has recovered possession of the property by an unlawful detainer action does not preclude the bringing of a later action to recover the damages to which he is entitled under this article. Some of the incidental damages to which the lessor is entitled may be recovered in either the unlawful detainer action or in an action to recover the damages specified here. Under Section 3327, such damages may be recovered in either action; but the lessor is entitled to but one determination of the merits of a damages claim for any particular detriment.

SEC. 10. Section 3308 of the Civil Code is repealed.

~~3308.--The-parties-to-any-lease-of-real-or-personal-property-may-agree therein-that-if-such-lease-shall-be-terminated-by-the-lessor-by-reason-of-any breach-thereof-by-the-lessee,-the-lessor-shall-thereupon-be-entitled-to-recover from-the-lessee-the-worth-at-the-time-of-such-termination,-of-the-excess,-if any,-of-the-amount-of-rent-and-charges-equivalent-to-rent-reserved-in-the lease--for-the-balance-of-the-stated-term-or-any-shorter-period-of-time-over the-then-reasonable-rental-value-of-the-premises-for-the-same-period.~~

~~The-rights-of-the-lessor-under-such-agreement-shall-be-cumulative-to-all other-rights-or-remedies--now-or-hereafter-given-to-the-lessor-by-law-or-by the-terms-of-the-lease;-provided,-however,-that-the-election-of-the-lessor-to exercise-the-remedy-hereinabove-permitted-shall-be-binding-upon-him-and exclude-recourse-thereafter-to-any-other-remedy-for-rental-or-charges-equivalent to-rental-or-damages-for-breach-of-the-covenant-to-pay-such-rent-or-charges accruing-subsequent-to-the-time-of-such-termination.--The-parties-to-such lease-may-further-agree-therein-that-unless-the--remedy-provided-by-this section-is-exercised-by-the-lessor-within-a-specified-time-the-right-thereto shall-be-barred.~~

Comment. Section 3308 is repealed because it is unnecessary. The remedy that Section 3308 states may be provided in a lease is made the general rule, whether or not provided in the lease, under the provisions of the remainder of the statute.

SEC. 11. Section 3387.5 is added to the Civil Code, to read:

3387.5. (a) A lease may be specifically enforced by any party, or assignee of a party, to the lease when:

(1) The lease provides for the transfer to the lessee at the termination of the term of the lease of title to buildings or other improvements affixed by the lessor to the leased property; or

(2) The lease contains an option which the lessee may exercise at the termination of the lease to acquire title to buildings or other improvements affixed by the lessor to the leased property.

(b) Nothing in this section affects the right to obtain specific or preventive relief in any other case where such relief is appropriate.

Comment. Under the existing California law, if a lessee defaults in the payment of rent, abandons the property, or otherwise breaches the lease, the lessor may refuse to terminate the lease and may sue to collect the rental installments as they accrue. Because the lessee's obligation under a lease has been, in effect, specifically enforceable through a series of actions, leases have been utilized by public entities to finance the construction of public improvements. The lessor constructs the improvement to the specifications of the public entity-lessee, leases the property as improved to the public entity, and at the end of the term of the lease all interest in the property and the improvement vests in the public entity. See, e.g., Dean v. Kuchel, 35 Cal.2d 444, 218 P.2d 521 (1950); City of Los Angeles v. Offner, 19 Cal.2d 483, 122 P.2d 14 (1942). Sometimes the public entity's right to acquire the property or the improvement is absolute under the terms of the agreement, sometimes it depends on the exercise of an option. In either event, this system of

financing public improvements would be seriously jeopardized if upon repudiation of the lease by the lessee the lessor's only right were the right to recover damages measured by the difference between the worth of the remaining rentals due under the lease and the rental value of the property. See Section 3320.

Section 3387.5 has been added to the Civil Code, therefore, to make it abundantly clear that a lease is specifically enforceable if it provides for the transfer of improvements constructed on the leased property to the lessee at the termination of the lease. Under Section 3387.5, it will be clear that a lessee may not avoid his obligation to pay the lessor the full amount due under the lease by abandoning the leased property and repudiating the lease.

Although Section 3387.5 may not be necessary inasmuch as agreements for the transfer of interests in real property are generally specifically enforceable, Section 3387.5 will avoid any uncertainty concerning the nature of the obligations that are assumed by the parties when entering into lease-purchase agreements.

SEC. 12. Section 1174 of the Code of Civil Procedure is amended to read:

1174. If upon the trial, the verdict of the jury, or, if the case be tried without a jury, the findings of the court be in favor of the plaintiff and against the defendant, judgment shall be entered for the restitution of the premises; and if the proceedings be for an unlawful detainer after neglect, or failure to perform the conditions or covenants of the lease or agreement under which the property is held, or after default in the payment of rent, the judgment shall also declare the forfeiture of such lease or agreement ~~if the notice required by Section 1161 of the code states the election of the landlord to declare the forfeiture thereof, but if such notice does not so state such election, the lease or agreement shall not be forfeited~~.

The jury or the court, if the proceedings be tried without a jury, shall also assess the damages occasioned to the plaintiff by any forcible entry, or by any forcible or unlawful detainer, alleged in the complaint and proved on the trial, and find the amount of any rent due, if the alleged unlawful detainer be after default in the payment of rent. Judgment against the defendant guilty of the forcible entry, or the forcible or unlawful detainer, may be entered in the discretion of the court either for the amount of the damages and the rent found due, or for three times the amount so found.

When the proceeding is for an unlawful detainer after default in the payment of rent, and the lease or agreement under which the rent is payable has not by its terms expired, and the notice required by Section 1161 has not stated the election of the landlord to declare the forfeiture thereof, the court may, and, if the lease or agreement is in

writing, is for a term of more than one year, and does not contain a forfeiture clause, shall order that execution upon the judgment shall not be issued until the expiration of five days after the entry of the judgment, within which time the tenant, or any subtenant, or any mortgagee of the term, or any other party interested in its continuance, may pay into the court for the landlord, the amount found due as rent, with interest thereon, and the amount of the damages found by the jury or the court for the unlawful detainer, and the costs of the proceedings, and thereupon the judgment shall be satisfied and the tenant be restored to his estate.

But if payment as here provided be not made within five days, the judgment may be enforced for its full amount, and for the possession of the premises. In all other cases the judgment may be enforced immediately.

Comment. The language deleted from Section 1174 was added to permit a lessor to evict a defaulting lessee and relet the premises without forfeiting his right to look to the lessee for any resulting deficiencies in the accruing rentals. Under the pre-existing law, a lessor whose lessee defaulted in the payment of rent had to choose between suing the lessee from time to time to collect the accruing rentals and completely terminating the lease and the lessee's obligation to pay any more rent. Costello v. Martin Bros., 74 Cal. App. 782, 786, 241 Pac. 588 (1925).

Inasmuch as Civil Code Section 1953.5 permits a lessor to terminate a lease without forfeiting his right to damages for the loss of the future rentals due under the lease, the deleted language is no longer necessary.

SEC. 13. This act does not apply to any lease executed before the effective date of this act.