

»Business Alert

March 2011—Cost of Repair Damages for Breach of Maintenance and Repair Covenants are not Recoverable During a Lease Term

A commercial tenant is typically obligated by its lease to maintain and repair the leased property and to not commit waste. If a tenant breaches those obligations, the landlord may notify the tenant of a default in the terms of the lease, and if not cured, the landlord may terminate the lease. However, if the landlord does not terminate the lease (or if the lease has not expired), the landlord under certain circumstances may not be able to sue to collect the cost of repairs for damage to the property.

In a recent case from California's Fourth Appellate District, *Avalon Pacific – Santa Ana, L.P. v. HD Supply Repair & Remodel, LLC*, a commercial tenant leased vacant warehouse and office property space intending to convert it into a retail facility. After demolishing the office space, the tenant halted the renovations due to economic conditions, and let the property fall into disrepair while trying to find a subtenant. The property was vandalized and became a campsite used by vagrants who started fires in the buildings. The landlord sued the tenant for breach of maintenance and repair obligations of the lease and for waste, but did not terminate the lease. The tenant continued to pay rent of \$50,000 per month.

The jury found in favor of the landlord, awarding \$677,000 in damages for breach of lease and \$561,000 in damages for waste, both awards based on the cost of repairs. The Court of Appeal, however, reversed the judgment and remanded with directions to the lower court to enter judgment for defendants. The Court ruled that under the terms of the lease, Civil Code Section 1951.2(a), California case law and prevailing law across the nation, the landlord could not recover the cost of repair damages for breach of maintenance and repair obligations, unless the lease had either expired or been terminated. The landlord was limited to the damages actually suffered, that of injury to the reversion interest.

Similarly, the Court found that to recover for waste while a lease remained in effect, a landlord must have proved the acts causing substantial and permanent injury to the landlord's reversion interest.

The Court reasoned that the landlord was not obligated to repair the property during the term of the lease and, thus, would be unjustly rewarded while continuing to receive rent. It was also entirely possible that the tenant might make the repairs by the time the lease term expired. The most significant facts driving its decision, however, were that the landlord had not terminated the lease, the lease had not expired, and the tenant continued to pay monthly rent, indicating that the lease had not been abandoned (contrary to the landlord's claim).

This decision does not mean that a commercial landlord is without any remedy for a tenant who fails to comply with its duties to maintain and repair the property. A landlord may sue the tenant for specific performance requiring the tenant to perform the necessary repairs. Self help may be another option, if available. However, the Court's ruling means that generally the availability of damages for breach of maintenance and repair will be limited to situations where the lease has expired or been terminated. Once the lease has ended, the landlord may then recover the cost of restoring the premises, the diminution in the market value of the premises, or specific performance of the covenant.

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