J. N. A. REALTY CORP. v. CROSS BAY CHELSEA, INC.

New York Court of Appeals
42 N.Y.2d 392, 366 N.E.2d 1313, 397 N.Y.S.2d 958 (1977)

Judges GABRIELLI, FUCHSBERG and COOKE concur with Judge WACHTLER; Chief Judge BREITEL dissents and votes to affirm in a separate opinion in which Judges JASEN and JONES concur.

WACHTLER, J.

J. N. A. Realty Corp., the owner of a building in Howard Beach, commenced this proceeding to recover possession of the premises claiming that the lease has expired. The lease grants the tenant, Cross Bay Chelsea, Inc., an option to renew and although the notice was sent, through negligence or inadvertence, it was not sent within the time prescribed in the lease. The landlord seeks to enforce the letter of the agreement. The tenant asks for equity to relieve it from a forfeiture.

The Civil Court, after a trial, held that the tenant was entitled to equitable relief. The Appellate Term affirmed, without opinion, but the Appellate Division, after granting leave, reversed and granted the petition. The tenant has appealed to this court.

Two primary questions are raised on the appeal. First, will the tenant suffer a forfeiture if the landlord is permitted to enforce the letter of the agreement. Secondly, if there will be a forfeiture, may a court of equity grant the tenant relief when the forfeiture would result from the tenant's own neglect or inadvertence.

At the trial it was shown that J. N. A. Realty Corp. (hereafter JNA) originally leased the premises to Victor Palermo and Sylvester Vascellaro for a 10-year term commencing on January 1, 1964. Paragraph 58 of the lease, which was attached as part of a 12-page rider, granted the tenants an option to renew for a 10-year term provided "that Tenant shall notify the landlord in writing by registered or certified mail six (6) months prior to the last day of the term of the lease that tenant desires such renewal." The tenants opened a restaurant on the premises. In February, 1964 they formed the Foro Romano Corp. (Foro) and assigned the lease to the corporation.

By December of 1967 the restaurant was operating at a loss and Foro decided to close it down and offer it for sale or lease. In March, 1968 Foro entered into a contract with Cross Bay Chelsea, Inc. (hereafter Chelsea), to sell the restaurant and assign the lease. As a condition of the sale Foro was required to obtain a modification of the option to renew so that Chelsea would have the right to renew the lease for an additional term of 24 years.

The closing took place in June of 1968. First JNA modified the option and consented to the assignment. The modification, which consists of a separate document to be attached to the lease, states: "the Tenant shall have a right to renew this lease for a further period of Twenty-Four (24) years, instead of Ten (10) years, from the expiration of the original term of said lease * * * All other provisions of Paragraph #58 in said lease, * * * shall remain in full force and effect, except as hereinabove modified." Foro then assigned the lease and sold its interest in the restaurant

to Chelsea for $ 155,000. The bill of sale states that "the value of the fixtures and chattels included in this sale is the sum of $ 40,000 and that the remainder of the purchase price is the value of the leasehold and possession of the restaurant premises." At that point five and one-half years remained on the original term of the lease.

In the summer of 1968 Chelsea reopened the restaurant. JNA's president, Nicholas Arena, admitted on the stand that throughout the tenancy it regularly informed Chelsea in writing of its obligations under the lease, such as the need to pay taxes and insurance by certain dates. For instance on June 13, 1973 JNA sent a letter to Chelsea informing them that certain taxes were due to be paid. When that letter was sent the option to renew was due to expire in approximately two weeks but JNA made no mention of this. A similar letter was sent to Chelsea in September, 1973.

Arena also admitted that throughout the term of the tenancy he was "most assuredly" aware of the time limitation on the option. In fact there is some indication in the record that JNA had previously used this device in an attempt to evict another tenant. Nevertheless it was not until November 12, 1973 that JNA took any action to inform the tenant that the option had lapsed. Then it sent a letter noting that the date had passed and, the letter states, "not having heard from you as prescribed by paragraph #58 in our lease we must assume you will vacate the premises" at the expiration of the original term, January 1, 1974. By letter dated November 16, 1973 Chelsea, through its attorney, sent written notice of intention to renew the option which, of course, JNA refused to honor.

At the trial Chelsea's principals claimed that they were not aware of the time limitation because they had never received a copy of paragraph 58 of the rider. They had received a copy of the modification but they had assumed that it gave them an absolute right to retain the tenancy for 24 years after the expiration of the original term. However, at the trial and later at the Appellate Division, it was found that Chelsea had knowledge of, or at least was "chargeable with notice" of, the time limitation in the rider and thus was negligent in failing to renew within the time prescribed.

Chelsea's principals also testified that they had spent an additional $ 15,000 on improvements, at least part of which had been expended after the option had expired. Toward the end of the trial JNA's attorney asked the court whether it would "take evidence from" Arena that he had negotiated with another tenant after the option to renew had lapsed. However, the court held that this testimony would be immaterial.

It is a settled principle of law that a notice exercising an option is ineffective if it is not given within the time specified (see, e.g., Restatement, Contracts 2d [Tent Draft No. 1, 1964], § 64, subd [b]; 1A Corbin, Contracts [1963], § 264; 1 Williston, Contracts [3d ed, 1957], § 87; *Sy Jack Realty Co. v Pergament Syosset Corp.*, 27 NY2d 449). "At law, of course, time is always of the essence of the contract" (De Funiak, Modern Equity, § 80, p 223). Thus the tenant had no legal right to exercise the option when it did, but to say that is simply to pose the issue; it does not resolve it. Of course the tenant would not be asking for equitable relief if it could establish its rights at law.

The major obstacle to obtaining equitable relief in these cases is that default on an option usually does not result in a forfeiture. The reason is that the option itself does not create any interest

in the property, and no rights accrue until the condition precedent has been met by giving notice within the time specified. Thus equity will not intervene because the loss of the option does not ordinarily result in the forfeiture of any vested rights (see, e.g., *Fidelity & Columbia Trust Co. v Levin,* 128 Misc 838, affd *221 App Div 786,* affd 248 NY 551; *Doepfner v Bowers,* 55 Misc 561; cf. *People's Bank of City of N. Y. v Mitchell,* 73 NY 406; but see *Noyes v Anderson,* 124 NY 175, 179-180, where it is indicated that the "rule may not be without exception"). The general rule is customarily stated as follows: "There is a wide distinction between a condition precedent, where no title has vested and none is to vest until the condition is performed, and a condition subsequent, operating by way of a defeasance. In the former case equity can give no relief. The failure to perform is an inevitable bar. No right can ever vest. The result is very different where the condition is subsequent. There equity will interpose and relieve against the forfeiture". *(Davis v Gray,* 16 Wall [83 US] 203, 229-230.) It has been suggested that even when the option has been paid for, nothing is forfeited when it expires, because the amount paid "is the exact agreed equivalent" of the power to exercise the right for the time allotted (see 1 Corbin, Contracts, § 35, p 147).

But when a tenant in possession under an existing lease has neglected to exercise an option to renew, he might suffer a forfeiture if he has made valuable improvements on the property. This of course generally distinguishes the lease option, to renew or purchase, from the stock option or the option to buy goods. This was a distinction which some of the older cases failed to recognize (see, e.g, *Fidelity & Columbia Trust Co. v Levin, supra; Doepfner v Bower, supra;* cf. *People's Bank of City of N. Y. v Mitchell, supra).* More recently it has been noted that "although the tenant has no legal interest in the renewal period until the required notice is given, yet an equitable interest is recognized and protected against forfeiture in some cases where the tenant has in good faith made improvements of a substantial character, intending to renew the lease, if the landlord is not harmed by the delay in the giving of the notice and the lessee would sustain substantial loss in case the lease were not renewed" (2 Pomeroy, Equity Jurisprudence [5th ed], § 453b, p 296).

The leading case on this point is *Fountain Co. v Stein* (97 Conn 619; 27 ALR 976) and the rule has been accepted by noted commentators (see, e.g., 1 Corbin, *op. cit.,* § 35, p 146; 1 Williston, Contracts [3d ed], § 76, p 249, n 4; 2 Pomeroy, *op. cit.,* § 453b, p 296). It has also been accepted and applied by this court. In *Jones v Gianferante* (305 NY 135, 138), citing the *Fountain* case we held that the tenant was entitled to "the benefit of the rule or practice in equity which relieves against such forfeitures of valuable lease terms when default in notice has not prejudiced the landlord, and has resulted from an honest mistake, or similar excusable fault." The rule was extended in *Sy Jack Realty Co. v Pergament Syosset Corp.* (27 NY2d 449, 453, *supra)* to preserve the tenant's interest in a "long-standing location for a retail business" because this is "an important part of the good will of that enterprise, [and thus] the tenant stands to lose a substantial and valuable asset."

In neither of those cases were we asked to consider whether the tenant would be entitled to equitable relief from the consequences of his own neglect or "mere forgetfulness" as the court had held in the *Fountain* case *(supra).* In *Gianferante* the default was due to an ambiguous lease, and in *Sy Jack* the notice was mailed but never delivered (but see *Roy's of North Syracuse v P & C Food Markets,* 51 AD2d 641, mot for lv to app den 38 NY2d 711; and the dissenting opn in *Sy Jack [supra,* p 456, n 1], where it is noted that the three cases cited in Williston--the principle one being the *Fountain* case--"obviously warranted equitable relief. For not only in those cases was

there excusable fault', but also in each one the tenant had made substantial improvements"). But the principle involved is well established in this State. A tenant or mortgagor should not be denied equitable relief from the consequences of his own neglect or inadvertence if a forfeiture would result *(Giles v Austin,* 62 NY 486; *Noyes v Anderson,* 124 NY 175; *Roy's of North Syracuse v P & C Food Markets, supra;* see, also, 2 Pomeroy, Equity Jurisprudence [5th ed], § 452, p 287). The rule applies even though the tenant or mortgagor, by his inadvertence, has neglected to perform an affirmative duty and thus breached a covenant in the agreement *(Giles v Austin, supra;Noyes v Anderson, supra).*

On occasion the court has cautioned that equitable relief would be denied where there has been a willful or gross neglect *(Noyes v Anderson, supra,* p 179), but it has been reluctant to employ the sanction when a forfeiture would result. In *Giles v Austin (supra,* p 491), for instance, the landlord sought to recover possession of the premises after the tenant had neglected to pay the taxes as required by a covenant in the lease. We held that although the tenant had not paid the taxes since the inception of the lease in 1859, and had only paid them after suit was commenced in 1868, the tenant's default was not "so willful, or his neglect so inexcusable, that a court of equity should have denied him any relief."

There are several cases in which this court has denied a tenant or mortgagor equitable relief because of his own neglect to perform within the time fixed in the lease or mortgage, but only when it has found that there was "no penalty, no forfeiture" *(Graf v Hope Bldg. Corp.,* 254 NY 1, 4; *Fidelity & Columbia Trust Co. v Levin,* 128 Misc 838, affd *221 App Div 786,* affd 248 NY 551, *supra; People's Bank of City of N. Y. v Mitchell,* 73 NY 406, *supra).* Cardozo took a different view. He felt that even though there may be no penalty or forfeiture "in a strict or proper sense" equity should "relieve against it if default has been due to mere venial inattention and if relief can be granted without damage to the lender". Even in those cases he would apply the general equitable principle that "the gravity of the fault must be compared with the gravity of the hardship" *(Graf v Hope Bldg. Corp., supra,* pp 9-10, 13 [Cardozo, Ch. J., dissenting]; see, also, 2 Pomeroy, Equity Jurisprudence [5th ed], § 439, p 220).

Here, as noted, the tenant has made a considerable investment in improvements on the premises--$ 40,000 at the time of purchase, and an additional $ 15,000 during the tenancy. In addition, if the location is lost, the restaurant would undoubtedly lose a considerable amount of its customer good will. The tenant was at fault, but not in a culpable sense. It was, as Cardozo says, "mere venial inattention." There would be a forfeiture and the gravity of the loss is certainly out of all proportion to the gravity of the fault. Thus, under the circumstances of this case, the tenant would be entitled to equitable relief if there is no prejudice to the landlord.

However it is not clear from the record whether JNA would be prejudiced if the tenant is relieved of its default. Because of the trial court's ruling, JNA was unable to submit proof that it might be prejudiced if the terms of the agreement were not enforced literally. Its proof of other negotiations was considered immaterial. It may be that after the tenant's default the landlord, relying on the agreement, in good faith, made other commitments for the premises. But if JNA did not rely on the letter of the agreement then, it should not be permitted to rely on it now to exact a substantial forfeiture for the tenant's unwitting default. This, however, must be resolved at a new trial.

Finally we would note, as the dissenters do, that it is possible to imagine a situation in which a tenant holding an option to renew might intentionally delay beyond the time prescribed in order to exploit a fluctuating market. However, as the dissenters also note, there is no evidence to suggest that that is what occurred here. On the contrary there has been an affirmed finding of fact that the tenant's late notice was due to negligence. Of course a tenant who has intentionally delayed should not be relieved of a forfeiture simply because this tenant, who was merely inadvertent, may be granted equitable relief. But, on the other hand, we do not believe that this tenant, or any tenant, guilty only of negligence should be denied equitable relief because some other tenant, in some other case, may be found to have acted in bad faith. By its nature equitable relief must always depend on the facts of the particular case and not on hypotheticals.

Accordingly, the order of the Appellate Division should be reversed and a new trial granted.

BREITEL, C.J. (dissenting).

Relieving the tenant of its negligent failure to exercise its option to renew a lease within the prescribed time upsets established precedent, introduces instability in business transactions, and disregards commercial realities. I therefore dissent.

This case involves an option to renew a lease, not a mortgage foreclosure or an acceleration clause in a lease or mortgage. The categories and applicable precedents are not to be confused.

In a summary holdover proceeding brought by J. N. A. Realty, a landlord, to recover possession of leased commercial premises, tenant, Cross Bay Chelsea, appeals. The Civil Court's dismissal of the petition, after trial, was affirmed at Appellate Term, but the Appellate Division reversed, one Justice dissenting, and awarded the landlord possession.

At issue is the availability of equitable relief to remedy a commercial tenant's failure, by the appointed date, to exercise its option to renew a lease when the only explanation is sheer negligence.

The order of the Appellate Division should be affirmed, and the landlord awarded possession. Mere negligence does not justify departing from the rule that notice of intention to exercise an option to renew must be given within the prescribed period. Equitable relief is never justified by the fact alone, always present, that the tenant will suffer some sort of economic detriment. …

Had an honest mistake or similar "excusable fault", as opposed to what is undoubtedly mere carelessness, occasioned the tenant's tardiness, absent prejudice to the landlord, equitable relief would be available (e.g., *Sy Jack Realty Co. v Pergament Syosset Corp.*, 27 NY2d 449, 453; *Jones v Gianferante,* 305 NY 135, 138). At issue, instead, is the availability of equitable relief where the only excuse for the commercial tenant's dilatory failure to exercise its option to renew is sheer carelessness.

Enough has been said to uncover a common situation. Experienced and even hardened businessmen at cross-purposes over the renewal of a valuable lease term seek on the one hand to stand by the written agreement, and on the other, to loosen the applicable rules to receive *ad hoc* adjustment of equities and relief from economic detriment. The landlord wants a higher return. The tenant wants to keep the old bargain. Which of the profit-seeking parties in this particular case should prevail as a matter of morals is not within the province of the courts. The well-settled doctrine is that with respect to options, whether they be lease renewal options, options to purchase real or personal property, or stock options, time is of the essence. The exceptions, namely, estoppel, fraud, mistake, accident, or overreaching, are few. Commercial stability and certainty are paramount, and always the dangers of unsolvable issues of fact and speculative manipulation (as with stock options) are to be avoided.

The landlord should be awarded possession of the premises in accordance with the undisputed language and manifested intention of the written lease, its 12-page rider, and modification. It does not suffice that the tenant may suffer an economic detriment in losing the renewal period. Nor does it suffice that the delay in giving notice may have caused the landlord no "prejudice", other than loss of the opportunity to relet the property or renegotiate the terms of a lease on a fresh basis. Once an option to renew a lease has been conditioned upon the tenant's giving timely notice, the commercial lessee should not be heard to complain that through carelessness a valued asset has been lost, anymore than one would allow the landlord to complain of the economic detriment to him in agreeing to an improvident option to renew.

The court unanimously accepts the general rule at law: an option to renew a commercial lease must be exercised within the appointed time period (e.g., *Sy Jack Realty Co. v Pergament Syosset Corp.*, 27 NY2d 449, 452, *supra*, and authorities cited; see Restatement, Contracts 2d [Tent Draft Nos. 1-7, 1973], § 64, Comment *f;* 34 NY Jur, Landlord and Tenant, §§ 418-419; 51C CJS, Landlord and Tenant, § 59). Underlying the bar to equitable relief is the theory that until the condition precedent is fulfilled, that is, until the required timely notice is given, there is no "forfeiture" for which equity will extend protection *(Fidelity & Columbia Trust Co. v Levin,* 128 Misc 838, 844-845, affd *221 App Div 786*, affd 248 NY 551; 2 Pomeroy, Equity Jurisprudence [5th ed], § 453b, p 296). While the rule has been bolstered by traditional concepts of estates in land, its basis has current commercial and economic validity.

In this State, as in others, relief has been afforded tenants threatened with loss of an expected renewal period (see, generally, Effect of Lessee's Failure or Delay in Giving Notice Within Specified Time, of Intention to Renew Lease, Ann., 44 ALR2d 1359, esp 1362-1369). But in New York, as elsewhere, the circumstances conditioning such relief have been carefully limited. It is only where the tenant can show, not mere negligence, but an excuse such as fraud, mistake, or accident, that is, one or more of the categories common and integral to invocation of equity, that courts have, despite the literal agreement and intention of the parties, stepped in to prevent a loss (see, e.g., *Jones v Gianferante*, 305 NY 135, 138-139, *supra;* 1 McAdam, Landlord and Tenant [5th ed], § 156, pp 721-722).

Even in the case of excusable default by the tenant the court looks to the investment the tenant has made to bolster his right to equitable relief. But the fact of tenant investment alone is

not enough to justify intervention. Thus, in the leading cases excusing the tenant's late notice, mention is perforce made of investments and improvements (e.g., *Sy Jack Realty Co. v Pergament Syosset Corp.,* 27 NY2d 449, 453, *supra; Jones v Gianferante,* 305 NY 135, 138, *supra).* But the loss or "forfeiture" of these investments was not alone the trigger to granting relief. Indispensable is the existence of some mistake or excusable default. Thus, in *Jones v Gianferante (supra,* p 138), an ambiguous term in the lease excused the tenant's failure. And in *Sy Jack v Pergament (supra,* p 453), it was reliance on the post office to deliver the notice, mailed three days before law day, that was forgiven. In no case of accepted or acceptable authority, however,were improvements alone enough to help the negligent tenant.

The majority facilely disposes of the tenant's delinquency in exercising its option by relying on cases in which a party, notwithstanding its negligence, was relieved from a forfeiture (e.g., *Giles v Austin,* 62 NY 486, 493-494, a conditional limitation in a lease; *Noyes v Anderson,* 124 NY 175, 182-183, mortgagor's failure to pay an assessment). But indiscriminate application of principles evolved to deal with mortgage foreclosures or a lessor's right to re-enter upon a tenant's failure to pay taxes and assessments when due does not withstand analysis. Since ever so long, enforcement of a mortgage has rested in equity (see *Jamaica Sav. Bank v M. S. Investing Co.,* 274 NY 215, 219; 38 NY Jur, Mortgages and Deeds of Trust, § 317). It is also significant that as to foreclosure, time is not of the essence (see 10 NY Jur, Contracts, § 270). Even where acceleration clauses are involved and a strong argument can be made for allowing relief, time has been of the essence and negligence has not been excused (see *Graf v Hope Bldg. Corp.,* 254 NY 1, 4, 7 [dissenting opn per Cardozo, Ch. J.]). It is equally inappropriate to analogize to a lessee's failure to comply with a lease requirement that taxes and assessments be paid as they become due (see *Giles v Austin, supra,* pp 493-494). For the loss of an existing lease term subject to a condition subsequent distinguishes that situation from the loss of a possible option period subject to a condition precedent. An option is a right to purchase or acquire an interest in personal or real property in the future, and, if precise, it carries an invulnerable requirement to comply with all conditions, including that of time which is therefore of the essence in law and equity.

There are cases, not binding on this court, which express the principles discussed. For reasons that are not persuasive they would distinguish, however, between mere neglect or forgetfulness and gross or willful negligence, whatever that might be (see *Fountain Co. v Stein,* 97 Conn 619, 626-627; *Xanthakey v Hayes,* 107 Conn 459, 469; see, generally, 1 Williston, Contracts [3d ed], § 76, p 249, n 4). This is not a distinction generally accepted and is hardly a pragmatic one to apply in an area where the opportunities for distortion and manipulation are so great. The instability and uncertainty would be dangerous and would allow for *ad hoc* dispensations in particular cases without reliable rule so essential to commercial enterprise.

To begin with, under the guise of sheer inadvertence, a tenant could gamble with a fluctuating market, at the expense of his landlord, by delaying his decision beyond the time fixed in the agreement. The market having resolved in favor of exercising the option, the landlord, even though the day appointed in the agreement has passed, could be held to the return set out in the option, although if the market had resolved otherwise, the tenant could not be held to the renewal period.

None of this is to say that the tenant in this case was guilty of any manipulation. Hardly so. But what the court is concerned with is a rule for this case which perforce must cover other cases of like kind, where there will be no assurance that the "forgetfulness" is no more than that. The worst of the matter is that the kind of paltry record made in this case is hardly one on which a new rule with potential for mischief should be based. When the option, especially one requiring notice well in advance of the expiration of the lease, permits of economic manipulation, in commercial fairness the parties, especially if represented by counsel, should be held to their bargain, if plainly expressed.

Considering investments in the premises or the renewal term a "forfeiture" as alone warranting equitable relief would undermine if not dissolve the general rule upon which there is agreement. For, it is difficult to imagine a dilatory commercial tenant, particularly one in litigation over a renewal, who would not or could not point, scrupulously or unscrupulously, to some threatened investment in the premises, be it a physical improvement or the fact of good will. As a practical matter, it is not unreasonable to expect the commercial tenant, as compared with his residential counterpart, to protect his business interests with meticulousness, a meticulousness to which he would hold his landlord. All he, or his lawyer, need do is red-flag the date on which he has to act.

Having established no excuse, other than its own carelessness, Chelsea's claim is unfounded. Even if Chelsea honestly thought it enjoyed a 30-year lease, it does not change the result. Nor is it helpful to argue that Chelsea, always represented by a lawyer, was unable to procure a copy of the entire lease agreement. Indeed, it borders on the utterly incredible that experienced, sophisticated businessmen and their lawyers would not have assembled and scrutinized every relevant document affecting a long-term lease covering, with a renewal, a 30-year period.

That adherence to well-settled principles, like a Statute of Limitations or a Statute of Frauds, works a hardship on some does not, alone, permit a court to depart from sound doctrine and principles. Even if precedent did not control the same doctrines and principles discussed should be applied.

Accordingly, I dissent and vote that the order of the Appellate Division should be affirmed, and the landlord awarded possession of the premises.