

New Jersey Law Journal

VOL. CLXXVI – NO. 12 – INDEX 1164

JUNE 21, 2004

ESTABLISHED 1878

Real Estate
&
Title Insurance

Lawyers Must Consider Tenant's Remedies

A tenant's remedies for a landlord's wrongful conduct are often as important as the financial terms of the lease

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In drafting and negotiating the terms of a lease agreement (particularly in the commercial context), lawyers often focus heavily on the economic terms affecting the lease transaction, but pay little attention to the tenant's remedies.

A tenant's remedies for a landlord's wrongful conduct are often as important as the financial terms of the lease. The failure of the tenant's lawyer to consider up front the remedies available to a tenant can be disastrous. It is imperative that every lawyer representing a tenant (or, for that matter, those representing a landlord) be fully aware of the rights and remedies available under the applicable law so that those rights and remedies are adequately protected. To do so, the lawyer must first recognize and understand the nature of the causes of action available and, as to each, the appropriate remedies.

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Common Law Fraud

Perhaps the most fundamental cause of action a tenant can assert against a landlord for unfair or deceptive practices in the context of entering into a lease agreement is common-law fraud (i.e., fraud in the inducement). Two general remedies are recognized to redress the fraudulent inducement of a tenant into entering a lease through misrepresentations or omissions of material fact: (1) monetary damages to redress the financial losses sustained as a direct and proximate result of the fraud; and (2) equitable remedies (such as rescission or reformation), which seek to "unmake" or modify the contract which would not have come into existence but for the fraud. The particular remedy or combination of remedies a court will award depends upon the nature of the fraud and the circumstances under which it was perpetrated.

Legal fraud is comprised of (1) a material representation of a presently existing or past fact, (2) made with knowledge of its falsity, (3) with the intention that the other party rely on it, and (4) the other party does so rely to its damage. *Dover Shopping Center, Inc. v. Cushman's Sons, Inc.*, 63 N.J. Super. 384, 391 (App. Div. 1960).

Equitable fraud is comprised of the same elements as legal fraud except that knowledge is not required. *Id.* Thus, whatever constitutes fraud at law will also constitute fraud in equity. Equity, however, goes farther and includes fraudulent misrepresentations that do not exist at law.

Bonnco Petrol, Inc. v. Epstein, 115 N.J. 599, 609 (1989). For example, silence in the face of an obligation to disclose amounts to an equitable fraud. See *Jewish Center of Sussex County v. Whale*, 86 N.J. 619, 624-25 (1981).

Equitable remedies (such as rescission or reformation) are intended to restore the parties to their positions just before the fraud (*status quo ante*) and prevent the party who made the misrepresentation from benefiting from it. See *Bonnco*, 115 N.J. at 612 (citations omitted). Rescission is the avoidance or "undoing" of the transaction and is usually accompanied by restitution (a return of the benefits received) on both sides. D. Dobbs, *Law of Remedies* (2d ed. 1993), §4.3(6) at 414.

Reformation, on the other hand, does not seek to avoid the entire agreement, but rather, to modify its terms such that it reflects the intent of the parties. *Id.* at §4.3(7) at 417. Equitable remedies of rescission or reformation are usually available early on in the transaction and must be sought promptly upon the discovery of the fraud to avoid any election or waiver of the fraud. See *Dover Shopping Center*, 63 N.J. Super. at 392.

Unlike rescission, reformation seeks to "fix" the agreement by eliminating the fraud from its terms. Reformation is the appropriate remedy for fraud in the written expression of the agreement whereas rescission is the appropriate remedy where the fraud is in the formation of the agreement. D. Dobbs, *Law of Remedies*, at 715-16. In essence, reformation does nothing more than conform the agreement

to the intent of the parties without the fraud.

In addition to the equitable remedies for fraud in the inducement, tenants can also seek any economic loss sustained as a proximate result of the landlord's fraud. *Zeliff v. Sabatino*, 15 N.J. 70, 74-75 (1954). Based on this general proposition, New Jersey has adopted a flexible approach to awarding damages for fraud as follows:

- (1) If the defrauded party is content with the recovery of only the amount that he lost, his damages will be measured under that rule;
- (2) if the fraudulent representation also amounts to a warranty, recovery may be had for loss of the bargain because a fraud accompanied by a broken promise should cost the wrongdoer as much as the latter alone;
- (3) where the circumstances disclosed by the proof are so vague as to cast virtually no light upon the value of the property had it conformed to the representations, the court will award damages equal only to the loss sustained; and
- (4) where the damages under the benefit-of-the-bargain rule are proved with sufficient certainty, that rule will be employed. *Id.*

Attorneys' fees and costs are *not* considered an element of damages and are not recoverable absent contractual language to the contrary. See *Magnet Resources, Inc. v. Summit MRI, Inc.*, 318 N.J. Super. 275, 292-93 (App. Div. 1998). Thus, a provision allowing for their recovery should be considered for inclusion in any lease.

Further, where the fraud is particularly egregious, punitive damages may also be available subject to the court's discretion. *Ballinger v. Delaware River Port Authority*, 172 N.J. 586, 605 (2002). However, because fraud in the inducement is usually a profit motivated tort, tenants are not permitted to recover for emotional distress unless they prove the landlord intended to cause the emotional distress through the fraud. See D. Dobbs, *Law of Remedies* (2d ed. 1993), §9.2(4) at 698-99.

Oftentimes the fraud or deception perpetrated by the landlord occurs during the term of the lease rather than at its inception. Thus, remedies such as rescission and reformation are usually not available. However, all of the remaining remedies for damages are applicable. In addition, where the unfair or deceptive practice renders the premises unusable for the leased purpose, the tenant may recover the "fair market value of the lease" as compensatory damages. Restatement (Second) of Property, §10.2 (1976).

The Consumer Fraud Act

Beyond traditional common-law fraud remedies, New Jersey (like most states) has enacted a statutory scheme, known as the Consumer Fraud Act (N.J.S.A. 56:8-1 et seq.), specifically designed to deter and protect consumers (including tenants)¹ against fraudulent and deceptive practices in commercial transactions. To accomplish this, the Act creates a private cause of action by a consumer for violations of the statute in commercial transactions. Unlike common-law fraud, a private plaintiff need not establish that the misrepresentation was made with intent to deceive or with knowledge of its falsity. Rather, the plaintiff need only show that the defendant made affirmative misrepresentations of fact or engaged in other affirmative acts prohibited under the Act. See *Gennari v. Weichert Co. Realtors*, 148 N.J. 582, 605 (1997). However, where liability under the Act is sought for a wrongful omission or failure to disclose, the plaintiff must show the defendant acted knowingly. *Gennari*, 148 N.J. at 605.

Further, a plaintiff is not (unlike common-law fraud) required to prove that he was actually misled, deceived or damaged by the fraud, deception or unreasonable commercial practice. N.J.S.A. 56:8-2. See also *Gennari*, 148 N.J. at 605. However, for a private plaintiff to recover damages under the Act, he must have sustained an ascertainable loss of money or property as a result of a violation of the Act. See *Weinberg v. Sprint Corp.*, 173 N.J. 233, 249-50 (2002). If shown, the Act mandates an award of treble damages, plus reasonable attorneys' fees and costs of suit. See *Wanetick v. OCT Partnership*, 163 N.J. 484, 490 (2000).² Expert fees are

not recoverable. *Josantos Const. v. Bohner*, 326 N.J. Super. 42, 48 (App. Div. 1999). A private cause of action does not exist for a tenant under the Act for purely injunctive relief. Such relief can only be sought by the Attorney General. See *Weinberg*, 173 N.J. at 604.³

Proving damages recoverable under the Act differs from the proof required under common-law fraud. While common-law fraud requires proof of damages by way of detriment, a consumer fraud plaintiff must prove an ascertainable loss of money or property. *Varacallo v. Massachusetts Mut. Life Ins. Co.*, 332 N.J. Super. 31, 43 (App. Div. 2000). The Act, however, does not pre-empt a common-law remedy for legal fraud and a private plaintiff can recover both damages for the legal fraud and treble damages under the Act. *Dreier Co., Inc. v. Unitronix Corp.*, 218 N.J. Super. 260, 274 (App. Div. 1986). Courts also have allowed a private plaintiff to recover treble damages under the Act and punitive damages under common-law fraud. *Wildstein v. Tru Motors, Inc.*, 227 N.J. Super. 331, 335 (Law Div. 1988).

Implied Covenant of Good Faith and Fair Dealing

Integrated by law into every contract in New Jersey is the implied covenant of good faith and fair dealing. See *Sons of Thunder, Inc. v. Borden, Inc.*, 148 N.J. 396, 420 (1997) (citations omitted). The courts have interpreted the implied covenant of good faith and fair dealing to mean that "neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract." *Palisades Properties, Inc. v. Bronetti*, 44 N.J. 117, 130 (1965). While the implied covenant of good faith and fair dealing cannot override an express contractual provision (such as, for example, a provision allowing a party to terminate without cause), it still requires the exercise of any express right granted by the contract to be done in good faith. See *Sons of Thunder*, 148 N.J. at 420-21 (provision allowing termination without cause must be exercised in good faith).

The implied covenant of good faith and fair dealing resembles the doctrines of promissory and equitable estoppel in that

the plaintiff must demonstrate unconscionable conduct by the defendant and detrimental reliance by the plaintiff. See *Borbely v. Nationwide Mutual Ins. Co.*, 547 F.Supp. 959, 973 (D.N.J. 1981). Often, courts require the plaintiff to demonstrate a heightened degree of egregiousness or economic oppression such as dishonesty, exploitation of a vulnerability or disparity of economic power, or destruction of some truly substantial investment or property interest. *Emerson Radio Corp. v. Orion Sales, Inc.*, 253 F.3d 159, 169-173 (3d Cir. 2001).

Where a landlord is found to have breached the covenant of good faith and fair dealing, New Jersey law provides a tenant with the same remedies available for any breach of contract action — i.e., the breaching party is liable for “all of the natural and probable consequences of the breach of that contract.” *Pickett v. Lloyd's*, 131 N.J. 457, 474 (1993). Courts tend to measure damages by looking at the nature and reasonableness of the detrimental

reliance to avoid injustice. See *Pop's Cones, Inc. v. Resorts International Hotel, Inc.*, 307 N.J. Super. 461, 466-70 (App. Div. 1998) (citing Restatement (Second) of Contracts, §90).

Lost profits are also a common form of damages awarded for breach of the implied covenant of good faith and fair dealing. The plaintiff must prove, with a reasonable degree of certainty (a) the wrongful conduct caused the loss of profit, and (b) the profits were reasonably within the contemplation of the parties at the time the contract was entered into. *Sons of Thunder*, 148 N.J. at 427 (quoting *Unique Systems, Inc. v. Zotos Int'l, Inc.*, 622 F.2d 373, 378 (8th Cir. 1980)).

With all of the potential harm that can befall a tenant unprepared to deal with a landlord's unfair or deceptive acts before, during and after the lease is signed, a lawyer should always consider and discuss with the tenant all available remedies for such conduct at the outset of any lease negotiation. Otherwise, the tenant will be

ill-equipped to make informed business decisions during the lease negotiation and may inadvertently surrender certain rights and remedies later critical to redress a landlord's bad faith. ■

Footnotes:

¹. The Consumer Fraud Act applies to the landlord-tenant relationship. See *49 Prospect Street Tenants Assoc. v. Sheva Gardens, Inc.*, 227 N.J. Super. 449, 468-69 (App. Div. 1988).

². Treble damages are not available to a private plaintiff if the Attorney General becomes involved in the case and directs the defendant to restore the plaintiff's money or property. *Skeer v. EMK Motors, Inc.*, 187 N.J. Super. 465 (App. Div. 1982).

³. There is one exception to this rule. A private party can seek both damages and injunctive relief if the private party pleads an ascertainable loss capable of surviving summary judgment. *Weinberg*, 173 N.J. at 604.