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WAIVING THE DUTY TO MITIGATE IN COMMERCIAL LEASES

ABSTRACT

This Note examines a largely unexplored consequence of jurisdictions adopting a default duty to mitigate for commercial leases: whether a contract provision waiving the duty should be enforced. Only a few courts across the country have addressed the waiver issue in a commercial setting. At least two different appeals courts have enforced a waiver clause and claim that public policy supports their decision. In contrast, a federal court has stated the opposite—that public policy demands waiver provisions be void. Another state has outright voided all waiver clauses by statute. Courts that have enforced waivers have asserted that commercial parties have equal bargaining power and that these parties are free to enter into whatever agreements they wish. This Note argues that courts should not enforce clauses purporting to waive the duty to mitigate, because waivers are against public policy and there is no guaranteed equal bargaining power between commercial landlords and tenants. Finally, this Note proposes that states should adopt a blanket rule outright voiding all waiver clauses.

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INTRODUCTION

The duty to mitigate is not a new legal principle. Rather, it is a well-settled doctrine used in contract law to limit the damages an injured party may receive from a breach.[1] Over the past few decades, courts have adopted the doctrine in lease disputes, requiring a landlord to make reasonable efforts to decrease the amount of due rent an abandoning tenant must pay.[2] Not all jurisdictions have adopted the doctrine, but most states have decided that it is a default rule for landlords in both residential and commercial leases.[3]

Once a state has adopted a default duty to mitigate, it may be confronted with the question of whether that duty can be contractually waived.[4] A waiver may occur when two parties agree in the language of the lease that if the tenant abandons, the landlord does not have a duty to mitigate the damages arising from the breach of the lease, even if the jurisdiction has ruled there to be a default duty.[5] In academia, this aspect of the duty to mitigate has received only minimal attention.[6] Until recently courts were not confronted with disputes over waiver in a commercial setting, and

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[1] *See* New Towne L.P. v. Pier 1 Imports (U.S.), Inc., 680 N.E.2d 644, 646 (Ohio Ct. App. 1996); RESTATEMENT (SECOND) OF CONTRACTS § 350 (1981).

[2] *See, e.g.*, Schneiker v. Gordon, 732 P.2d 603, 611 (Colo. 1987); Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 299 (Tex. 1997); O'Brien v. Black, 648 A.2d 1374, 1376 (Vt. 1994).

[3] *See Austin Hill*, 948 S.W.2d at 296.

[4] This is as opposed to "waiving" the *defense* of the duty to mitigate. The duty to mitigate can be an affirmative defense used by a tenant when a cause of action is brought against him. Courts will often rule a tenant "waived" the defense of the duty to mitigate by not pleading it. *See, e.g.*, Stein v. Spainhour, 521 N.E.2d 641, 644 (Ill. App. Ct. 1988). This Note discusses only a contractual provision to waive the landlord's duty to mitigate damages when a tenant abandons a lease and not the "waiving" of the affirmative defense during litigation.

[5] *See* Woodland Investor Member, L.L.C. v. Soldier Creek, L.L.C., No. 11-2013-JTM, 2013 WL 1893512, at *13 (D. Kan. May 23, 2012).

[6] *See* Dawn R. Barker, Note, *Commercial Landlords' Duty Upon Tenants' Abandonment—To Mitigate?*, 20 IOWA J. CORP. L. 627, 648 (1995) (mentioning briefly that it is an issue "that the statutes do not address"); Jeremy K. Brown, *A Landlord's Duty to Mitigate in Arkansas: What It Was, What It Is, and What It Should Be*, 55 ARK. L. REV. 123, 144 (2002) ("Most jurisdictions have not addressed this issue, but the ones that have are split as to whether a waiver will be valid."); Stephanie G. Flynn, *Duty to Mitigate Damages upon a Tenant's Abandonment*, 34 REAL PROP. PROB. & TR. J. 721, 766–67 (1999) (stating that "[c]ases and statutory law in many states do not address whether the duty to mitigate may be waived by the parties in the lease"). Despite largely discussing it in a residential lease, for a more in-depth discussion of waiver in the Illinois statute concerning the duty to mitigate, see Anthony J. Aiello, Legislative Note, *Illinois Landlords' New Statutory Duty to Mitigate Damages: Ill. Rev. Stat. Ch. 110, § 9-213.1*, 34 DEPAUL L. REV. 1033, 1054–58 (1984–85).

even now only a few courts and legislatures have resolved this issue.[7] A number of states have fundamentally rejected attempts by landlords to waive their duty to mitigate damages arising out of breach of residential leases.[8] In a commercial lease, however, the issue is not as simple. This Note will focus on the law applying to commercial leases.

States are split on whether parties to a commercial lease can contractually waive the duty to mitigate. In North Carolina and Ohio, appellate courts have ruled that despite the default rule requiring the duty to mitigate, waiver is allowed.[9] At least one other state—Texas—has ruled that a waiver is unenforceable, but has only done so with legislative intervention.[10] Likewise, while attempting to predict New Jersey law, a federal court has ruled against enforcing waiver.[11]

In Part I, this Note will review the evolution of the duty to mitigate in both residential and commercial leases. In Part II, the Note will consider how the states have justified adopting the duty as a default rule. Then, following a discussion of why states have chosen to enforce or void waivers in Part III, the Note will recommend in Part IV that states follow the lead of Texas and forbid contractual waiver in commercial leases.

I. AN INTRODUCTION AND HISTORY OF THE DUTY TO MITIGATE

A. The Duty to Mitigate

Parties to a property lease agree that a tenant will occupy a property owned by the landlord for a certain amount of time.[12] One of the many ways that a breach may arise occurs when the tenant abandons the premises before the end of the lease and refuses to pay the remainder of rent due

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[7] *See* Brown, *supra* note 6, at 144.

[8] When approaching residential leases in states, these rejections have been by statute. *See, e.g.*, MICH. COMP. LAWS ANN. § 554.633(1)(k) (West 2013); MONT. CODE ANN. § 70-24-404(1)(b) (West 2013); TEX. PROP. CODE ANN. § 91.006 (West 2013). The Uniform Residential–Landlord Tenant Act, on which many states base their statutes, "apparently" forbids waiver clauses. Aiello, *supra* note 6, at 1056–57.

[9] *See infra* Part III.B.

[10] *See infra* Part III.A.1.

[11] New Jersey's highest court has not ruled on waiver. A lower state court held that the duty may be contracted away, but the Southern District of New York, in attempting to predict New Jersey law, held waivers unenforceable. Though not binding on a state court, this case is used as an example of a court supporting the unenforceability of waiver clauses. *See* discussion *infra* Part III.A.2.

[12] *E.g.*, Franklin v. Jackson, 847 S.W.2d 306, 308 (Tex. Ct. App. 1992).

under the agreement.[13] At common law, a landlord facing a breach has three options: (i) he may accept the surrender of the premises and agree to a premature termination of the contract; (ii) he may reenter, attempt to re-let the premises, and hold the original tenant liable for accrued rent between the time of reentry and the abandonment; or (iii) he may do nothing and hold the tenant liable for the entire term.[14]

The law has evolved to generally disfavor landlord inaction; doctrine says that he cannot be allowed to sit idle and attempt to collect damages as rent becomes due or at the end of the contract when all damages have accumulated.[15] Economic rationale supports a regime that disallows landlords to rest apathetically.[16] As a result, jurisdictions implement a default duty to forbid landlord inaction.[17]

The duty to mitigate in a lease prevents a landlord from recovering avoidable damages,[18] typically unpaid rent.[19] The reality of the duty to

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[13] *See, e.g.*, New Towne L.P. v. Pier 1 Imports (U.S.), Inc., 680 N.E.2d 644, 645 (Ohio Ct. App. 1996).

[14] *See, e.g.*, Wilson v. Ruhl, 356 A.2d 544, 546 (Md. 1976), *overruled on other grounds by* Millison v. Clarke, 413 A.2d 198 (Md. 1980). When the landlord re-lets the property, the original tenant is also liable for any deficiency between the original rent and the new rental amount. *Id.*

[15] *See, e.g.*, *id.*

[16] For discussion, *see infra* Part II. *Contrast* Sommer v. Kridel, 378 A.2d 767, 773 (N.J. 1977) (stating with respect to residential leases that "claims must be governed by more modern notions of fairness and equity.").

[17] "The landlord is not required to simply fill the premises with any willing tenant; the replacement tenant must be suitable under the circumstances." Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 299 (Tex. 1997). Courts usually state the standard as using reasonable efforts. *See, e.g.*, *id.* (asserting that the "duty to mitigate requires the landlord to use objectively reasonable efforts to fill the premises"); Frenchtown Square P'ship v. Lemstone, Inc. 791 N.E.2d 417, 421 (Ohio 2003) (declaring it "requires only reasonable efforts").

[18] *See* Flynn, *supra* note 6, at 723–24.

[19] *See, e.g.*, Kotis Props., Inc. v. Casey's, Inc. 645 S.E.2d 138, 139 (N.C. Ct. App. 2007) (stating that landlord filed suit "for breach of the Lease. [Landlord] sought the accrued unpaid rent...."); New Towne L.P. v. Pier 1 Imports (U.S.), Inc., 680 N.E.2d 644, 645 (Ohio Ct. App. 1996) (stating that the landlord filed an "action to recover rent on the breach of a commercial lease."). A landlord may also sue for anticipatory breach of the lease in anticipation of the tenant not paying rent. *See Austin Hill*, 948 S.W.2d at 295. Anticipatory breach is a well-settled cause of action under contract law. *See generally* W. W. A., Annotation, *Doctrine of Anticipatory Breach as Applicable to a Contract which the Complaining Party has Fully Performed*, 105 A.L.R. 460 (2012). When applying the duty to mitigate to a lease, some courts consider collection of rent as separate from an action like anticipatory breach. *See, e.g.*, M & V Barocas v. THC, Inc., 549 N.W.2d 86, 87–88 (Mich. Ct. App. 1996) ("A landlord's action for rent has been recognized as a

mitigate can make the label misleading,[20] for failure of the duty does not create an independent cause of action.[21] It does not place an obligation on the landlord to re-let the premises, but only requires the landlord to make reasonable efforts to limit damages caused by the abandoning tenant.[22] If the landlord does not attempt to mitigate, unpaid rent that could have been collected from another tenant (had efforts been made to re-let) is unrecoverable.[23]

The duty to mitigate is an original feature of contract law and has become a default rule for commercial leases in most states today.[24] That default rule has developed through legislation or judicial mandate within the past few decades.[25] The trend is part of a larger historical push away from approaching leases through the lens of property law and toward interpreting a lease using contract principles.[26] As with many legal doctrines, the United States inherited the duty to mitigate from English law.[27]

B. A History of Leases: Property, Contract, or Both?

In early common law England, leases were originally interpreted by courts as contracts, but as the demands of tenants began to change, courts transformed the lease into a legal conveyance of land.[28] As such, property law governed and the tenant gained some "abstract portion of the land" for the limited time of the lease.[29]

The property interest was born from the historical agricultural relationship between landlords and tenants.[30] When a tenant needed land for

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distinct cause of action that differs from other available remedies for breach of a lease contract.").

[20] *See* Flynn, *supra* note 6, at 723–24. The *Restatement (Second) of Contracts* calls the duty to mitigate "[a]voidability as a [l]imitation on [d]amages." RESTATEMENT (SECOND) OF CONTRACTS § 350 (1981).

[21] *E.g.*, *Austin Hill*, 948 S.W.2d at 299; Flynn, *supra* note 6, at 723–24.

[22] Flynn, *supra* note 6, at 723–24.

[23] *Id.* at 724.

[24] *See generally* Barker, *supra* note 6.

[25] *E.g.*, 735 ILL. COMP. STAT. ANN. 5/9-213.1 (West 2013); *Austin Hill*, 948 S.W.2d 293, 295–96 (2003).

[26] *See* Glen Weissenberger, *The Landlord's Duty to Mitigate Damages on the Tenant's Abandonment: A Survey of Old Law and New Trends*, 53 TEMP. L.Q. 1, 3–7 (1980).

[27] *See* Edwin Smith, Jr., *Extending the Contractual Duty to Mitigate Damages to Landlords when a Tenant Abandons the Lease*, 42 BAYLOR L. REV. 553, 555–57 (1990).

[28] *See* Flynn, *supra* note 6, at 724. The trends of the landlord-tenant relationship have usually changed as a result of granting greater rights for the tenant. Weissenberger, *supra* note 26, at 3–7; Smith, *supra* note 27, at 556–57.

[29] Frenchtown Square P'ship v. Lemstone, Inc., 791 N.E.2d 417, 419 (Ohio 2003).

[30] *See S*mith, *supra* note 27, at 555–57.

farming or other agrarian purposes, the property was not just a living space but a livelihood.[31] The property approach was designed to benefit a tenant with causes of actions that go along with a possessory interest in the land.[32] The practical result was that the tenant was left, for the most part, to do what he wanted with the leased land while the landlord no longer had any obligations.[33]

The legal ramifications of viewing the lease as a land conveyance produced results that did not include the duty to mitigate.[34] In a property framework, "a tenant who vacated was considered to have abandoned his estate, not the landlord's, thus negating any duty on the part of the landlord to mitigate the loss."[35] Courts generally followed property doctrine and reasoned that because the landlord did not have an obligation to the property, he did not have a duty to mitigate.[36] However, the law began to change once courts returned to contract law for interpreting leases.[37]

Since the 1800s, the societal shift toward urban centers and industrial commerce changed the dynamic of the landlord-tenant relationship.[38] Land became less valuable for agricultural purposes and more important for the residential or commercial buildings that could be placed on top of it.[39] As the motives for renting started to change, tenants began to demand different rights and leases began to be interpreted through contract law.[40] The reintroduction of contract principles as applied to leases came from a "growing realization that the conveyance fiction fails to comport with the realities of most modern tenancies...."[41] As the lease came to be viewed more as a contract, courts interpreted it in accordance with contract law.[42]

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[31] *See id.*

[32] Flynn, *supra* note 6, at 725. *See* Schneiker v. Gordon, 732 P.2d 603, 606 (Colo. 1987) (en banc).

[33] *See* Flynn, *supra* note 6, at 725.

[34] *See infra* Part II.

[35] Rubin v. Dondysh, 549 N.Y.S.2d 579, 581 (Civ. Ct. 1989).

[36] *Id.*

[37] *Id.*

[38] *See* Smith, *supra* note 27, at 557.

[39] *See id.*

[40] *See id.*

[41] Weissenberger, *supra* note 26, at 5.

[42] *See* Reid v. Mutual of Omaha Ins. Co., 776 P.2d 896, 904 (Utah 1989) ("The trend rule reflects the more modern view that leases are essentially commercial transactions, contractual in nature."). Along with the duty to mitigate, courts started enforcing the contractual issue of the duty of good faith and fair dealing. In *Brennan Associates v. OBGYN Specialty Group, P.C.*, the court clearly analogizes the commercial lease as a contract while discussing the application of the implied covenant of good faith and fair

The process of transformation has left leases to be seen as hybrid documents; property is involved, but contract principles are often applied.[43] As one court noted:

> [T]he present law of leases is a blend of property concepts and of contractual doctrines, made for the service of a wide variety of objectives; agrarian, urban and financial. This historical background makes it clear that we can expect varying proportions of these basic ingredients in the decision of cases litigated now and in the future. Any fixity of proportions would destroy the elasticity of the law, which is, at once, its glory, its challenge and its factor of uncertainty.[44]

The law has embraced the combination of legal doctrines. Neither body of law can be looked to exclusively when attempting to find a solution to a case involving a lease.[45]

II. THE DUTY TO MITIGATE FOR COMMERCIAL LEASES AS ADOPTED BY THE STATES

While jurisdictions disagreed on whether to apply contract law to leases, those that did were confronted with the question of forcing the duty to mitigate upon landlords. At first, courts followed the common law and interpreted leases as a land conveyance, ruling a landlord had no duty to mitigate.[46] For a time, this remained the majority rule.[47] The no-mitigation rule was supported by opinions finding that the landlord-tenant relationship was personal and a landlord should not be compelled to take a new tenant.[48] Courts stated that an abandoning tenant should not benefit from

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dealing. The court does not address why it is interpreting the lease as a contract, it simply performs the analysis. *See* 15 A.3d 1094, 1103 (Conn. App. Ct. 2011).

[43] *See, e.g.*, Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 299 (Tex. 1997); O'Brien v. Black, 648 A.2d 1374, 1376 (Vt. 1994); Flynn, *supra* note 6, at 725.

[44] Schneiker v. Gordon, 732 P.2d 603, 607 (Colo. 1987) (en banc) (quoting 2 R. POWELL, THE LAW OF REAL PROPERTY ¶ 221[1], at 187 (1986)).

[45] *See id.* at 606.

[46] *E.g.*, Holy Props. Ltd., L.P. v. Kenneth Cole Prods., Inc., 661 N.E.2d 694, 696 (N.Y. 1995) ("Leases are not subject to this general rule [of the duty to mitigate], however, for, unlike executory contracts, leases have been historically recognized as a present transfer of an estate in real property." (citations omitted)).

[47] *E.g.*, Dulworth v. Hyman, 246 S.W.2d 993, 996 (Ky. Ct. App. 1952) (stating that as of that date a landlord is not bound to mitigate damages in "a majority of the jurisdictions").

[48] *See, e.g.*, Weissenberger, *supra* note 26, at 6; *see also* N. Haven Crossing L.P. v. C & C Inc., No. CVNH 97078350, 1997 WL 630012, at *3 (Conn. Super. Ct. Sept. 29, 1997) ("The reasons offered for this rule are that the landlord has expressed a personal choice in selecting the tenant, and is not required to accept a substitute …." (quoting

his own breach,[49] and that landlords should be able to reasonable rely on the established majority, no-mitigation rule.[50] These rationales "largely depend[ed] on acceptance of the rationality of the common law fiction that a lease is a conveyance of property, not a contract."[51] Commentators criticized these no-mitigation arguments and predicted a mitigation rule would eventually be widely adopted.[52]

Court decisions have shown there are compelling arguments in favor of following the contractual approach to leases and adopting the duty to mitigate along with it.[53] Most states have adopted common law or legislative changes requiring mitigation or something similar.[54] Courts slowly began to adopt the obligation in a commercial setting[55] and have determined that commercial leases, in particular,

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2 RICHARD R. POWELL, POWELL ON REAL PROPERTY § 17.05 (rev. ed. 1991) (internal quotation marks omitted))).

[49] Weissenberger, *supra* note 26, at 6. *E.g.*, Reget v. Dempsey-Tegeler & Co., 238 N.E.2d 418, 419 (Ill. App. Ct. 1968) ("The rationale is that the tenant cannot by his own wrong in abandoning the premises impose a duty upon the landlord.").

[50] Weissenberger, *supra* note 26, at 6. *E.g.*, *Holy Props.*, 661 N.E.2d at 696 ("Parties who engage in transactions based on prevailing law must be able to rely on the stability of such precedents. In business transactions, particularly, the certainty of settled rules is often more important than whether the established rule is better than another or even whether it is the 'correct' rule." (citations omitted)).

[51] Weissenberger, *supra* note 26, at 6–7.

[52] For an in-depth discussion of why these arguments fail, *see* Weissenberger, *supra* note 26, at 6–7. These arguments are beyond the scope of this Note.

[53] *E.g.*, Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 296 (Tex. 1997).

[54] According to *Austin Hill*, only six states follow a no-mitigation rule: Alabama (Ryals v. Laney, 338 So.2d 413, 415 (Ala. Civ. App. 1976) (residential); Crestline Ctr. v. Hinton, 567 So.2d 393, 396 (Ala. Civ. App. 1990) (commercial)), Georgia (Love v. McDevitt, 152 S.E.2d 705, 706 (Ga. Ct. App. 1966) (residential); Lamb v. Decatur Fed. Sav. & Loan Ass'n, 411 S.E.2d 527, 530 (Ga. Ct. App. 1991) (commercial)), Minnesota (Markoe v. Naiditch & Sons, 226 N.W.2d 289, 291 (Minn. 1975) (residential and commercial)), Mississippi (Alsup v. Banks, 9 So. 895, 895 (Miss. 1891) (residential)), New York (Holy Properties, Ltd. v. Kenneth Cole Prods., Inc., 661 N.E.2d 694, 696 (N.Y. 1995) (commercial)), and West Virginia (Arbenz v. Exley, Watkins & Co., 44 S.E. 149, 151 (W. Va. 1903) (commercial)). *Id.* at 297 n.2.

[55] Many courts seem to have adopted the rule for residential leases before accepting it in a commercial setting. *See, e.g.*, Frenchtown Square P'ship v. Lemstone, Inc., 791 N.E.2d 417, 421 (Ohio 2003) (discussing whether the duty to mitigate extends to commercial leases). New York has a peculiar situation in which its lower courts disagree on whether to extend the duty to mitigate. *See* Rubin v. Dondysh, 588 N.Y.S.2d 504, 505 (App. Term 1991) ("However, although there may be a duty placed upon residential landlords to attempt to rerent and thereby mitigate damages, no such requirement exists in the context of commercial leases." (internal citations omitted)). *But see* 29 Holding Corp. v. Diaz, 775 N.Y.S.2d 807, 808 (Sup. Ct. 2004) ("Although most persons appear to

> reflect numerous and complex negotiations similar to other contracts. There are an increasing number of covenants included in commercial leases, emphasizing the idea that a modern commercial lease is essentially an exchange of promises, and should be viewed under the principles governing the law of contracts. It is a general principle of contract law that one who suffers a breach must take reasonable steps to mitigate damages.[56]

The complexity of commercial leases incentivized courts to treat them as commercial contracts and the duty to mitigate followed from the decision.

Among other reasons, imposing the duty ensures economic efficiency.[57] It "promotes the most productive use of the land while at the same time, it discourages injured parties from suffering avoidable economic losses."[58] While promoting economic efficiency, the obligation does not benefit one party at the expense of the other; the landlord is "in as good [of] a position" as if the tenant had not abandoned the property while the tenant is relieved from paying the due rent.[59]

Due to the varied options landlords are given when faced with an abandoning tenant, states have varying and nuanced approaches as to when a landlord has a duty to mitigate damages.[60] As is expected with multiple jurisdictions and differing opinions, states also disagree about the ability to waive the duty to mitigate.

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believe that a lessor has a duty to mitigate in a residential setting but not a commercial setting, this view is an uninformed and oversimplified construction of the law."). The New York Supreme Court, Appellate Division (the second highest court in New York) quickly stated that a lease at issue "itself provided that the landlord was under no obligation to mitigate damages" but there is no further analysis of the waiver provision. Comar Babylon Co. v. Goldberg, 116 A.D.2d 551, 552 (N.Y. App. Div. 1986). Because of this myriad of decisions, New York law is not used for this paper.

[56] New Towne L.P. v. Pier 1 Imports (U.S.), Inc., 680 N.E.2d 644, 646 (Ohio Ct. App. 1996) (internal citations omitted).

[57] *Id.*

[58] *Id.*

[59] *Id.*

[60] *Compare* K & R Realty Assocs. v. Gagnon, 639 A.2d 524, 526 (Conn. App. Ct. 1994) (holding that when a landlord refuses to accept a tenant's surrender, there is no duty to mitigate, but "[w]hen the landlord elects to terminate the tenancy, however, the action is one for breach of contract ... and, when the tenancy is terminated, the landlord is obliged to mitigate his damages.") *with* Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 300 (Tex. 1997) (stating that "the landlord has a duty to mitigate only if (1) the landlord actually reenters, or (2) the lease allows the landlord to reenter the premises without accepting surrender, forfeiting the lease, or being constructed as evicting the tenant").

III. WAIVING THE DUTY TO MITIGATE IN COMMERCIAL LEASES

As stated above, waiving the duty to mitigate in a commercial lease has not often been discussed in detail.[61] When the issue is mentioned, the general conclusion is that most states simply have not addressed waiver.[62] However, a select number of states have recently ruled or enacted statutes addressing it.[63]

A. Waiver is Forbidden

1. Texas

Texas is one of a few states that directly addresses contracting away the duty to mitigate. Under a statute titled "Landlord's Duty to Mitigate Damages," the law reads: "A provision of a lease that purports to waive a right or to exempt a landlord from a liability or duty under this section [i.e., the landlord's duty to mitigate] is void."[64] A closer examination of the statute reveals a conflicted history.

Common law in Texas allowed waiver. *Austin Hill Country Realty v. Palisades Plaza, Inc.* is the seminal Texas Supreme Court decision on the duty to mitigate in commercial leases.[65] Palisades Plaza entered into a five-year commercial lease with Austin Hill.[66] Palisades, as the landlord, owned and operated an office complex.[67] Due to the action of the tenant-defendants, collectively "Austin Hill," Palisades sued for anticipatory breach[68] of the lease.[69] At trial, Austin Hill introduced evidence that

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[61] *See supra* text accompanying note 6.

[62] *E.g.*, Flynn, *supra* note 6, at 766.

[63] In addition to the cases discussed here, Arkansas has also decided a case relating to waiver of the duty to mitigate. Weingarten/Arkansas, Inc. v. ABC Interstate Theatres, Inc., 811 S.W.2d 295, 298 (Ark. 1991); *see also* Sylva Shops L.P. v. Hibbard, 623 S.E.2d 785, 791 (N.C. Ct. App. 2006) (citing *Weingarten/Arkansas* as "holding that the parties to a lease agreement can provide that the landlord has no duty to mitigate damages upon the tenant's default"). However, this case was decided mostly within the context of a surrender clause, so its wider applicability is limited and is not used for this Note. Additionally, the New York case *Comar Babylon Co. v. Goldberg*, cited by *Sylva Shops* as support, is also not used for this paper. *See supra* text accompanying note 55.

[64] TEX. PROP. CODE ANN. § 91.006(b) (West 2013).

[65] 948 S.W.2d 293 (Tex. 1997).

[66] *Id.* at 294.

[67] *Id.*

[68] For a discussion on how anticipatory breach as a cause of action may factor into an analysis of the duty to mitigate, see *supra* note 19.

[69] "Palisades received conflicting instructions about the completion of the suite [contracted over in the lease] from" the two owners of Austin Hill, and the defendant's failure

attempted to prove Palisades had failed to mitigate damages that resulted from the breach.[70]

In its opinion, the Texas Supreme Court imposed the duty to mitigate on commercial leases, citing economic efficiency among its justifications.[71] The court also framed its decision in the context of public policy, stating that "policy requires that the law discourage even persons against whom wrongs have been committed from passively suffering economic loss which could be averted by reasonable efforts."[72] Incentivizing the landlord to re-let fosters productive use of property and benefits the public.[73] The court considered the increased possibility that unoccupied property may be vandalized,[74] its own aversion to imposing contract penalties,[75] and the growing trend to view leases as "business arrangements."[76]

The court did not discuss waiver in-depth, but in its conclusion it recognized the duty to mitigate "*unless the commercial landlord and tenant contract otherwise*."[77] No other mention of waiver was made. This statement alone is directly opposed to the statute enacted by the Texas legislature, which expressly forbids waiver in any lease situation.[78] The statute overrides *Austin Hill*'s dicta, but the court's opinion is evidence of the divergent positions of the legislature and judiciary.

In addition, the Texas statute was enacted at nearly the same time as the *Austin Hill* decision.[79] *Austin Hill* was decided in July 1997, while the public law for this statute was signed by the Texas Governor in June 1997.[80]

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to designate a representative in which Palisades could keep in contact with was treated as an anticipatory breach. *Austin Hill*, 948 S.W.2d at 295.

[70] *Id.*

[71] *Id.* at 299 (stating that "the state of Texas calls for productive use of property as opposed to avoidable economic waste").

[72] *Id.* at 298 (internal quotation marks omitted).

[73] *Id.*

[74] *Id.* ("If the landlord is encouraged to let the property remain unoccupied, 'the possibility of physical damage to the property through accident or vandalism is increased.'" (quoting Schneiker v. Gordon, 732 P.2d 603, 610 (Colo. 1987))).

[75] *Id.* (stating that "allowing a landlord to leave property idle ... permits the landlord to recover more damages than it may reasonably require to be compensated for the tenant's breach. This is analogous to imposing a disfavored penalty upon the tenant." (quoting Reid v. Mutual of Omaha Ins. Co., 776 P.2d 896, 905–06 (Utah 1989)) (internal quotation marks omitted)).

[76] *Id.*

[77] *Id.* at 299 (emphasis added).

[78] *See* TEX. PROP. CODE ANN. § 91.006(b) (West 2013).

[79] 1997 Tex. Gen. Laws 1205.

[80] *Id.*

This timeline places the common law case decision *after* the statute,[81] but *Austin Hill* was argued in September 1996, before the bill was first filed in the Texas Senate.[82] Perhaps it can be argued the legislature voided waiver provisions in commercial leases for the reasons the duty to mitigate became a default rule, as described in *Austin Hill*.[83]

2. The Federal Decision in New Jersey

New Jersey currently has unsettled state law about whether contractual clauses waiving the duty to mitigate should be enforced, but at least one federal court interpreting New Jersey law has addressed the issue.[84] In *Carisi v. Wax*,[85] a New Jersey lower court held that a waiver is enforceable, stating that the parties may contractually "obviate [the] tenant's right to have the landlord mitigate damages."[86] A few years later, an appellate court decided to "leave that determination [of waiver] for a case in which the issue is squarely presented."[87] After that, *Carisi* was parenthetically referred to, but the highest court in New Jersey, the Supreme Court, did not indicate whether it agreed with the ruling.[88] It cited *Carisi* to support that "on several occasions lower courts have extended the mitigation rule to commercial leases."[89]

The Southern District of New York, in *Drutman Realty Co. v. Jindo Corp.*, received a case almost directly on point. The court needed to apply New Jersey law to decide whether a waiver provision was valid.[90] The court discussed the unresolved status in New Jersey and mentioned that it must "look to the treatment of commercial leases under New Jersey law generally" to determine what its Supreme Court would do if confronted with the issue.[91] Choosing to follow the state's contractual foundations, the district court did not enforce the waiver.[92]

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[81] At least one author stated that *Austin Hill* "provoked" the Texas statute. Kent Altsuler, *A Landlord's Duty to Mitigate in Texas: What if You Build It, And They Don't Come?*, HOUS. LAW., July/Aug. 2011, at 27.

[82] 1997 Tex. Gen. Laws 1205.

[83] *See infra* Part IV for further discussion.

[84] The rest of this paragraph is adopted from *Drutman Realty Co. v. Jindo Corp.*, 865 F. Supp. 1093, 1100 (S.D.N.Y. 1994).

[85] 471 A.2d 439 (N.J. Bergen Dist. Ct. 1983).

[86] *Id.* at 443.

[87] Fanarjian v. Moskowitz, 568 A.2d 94, 99–100 (N.J. Super. Ct. App. Div. 1989).

[88] McGuire v. City of Jersey City, 593 A.2d 309, 314 (N.J. 1991).

[89] *Id.*

[90] Drutman Realty Co. v. Jindo Corp., 865 F. Supp. 1093, 1100 (S.D.N.Y. 1994).

[91] *Id.* at 1100–01.

[92] *Id.* at 1099.

The federal court did not cite any case in New Jersey that examined waiver as closely as did *Carisi*. Instead, the court cited a case discussing the duty to mitigate generally[93] and stated that the New Jersey "court based its determination on the strong public policy in favor of ensuring that a landlord make reasonable efforts to mitigate damages."[94] The *Drutman* court followed the policy argument, stating that "[c]ourts will not enforce provisions ... that are contrary to public policy."[95] Further examining New Jersey contract principles, the *Drutman* court concluded that there was "an absolute duty to mitigate damages" and that a clause relieving the landlord of that duty was unenforceable.[96]

Of course, the *Drutman* case is not binding on any New Jersey state court, nor can it be said to be the law in New Jersey.[97] However, the case may be indicative of a court's rationale when not enforcing a waiver clause in a commercial lease. It was public policy to promote the absolute duty to mitigate damages, and contract law forbids a clause waiving it.[98] The court relied on the same component of contract law as *Austin Hill*—public policy.[99] However, while analyzing public policy the federal court decided not to enforce the waiver. The courts in North Carolina and Ohio discussed public policy further but landed opposite of *Drutman*.

B. Waiver is Allowed

1. North Carolina

The North Carolina Court of Appeals recently ruled on waiver in *Sylva Shops L.P. v. Hibbard*.[100] Taking the opposite stance of the Texas legislature, the North Carolina court thoughtfully spelled out why it believed waiver of the duty to mitigate is not against public policy and is enforceable.[101]

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[93] Carter v. Sandberg, 458 A.2d 924 (N.J. Super. Ct. 1983).

[94] *Drutman*, 865 F. Supp. at 1100 (quoting Carter v. Sandberg, 458 A.2d 924, 926 (N.J. Super. Ct. 1983) (internal quotation marks omitted)).

[95] *Id.* at 1101.

[96] *Id.* During this analysis, the court alluded to the economic waste theory as a support for its argument.

[97] *See generally* Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938).

[98] *Drutman*, 865 F. Supp. at 1101.

[99] The examination of public policy was for the duty to mitigate generally and not for waiver. *See* Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 298 (Tex. 1997).

[100] 623 S.E.2d 785 (N.C. Ct. App. 2006).

[101] *Id.* at 790–92.

The case arose when the loss of business from college students during the summer forced a tenant—a family-owned bagel shop—to close.[102] The landlord attempted to find a new tenant, but the original tenant claimed that the landlord's refusal to lower rent price led to difficulties in finding a replacement occupant.[103] The lease between the landlord and the original tenants contained a provision relieving the landlord of any obligation to mitigate,[104] and the landlord relied on this clause in arguing it owed no duty to the original tenants.[105]

The North Carolina court recognized that state law imposed a general duty to mitigate, but there was still a dispute because "[t]he existence of a common law duty of care does not, however, absolutely preclude parties from agreeing in a contract to relieve a party of that duty."[106] To hold a contract clause unenforceable in North Carolina, it must either violate a statute or be against public policy.[107] No statute was violated, so the court examined the provision under public policy.[108]

While alluding to contract law, the court stated that it was "the broad policy of the law which accords to contracting parties freedom to bind themselves as they see fit...."[109] Parties to a contract have the freedom to "exercise poor judgment" and the law will not protect them from a legal agreement that is unwise in hindsight.[110] Though not specifically referenced in the opinion, this rationale can be known as the freedom to contract.[111] The court also analogized that clauses relieving parties from negligence liability are enforceable.[112]

The court quickly dismissed an argument about possible unequal bargaining power between the parties, stating that "[t]he lease represents an arm's length commercial transaction with both parties using brokers or

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[102] *Id.* at 788.

[103] *Id.*

[104] *Id.* at 789 (quoting the lease provision which stated, "[l]andlord shall have no obligations to mitigate Tenant's damages by reletting the Demised Premises.").

[105] *Id.* at 788.

[106] *Id.* at 790.

[107] *Id.* at 789 (quoting Hlasnick v. Federated Mut. Ins. Co., 539 S.E.2d 274, 276 (N.C. 2000)).

[108] *Id.* at 790–92.

[109] *Id.* (quoting Hall v. Sinclair Ref. Co., 89 S.E.2d 396, 397–98 (N.C. 1955)) (internal quotation marks omitted).

[110] *Sylva Shops*, 623 S.E.2d at 789 (quoting Troitino v. Goodman, 35 S.E.2d 277, 283 (N.C. 1945)).

[111] *See generally* 16B AM. JUR. 2D *Constitutional Law* § 641 (2009).

[112] *Id.*

advisors to assist them in obtaining the best possible bargain."[113] It claimed that commercial leases "generally involve relatively equal bargaining power due to the availability of other space and the fact that neither party is compelled to make a deal."[114] The contract created no "risk of injury to the public or the rights of third parties,"[115] and in support of its arguments, the court cited cases from jurisdictions that ruled such clauses had not violated public policy.[116] In a subsequent case the next year, the Court of Appeals affirmed its decision in *Sylva Shops*.[117]

2. Ohio

An Ohio appellate court ruled similarly to North Carolina when confronted with a waiver of the duty to mitigate. The court in *New Towne L.P. v. Pier 1 Imports (U.S.), Inc.*[118] started from the same analytical position as the Texas and North Carolina courts, namely, that there was a default duty to mitigate in commercial leases, but the Ohio court decided similar to North Carolina and ruled that a waiver clause was enforceable.[119]

Pier 1 Imports, as tenant, entered into a ten-year contract with New Towne.[120] After nearly five years, Pier 1 defaulted on the rent and notified New Towne of its intent to abandon the premises.[121] Within the original lease, there was a provision waiving any duty New Towne may have to mitigate damages.[122] New Towne decided against reclaiming the property or terminating the lease and instead sued for the monthly rent as it became

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[113] 623 S.E.2d at 790 (stating also that the defendants "admitted that '[n]obody was holding a gun to [their] head' to sign the lease").

[114] *Id.* at 791. While concluding its discussion, the court stated that "[u]nder these circumstances, the public policy of this State cannot relieve a party of the consequences of a commercial agreement that, in hindsight, proved not to be advantageous." *Id.* at 792.

[115] *Id.* at 790.

[116] *Id.* at 791. These cases include *Austin Hill* and *New Towne*, both discussed in this Part. For discussion about the Arkansas and New York cases cited, see *supra* note 63.

[117] *See* Kotis Props., Inc. v. Casey's, Inc., 645 S.E.2d 138, 140 (N.C. Ct. App. 2007) (examining the exact language of the contract to determine whether there truly was a waiver).

[118] 680 N.E.2d 644, 647 (Ohio Ct. App. 1996).

[119] *Id.* at 646–47.

[120] *Id.* at 645.

[121] *Id.*

[122] *Id.* ("If LANDLORD does not elect to terminate this Lease on account of any default by TENANT, LANDLORD may, from time to time, without terminating this Lease, recover all rent as it becomes due under this Lease.") (quoting the Lease Agreement).

due.[123] The trial court ruled for summary judgment in favor of New Towne and Pier 1 appealed.[124]

The Court of Appeals focused on the duty to mitigate more than the waiver issue.[125] When it shifted to waiver, the court examined the lease at issue minimally, stating that "[p]arties of equal bargaining power are free to enter into any agreement."[126] It stated that only a violation of law or public policy could render an otherwise valid contract unenforceable.[127] Instead of diving in-depth into a discussion of public policy, as the *Sylva Shops* court did, the court simply stated the lease "does not injure the welfare of the public in any way."[128] The court made no further inquiry into public policy[129] and concluded that the waiver clause was enforceable.[130] The Ohio Supreme Court affirmed *New Towne* through dicta, stating that "*barring contrary contract provisions*, a duty to mitigate damages applies to all leases."[131]

IV. ANALYSIS

As demonstrated in the cases above, the enforceability of a provision waiving the duty to mitigate has largely revolved around the idea that the public welfare is not harmed by transactions in which the parties had equal bargaining power.[132] This overall analysis stems from contract law, where contracts are enforceable unless they are illegal or are against

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[123] *Id.*

[124] *Id.* The trial court originally granted summary judgment based on reasoning that New Towne had no duty to mitigate damages. The court of appeals changed its reasoning, but affirmed the summary judgment ruling. *Id.* at 647.

[125] The court used some of the already mentioned arguments in favor of mitigation. *Id.* at 646; *see supra* discussion in Part II.

[126] *New Towne*, 680 N.E.2d at 647.

[127] *Id.* ("A rental agreement may include any terms which are not inconsistent with or prohibited by law, or against public policy." (internal citations omitted)).

[128] *Id.*

[129] *Id.* The court did cite an Ohio Supreme Court case discussing public policy—*Chickerneo v. Society National Bank. Id.* (citing Chickerneo v. Soc'y Nat'l Bank, 390 N.E.2d 1183 (Ohio 1979)). The *Chickerneo* court stated that "[p]ublic policy is a legal principle which declares that no one can lawfully do that which has a tendency to be injurious to the public welfare. The principle must be applied with caution and limited to those circumstances patently within the reasons upon which the doctrine rests." 390 N.E.2d at 1186.

[130] *New Towne*, 680 N.E.2d at 647.

[131] Frenchtown Square P'ship v. Lemstone, Inc. 791 N.E.2d 417, 421 (Ohio 2003) (emphasis added). There was no further discussion of waiver. Note how this is similar to the dicta in *Austin Hill* for Texas, except in Ohio it has not been overruled by statute.

[132] *See supra* Part III.B.

public policy.[133] The rest of this Note will argue that (i) enforcing waiver of the duty to mitigate injures the public welfare; (ii) it should not be assumed that parties to a commercial lease have equal bargaining power; and (iii) blanket rules voiding waiver clauses, as in Texas, should be issued.[134] Through examination of these three arguments, it is clear that rejecting waivers of the duty to mitigate provides the greatest safeguard against abuses for all commercial tenants.

A. Injury to the Public Welfare

There are many different ways to define public policy. The *Restatement (Second) of Contracts* provides guidelines,[135] but many states have chosen their own interpretation. North Carolina, for example, defines public policy "as the principle of law which holds that no citizen can lawfully do that which has a tendency to be injurious to the public or against the public good."[136] While analyzing public policy, the North Carolina Court of Appeals discussed how leases are private and "[n]o rights of third parties are involved."[137] Though no third parties may be present in private commercial leases, it is an assumption that the public goes unharmed by

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[133] *E.g.*, *New Towne*, 680 N.E.2d at 647; RESTATEMENT (SECOND) OF CONTRACTS § 178(1) (1981) ("A promise or other term of an agreement is unenforceable on grounds of public policy if legislation provides that it is unenforceable or the interest in its enforcement is clearly outweighed in the circumstances by a public policy against the enforcement of such terms.").

[134] At least one author has proposed that courts "should undergo a case-by-case analysis of the circumstances surrounding the [waiver] provision to ensure that it was freely negotiated and is fair and reasonable." Brown, *supra* note 6, at 145–46. This approach seems costly and time consuming. For reasons discussed *infra*, a blanket rule would be more favorable.

[135] RESTATEMENT (SECOND) OF CONTRACTS § 178(2)–(3) (1981). These sections discuss what to consider when weighing the enforceability of a contract provision. For example, when a clause is considered for refusal due to public policy, a court should consider:

> (a) the strength of that policy as manifested by legislation or judicial decisions;
> (b) the likelihood that a refusal to enforce the term will further that policy;
> (c) the seriousness of any misconduct involved and the extent to which it was deliberate; and
> (d) the directness of the connection between that misconduct and the term.

Id.

[136] Sylva Shops L.P. v. Hibbard, 623 S.E.2d 785, 790 (N.C. App. Ct. 2006) (quoting Coman v. Thomas Mfg. Co., 381 S.E.2d 445, 447 n.2 (N.C. 1989)).

[137] *Id.* (quoting New River Crushed Stone, Inc. v. Austin Powder Co., 210 S.E.2d 285, 287 (N.C. App. Ct. 1974)).

enforcing a waiver clause. States that chose to adopt the duty to mitigate did so largely for economic reasons, and those economic benefits are extended when parties cannot contract them away.

When the law does not force landlords to mitigate an abandoning tenant's damages, usable property is more likely to lay idle for an extended amount of time.[138] Sophisticated landlords may include a clause waiving mitigation simply because of self-interest,[139] and when property is underutilized there is economic waste resulting in a loss of economic efficiency.[140] Usable property should not remain idle for extended periods of time in order to benefit a landlord while the public is harmed.

Enforcing a waiver provision violates the contract doctrine that renders the duty unwaivable.[141] Although leases are still considered hybrid documents,[142] courts could provide consistency by maintaining the contractual principles they have already adopted. The failure to extend contract law is a departure from the traditional analysis of the duty to mitigate that does not provide any concrete advantages.[143]

When discussing public policy, the consequences of allowing waiver of the duty to mitigate should not be forgotten. A court could very likely push a tenant into bankruptcy by finding a waiver provision enforceable. It can be argued that many tenants initially breach a lease and fail to pay rent because they cannot afford it. Most abandoning commercial tenants are not corporations with deep pockets able to absorb judgments that make them liable for an entire lease.[144] For every Pier 1 Imports there is an independent, small business-tenant similar to the bagel shop owners in *Sylva Shops*.

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[138] *Id.*

[139] *Id.* (stating that "allowing a landlord to leave property idle when it could be profitably leased and forc[ing] the absent tenant to pay rent for that idled property permits the landlord to recover more damages than it may reasonably require to be compensated for the tenant's breach" (quoting Reid v. Mut. of Omaha Ins. Co., 776 P.2d 896, 905–06 (Utah 1989))).

[140] *See* Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 298 (Tex. 1997).

[141] *See* John V. Orth, *LEASES: Like Any Other Contract?*, 12 GREEN BAG 2D 53, 65 (2008) (adding that "contracts may include a provision for liquidated damages—so long, of course, as it is not simply a disguised penalty"). But contracted-for liquidated damages cannot be "unreasonably large." RESTATEMENT (SECOND) OF CONTRACTS § 356(1) (1981).

[142] *See* discussion *supra* Part I (addressing the lease as a hybrid document of contract and property law).

[143] Consistency was often an argument *against* adopting the duty to mitigate at all. Weissenberger, *supra* note 26, at 6.

[144] Sylva Shops L.P. v. Hibbard, 623 S.E.2d 785 (N.C. Ct. App. 2006).

In the United States, there are 27.9 million small businesses, whereas only 18,500 companies have 500 or more employees.[145] Most are sole-proprietorships, making up 73.2 percent of all small businesses.[146] For small businesses that employ others in addition to the owner, 27 percent are partnerships or sole-proprietorships and another 44 percent are S corporations that can be taxed at personal rates.[147] When these businesses are unable to pay rent their owners may be personally liable for the judgments against them. If the abandoning commercial tenant is just a small mom-and-pop store, a judgment of only a couple thousand dollars can be disastrous, as it likely was for the tenants in *Sylva Shops*, where the court referenced a separate case in which the bagel shop filed for bankruptcy.[148]

According to the U.S. Small Business Administration, small "[b]usiness bankruptcies numbered 48,000 in 2011 ... [and remember that] not all firm deaths are business bankruptcies, and many business owners file personal bankruptcy instead of business bankruptcy."[149] When businesses and owners are filing for bankruptcy, the economy suffers and the public is injured.[150] The societal costs of bankruptcy are large, with "[a]t least some of the costs of the consumer bankruptcy system ... are borne by all borrowers as a group; other costs are borne by lenders, and still other costs are *social deadweight loss*."[151] Landlords do not appear to face the same threat of bankruptcy when courts enforce the duty to mitigate—it is likely the landlord will be able to find another tenant. Even if the landlord reasonably searches for but does not find a new tenant, he will still get damages and legally be made whole.[152] Forcing the duty to mitigate is the easiest, most straightforward way to avoid placing unnecessary economic burdens on the public.

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[145] *Frequently Asked Questions*, U.S. SMALL BUS. ADMIN., OFFICE OF ADVOCACY 1 (Sept. 2012), http://www.sba.gov/sites/default/files/FAQ_Sept_2012.pdf.

[146] *Id.*

[147] *Id.* at 4.

[148] Sylva Shops, 623 S.E.2d at 788 n.1.

[149] U.S. SMALL BUS. ADMIN., OFFICE OF ADVOCACY, *supra* note 145, at 3.

[150] *See* Todd J. Zywicki, *An Economic Analysis of the Consumer Bankruptcy Crisis*, 99 NW. U. L. REV. 1496, 1499 (2005) (stating that "the option of bankruptcy creates a moral hazard problem and increases the risk associated with consumer lending, leading creditors to charge higher interest rates, demand collateral or a larger down payment, increase monitoring to prevent default, or increase penalties for risky behavior such as late payments.").

[151] *Id.* (emphasis added).

[152] Even if the landlord is a small business owner himself, the reasonable costs of attempting to mitigate damages are typically paid for by the breaching party. *E.g.*, Sommer v. Kridel, 378 A.2d 767, 773 (N.J. 1977). Thus, the landlord does not incur any additional losses to his business.

B. The Possibility of Unequal Bargaining Power

Besides the economic risks, allowing waiver of the duty to mitigate puts many potential tenants at risk of manipulation. Unlike residential leases—where the parties are automatically deemed to have unequal bargaining power[153]—courts that allow waiver seem to assume that both parties to a commercial transaction are on a level playing field.[154] While this could be true for cases involving corporate giants (such as Pier 1 Imports in *New Towne*), the truth is that many commercial tenants are small businesses or those not sophisticated in legal matters.

Most businesses in the United States are not large corporations.[155] Of the 27.9 million small businesses in the United States, 48 percent are *not* home-based.[156] These statistics lead to the conclusion that for nearly half of small businesses, a commercial location outside of the owner's home is viewed as a necessity by the small business owners. Likely more than a nominal amount of commercial tenants are small business owners without the resources necessary to equalize bargaining power with a counter-party who engages in lease transactions more frequently.

In *Sylva Shops*, the tenants were bagel store owners that had to close down their shop because college students went away for the summer.[157] It is possible these individuals had as little bargaining power in signing a commercial lease as they may have had signing a residential lease. While tenants are not forced into an agreement,[158] the risk of naivety and possible exploitation of small business owners is substantial. Unknowledgeable potential tenants are unaware of the legalities inherent in leases and

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[153] *See, e.g.*, Taylor v. Leedy & Co., 412 So. 2d 763, 766 (Ala. 1982) ("Clearly, landlords have greater bargaining power than tenants in residential leases. A tenant must live somewhere. The tenant has no meaningful choices. He can accept this landlord or go to another landlord who charges the same rent and asks the tenant to sign the same standard form lease. In other words, the modern standard form lease is in essence an adhesion contract. A survey of residential leases in Alabama would show that almost all leases contain these exculpatory clauses.").

[154] *See, e.g.*, Sylva Shops L.P. v. Hibbard, 623 S.E.2d 785, 791 (N.C. Ct. App. 2006) ("In examining commercial real estate lease transactions in light of public policy considerations, we recognize that negotiations generally involve relatively equal bargaining power....").

[155] U.S. SMALL BUS. ADMIN., OFFICE OF ADVOCACY, *supra* note 145, at 1.

[156] *Id.*

[157] *Sylva Shops*, 623 S.E.2d at 788.

[158] *See, e.g.*, *id.* at 790 (stating the tenants "admitted that '[n]obody was holding a gun to [our] head.'").

many cannot afford a lawyer, if they even believe they need one.[159] Hiring real estate brokers may be argued to equalize the bargaining power, but there is no guarantee that a short waiver provision in a lease will be flagged as threatening. Furthermore, one would be holding a real estate broker to have the legal sophistication of a lawyer. Also, unlike the court in *Sylva Shops* urges, many of these small business owners cannot just "look for another location,"[160] either because they may be unable to afford another location or the location chosen is the one necessary for the business.[161] Overall, the presumption that all parties to every commercial lease have equal bargaining is not always true and courts should err in favor of protecting tenants.

When courts analyze public policy, they are attempting to balance the possible benefits of enforcing the transaction against the harm to the public welfare. All businesses are injured when there is empty space due to a landlord's inaction. Furthermore, millions of small business owners may endure harm by unwittingly contracting to a waiver clause. While small businesses need to be protected, the general benefits a large corporation could receive from a court voiding waiver clauses need to be addressed.[162] A blanket rule approach to forbidding waivers of the duty to mitigate does not address the advantages larger companies may receive, but it is the best method to easily follow public policy.

C. Adoption of a Blanket Rule

In order to avoid the economic consequences of allowing waiver of the duty to mitigate, courts should adopt a blanket rule similar to Texas's

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[159] Typically the reasoning for residential leases. *See* Ian Davis, *Better Late Than Never: Texas Landlords Owe A Duty to Mitigate Damages When A Tenant Abandons Leased Property:* Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc.*, 40 Tex. Sup. Ct. J. 228 (Jan. 10, 1997)*, 28 TEX. TECH L. REV. 1281, 1303 (1997) (quoting Respondent's Motion for Rehearing at 7, Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 40 Tex. Sup. Ct. J. 228 (Jan. 10, 1997) (No. 03-94-00485-CV) ("A promitigation rule perhaps makes sense in the area of residential tenancies where the tenants are most often not familiar by education or experience with the intricacies of a lease and the effects of their decisions, and in which they rarely have the same bargaining power as the landlord.")).

[160] *Sylva Shops*, 623 S.E.2d at 791.

[161] Typically, "[c]hoosing a business location is perhaps the most important decision a small business owner or startup will make...." *Tips for Choosing Your Business Location*, U.S. SMALL BUS. ADMIN., http://www.sba.gov/content/tips-choosing-your-business-location (last visited Feb. 24, 2014).

[162] This will be discussed more in depth *infra* Part IV.C.

statute.[163] Section 91.006(b) of the Texas Property Code states that "[a] provision of a lease that purports to waive a right or to exempt a landlord from a liability or duty under this section [i.e., the duty to mitigate] is void."[164] Such a bright line rule solves any issues that are consequences of other "as applied" tests.

A blanket rule is easy to enforce and provides certainty to contracting parties.[165] Not only do landlords benefit by knowing that they must always attempt to mitigate, but a court can easily adjudicate disputes brought before it, conserving judicial resources. There is no confusion as to the illegality of the clause. The court will not have to conduct any sort of analysis of the specifics of the parties at hand. The size and dynamics of a tenant's business are different for every lease, along with the relative bargaining power of the two parties at issue. Bargaining power especially is dependent on numerous factors in any given case, some of which may be quantifiable (wealth or number of previous similar transactions) and others not (expertise or knowledge of the transaction). If a court were to attempt to analyze all factors in all waiver disputes, substantial expenses would be incurred.

A potential problem with a blanket rule approach is that it confers an advantage to large corporations that would not exist under another scheme. It can be argued that large corporations benefit from an absolute rule voiding a wavier clause when the corporation should be held the agreement it had the sophistication to bargain away during lease negotiations. Proponents of enforcing the waiver clause tend to justify their support with ideas similar to the freedom to contract.[166] The freedom to contract is the belief that courts should not interfere with agreements between private parties.[167] Large corporate tenants, equipped with in-house legal departments[168] or hired attorneys, likely know better than to contract away the duty to mitigate. Or, perhaps a large corporation will take the risk and

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[163] TEX. PROP. CODE ANN. § 91.006 (West 2013).

[164] *Id.*

[165] *See, e.g.*, Niesig v. Team I, 558 N.E.2d 1030, 1034 (N.Y. 1990) ("The single indisputable advantage of a blanket preclusion—as with every absolute rule—is that it is clear. No lawyer need ever risk disqualification or discipline because of uncertainty as to which [parties] are covered by the rule and which not.").

[166] *See, e.g.*, New Towne L.P. v. Pier 1 Imports (U.S.), Inc., 680 N.E.2d 644, 647 (Ohio Ct. App. 1996).

[167] *See* Sylva Shops L.P. v. Hibbard, 623 S.E.2d 785, 790 (N.C. Ct. App. 2006).

[168] According to at least one survey company, businesses are increasing the size of their legal in-house departments. *See* Press Release, HBR Consulting, Law Departments Increase Internal Staff and Keep More Work In-House, According to 2011 HBR Law Department Survey (Oct. 7, 2011), http://www.hbrconsulting.com/downloads/HLDS_2011_Press_%20Release_111007.pdf.

bargain away the duty for some other more desirable clause in the lease. Supporters of the freedom to contract believe that businesses should be able to make these strategic (or mistaken) decisions and should not look to the courts to relieve them of their obligations.[169] But the benefits that a large corporate tenant might attain by a blanket rule do not outweigh the costs of allowing waiver of the duty to mitigate. The risks to small business tenants who have unequal bargaining power are just too great. Preventing the suffering of a larger[170] class of businesses is worth the possible unfair benefits to another.[171]

An effort to divide leases between "small business tenants" and "larger business tenants" would help alleviate the worries of allowing large corporations to profit unfairly from the rule. A possible distinction for a court could mirror the U.S. Small Business Administration's definition of a small business: companies with less than 500 employees are considered small.[172] But this division may be arbitrary; a tenant with 499 employees is still relatively large and its owners may have the expertise that other smaller businesses may not. Any attempt to categorically enforce waiver based on available resources and the number of personnel fails because these quantitative distinctions do not fully address the fundamental problem of unequal bargaining power between parties.

Another attempt could be to decide on a case-by-case basis and weigh factors to determine a tenant's ability to waive. Some considerations could be the number of employees in a tenant's business and whether the tenant had legal representation. Parol evidence could be used to learn more about the negotiations between the parties at hand.[173] This sort of review, however, would be costly to courts and unnecessarily extend discovery and litigation.[174] In contrast, a blanket rule would prevent all inquiry into the evidence at hand and conserve judicial resources.

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[169] *See, e.g.*, *New Towne*, 680 N.E.2d at 647.

[170] *See* U.S. SMALL BUS. ADMIN., OFFICE OF ADVOCACY, *supra* note 145, at 1.

[171] A possible alternative, if a state was adamant for allowing parties to waive, but still had concerns, could be to require a clause in all leases that explicitly and conspicuously states that the tenant is waiving the landlord's duty. A requirement would be similar to that required under U.C.C. § 2-316(2) for waiving the implied warranty of merchantability. *See* U.C.C. § 2-316(2) (2012).

[172] *See* U.S. SMALL BUS. ADMIN., OFFICE OF ADVOCACY, *supra* note 145, at 1.

[173] For more about parol evidence inclusion in contracts see Ferdinand S. Tinio, Annotation, *The Parol Evidence Rule and Admissibility of Extrinsic Evidence to Establish and Clarify Ambiguity in Written Contract*, 40 A.L.R.3d 1384 (1971).

[174] As is true with nearly every case, a goal of the courts is to avoid costly litigation. *See, e.g.*, Hansen v. Hansen, 770 A.2d 1278, 1285 (N.J. Super. Ct. App. Div. 2001) ("The ultimate goal must be to avoid piecemeal litigation and the possibility of inconsistent results.").

Though sophisticated tenants may unfairly benefit from a bright line rule, this advantage does not outweigh the benefit of helping tenants at risk of being taken advantage of through a waiver clause. A blanket rule similar to Texas's would prevent injustice to small business owners, while also saving the legal system money and time by not having to examine the bargaining powers of parties to every lease.

CONCLUSION: CONTINUE TO PROTECT TENANTS

Leases are important instruments used every day in America. Their prevalence is undeniable. Throughout the course of legal history, leases have gone through several transformations, eventually becoming the documents used today. In an effort to increase tenant rights, leases have become a mixture of property and contract doctrine. For residential leases, courts have near unanimously determined that leases should reflect the fact that tenants can be manipulated through the unequal bargaining power possessed by landlords. It is now time to adopt the same mentality for their commercial counterparts. The waiver of the duty to mitigate should be universally unenforceable.

With a diverse commercial landscape, a landlord and tenant can differ significantly in bargaining power. Parties to a commercial lease should not be assumed to be sophisticated in business and law and a court should not assume a tenant to have mastery simply because the lease is commercial in nature.

The duty to mitigate was originally applied to leases in part to help prevent unnecessary tenant misfortune. A tenant can waive the duty without any knowledge of the consequences of his action. The economic disadvantages of having no duty to mitigate are well known and largely accepted. The results of not enforcing the duty to mitigate are also readily apparent. Tenants are at a greater risk of bankruptcy if they do not receive the protection that most states have claimed they are allowed to obtain. When parties declare bankruptcy, society is burdened with the economic consequences.

By universally forbidding any contractual waiver of the duty to mitigate, courts can protect vulnerable tenants while preventing costly litigation and serving the public welfare. The protection granted by the legal system should not be waivable by the same parties the law is seeking to protect.

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