IN THE COURT OF APPEALS OF IOWA

No. 0-092 / 09-0999
Filed April 8, 2010

DUCK CREEK TIRE SERVICE, INC., an Iowa Corporation, and MIDWEST MEXICAN CONNECTION, LTD., An Iowa Corporation,
Plaintiffs-Appellants,

vs.

GOODYEAR CORNERS, L.C.,
Defendant-Appellee.

Appeal from the Iowa District Court for Scott County, Mark J. Smith, Judge.

Duck Creek Tire Service, Inc. and Midwest Mexican Connection, Ltd., sub-sublessees, appeal the ruling of the district court finding they failed to prove Goodyear Corners, L.C., assignee of the sub-sublessor, breached their sub-subleases. **REVERSED AND REMANDED WITH INSTRUCTIONS.**

Michael J. McCarthy of McCarthy, Lammers & Hines, Davenport, for appellants.

Richard A. Davidson of Lane & Waterman L.L.P., Davenport, for appellee.

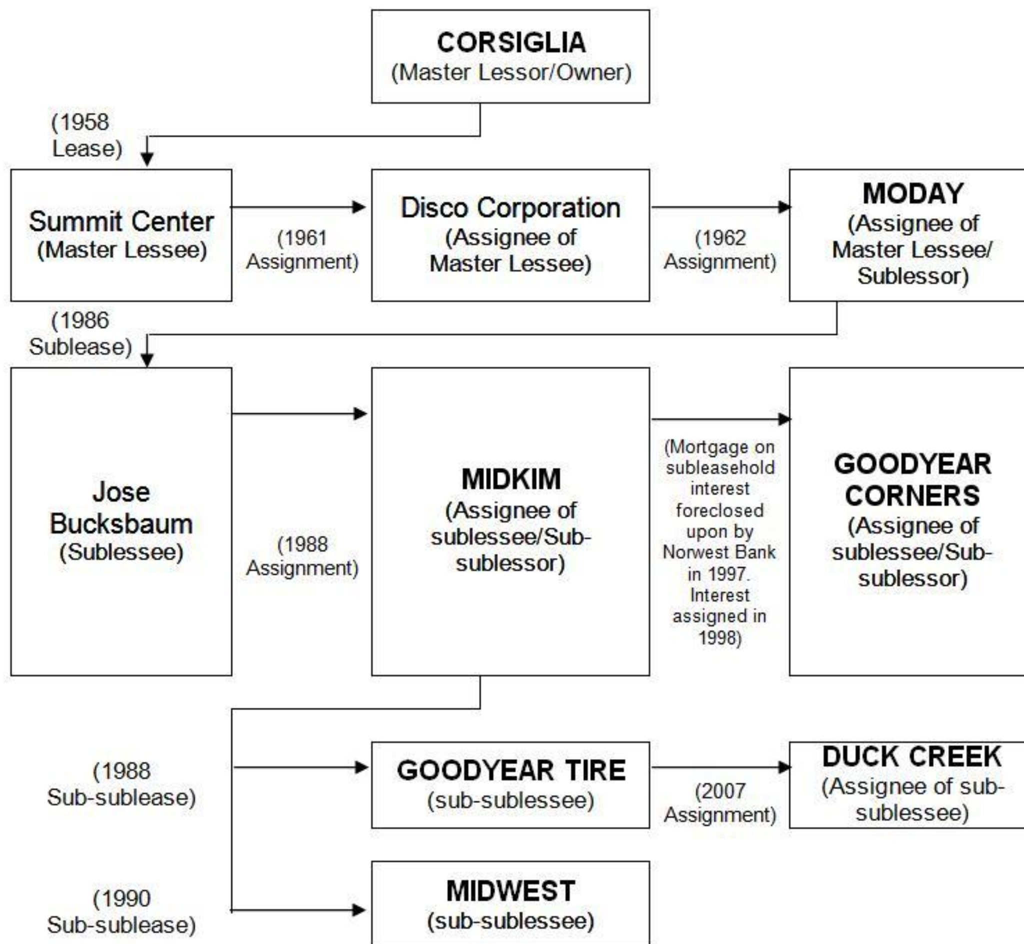
Considered by Sackett, C.J., and Doyle and Danilson, JJ.

DOYLE, J.

Duck Creek Tire Service, Inc. and Midwest Mexican Connection, Ltd., shopping center sub-sublessees, appeal the ruling of the district court finding they failed to prove Goodyear Corners, L.C., assignee of the sub-sublessor, breached their sub-subleases. Upon our review, we reverse and remand for the district court to determine damages based upon the existing trial record and to enter an order granting judgment in favor of Duck Creek Tire Service, Inc. and Midwest Mexican Connection, Ltd.

***I. Background Facts and Proceedings*.**

The current controversy centers upon two sub-subleases containing express covenants for quiet enjoyment. To assist the reader in following the complex lease transactions at issue in this case, to be described below, we present the following flow chart:



On November 21, 1958, Antonio Corsiglia entered into a lease with Summit Center for approximately fifteen acres of property located in Bettendorf, Iowa. Summit Center assigned its interest as lessee in the lease to Disco Corporation in 1961. In 1962, Disco Corporation assigned its interest as lessee to individuals doing business as Moday Realty Co. (Moday).

In 1986, Moday subleased approximately one acre of its leased land to Jose Bucksbaum.[1] Buckbaum assigned his interest in the sublease to Midkim, Inc. in February 1988. In December 1988, the sublease was amended by Moday and Midkim, changing terms of the lease not relevant to this appeal.

In September 1988, Midkim entered into a sub-sublease with The Goodyear Tire & Rubber Company (Goodyear Tire) for the lease of 5789 square feet of floor space in a building on Midkim's subleased property. The term of the lease was for twenty years. Additionally, the lease provided, in relevant part:

> If [Goodyear Tire] shall perform all and singular the covenants herein imposed upon it, [Midkim] warrants and will defend [Goodyear Tire] in the enjoyment and peaceful possession of the Demised Premises during the term hereof. . . .
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> . . . .
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> [Midkim] represents and warrants to [Goodyear Tire] that [Midkim] has heretofore entered into a Ground Sublease agreement with the Ground Lessee of the demised premises whereunder [Midkim] has been granted possession and control of the premises and has been granted all rights and privileges necessary for [Midkim] to perform and satisfy all the terms, conditions and obligations and make the covenants contained herein. A true copy of said Ground Sublease agreement shall be delivered to [Goodyear Tire] upon request.

In March 1990, Midkim entered into another sub-sublease with Midwest Mexican Connection, Ltd. ("Midwest") for the lease of 3000 square feet of floor

[1] This sublease contained an express covenant of quiet enjoyment.

space on Midkim's subleased property next to the property sub-subleased to Goodyear Tire. The Midkim–Midwest sub-sublease provided, in relevant part:

> [Midkim] covenants that its interest in said premises is by leasehold interest and that [Midwest] on paying the rent herein reserved and performing all the agreements by [Midwest] to be performed as provided in this Lease, shall and may peaceably have, hold and enjoy the demised premises for the term of this Lease free from molestation, eviction or disturbance by [Midkim] or any other persons or legal entity whatsoever. . . .[2] [Midkim] shall provide [Midwest] with written evidence of [Midkim's] valid leasehold interest.

Some point after Midkim was assigned the sublease from Bucksbaum, Midkim mortgaged its leasehold interest in the property to Norwest Bank. Thereafter, Midkim defaulted on its mortgage, and Norwest Bank foreclosed on its leasehold interest. Norwest Bank obtained a sheriff's deed on February 26, 1997, conveying Midkim's interest in the sublease to Norwest Bank. The deed specifically named Midkim, Goodyear Tire, and Midwest, among others, as defendants to the sale.

In February 1998, Norwest Bank, for valuable consideration, assigned its interest in the sublease to Goodyear Corners, L.C. (Goodyear Corners). The assignment specifically referred to the Buckbaum–Moday 1986 sublease and the subsequent amendment of that lease in 1988 by Midkim and Moday. Additionally, the assignment states, in relevant part:

> [Northwest Bank] hereby covenants with [Goodyear Corners], and its successors in interest, that it holds the lessee's interest in the ground lease; that it has good and lawful authority to sell and convey the ground lease; that the lessee's interest in the ground lease is free and clear of all liens and encumbrances, subject to easements and restrictions of record; and it covenants to

[2] The sub-sublease expressly provided an exception to its covenant of quiet enjoyment in the event of condemnation of the subject property.

> warrant and defend the ground lease against the lawful claims of all persons, except as may be above stated.

In December 2006, Corsiglia sent a notice to quit, notice of nonpayment of rent, and notice of voiding rental agreement to Moday, stating that Moday's lease would terminate in fifteen days if the rental delinquency was not cured. On January 3, 2007, Goodyear Corners was notified by Corsiglia that the original ground lease with Moday on the entire property had been terminated. Goodyear Corners was current in its rent payments and in full compliance of its sublease with Moday when the underlying lease was terminated. Goodyear Corners in turn notified Goodyear Tire and Midwest of the notice from Corsiglia, and Goodyear Tire and Midwest were ultimately forced out of the premises. In February 2007, Goodyear Tire assigned its right in the sub-sublease to Duck Creek Tire & Service, Inc. (Duck Creek). In November 2007, Corsiglia sold the property.

At some point, Corsiglia brought suit against Moday. Goodyear Corners joined in the suit, asserting a third-party claim against Moday. Thereafter, Duck Creek and Midwest intervened, asserting claims against Goodyear Corners for breach of their covenant of quiet enjoyment under the terms of their sub-subleases.

A bench trial on Duck Creek and Midwest's claims against Goodyear Corners was held on December 18, 2008. In February 2009, the district court entered its findings of fact, conclusions of law, and judgment entry in favor of Goodyear Corners. The court found:

> [W]hen Goodyear [Corners] purchased an assignment of interest from Norwest Bank, who had foreclosed on its leasehold mortgage, Goodyear Corners proceeded to collect rents from Duck Creek and [Midwest] as well as collect amounts for common area expenses. They did nothing to indicate to either of the [sub-sublessees] that they did not assume all provisions of the lease previously entered into by the [sub-sublessees] with Midkim. Given these actions by [Goodyear Corners], the court finds that [Goodyear Corners] assumed all obligations under the lease and were bound thereby.

Additionally, the district court found that because Goodyear Corners did not notify Midwest or Duck Creek of any other aspect of the lease which they did not intend to honor, Goodyear Corners was estopped from now denying its obligations to the sub-sublessees. However, the court found Duck Creek and Midwest were "under a duty to ascertain the terms of these prior and superior [master] leases and could have obtained guarantees from the superior leaseholders who agree to be bound by the sublease terms." The court further found that because Goodyear Corners was not at fault in the termination of the lease between Moday and Corsiglia, it was impossible for Goodyear Corners to perform the provision allowing quiet enjoyment by the sub-sublessees. The court concluded:

> Since neither [Duck Creek] nor [Midwest] took steps to protect their interest prior to signing [their sub-subleases], they cannot now complain that the termination of the lease between Moday and Corsiglia should not have affected their leasehold interest. Given these facts, the court finds that [the sub-sublessees] cannot obtain damages from Goodyear Corners for termination of the master lease between Moday and Corsiglia.

The court then ruled that Duck Creek and Midwest's claims against Goodyear Corners "should fail for lack of proof of a breach of the lease by [Goodyear Corners]."

Duck Creek and Midwest now appeal.

***II. Scope and Standards of Review*.**

"We review the judgment of a district court following a bench trial in a law action for correction of errors at law." *Chrysler Fin. Co. v. Bergstrom*, 703 N.W.2d 415, 419 (Iowa 2005); *see also* Iowa R. App. P. 6.907 (2009).

> The district court's findings of fact have the effect of a jury verdict, and we are bound by them if they are supported by substantial evidence, i.e., evidence that a reasonable mind would accept as adequate to reach the same findings.

Nathan Lane Assocs., L.L.P. v. Merchs. Wholesale of Iowa, Inc., 698 N.W.2d 136, 138 (Iowa 2005). "[W]e view the evidence in the light most favorable to the district court's judgment." *Chrysler Fin. Co.*, 703 N.W.2d at 419.

***III. Discussion*.**

This is an action for breach of a covenant of quiet enjoyment by sub-sublessees seeking damages against their sub-sublessor. The breach of the covenant of quiet enjoyment resulted from termination of the master lease upon the lessee's failure to pay rent and taxes due.

It is not disputed that Duck Creek and Midwest knew they were not leasing from the owner of the property and that the sub-subleases were subject to prior leases. The district court correctly found that Duck Creek and Midwest had a duty to determine the terms of the prior and superior leases.[3] But notice by Duck Creek and Midwest of the provisions of the master lease is not dispositive of their

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[3] The court cited to *McDuffie v. Noonan*, 29 P.2d 684 (Wash. 1934), and *Baranov v. Scudder*, 170 P. 1122 (Cal. 1918), for this proposition; *see also* 1 Milton R. Friedman and Patrick A. Randolph, Jr., *Friedman on Leases* § 7:7.1, at 7-123 (5th ed. Nov. 2009) ("A subtenant has been said to be under a 'duty' to ascertain the terms of the head lease. This means merely that he is charged with knowledge of its terms.") (hereinafter "Friedman").

claims against Goodyear Corners. In one of the cases cited by the district court, it is stated:

> While, as we have above indicated, a sublessee takes notice of the provisions of the overlease, it does not follow that such notice concludes his rights under his contract with his immediate lessor. He cannot, for instance, hold against the overlandlord for a term longer than that limited in the overlease. There may be other respects in which his knowledge might affect his relations with the overlandlord, or, perhaps, even with his immediate landlord; but that is far from saying that such knowledge deprives him of his right to damages against his lessor for an eviction at the hands of the landlord superior to them both, under some provision of the overlease.

Baranov v. Scudder, 170 P. 1122, 1124 (Cal. 1918).

The district court suggested the sub-sublessees, with knowledge they were sub-sublessees, could have obtained guarantees from the superior leaseholders with the superior leaseholders agreeing to be bound by the sub-sublease terms.[4] The court then concluded that because neither of the sub-sublessees took such steps to protect their interests prior to signing the sub-subleases, they could not now complain the termination of the master lease should not have affected their leasehold interest. No one disputes that Duck Creek and Midwest could have sought to obtain such guarantees, and if they had done so, they could have sought recovery against the guarantors.[5] But, this is

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[4] *See*, *e.g.*, *Chrysler Reality Corp. v. Davis*, 877 So.2d 903, 906 (Fla. Ct. App. 2004), *aff'd on reh'g*, 894 So.2d 971 (Fla. 2005) (holding separate non-disturbance agreement between landlord and sublessee may guarantee the sublessee's rights under the sublease in the event the sublessor defaults on the prime lease.)

[5] Without such guarantees, Duck Creek and Midwest would not have a right to recover against the superior leaseholders, as it has been said:

> The reason for the general rule that a sublessee may not sue the lessor for breach of covenant [of quiet enjoyment] is that, as between an original lessor and a sublessee, there is no privity of contract. The sublessee is in privity only with his own sublessor.

not an action against the superior leaseholders, and whether or not the sub-sublessees obtained guarantees from superior leaseholders only relates to their right to recover from those superior leaseholders. The sub-sublessees' right to recover from Goodyear Corners, on the other hand, is founded in their sub-subleases with Goodyear Corners. In our view, whether or not Duck Creek and Midwest obtained guarantees from superior leaseholders is neither dispositive of, nor a bar to, their right to recover as against Goodyear Corners.

It appears to us that the basis of the court's ruling, that the sub-sublessees' claims against Goodyear Corners should fail because of lack of proof of a breach of the lease by Goodyear Corners, lies in the court's conclusion that Goodyear Corners was not at fault for the termination of the master lease thus making it impossible for it to perform the provision in the sub-subleases allowing quiet enjoyment by the sub-sublessees. Accordingly, the question we must answer is whether a sublessor, under the circumstances presented in this case, is insulated from breach of quiet enjoyment claims from its sublessees when the master lease is terminated through no fault of the sublessor. For a

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Marchese v. Standard Realty & Dev. Co., 141 Cal. Rptr. 370, 373 (Cal. Ct. App. 1977). Additionally:

> There is no privity of contract or estate between the original lessor and the sublessee because the lease does not pass to the subtenant, and there is no contractual relation between the subtenant and the lessor. . . .
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> Because of lack of privity, the sublessee does not acquire, merely as a result of the sublease, any right to enforce the covenants or agreements of the lessor contained in the original lease. Sublessees may not maintain actions against the landlord on the original lease, but must seek redress against the sublessor.

49 Am. Jur. 2d *Landlord and Tenant* § 999, at 912-13 (2006) (internal footnotes omitted); *see also Mark-It Place Food, Inc. v. New Plan Excel Realty Trust*, 804 N.E.2d 979, 989 (Ohio Ct. App. 2004); 52 C.J.S. *Landlord & Tenant* § 62, at 128-29 (2003); 1 Friedman § 7:7.1, at 7-122; 1 Arthur R. Gaudio, *The American Law of Real Property* § 5.07[1][b], at 5-139 (1994).

seemingly not uncommon situation, there is a dearth of applicable case law. This case appears to be one of first impression. Although the parties' briefs demonstrate careful research, we are not directed to any Iowa case directly on point. Our research did not uncover any cases on point from Iowa or other jurisdictions.

In Iowa, a covenant of quiet enjoyment is implied in every lease. *Cohen v. Hayden*, 180 Iowa 232, 245, 157 N.W. 217, 221 (1916), *aff'd on reh'g*, 163 N.W. 238, 239 (Iowa 1917). "The implied covenant is a promise that, during the term of his tenancy, the tenant shall not be disturbed in the enjoyment of the premises by the lessor or anyone claiming under him *or by anyone claiming paramount title*." *Rahman v. Fed. Mgmt. Co.*, 505 N.E.2d 548, 550 (Mass. App. Ct. 1978) (emphasis added); *see also Kane v. Mink*, 64 Iowa 84, 19 N.W. 852, 853 (1884) ("The covenant for quiet enjoyment is for the protection of the lessee from the claims of third persons having title paramount to the lessor.").

> It is universally held, except as hereinafter mentioned, that a lease implies a covenant of quiet enjoyment. The covenant is to the effect that the tenant shall have quiet and peaceful possession, as against the lessor or anybody claiming through or under the lessor or anybody with a title superior to the lessor.

3 Friedman § 29:2.1, at 29-2-3.

Here, the sub-subleases at issue contained express covenants of quiet enjoyment, and there is no argument or suggestion from the parties that the express covenants are of a more limited character inconsistent with an implied covenant. The Midwest sublease specifically covenants to Midwest quiet enjoyment "free from molestation, eviction or disturbance by the Landlord *or any*

other persons or legal entity whatsoever." (Emphasis added.) In the Duck Creek sublease, Midkim "warrants and will defend Lessee in the enjoyment and peaceful possession of the Demised Premises for the term hereof." "Generally, the right to or covenant of quiet enjoyment obligates the landlord to refrain from interferences with the tenant's possession during the tenancy, and protects the tenant's right to the peaceful and undisturbed enjoyment and possession of the leasehold." 52A C.J.S. *Landlord & Tenant* § 735, at 98 (2003) (internal footnotes omitted).

> [A]n express covenant in the usual general form, for quiet enjoyment, generally is interpreted to secure the lessee against the acts or hindrances of the lessor and persons deriving their right or title through the lessor or from paramount title, or against all persons lawfully claiming the premises.
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> . . . .
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> Generally, the covenant of quiet enjoyment does not extend to acts of other tenants or third parties unless such acts are performed on behalf of the landlord *or by one claiming paramount title*. The lessor is not responsible for the conduct of the tenants acting within their rights in their own premises. The lessor may, by express provisions, restrict the operation of the covenant to evictions by the lessor or persons claiming under the lessor or by particular third persons or so as to exclude liability for interference by particular parties.
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> Ordinarily the covenant runs with the land and passes to any person as assignee in law who becomes possessed of the term, and is enforceable against the assignee of the reversion, although the lessor's assigns are not mentioned in the lease.

Id. at 98-99 (internal footnotes omitted) (emphasis added). As one treatise further explains:

> The sublease stands on the prime lease and falls with it, whether the prime lease ends by normal expiration, by some limitation based on breach, or by privilege of cancelation. The prime lease may give the prime landlord a privilege to cancel in case of sale, demolition, long-term lease, or for personal use. Cancelation of the prime lease, and with it the sublease, may begin

> with an election by the prime landlord. In the usual situation the subtenant is insulated from the prime landlord and can look only to his immediate landlord, who is both the prime tenant and the sublessor. The sublease may include a covenant of quiet enjoyment, which will give the subtenant a cause of action against his sublessor, but not until he has been evicted.

1 Friedman § 7:7.5, at 7-143.

When Midkim entered into the written sub-subleases, it gave to the sub-sublessees the right to the possession of the property described therein, for the term provided, to which the sub-sublessees became entitled. *See Cohen*, 180 Iowa at 244, 157 N.W. at 220. By their sub-sublease, Midkim guaranteed the sub-sublessees this right. *Id*. The lease itself was an assurance to the parties of the possession, and the right to the enjoyment of the possession, during the term of their sub-subleases. *Id*. Midkim, in executing the lease, bound itself to the performance of the conditions of the sub-subleases. *Id*.

> When a written lease is entered into between two parties competent to make a lease, the purpose of it is to give to the lessee the possession, or the right to the possession, of the property leased, for the period provided in the lease. That is what the lessee contracts for. That is what he is entitled to under his contract. By the making of the lease, this right is guaranteed to him by the assumed lessor. Take this away from the lessee, and you take away all that he has contracted for, and destroy the efficacy of the lease as an assurance of the right to the enjoyment of the premises.
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> . . . .
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> [T]here was [a] . . . covenant for a quiet enjoyment in the lease in question, and this covenant was broken by ouster. It is the very meat of the contract; it is the very purpose, essence, and spirit of the contract; it is what one agrees to give for the consideration to be paid, and it is what the other agrees to pay the consideration for.

Id. at 244-45, 157 N.W. at 220-21.

Midkim, could have, but did not include an exculpatory clause insulating itself from defaults by its lessor.[6] Likewise, Goodyear Corners could have chosen not to take on the assignment because it did not contain such clause or because it found the sub-sublease's terms to be unfavorable. Regardless, Goodyear Corners took the assignment of Midkim's lease from Norwest Bank, and with it, assumed all of Midkim's interest and obligations thereunder in the sub-subleases.[7] Therefore, Goodyear Corners stands in the place of Midkim. *See Farmers & Merchs. Sav. Bank v. Farm Bureau Mut. Ins. Co.*, 405 N.W.2d 834, 838 (Iowa 1987). Similarly, Duck Creek stands in the place of Goodyear Tire. *See id.* Because the sub-subleases provided express covenants of quiet enjoyment to the sub-sublessees, and the sub-sublessees were evicted from the premises through no fault of their own, their express covenants of quiet enjoyment were breached. *Cohen*, 180 Iowa at 245, 157 N.W. at 221. We agree that the sub-sublessees' possessory rights can be no greater than the sub-sublessor's as urged by Goodyear Corners. However, this claim is upon the unrestricted contractual promise of quiet enjoyment, not an action contesting the

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[6] *See*, *e.g.*, *Tapps of Nassau Supermarkets, Inc. v. Linden Blvd., L.P.*, 704 N.Y.S.2d 27, 29 (N.Y. App. Div. 2000) (stating "[t]he lease between [sublessee] and [sublessor] provided that all of [sublessee's] rights 'are subject and subordinate to the rights of landlord under the Master Lease . . . and any termination of the Master Lease shall cause a termination of this lease . . . and [sublessee] shall not be entitled to any compensation . . . for such termination," and holding that the clause made the sublessee's lease dependent upon the continued existence of sublessor's tenancy under the Master Lease, but did not insulate the sublessor from potential liability for its willful actions causing expiration of its own tenancy).

[7] Goodyear Corners states, in its brief, that it "was not the original party to, and did not assume any liabilities or obligations under, the [Goodyear Tire or Midwest] sub-subleases." However, as stated above, the district court found that Goodyear Corners assumed all obligations under the lease when it purchased an assignment of interest in the lease from Norwest Bank, and it was bound thereby. Since Goodyear Corners did not cross-appeal and assert an error concerning whether it assumed all obligations under the lease, this is not an issue before us.

right to possession. Goodyear Corners is liable to its sub-sublessees for the breach of quiet enjoyment, even though the breach was caused by a superior leaseholder.[8] We therefore conclude the district court erred in ruling that Duck Creek and Midwest's claims against Goodyear Corners "should fail for lack of proof of a breach of the lease by [Goodyear Corners]."

***IV. Conclusion*.**

We find that the district court erred in determining the sub-sublessees' claims against Goodyear Corners should fail for lack of proof of breach of the lease by Goodyear Corners. Accordingly, we reverse and remand for the district court to determine damages resulting from Goodyear Corner's breach of the sub-sublease's express covenants of quiet enjoyment, based upon the existing trial record, and to enter an order granting judgment in favor of Duck Creek and Midwest.

REVERSED AND REMANDED WITH INSTRUCTIONS.

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[8] It is noted that the court file reflects that the district court entered a ruling in favor of Goodyear Corners on its motion for partial summary judgment against Moday. The court found that Moday had breached its contract/lease and that Goodyear Corners suffered damages as a result of that breach, for which Goodyear Corners was entitled to judgment.