IN THE COURT OF APPEALS OF IOWA

No. 6-163 / 05-0982
Filed May 10, 2006

SUSAN L. HORTON,
RAY'S UPTOWN DRUG COMPANY,
an Iowa Corporation, and
CENTRAL IOWA COMPOUNDING, INC.,
an Iowa Corporation,
Plaintiffs-Appellees,
vs.

UPTOWN PARTNERS, L.P.,
Defendant-Appellant.

Appeal from the Iowa District Court for Polk County, Michael D. Huppert, Judge.

Uptown Partners, L.P., appeals from adverse rulings of the district court.

REVERSED AND REMANDED.

Michael M. Sellers of the Sellers Law Office, West Des Moines, for appellant.

Joseph M. Borg and William B. Serangeli of Smith, Schneider, Stiles & Serangeli, P.C., Des Moines, for appellees.

Heard by Mahan, P.J., and Hecht and Eisenhauer, JJ.

HECHT, J.

Uptown Partners, L.P., appeals from the district court's adverse rulings on its motions for summary judgment and for new trial following a jury verdict resulting in judgment in favor of Susan Horton. We reverse and remand for proceedings consistent with this opinion.

I. Background Facts and Proceedings.

The record on summary judgment, when viewed in the light most favorable to the plaintiff, Susan Horton, reveals the following. Horton was at all relevant times the owner and operator of Ray's Uptown Drug Company (Ray's Uptown) and Central Iowa Compounding, Inc. (CIC), in Des Moines. Horton purchased Ray's Uptown in 1989 and assumed a lease of the company's business premises located in the Uptown Shopping Center (shopping center). In December of 1993, Horton and Hubbell Realty Company (Hubbell), the owner of the shopping center, entered into a new two-year lease which included an express "non-exclusivity" clause that permitted Hubbell to lease other space in the shopping center to any business, including to a direct competitor of Ray's Uptown. In 1993, Horton began providing specific drug compounding[1] services that were not being provided by any other retail pharmacies in central Iowa at that time.

[1] Drug compounding is a specialty service apart from retail pharmacy. While retail pharmacy involves filling prescriptions with brand-name and generic medications, compounding involves combining medications, pursuant to a physician's prescription, for persons with allergies or swallowing problems. Horton specialized in compounding bio-identical hormone replacement products, but also made compounds for children and pets.

In January of 1996, the shopping center was purchased by Uptown Partners, L.P. (Partners). Soon thereafter, Horton was approached by a representative of Partners, who inquired if Horton would be interested in moving into a larger shopping center space then occupied by Tait's Super Valu (Tait's), a grocery store. Horton declined the opportunity to move her businesses into the larger space, but did receive oral assurance from Partners that no pharmacy competitor would become a tenant without Horton's knowledge, consent, or approval.

In July of 1996, Horton incorporated her compounding business, forming CIC. CIC was housed with Ray's Uptown at the shopping center. In December of 1996, Horton and Partners entered into a new four-year lease[2] that ran from January of 1997 through December of 2001. Horton and Partners negotiated a term in the new lease permitting Ray's Uptown to sublet the premises to CIC. The lease also included a standard integration clause which read:

> This Lease, along with the Lease Guaranty attached hereto, contains the entire agreement between the parties; and no agreement, representation or inducement shall be effective to change, modify or terminate this Lease in whole or in part, unless in writing and signed by the parties. All prior conversations or writings between the parties hereto or their representatives are merged herein and extinguished.

Unlike the previous Hubbell lease, the Partners lease was entirely silent on the issue of whether Partners could lease space in the shopping center to a competitor of Ray's Uptown. There is no evidence tending to prove the

[2] Horton executed the lease d/b/a Uptown Pharmacy, Inc.

exclusivity of Horton's businesses within the shopping center was discussed or negotiated by Horton and Partners in connection with the new lease.[3]

After executing the lease for the period commencing January 1, 1997, Horton expended approximately $50,000 to remodel the leased space to accommodate several laboratories and a consulting space necessary for her compounding business. Despite Horton's successful entry into the compounding business, she was losing money on her retail prescription business. By October of 1998, Horton had stopped accepting third party (insurance) reimbursements.[4]

In 1999, Partners began searching for a new tenant to occupy the shopping center space formerly occupied by Tait's. In December of 1999, representatives from Hy-Vee Foods contacted Horton to inquire if she would like to move her compounding business to a Hy-Vee store located in Windsor Heights. Horton declined. Hy-Vee began providing compounding services at the Windsor Heights location sometime in the spring of 2000.

In July of 2000, Partners signed a written lease with Drug Town, a subsidiary of Hy-Vee providing pharmacy services. Plans for Drug Town's future presence in the shopping center, however, were made public in February. When Horton learned of those plans, she began actively searching for a different business location. She chose a location in Urbandale, and Ray's Uptown ceased

[3] There is also no evidence that any portion of the consideration paid by Horton for the new lease was for exclusivity assurances she had received from Partners earlier that year.

[4] Horton continued to accept Medicaid reimbursements after she abandoned insurance plan reimbursements; however it is undisputed that the bulk of Horton's retail pharmacy business had come from insurance plans, business which she had essentially abandoned by 1999.

doing business in the shopping center on July 27, 2000. Prior to moving her compounding business to Urbandale, Horton negotiated the sale of her retail pharmacy business to Drug Town. Drug Town agreed to purchase that business for $54,000 in exchange for a covenant from Horton not to do any retail prescription-filling business within one-square mile of the shopping center.[5]

Horton, Ray's Uptown, and CIC sued Partners claiming the lease of shopping center space to Drug Town (1) violated the implied covenant of good faith and fair dealing, and (2) constituted tortious interference with prospective business advantage. Following discovery, Partners sought and the district court granted summary judgment on the tortious interference claim, but denied summary judgment on the implied covenant of good faith and fair dealing claim.

The matter was later tried to a jury who returned a verdict in favor of the plaintiffs in the amount of $77,487.99 for damages incurred in the relocation of CIC. Partners filed motions for new trial and for judgment notwithstanding the verdict (JNOV) generally challenging the sufficiency of the evidence to support the verdict. The district court found substantial evidence supporting the jury's verdict and overruled the motion for new trial. The court further determined that the JNOV motion was without merit because Partners failed to renew its motion for directed verdict at the close of all the evidence.

Partners now appeals, claiming the district court erred in denying the motion for summary judgment on the implied covenant of good faith and fair dealing claim. In the alternative, Partners also claims entitlement to a new trial

[5] It should be noted that the covenant not to compete with Drug Town did not prohibit Horton from conducting her compounding business in the shopping center.

because the evidence was insufficient in several particulars to support the jury's verdict.

II. Scope and Standard of Review.

We review the district court's ruling on summary judgment for correction of errors at law. *Kelly v. Iowa Mut. Ins. Co.,* 620 N.W.2d 637, 641 (Iowa 2001). Summary judgment is only appropriate where no genuine issue of material fact presents itself in relation to a particular issue and the moving party is entitled to judgment as a matter of law. Iowa R. Civ. P. 1.981(3). In deciding that issue, we review the record in the light most favorable to the party opposing the motion. *Campbell v. Delbridge,* 670 N.W.2d 108, 109 (Iowa 2003).

We review the denial of Partners' motion for new trial for abuse of discretion. *Gorden v. Carey,* 603 N.W.2d 588, 590 (Iowa 1999). An abuse of discretion occurs when the court's decision is based on a ground or reason that is clearly untenable or when the court's discretion is exercised to a clearly unreasonable degree. *Graber v. City of Ankeny,* 616 N.W.2d 633, 638 (Iowa 2000).

III. Discussion.

A. Exclusivity Covenants Generally.

Our courts imply a covenant of good faith and fair dealing in every contract, *Engstrom v. State,* 461 N.W.2d 309, 314 (Iowa 1991), and we have no doubt that this covenant is likewise operative in a commercial real estate setting. *See also* Restatement (Second) of Contracts § 205, at 99 (1981). "The underlying principle is that there is an implied covenant that neither party [to a contract] will do anything which will have the effect of destroying or injuring the

right of the other party to receive the fruits of the contract." 13 Richard A. Lord, *Williston on Contracts* § 38:15, at 437 (4th ed. 1999) (hereinafter *Williston on Contracts*).

As we have noted above, the lease in question does not address the subject of exclusivity. Horton nonetheless contends an exclusivity term was supplied by Partners' implied covenant of good faith and fair dealing. Because an exclusivity covenant protects a tenant from competition, it takes on characteristics of a restraint of trade. We must construe such covenants narrowly. *Uptown Food Store, Inc. v. Ginsberg,* 255 Iowa 462, 467, 123 N.W.2d 59, 62 (Iowa 1963). Because exclusivity clauses necessarily limit the types of tenants to which a landlord is able to lease commercial real estate, they may also be reasonably viewed as restrictions on the free use of property. *See Maher v. Park Homes, Inc.,* 258 Iowa 1291, 1296-1297, 142 N.W.2d 430, 434 (1966) (stating that restrictions on the free use of property are strictly construed against parties seeking to enforce them and will not be extended by implication or construction beyond the clear meaning of their terms, with all doubts being resolved in favor of unrestricted use of property).

We note that generally the implied covenant of good faith and fair dealing operates upon an express condition of a contract, the occurrence of which is largely or exclusively within the control of one of the parties. *Williston on Contracts* § 38.15, at 435. The implied covenant requires the party in control to exercise their express discretion in a manner which avoids harm to the other party. *See Warner v. Konover*, 553 A.2d 1138, 140-41 (Conn. 1989) (holding that where a commercial lease requires landlord's consent before assigning the

lease or subletting the leased premises, implied covenant prohibited landlord from withholding consent unreasonably); *c.f. Retrofit Partners I, L.P. v. Lucas Industries, Inc.*, 201 F.3d 155, 162 (2nd Cir. 2000) (stating that because the agreement did not require defendant to decide whether or not to invest in plaintiff's enterprise, defendant's failure to make either choice in a timely fashion did not violate the implied covenant of good faith and fair dealing).

Despite Horton's contention that Partners' conduct violated the implied covenant of good faith and fair dealing, she has not cited any cases in which the covenant was construed to prohibit a landlord from entering into a lease with an existing tenant's competitor in the absence of an express provision granting the existing tenant the exclusive right to maintain a certain business within a given area under the landlord's control. Apparently no jurisdiction has gone so far in its interpretation of the implied covenant.

Instead, several jurisdictions have clearly stated that a commercial tenant is not protected from competition without an express covenant clearly stating the same. *See e.g.*, *Leebron and Robinson Rent A Car, L.L.C. v. City of Monroe*, 907 So.2d 875, 879 (La. Ct. App. 2005) (concluding city was not prohibited from constructing and leasing additional car rental booth in municipal airport to plaintiff's competitor where the city was authorized to provide service needs of airport and there were no exclusivity clauses in any of the city's lease agreements with car rental companies);*Timber Ridge Invest. Ltd. v. Marcus*, 667 N.E.2d 1283, 1286 (Ohio Ct. App. 1995) (concluding landlord could lease space on adjacent land to a competing video rental business where no express terms in lease provided that tenants would be exclusive video tenant in landlord's

commercial space). Not only do other jurisdictions require an express exclusivity clause for the anti-competitive protections claimed here by Horton, a relevant illustration supplied in the second Restatement of Contracts presumes an express exclusivity covenant exists before finding a breach of the implied covenant in the commercial tenancy context.[6]

Although we recognize and give proper effect to exclusivity covenants in commercial leases, they restrain trade and we must therefore construe them narrowly. *Uptown,* 255 Iowa at 467, 123 N.W.2d at 62. The New Jersey supreme court in *Davidson Brothers, Inc. v. D. Katz & Sons, Inc.*, 579 A.2d 288 (N.J. 1990), applied a series of reasonableness factors in deciding whether to give effect to anti-competitive clauses in contracts generally. Those factors include (1) whether the covenant had an impact on the considerations exchanged when the covenant was originally executed, (2) whether the covenant clearly and expressly sets forth the restrictions, (3) whether the covenant was in writing and recorded, and (4) whether the covenant is reasonable concerning area, time, or duration. *Davidson Bros.*, 579 A.2d at 295-96. In the absence of an express exclusivity covenant, we cannot assess whether Partners was compensated for the claimed covenant not to lease its commercial space to a

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[6] In a closely analogous fact-pattern, the Restatement gives the following example of a breach of the implied covenant:

> A, owner of a shopping center, leases part of it to B, *giving B the exclusive right to conduct a supermarket*, the rent to be a percentage of B's gross receipts. During the term of the lease A acquires adjoining land, expands the shopping center, and leases part of the adjoining land to C for a competing supermarket. Unless such action was contemplated or is otherwise justified, there is a breach of contract by A.

Restatement (Second) of Contracts § 205 cmt. d, illus. 2 at 101 (1981) (emphasis supplied).

business that sells pharmaceuticals, nor can we measure the duration or scope of the protection implied. In essence, the covenant of exclusivity Horton would have the court imply into her lease with Partners is without boundary.

Further, exclusivity protection of the type claimed by Horton would clearly increase the value of a commercial real estate lease to the tenant. If such protection is implied as a matter of law in a commercial lease notwithstanding the absence of an express exclusivity lease provision, landlords would fail to realize this increased value and the tenant would achieve a benefit for which she did not bargain. If we were to read exclusivity covenants into every commercial lease, we would effectively remove all incentive for commercial tenants to bargain for such anti-competitive protection. Commercial tenants understand they must endure the travails of competition as part and parcel of a market-based economy. If the protection of an exclusivity provision is desired, tenants are free to bargain for and purchase it from willing landlords in exchange for higher rent or a longer lease term. We therefore conclude as a matter of law that the implied covenant of good faith and fair dealing does not preclude a commercial landlord from leasing space to a competitor of an existing tenant in the absence of a lease term expressly granting exclusivity. *See Oakwood Village LLC v. Albertsons, Inc.*, 104 P.3d 1226, 1240 (Utah 2004) (holding the implied covenant "cannot be read to establish new, independent rights or duties to which the parties did not agree ex ante," nor can it compel a party to exercise its contractual discretion to its own detriment and for the benefit of the other party).

B. Appellees' Claim of Oral Exclusivity Promise.

It is undisputed that the lease in effect between Partners and Horton did not expressly confer exclusivity. Despite the absence of a written exclusivity clause, however, there is evidence in the summary judgment record from which a reasonable person could find Partners' agent provided Horton with oral assurance that her pharmacy would be the only one in the shopping center unless she consented to the presence of a competitor. When viewed in the light most favorable to appellees, the summary judgment record tends to prove this oral assurance was given shortly after Partners purchased the shopping center and prior to December of 1996, when Partners and Horton signed the lease at issue here.

In the case before this court, the lease between Horton and Uptown contained an integration clause that is quoted above. A fully integrated agreement is found where, based on the totality of the evidence, the writing appears to be the final and complete expression of the agreement. *Montgomery Props. Corp. v. Economy Forms Corp.,* 305 N.W.2d 470, 476 (Iowa 1981). Where a written agreement is deemed fully integrated, any extrinsic evidence that tends to contradict or even supplement the express terms of the writing is inadmissible. *Whalen v. Connelly*, 545 N.W.2d 284, 290 (Iowa 1996).

We believe the circumstances presented here and the presence of a clear and unambiguous integration clause together compel a conclusion that the lease was fully integrated. *Montgomery Props. Corp.*, 305 N.W.2d at 476. Horton has not adduced any evidence that would suggest the written lease did not constitute a final expression of the parties' agreement. *See* Restatement (Second) of

Contracts § 209(3), at 115. We also believe the alleged oral assurance of exclusivity given to Horton (1) was not given in exchange for a separate consideration and (2) was not the type of term that "might naturally be omitted from the writing," and therefore the oral promise cannot itself serve as proof that the writing was not fully integrated. *See* Restatement (Second) of Contracts § 216(2), at 137. Because we conclude as a matter of law that the lease was fully integrated, even a consistent additional term such as an exclusivity covenant, may not be proven by extrinsic evidence. *Whalen*, 545 N.W.2d at 290; *see also Vu, Inc. v. Pacific Ocean Marketplace, Inc.*, 36 P.3d 165, 167-68 (Colo. 2001) (holding that tenant's failure to reduce an oral exclusivity agreement to writing barred its enforcement against successor landlord where the lease was fully integrated and the tenant signed a writing stating that no agreements beyond the written lease existed).

Finding no enforceable written or oral promise imposed a duty on Partners to protect Horton and her companies from competition by agreeing not to lease space in the shopping center to any business engaged in retail pharmacy or compounding, we conclude the appellees' implied covenant of good faith and fair dealing claim must fail as a matter of law. Because the district court erred in failing to conclude Partners is entitled to summary judgment, we reverse and remand for dismissal of the appellees' petition. We therefore need not and do not address Partners' alternative claim on appeal concerning the denial of its motion for new trial. The costs of this appeal are taxed to appellees.

REVERSED AND REMANDED.