ARE YOU TRYING TO IMPLY SOMETHING?: UNDERSTANDING THE VARIOUS STATE APPROACHES TO IMPLIED COVENANTS OF CONTINUOUS OPERATION IN COMMERCIAL LEASES.

Jerald Clifford McKinney, II[*]

I. INTRODUCTION

This article is being written during tough economic times. In September and October 2008, the Dow Jones Industrial Average dropped a couple thousand points. When economic times are this dire, companies may begin to rethink strategies and may look at store closings as a way to save money. For instance, Circuit City considered closing at least 150 stores in an unsuccessful effort to avoid bankruptcy.[1] Many other retailers have either done the same or considered it. The same thing, however, can happen when the economy is good. Businesses may decide to abandon an existing store and relocate to a better location to follow shoppers or community trends. Businesses may also decide to leave a site that is simply unprofitable for whatever reason.

In many of these cases, the relocating or closing business may be in a long-term lease for its current building. The business could decide to close-up shop and keep paying rent for the remainder of the term.[2] Alternatively, the business may try to find a sublessee or assignee to take over the space. Whichever option is chosen, however, businesses need to carefully consider the potential legal consequences. Many commercial leases address this situation by expressly requiring the tenant to remain open for business known as a "covenant of continuous

∗. Mr. McKinney practices real estate law at the Little Rock firm of Quattlebaum, Grooms, Tull & Burrow PLLC. He earned a Bachelor of Arts from Baylor University, a Master of Public Administration from the University of Arkansas, a Juris Doctor from the University of Arkansas and a Master of Laws from Southern Methodist University. Mr. McKinney is licensed to practice in Arkansas, Mississippi and Texas. Mr. McKinney is currently serving his third term as Chair of the Real Estate Law Section of the Arkansas Bar Association, and he is an editor and founder of the Arkansas Real Estate Review. Mr. McKinney also serves as an Adjunct Professor of Law at the UALR William H. Bowen School of Law where he teaches Real Estate Finance and Real Estate Transactions Skills.

1. Shopping Centers Today Week, International Council of Shopping Centers, Vol. 13, No. 42 (October 27, 2008).

2. Of course, bankruptcy could change the analysis discussed in this article.

operation."[3] Alternatively, the lease may expressly permit the tenant to cease operations at will so long as the tenant continues to pay rent through the end of the lease.[4]

Some commercial leases, however, do not address this situation. What happens then? Many states recognize an implied covenant of continuous operation that could force a tenant to keep its doors open even though there is no requirement to do so written in the four corners of the lease.[5] Arkansas has very limited case law on this issue; there is, however, a federal district court case addressing the concept of an implied covenant of continuous operation.[6] This article will first discuss implied covenants generally, including the "Standard Factors" that many jurisdictions apply. [7] Next, the article will explore the sparse Arkansas case law currently available.[8] This article will also examine how courts in other jurisdictions have addressed the issue.[9] Finally, this article will make suggestions for approaches to implied covenants of continuous operation that could be utilized in Arkansas.[10]

II. IMPLIED COVENANTS IN GENERAL

As noted in the introduction, Arkansas has very little case law on implied covenants of continuous operation. There is some case law on implied covenants in general, and the law is decidedly against finding implied covenants.[11] According to the Arkansas Supreme Court:

> An implied covenant is one that may be reasonably inferred from the whole agreement and the circumstances attending its execution. They are not favored by the law and can be justified only upon the

3. Covenants of continuous operation are sometimes referred to in the industry as "covenants against going dark." *See generally* Austin Hood, *Continuous Operation Clauses and Going Dark*, 36 REAL PROP. PROB. & TR. J. 365, 367 (2001).

4. *See id.* at 370.

5. *See, e.g.*, EMRO Mktg. Co. v. Plemmons, 855 F.2d 528 (8th Cir. 1988); Evans v. Grand Union Co., 759 F. Supp. 818 (M.D. Ga. 1990); First Am. Bank & Trust Co. v. Safeway Stores, Inc., 729 P.2d 938 (Ariz. Ct. App. 1986); Casa D'Angelo, Inc. v. A & R Realty Co., 553 N.E.2d 515 (Ind. Ct. App. 1990).

6. *See* William L. Patton Jr., Family Ltd. P'ship, LLLP v. Simon Prop. Group, Inc., 370 F. Supp.2d 846 (E.D. Ark. 2005); *infra* Part III.A.

7. *See infra* Part II.

8. *See infra* Part III.

9. *See infra* Part IV.

10. *See infra* Part V.

11. *See generally* William L. Patton, Jr. Family Ltd. P'ship., LLLP v. Simon Prop. Group, Inc., 370 F. Supp.2d 846, 848 (E.D. Ark. 2005); Blake v. Scott, 92 Ark. 46, 46, 121 S.W. 1054, 1055 (1909); State v. Real Estate Bank, 5 Ark. 595, 602, 1844 WL 443, at *5 (1844).

> ground of legal necessity arising from the terms of the contract and the circumstances attending its execution.[12]

The Arkansas Supreme Court held that it is the "duty of the Court to construe a contract according to its unambiguous language without enlarging or extending its terms."[13] Nevertheless, Arkansas courts will find implied covenants when necessary.[14] Arkansas case law, however, does not provide a clear protocol for determining when to imply a covenant, but other states do. For example, California, and many other states, have adopted a general protocol that can be applied to evaluate a variety of implied contractual covenants known as the "Standard Factors" that provide the following:

> The rules which govern implied covenants have been summarized as follows: "(1) The implication must arise from the language used or it must be indispensible to effectuate the intention of the parties; (2) it must appear from the language used that it was so clearly within the contemplation of the parties that they deemed it unnecessary to express it; (3) implied covenants can only be justified on the grounds of legal necessity; (4) a promise can be implied only where it can be rightfully assumed that it would have been made if attention had been called to it; (5) there can be no implied covenant where the subject is completely covered by the contract."[15]

12. Amoco Prod. Co. v. Ware, 269 Ark. 313, 320–21, 602 S.W.2d 620, 623 (1980).

13. North v. Phillliber, 269 Ark. 403, 406, 602 S.W.2d 643, 645 (1980). *See also* Koppers Co. v. Mo. Pac. RR. Co., Inc., 34 Ark. App. 273, 277, 809 S.W.2d 830, 832 (1991) (stating, "[i]f there is no ambiguity in the language of a contract, then there is no need to resort to rules of construction. And 'the first rule of interpretation is to give to the language employed by the parties to a contract the meaning they intended.'" (internal citations omitted)).

14. *See generally* SEECO, Inc. v. Hales, 341 Ark. 673, 695, 22 S.W.3d 157, 170 (2000); Sunbelt Exploration Co. v. Stephens Prod. Co., 320 Ark. 298, 305, 896 S.W.2d 867, 871–72 (1995) (noting that there are five types of implied covenants in oil and gas leases and holding that the evidence supported determination that gas producer breached implied duty not to compromise or amend the contract with utility).

15. Lippman v. Sears Roebuck & Co., 280 P.2d 775, 779 (Cal. 1955).
See also First Am. Bank & Trust Co. v. Safeway Stores, Inc., 729 P.2d 938, 940 (Ariz. App. 1986); Danby v. Osteopathic Hosp. Ass'n of Del., 101 A.2d 308, 313–14 (Del. Ch. 1953); Piggly Wiggly S., Inc. v. Heard, 405 S.E.2d 478, 481 (Ga. 1991) (Bell and Benham, JJ., dissenting) (dissent encouraged the state to adopt these standards); Conservative Fed. Sav. and Loan Ass'n v. Warnecke, 324 S.W.2d, 471, 479 (Mo. App., 1959); Downtown Ass'n., Ltd. v. Burrows Bros. Co., 518 N.E.2d 564, 566 (Ohio App. 1986); Frederickson v. Cochran, 449 S.W.2d 329, 333 (Tex. Civ. App. 1969); Brown v. Safeway Stores, Inc., 617 P.2d 704, 710–11 (Wash. 1980); Oliver v. Flow Int'l Corp., 155 P.3d 140, 143 (Wash. App. 2006).

Arkansas has not expressly adopted the Standard Factors. These factors are similar to the language in *Amoco Production Co. v. Ware*[16], where the Arkansas Supreme Court stated that "an implied covenant is one that may be reasonably inferred from the whole agreement and the circumstances attending its execution."[17] This statement seems to at least embody the spirit of the five Standard Factors. Therefore, it is instructive to briefly consider the meaning of each of the five Standard Factors because it is conceivable that Arkansas will either adopt these factors or some close variation of them if Arkansas decides to adopt a factor test to analyze implied covenant cases.

A. The Implication Must Arise From the Language Used or It Must Be Indispensible to Effectuate the Intentions of the Parties

This factor allows an implied term to enter a contract when the implication arises from the language used or when the term is indispensible to effectuate the intentions of the parties. For instance, in *Galier v. Feder Pontiac, Inc.*,[18] the parties entered into a lease agreement which required the tenant to "comply with the 'requirements of all public authorities.'"[19] The tenant allegedly failed to adequately maintain the premises.[20] The landlord sued the tenant for various claims including breach of an implied warranty to maintain the property.[21] The court, however, found that the lease did not include an express warranty to maintain the property.[22] Nevertheless, the court determined that the express covenant in the lease to meet the "requirements of public authorities" necessarily implied a covenant to maintain the property because maintenance would be necessary to meet applicable city ordinances.[23]

B. It Must Appear From the Language Used That It Was So Clearly Within the Contemplation of the Parties that They Deemed It Unnecessary to Express It

This factor allows a term to be implied when it appears from the language used that the omitted term was so clearly within the contem-

16. 269 Ark. 313, 602 S.W.2d 620 (1980).
17. *Id.* at 320–21, 602 S.W.2d at 623.
18. No. 56233, 1989 WL 142397 (Ohio App. 1989).
19. *Id.* at *4 (internal citations omitted).
20. *Id.* at *2–3.
21. *Id*.
22. *Id.* at *4.
23. *See Galier v. Feder Pontiac, Inc.*, 1989 WL 142397 at *4 (Ohio App. 1989).

plation of the parties that they deemed it unnecessary to express it. For instance, in *Tiegs v. Boise Cascade Corp.*,[24] Mr. Don Watts leased a farm to Mr. Frank Tiegs.[25] The lease expressly stated that, "[i]t was 'contingent on [Mr. Watts] finding adequate water for [the] property,' and provided the irrigation for the acreage would apply 7.5 gallons per minute."[26] Mr. Watts provided the water, but Mr. Tiegs alleged that the well water was contaminated by a paper mill's wastewater and was consequently unusable for irrigation.[27] The court concluded that there was an implied covenant that the water would not be contaminated so that it could be used for irrigation.[28]

C. Implied Covenants Can Only Be Justified on the Grounds of Legal Necessity

Sometimes a covenant must be implied to supply a necessary element of consideration without which there would not be a valid contract.[29] In *Oliver v. Flow International Corp.*,[30] Michael Oliver tried to argue for an implied covenant to make reasonable efforts to patent, manufacture, and market a robot that was designed to clean the inside of industrial liquid storage tanks.[31] Mr. Oliver, the robot's inventor, signed an agreement with Flow International Corporation ("Flow").[32] Flow agreed to pay Mr. Oliver $150,000 upon completion of the prototype with additional payments and royalties upon the future sale of robots.[33] Flow paid the $150,000 but made minimal efforts to market the robot.[34] Mr. Oliver argued that the future payments implied a duty to patent, manufacture and market the robot.[35]

The court disagreed with Mr. Oliver because the court believed the $150,000 initial payment was adequate consideration for the agreement. The court contrasted the situation with the case of *Wood v. Lucy, Lady Duff-Gordon*.[36] In *Wood*, Lady Duff-Gordon gave a fashion marketer

24. 922 P.2d 115 (1996).
25. *Id.* at 117.
26. *Id*.
27. *Id.* at 118.
28. *Id.* at 124.
29. *See, e.g.*, Oliver v. Flow Int'l Corp., 155 P.3d 140, 143 (Wash. App. 2006).
30. 155 P.3d 140, 143 (Wash. App. 2006).
31. *Id.* at 142.
32. *Id*.
33. *Id*.
34. *Id*.
35. *See* Oliver v. Flow Int'l Corp., 155 P.3d 140, 142 (Wash. App. 2006).
36. *Id.* at 143 (citing to Wood v. Lucy, Lady Duff-Gordon, 118 N.E. 214, 214–15

the exclusive right to use her name on dress labels.[37] The *Wood* court found an implied covenant to use best efforts to market the dresses because it was the only way that she could get any money.[38] If Lady Duff-Gordon could not be paid, the contract would be unsupported by consideration. Such was not the case in *Oliver,* as the plaintiff had already received a large upfront sum.

D. A Promise Can Be Implied Only Where It Can Be Rightfully Assumed that It Would Have Been Made If Attention Had Been Called to It

This factor requires that a term can be implied only if the court believes that the implied covenant would have been expressly made if attention had been called to it at the time the contract was negotiated. In other words, before a covenant can be implied, there must be no doubt that the parties would have agreed to the term during negotiations if they had thought about it. For instance, in *City of Glendale v. Superior Court*,[39] the City of Glendale entered into a twenty-year written lease to Giovanetto Enterprises, Inc. for Giovanetto to operate a restaurant in city-owned property.[40] Five years later, the City condemned the lease to demolish the building for construction of a public project.[41] Giovanetto sued for breach of contract damages instead of relying on the condemnation award.[42] Giovanetto argued that the twenty-year lease constituted an implied term that the City would not exercise its eminent domain power to terminate the lease early, especially when the parties knew at the time the lease was executed that Giovanetto would have to expend considerable funds to improve the leased space.[43] The court, however, concluded that the City could not have abridged by contract its sovereign authority to take property by eminent domain and that the City likely would not have been willing to make such a promise when it entered into the lease.[44] Therefore, the court concluded that there was no implied agreement not to exercise eminent domain because the conditions might not have been agreed to

(1917)).

37. *Wood*, 118 N.E. at 214.
38. *Id.* at 214–15.
39. 23 Cal. Rptr. 2d 305 (1993).
40. *Id.* at 308.
41. *Id*.
42. *Id.* at 309.
43. *Id.* at 311.
44. *See* City of Glendale v. Super. Ct., 23 Cal. Rptr. 2d 305, 311 (1993).

had the parties contemplated the situation at the time the lease was signed.[45]

E. There Can Be No Implied Covenant Where the Subject Is Completely Covered by the Contract

This factor prohibits finding an implied covenant when the subject is completely covered by the contract. For instance, in *Lowe v. Massachusetts Mutual Life Insurance Co.*,[46] Mr. Karl Lowe's predecessor in interest signed a loan application with the Massachusetts Mutual Life Insurance Company (the "Insurance Company") to borrow $4,700,000 for a real estate development project.[47] The application required a total of $94,000 be paid to the Insurance Company as a deposit that would become liquidated damages if the loan did not close.[48] In exchange for the $94,000, the Insurance Company became irrevocably committed to extend the $4,700,000 loan as long as the borrower satisfied certain conditions.[49] Mr. Lowe did not satisfy the required conditions, and the Insurance Company retained the $94,000 as liquidated damages.[50] Mr. Lowe tried to classify the liquidated damages as punitive to seek a return of the money.[51] In order to trigger a specific California statute that would have made the liquidated damages punitive, Mr. Lowe tried to argue that there was an implied covenant that Mr. Lowe was bound to take out a loan from the Insurance Company.[52] The court dismissed this claim because the required conditions were completely covered by the contract by the parties.[53] Thus, the court could not find an implied covenant.[54]

III. THE IMPLIED COVENANT OF CONTINUOUS OPERATION

This article has considered implied covenants in general, including Arkansas' general approach. The question is how, specifically, will Arkansas courts approach an implied covenant of continuous operation when a case eventually presents itself? So far, there is only one case in

45. *Id*.
46. 127 Cal. Rptr. 23 (1976).
47. *Id.* at 25.
48. *Id.*
49. *Id.*
50. *Id.*
51. *See* Lowe v. Mass. Mut. Life Ins. Co., 127 Cal. Rptr. 23, 25 (1976).
52. *Id.* at 29.
53. *Id.*
54. *Id*.

Arkansas on point, but it is a federal case interpreting Arkansas law, so it is merely persuasive.

In this section, this article will look at the aforementioned federal case and look at how other states have addressed the same issue. Do other states simply apply the Standard Factors or do they use special factor tests to examine implied covenants of continuous operation? Are there commonly used factor tests? Should Arkansas have a special approach to this issue? Does the federal case from Arkansas adequately address the issue as an Arkansas state court would (or should)?

To start, it is useful to consider exactly what an implied covenant of continuous operation is and what it does. An implied covenant of continuous operation, which is also known as a covenant against going dark, arises when a landlord alleges that the tenant has a duty to operate a business within the leased premises at all times during the term of the lease.[55] The opposite of a covenant of continuous operation is the right of a tenant to cease business operations (*i.e.*, let the store go dark) as long as the tenant continues to pay rent and fulfill its other express obligations, such as maintaining the building. A tenant may have a variety of reasons for abandoning a leased building while still paying the rent, including shutting down an unprofitable store or relocating to a better location.[56]

Conversely, a landlord may have many reasons why it wants a tenant to maintain an operating business and is not satisfied with just receiving rent. There are three principal reasons, however, why a landlord would want a continuous operation obligation: (1) the tenant's rental obligations include percentage rent (i.e., the amount of rent is tied to the store's gross sales—if there are no sales, there is no percentage rent);[57] (2) the landlord has co-tenancy obligations with other tenants in the shopping center (i.e., the landlord has either made promises to other tenants that certain anchor tenants[58] will be in the shopping center or that a certain percentage of the shopping center will be occupied by open and operating businesses);[59] and (3) the general appearance and safety of the shopping center may be adversely impacted by

55. *See, e.g.*, William L. Patton, Jr. Family Ltd. P'ship., LLLP v. Simon Prop. Group, Inc., 370 F. Supp.2d 846, 848 (E.D. Ark. 2005).

56. *See* Forrest Drive Assoc. v. Wal-Mart Stores, Inc., 72 F. Supp. 2d 576, 584 (M.D.N.C. 1999).

57. *See, e.g.*, Papa Gino's, Inc. v. Assembly Square Mall, LLC, No. 9804879, 1998 WL 1181159, at *1 (Mass. Super. Ct. 1998).

58. An anchor tenant is a major business that attracts customers to a shopping center.

59. *See, e.g.*, Lilac Variety, Inc. v. Dallas Tex. Co., 383 S.W. 2d 193, 196 (Tex. Civ. App. 1964).

an empty business (i.e., an unoccupied building makes the shopping center look unsuccessful and could become a place for criminals or vagrants to congregate).[60]

Ideally, the parties should address this issue in the lease agreement, but this does not always happen. Also, even if the issue is addressed, a party may allege that the language is somehow deficient, ambiguous or does not adequately address the situation. When there is ambiguity or uncertainty, the opportunity arises for a lawsuit.

A. The *Patton* Case

The only Arkansas case to address implied covenants of continuous operation is an Eastern District Court case, *William L. Patton Jr. Family Ltd. Partnership, LLLP v. Simon Property Group, Inc.* ("*Patton*").[61] The *Patton* case involved a dispute between the owners of University Mall (Patton) in Little Rock, Arkansas and the ground lessee/operator of the mall (Simon Property Group).[62]

1. *Background*

University Mall was one of the first enclosed malls in Arkansas. On October 1, 1965, Patton and Simon's predecessor in interest signed a ground lease to allow Simon's predecessor to build a shopping mall on Patton's property.[63] The lease had a term through December 31, 2026.[64] Over the years, University Mall fell into disrepair.[65] The mall lost one of its main anchors when Montgomery Ward, a large retail chain, went bankrupt.[66] Then another anchor, M.M. Cohn, shut down a significant portion of its operations before eventually being bought out and subsequently entering bankruptcy.[67] The third main anchor, J.C. Penney, decided to leave the mall and relocate to a new shopping center.[68] The

60. *See, e.g.*,*Patton*, 370 F. Supp. 2d at 848–49.
61. 370 F.Supp.2d 846 (E.D. Ark. 2005).
62. *Id.* at 847.
63. *Id*.
64. *Id*.
65. *See* Edward Klump, *University Mall Landowners, Leaseholder in Discussions over Future of Premier Site*, ARK. DEMOCRAT-GAZETTE, June 13, 2004, at 1G & 2G; Leroy Donald & Laura Stevens, *University Mall Was First of Its Kind in State*, ARK. DEMOCRAT-GAZETTE, N.W. ARK. ED., Sept. 16, 2007; *University Mall Empties as Retailers Wait for Summit*, ARK. BUS., Jan. 28, 2002.
66. Donald & Stevens, *supra* note 66.
67. Donald & Stevens, *supra* note 66.
68. Donald & Stevens, *supra* note 66.

mall had many vacancies and serious maintenance problems, including allegations by Patton that the mall was infested with mold and had problems, such as when a large segment of roof that blew off the building into a busy street one night.[69]

Patton sued Simon for breach of its express obligation to maintain the mall in "good and tenantable repair."[70] Patton also claimed that Simon breached an implied obligation under the lease agreement to locate and maintain viable retail tenants at University Mall so that percentage rental income would be generated.[71] Simon responded to the suit by asserting that Arkansas does not recognize the implied covenant of continuous operation.[72]

2. The Court Defining the Factors

To analyze the implied covenant claim, the *Patton* court started by looking at Arkansas' law on implied covenants and observed that Arkansas law states:

> The construction and legal effect of a written lease contract are to be determined by the court as a question of law, except where the meaning of the language depends on disputed extrinsic evidence... When contracting parties express their intention in a written instrument in clear and unambiguous language, it is the court's duty to construe the writing in accordance with the plain meaning of the language employed.[73]

The court pointed out that, as a general rule, implied covenants are not favored in Arkansas law.[74] Specifically, the court said the following with regards to Arkansas law on implied covenants:

> This view [that implied covenants are not favored by Arkansas law] owes its force to the presumption that when the parties have entered into a written agreement that embodies their obligations, they have expressed all of the conditions by which they intend to be bound. Courts are reluctant to imply covenants where the obliga-

69. *See* Plaintiffs' Brief in Opposition to Defendants' Motion for Any Further Continuance, William L. Patton Jr. Family Ltd. P'ship, LLLP et al. v. Simon Prop. Group, Inc. et al., No. 4:04-CV-1477GH (E.D. Ark. Mar. 8, 2006).

70. *Patton*, 370 F. Supp. 2d at 847.

71. *Id*.

72. *Id*. The court analyzed the plaintiff's claim as an implied covenant of continuous operation. *Id*

73. *Id.*at 848 (quoting Holytrent Props., Inc. v. Valley Park Ltd. P'ship, 71 Ark. App. 336, 339, 32 S.W.3d 27, 29 (2000)).

74. *Patton*, 370 F. Supp. 2d at 848.

> tions sought to be imposed on the contracting parties are not expressed in the written text.[75]

The court also determined that Arkansas law holds:

> The courts will declare implied covenants to exist only where there is a satisfactory basis in the express contract for the parties which makes it necessary to imply certain duties and obligations in order to effect the purposes of the parties to the contract made.[76]

The court acknowledged, however, that courts in other states have recognized an implied covenant of continuous operation under circumstances similar to those present in the *Patton* case.[77] The court determined that Patton's claim that Simon breached an implied obligation under the lease agreement to locate and maintain viable retail tenants at University Mall equated to an implied covenant of continuous operation.[78] The court also recognized that there are numerous tests for determining when to imply a covenant of continuous operation.[79] The court specifically noted six factors from a Kentucky case[80] and two more from an Oklahoma case:[81]

> (1) whether base rent is below market value;
>
> (2) whether percentage payments are substantial in relation to base rent;
>
> (3) whether the term of the lease is lengthy;
>
> (4) whether the tenant may sublet;
>
> (5) whether the tenant has rights to fixtures;
>
> (6) whether the lease contains a noncompetitive provision;[82]

75. *Id.* (quoting Mercury Inv. Co. v. F.W. Woolworth Co., 706 P.2d 523, 530 (Okla. 1985)).

76. *Patton*, 370 F. Supp. 2d at 848 (quoting 20 AM. JUR. 2D, *Covenants, Conditions, and Restrictions* §29 (2004)).

77. *Patton*, 370 F. Supp. 2d at 848–49.

78. *Id*.

79. *Id.* at 849.

80. Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995).

81. Mercury Inv. Co. v. F.W. Woolworth Co., 706 P.2d 523 (Okla. 1985).

82. For the first six factors, see *Patton*, 370 F. Supp. 2d at 849 (quoting *Lagrew,* 905 F. Supp. at 405 (E.D. Ky. 1995)). It is worth noting, as discussed in greater detail later in this article, that the *Lagrew* case is not favorable to tenants. *See infra* Part IV.M. In *Lagrew*, the Kentucky court interpreted the factors in a manner to find a covenant of continuous operation. The holding in *Lagrew*, however, is not consistent with the rest of

> (7) the obligation must arise from the presumed intention of the parties as gathered from the language used in the written instrument itself or must appear from the contract as a whole that the obligation is indispensable in order to give effect to the intent of the parties; and
>
> (8) it must have been so clearly within the contemplation of the parties that they deemed it unnecessary to express it.[83]

The court also noted a Utah decision that found "the existence of a ground lease rather than a lease of an already constructed commercial building is detrimental to the claim that the lease implies a covenant of continuous operation."[84] The *Patton* court did not list this as one of the enumerated factors; however, based on the court's analysis, this probably should have been listed as a factor as well. The court stated that "the law has clearly established that a tenant has significantly more flexibility and control over the premises under a ground lease than it has under a building lease."[85] The court observed that a ground lease bears a close relationship to a fee purchase of real property and conveys the functional equivalent of fee simple ownership.[86] The court interpreted this to mean that the landlord has a higher burden to prove that a term should be implied (i.e., the covenant of continuous operation).[87] The court even went so far as to say, "Even assuming that the implied covenant of continuous operation was applicable to a ground lease, the Court could not find it applicable here."[88] This dictum seems to imply that it might be impossible to find an implied covenant of continuous operation in a ground lease. If this dictum is followed by Arkansas state courts, then it would eliminate a significant number of leases from the analysis without having to consider other factors.

---

the *Patton* decision. The court's decision to cite these factors from the *Lagrew* case is somewhat perplexing. An Arkansas court's analysis might change if it used the rationale from *Lagrew* and not just the factors cited in the case.

83. For the last two factors, see *Patton*, 370 F. Supp. 2d at 849 (citing *Mercury Inv. Co.*, 706 P.2d at 530–31). The court separated the list into two parts: the Kentucky factors and the Oklahoma factors. The lists are combined in this article for convenience.

84. *Patton*, 370 F. Supp. 2d at 850 (citing Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226 (Utah 2004)). Interestingly, the *Patton* court cited both Utah's *Oakwood Village* decision and Kentucky's *Lagrew* decision. As discussed in more detail later in this article, these two decisions are at strong odds, and *Oakwood Village* contains a strong rebuke of *Lagrew*.

85. *Patton*, 370 F. Supp. 2d at 850.

86. *Id.* at 850–51.

87. *Id.* at 851.

88. *Id*.

Perhaps even more interesting than the dicta regarding a ground lease, the court stated, "The presence of an 'any lawful use' provision in the lease also precludes the finding of an implied covenant of continuous operation."[89] The court did not elaborate on this statement other than to cite a Georgia case as standing for the same proposition.[90] This is very strong language if interpreted as an absolute bar on finding an implied covenant of continuous operation when there is an "any lawful use" clause in a lease, which is a common term. If this dictum is followed by Arkansas courts, then the remainder of the analysis is unnecessary when this clause is present.

The court noted that, among the enumerated factors, "the adequacy of rent has been the most influential" factor.[91] The "adequacy of rent," however, is not one of the six listed factors, at least not in so many words.[92] Presumably, the court was referring to the first and second factors (whether the base rent (i.e., fixed rent) is below market value and whether percentage payments are substantial in relation to base rent) since these are the only two factors that deal directly with the rent. Therefore, presumably, the court believes the first two factors are due the most weight in the analysis. This view seems to be supported by the court's statement:

> Recognized as a corollary to the general rule governing covenants that could be inferred from a written instrument is the principle that when the rental reserved in a lease is based upon a percentage of the gross receipts of a business and a guaranteed substantial minimum rent, a covenant would not be implied; but if the minimum rental is so low as to be nominal, or where there is no minimum rental, then a covenant might be implied.[93]

In addition to analysis focused on the rent provisions, the *Patton* court pointed out that "[t]he court [in *Woolworth*] noted that there was nothing contained in the lease by which Woolworth promised to operate its business in such a way as to increase gross receipts or to 'accel-

89. *Id*.

90. *See id.* at 852 (citing Piggly Wiggly S., Inc. v. Heard, 405 S.E.2d 478 (Ga. 1991)).

91. *Patton*, 370 F. Supp. 2d at 849 (quoting Joel R. Hall, *Operations Covenant*, ALI-ABA CONTINUING LEGAL EDUCATION, 36TH ANNUAL ADVANCED ALI-ABA, MODERN REAL ESTATE TRANSACTIONS 2143 (July 28–31, 2004).

92. *See* Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995); *supra* Part III.A.2.

93. *Patton*, 370 F. Supp. 2d at 849 (citing Mercury Inv. Co. v. F.W. Woolworth Co., 706 P.2d 523, 531 (Ok. 1985)).

erate customer traffic flow for the benefit of other tenants.'"[94] The court also cited with favor the Oklahoma court's finding in *Woolworth* that:

> The lease is cast in the form of a highly sophisticated document employing clear, precise and unambiguous language that covers a myriad of details regarding the parties' relationship as landlord vis-a-vis tenant. In the face of comprehensive terms, this court is powerless to add a covenant requiring Woolworth to generate sales that would subject it to liability for percentage rental.The parties could have inserted an explicit termination clause to be triggered by continued failure of Woolworth to reach some agreed level of gross receipts within a specified period. To now imply the covenant pressed for by Mercury would be to rewrite the parties' agreement.We should be loath to hold Woolworth to any greater level of business productivity than Mercury itself was able to exact from a willing tenant.[95]

3. *The Court's Analysis of the Factors*

Even though the court listed a number of factors, the court only partially analyzed some of them.[96] The court did not address the factors of whether the tenant has rights to fixtures and whether the lease contains a noncompetitive provision.[97] Although the court noted that the lease was lengthy and that Simon had the right to sublet, the court did not analyze these factors.[98] The court blended the analysis for the remaining factors. The following is a discussion of the court's analysis of the factors that it did discuss.

a. Whether base rent is below market value *and* whether percentage payments are substantial in relation to base rent

As mentioned above, the court seemed to blend these two factors in its analysis. Simon had an obligation to pay both fixed rent[99]—a certain amount of rent that was not dependent on the revenue of the

94. *Patton*, 370 F. Supp. 2d at 849–50 (quoting *Mercury*, 706 P.2d at 531).
95. *Patton*, 370 F. Supp. 2d at 850.
96. *See Patton*, 370 F. Supp. 2d 846.
97. *See id.*
98. *Id.*
99. Fixed rent is also sometimes referred to as "base rent," "minimum rent" or "guaranteed rent." The *Patton* court used the base rent terminology. *Patton*, 370 F. Supp. 2d at 847. The term "fixed rent" is more often used in the industry, so this article uses that term instead.

shopping center—and percentage rent—a portion of Simon's revenue from operating the shopping center.[100] As the mall operator, Simon's revenue depended on leasing the mall to subtenants who would pay rent to Simon, who in turn would pay a portion of the subtenant's rent to Patton as percentage rent.[101] Even though the lease did not contain an express obligation for Simon to lease the mall to subtenants, Patton alleged that Simon had an implied duty to do so to generate percentage rent.[102] Patton also relied on several references in the lease and subsequent amendments to paying mortgage obligations with rent received from subtenants.[103] The court noted, however, that the fixed rent was substantial at $210,000 per year, which precluded a finding of an implied covenant of continuous operation.[104]

The court also dismissed Patton's attempt to analogize Simon's obligations to that of an oil and gas lessee who has an implied covenant under Arkansas law to diligently explore and develop the minerals.[105] The court stated that an oil and gas lessors "sole compensation" is from the royalties received from the oil and gas development.[106] Because the oil and gas lessor has no other source of revenue from the lease, the court noted that the implied covenant is necessary for the lease to make economic sense, but the same is not true in a situation where the tenant is paying $210,000 per year in fixed rent.[107] The court, however, did not address the fact that many oil and gas leases contain upfront bonus rental payments that can be very substantial.[108] A bonus payment is an upfront payment to the lessor upon signing the lease before any exploration takes place. These upfront payments arguably conflict with the court's analysis, which relied on a case from 1911.[109] The court's analysis might have been different had it considered that bonus payments are often part of modern oil and gas leases because the lessor's sole

100. *Id*.
101. *Id*.
102. *Id.*
103. *Id.* at 847–48.
104. *Id.* at 852.
105. William L. Patton Jr., Family Ltd. P'ship, LLLP v. Simon Prop. Group, Inc., 370 F. Supp.2d 846, 852 (E.D. Ark. 2005).
106. *Id*.
107. *Id*.
108. *See*, *e.g.*, Rothwell v. Steven L. Yeager, LLC, No. CA07-1004, 2008 WL 1961480, at *1 (Ark. App. May 7, 2008) (noting an $11,175 bonus payment for a 111.75 acre tract); Lindquist v. Ark. Oil & Gas Comm'n, No. CA99-1306, 2000 WL 696414, at *1 (Ark. App. May 31, 2000) (noting a $100 per acre bonus payment); Ark. Oil & Gas, Inc. v. Diamond Shamrock Corp., 281 Ark. 207, 208, 662 S.W.2d 824, 825 (Ark. 1984).
109. *Id.* at 852 (relying on Mansfield Gas Co. v. Alexander, 97 Ark. 167, 133 S.W. 837 (1911)).

compensation is not solely from the royalties that depend on the exploration or development of the minerals.

> b. The obligation must arise from the presumed intention of the parties as gathered from the language used in the written instrument itself or it must appear from the contract as a whole that the obligation is indispensable in order to give effect to the intent of the parties *and* it must have been so clearly within the contemplation of the parties that they deemed it unnecessary to express it

Like the previous factors, the court blended the two Oklahoma factors into essentially one analysis. The court noted that the lease was negotiated by sophisticated parties and was a detailed document.[110] The court found it particularly persuasive that the parties amended the lease on six separate occasions and the amendments addressed fixed and percentage rent.[111] The court felt the parties had more than ample opportunity to include a covenant of continuous operation if desired. As the court stated:

> [i]f the parties had wanted to include a duty on defendants to locate and maintain suitable retail tenants, they had ample opportunity to include such language in the amendments. "Faced with the clear language of the document negotiated by the parties themselves, this Court will not imply a covenant which would restrict one party's freedom to conduct its own business as it sees fit. The parties were capable of including such a provision in the express language of the contract and failed to do so. To imply such a covenant would amount to rewriting the parties' agreement; an act this Court will not perform."[112]

The court also observed that language in one of the amendments seemed to indicate that an implied covenant would be inconsistent with the parties' intentions.[113] The Fourth Amendment, which addressed fixed rent and percentage rent, stated:

> It is understood and agreed by Lessors and Lessee that upon their execution of this Fourth Amendment, the first Letter Agreement, Second Letter Agreement and 1980 Amendment shall be of no fur-

110. *Patton*, 370 F. Supp. 2d at 851.
111. *Id*.
112. *Id.* (quoting Keystone Square Shopping Ctr. Co. v. Marsh Supermarkets, Inc., 459 N.E.2d 420, 423 (Ind. App. 1984)).
113. *See Patton*, 370 F. Supp. 2d at 851.

> ther force or effect and the entire agreement of the parties shall consist of those written terms, covenants and conditions contained in the agreement, the April, 1968 Amendment, the June, 1968 Amendment, and this Fourth Amendment.[114]

The court interpreted this language from the Fourth Amendment as the parties agreeing that there were no implied covenants in the agreement.[115] Based on this, the court felt that it could not imply a covenant of continuous operation.

Even though the court enumerated eight factors for determining whether to imply a covenant of continuous operation, it really did not discuss or use the factors in a traditional point-by-point analysis. The *Patton* court primarily relied on the following factors: (i) the comprehensiveness of the written lease; (ii) the sophistication of the parties; (iii) the adequacy of the fixed rent; and (iv) the permitted uses of the leased property. Other states, however, approach this issue differently. The following segment of this article will address the way that other states have approached the same issue. Because the *Patton* decision is not binding on Arkansas state courts, it is possible that Arkansas may adopt some of the analysis utilized by other states or reject some of the *Patton* court's analysis.

IV. THE APPROACH OF OTHER STATES

The doctrine of the implied covenant of continuous operation is not very well developed outside of a few states. Some states may not have any case law addressing the situation.[116] Therefore, it is useful to

114. *Id*.

115. *Id*.

116. I ran a search for cases on Westlaw on November 7, 2008. The Boolean search terms were as follows: "implied covenant of continuous operation" or "implied covenant of continued operation" or "covenant against going dark" or "implied covenant to operate." Based on this search, the following states did not return any relevant results, although the states with an asterisk (*) have relevant case law found using different terminology: Alabama*, Alaska, Delaware, District of Columbia*, Colorado, Florida*, Hawaii, Idaho*, Kansas*, Louisiana* (Louisiana had one case using these search terms, but it was applying Mississippi law), Maine, Maryland, Michigan* (Michigan has a case that falls within the search terms, but the case addressed an implied covenant to explore for minerals under a mineral rights lease), Montana, Nebraska, New Hampshire, New Jersey*, New Mexico, New York*, North Dakota, Oregon, Rhode Island*, South Carolina*, South Dakota, Vermont, Virginia, Washington* and Wyoming*. The following states had relevant cases (in some instances, like Arkansas, the relevant case was federal): Arizona, Arkansas, California, Connecticut, Georgia, Illinois, Indiana, Iowa, Kentucky, Massachusetts, Minnesota, Mississippi, Missouri, Nevada, North Carolina, Ohio, Oklahoma, Pennsylvania, Tennessee, Texas, Utah, West Virginia and Wisconsin.

examine some demonstrative cases from states that have case law on the issue to see the types of tests courts apply.[117]

A. Alabama

Alabama does not have a case that uses the term "implied covenant of continuous operation," but it does have a case that deals with a very similar issue. In *Percoff v. Solomon*,[118] the parties signed a lease with a percentage rent clause.[119] The tenant opened another business near the leased premises where he competed with his own business, which caused a reduction in the percentage rent collected by the landlord.[120] In considering whether the tenant had an implied obligation not to impair the percentage rent obligation, the Alabama Supreme Court stated that:

> [a]n implied covenant must rest entirely on the presumed intention of the parties as gathered from the terms as actually expressed in the written instrument itself, and it must appear that it was so clearly within the contemplation of the parties that they deemed it unnecessary to express it, and therefore omitted to do so; or it must appear that it is necessary to infer such a covenant in order to effectuate the full purpose of the contract as a whole gathered from the written instrument. It is not enough to say that an implied covenant is necessary in order to make the contract fair, or that without such a covenant it would be improvident or unwise, or that the contract would operate unjustly. It must arise from the presumed intention of the parties as gathered from the instrument as a whole.[121]

In analyzing the situation, the Alabama Supreme Court did not believe that the existence of percentage rent made it necessary to find an implied covenant.[122] The court analogized the situation to an earlier decision where the court determined "that a covenant not to engage in

117. Some of the omitted states may have cases on the issue. I did not undertake exhaustive attempts to find every possible alternate search term for an "implied covenant of continuous operation," so some of these excluded states may have relevant case law. I believe, however, the included cases sufficiently present the various approaches used throughout the country. The excluded states are Alaska, Colorado, Delaware, Hawaii, Maine, Maryland, Montana, Nebraska, New Hampshire, North Dakota, Oregon, South Dakota, Vermont and Virginia. I also excluded Arkansas from this list since it is the primary subject of this article.

118. 67 So.2d 31 (Ala. 1953).

119. *Id.* at 33.

120. *Id.* at 35.

121. *Id.* at 40.

122. *Id.* at 41.

competing business is not implied from a sale of the 'good will' of a business."[123]

The court also stated that "[n]o case has come to our attention which holds as a matter of law that under a percentage lease with a guaranteed substantial minimum rental, covenants are to be implied of the kind which appellee seeks to have implied in the lease under consideration."[124] This last sentence indicates the possibility that Alabama might find an implied covenant of continuous operation when the lease contains no fixed rent or an insignificant amount of fixed rent.

B. Arizona

When analyzing implied covenants of continuous operation, Arizona uses the Standard Factors used generally for implied covenants discussed earlier in this article, which read as follows:

> (1) the implication must arise from the language used ...; (2) it must appear from the language used that it was so clearly within the contemplation of the parties that they deemed it unnecessary to express it; (3) implied covenants can only be justified on the grounds of legal necessity; (4) a promise can be implied only where it can be rightfully assumed that it would have been made if attention had been called to it; (5) there can be no implied covenant where the subject is completely covered by the contract.[125]

In addition to the Standard Factors, Arizona applies one additional test when an implied covenant of continuous operation is alleged. The court stated that, "[i]n agreements where the rental is based either upon a straight percentage of sales, or upon a minimum fixed rental and additional rental based upon a percentage of sales, the inadequacy of the base rent implies a covenant of continuous operation."[126]

In Arizona, a provision allowing assignment or subletting does not affect the determination of whether there is an implied covenant of continuous operation. The court was clear that "[t]he presence of a right to assign or sublet is not necessarily inconsistent with an implied covenant of continuous operation. The two covenants can be harmo-

123. *Id*.

124. *Percoff*, 67 So. 2d at 39 (Ala. 1953).

125. First Am. Bank & Trust Co. v. Safeway Stores, Inc., 729 P.2d 938, 940 (Ariz. Ct. App. 1986) (citing Walgreen Ariz. Drug Co. v. Plaza Ctr. Corp., 647 P.2d 643, 646 (Ariz. Ct. App.1982)).

126. *First Am. Bank*, 729 P.2d at 940 (citing *Walgreen*, 647 P.2d at 646).

nized to permit subletting or assignment to a business of the same character."[127]

C. California

California uses essentially the same test as Arizona. In addition to the Standard Factors, California compares the fixed rent and percentage rent.[128] An implied covenant of continuous operation will only be found when the lease relies on percentage rent without fixed rent or with only minimal fixed rent that is not substantial.[129] California courts have also found the existence of noncompetition clauses limiting a landlord's ability to lease property to competitors of a tenant to be a factor that may weigh in favor of finding an implied covenant of continuous operation.[130]

D. Connecticut

Connecticut follows a six-part test to determine when to imply a covenant of continuous operation, citing Kentucky's *Lagrew* decision that the *Patton* case cited, but did not actually analyze. The factors are as follows:

> (1) whether base rent is below market value, (2) whether percentage payments are substantial in relation to base rent, (3) whether the term of the lease is lengthy, (4) whether the tenant may sublet, (5) whether the tenant has rights to fixtures, and (6) whether the lease contains a noncompetitive provision.[131]

In applying this test, Connecticut begins with an examination of the fixed rent.[132] The court in *Pequot Spring Water Co. v. Brunelle*[133] stated

127. *First Am. Bank*, 729 P.2d at 941 (quoting with approval from the finding of the trial court).

128. *See* Brentwood Investors v. Wal-Mart Stores, Inc., No. 98-16387, 2000 WL 734384, at *1 (9th Cir. June 7, 2000). *See also* Brentwood Investors v. Wal-Mart Stores, Inc., No. C-95-0856, 1998 WL 337968, at *8 (N.D. Cal. June 19, 1998).

129. *See Brentwood Investors*, 2000 WL 734384, at *1.

130. *See* College Block v. Atl. Richfield Co., 254 Cal. Rptr. 179, 183 (Cal. Ct. App. 1988).

131. William L. Patton Jr., Family Ltd. P'ship, LLLP v. Simon Prop. Group, Inc., 370 F. Supp.2d 846, 849 (E.D. Ark. 2005) (quoting Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995)). *See also* Pequot Spring Water Co. v. Brunelle, 698 A.2d 920, 923–24 (Conn. App. Ct. 1997) (quoting Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995)).

132. *See Pequot*, 698 A.2d at 924.

133. 698 A.2d 920 (Conn. App. Ct. 1997).

that "[t]he reason for the applicability of this factor in relation to the implied covenant is that the amount of minimum rent can be tested by a trier to determine its adequacy."[134] In *Pequot*, there was no fixed rent, so it was easy for the court to conclude that this factor weighed in favor of implying the covenant.[135]

The second factor is whether the percentage rent is substantial in relation to the fixed rent.[136] In *Pequot*, the total lack of fixed rent clearly made the percentage rent substantial in relation to the fixed rent.[137]

The third factor is whether the term of the lease is lengthy.[138] In *Pequot*, the lease had a twenty-five year term.[139] The court felt that this length was indicative of intent by the parties that the tenant remains in business the entire time.[140] The court said that

> Pequot [the tenant] would not have entered into a lease with such a length and Brunelle [the landlord] would not have accepted rental payments based solely on Pequot's sales if both parties had not intended that Pequot remain in business for the full length of the lease.[141]

The fourth factor is the tenant's ability to sublet (which presumably also includes the tenant's right to assign).[142] In *Pequot*, the lease gave the tenant a limited right to sublease, which the tenant argued was indicative of the intent that the parties did not contemplate a covenant of continuous operation.[143] The court, however, disagreed and found that the fact that the landlord retained the right to refuse a sublease implied that only a suitable replacement would occupy the leased premises, thus indicating an intent that the premises continue to be occupied.[144]

The fifth factor is whether the tenant has the right to remove fixtures from the leased premises.[145] Even though the tenant in *Pequot* had rights to the fixtures, the court did not believe that this fact alone

134. *Id.* at 924.
135. *Id*.
136. *See id.* at 924.
137. *Id*.
138. *See id.*.
139. Pequot Spring Water Co. v. Brunelle, 698 A.2d 920, 924 (Conn. App. Ct. 1997).
140. *Id*.
141. *Id*.
142. *See id*.
143. *Id*.
144. *Id*.
145. *See* Pequot Spring Water Co. v. Brunelle, 698 A.2d 920, 924 (Conn. App. Ct. 1997).

was fatal to finding an implied covenant of continuous operation.[146] The court agreed that this factor weighed against implying the covenant, but the court held that it did not outweigh the other factors in the overall analysis.[147]

The sixth factor is whether the landlord is subject to a noncompetitive provision.[148] In *Pequot*, the court determined that the nature of the lease made a noncompetitive provision unnecessary, so the factor did not seem to make a significant difference to the analysis.[149]

E. District of Columbia

The District of Columbia has limited case law on the subject of implied covenants of continuous operation. The District of Columbia may imply a covenant of continuous operation when the lease contains a percentage rent clause.[150] Although there does not appear to be a formula recognized in the District of Columbia to analyze alleged implied covenants of continuous operation, the District of Columbia is clear that merely including a restriction on the use of the premises will not create an implied covenant of continuous operation.[151]

The District of Columbia addressed this situation in a case where a tenant leased a building and agreed "[t]hat he [the tenant] will use said premises for the sale of alcoholic beverages and other items usually associated with the sale of liquor for 'Off Sale' consumption and for no other purpose whatsoever."[152] The District of Columbia held that "[t]he law does not say that by accepting the grant of premises for a particular purpose, with a prohibition against its use for any other purpose, a lessee becomes affirmatively obligated to use it continually for such purpose."[153]

146. *Id*.
147. *Id*.
148. *See id.* at 925.
149. *Id*.
150. *See* Cong. Amusement Corp. v. Weltman, 55 A.2d 95, 96 (D.C. 1947) (stating that "[t]he situation would also be different if the rent were based on a percentage of lessees' sales, for then the lessor would have a contractual right not to have his rent diminished by an arbitrary shutdown of lessees' business.").
151. *Id*.
152. *Id.* at 95.
153. *Id.* at 96.

F. Florida

Florida may imply a covenant of continuous operation when "required to vitalize the full intent of the parties to the lease."[154] Florida does not have a formal set of factors for analyzing implied covenants of continuous operation.[155] Florida, however, examines the use restrictions, the sufficiency of the fixed rent, the tenant's promises related to the percentage rent and the tenant's right to remove fixtures.[156]

The use restrictions are one of the most important factors in Florida.[157] In Florida,

> [t]he general rule seems to be that in the absence of a specific provision therefor, the lessee is under no obligation to occupy or use the leased premises for the purposes for which they are adapted and that a covenant granting the privilege to use the premises for a particular purpose or prohibiting its use for other purposes does not necessarily involve an obligation on the part of the tenant to use it for that purpose.[158]

If, however, the lease includes specific provisions about how the tenant is supposed to operate its business, such as stating that the tenant will operate a restaurant and specifying the hours of operation, then the general rule can be overcome.[159]

Florida courts may imply a covenant of continuous operation when the percentage rent composes a significant amount of the rent received by the landlord.[160] In *Mayfair Operating Corp. v. Bessemer Properties*,[161] the court found the percentage rent significant because the total rent was "substantially reduced" as a result of the lost percentage rent when the tenant ceased operations.[162]

Florida also looks at any promises the tenant made concerning the percentage rent. In *Mayfair*, the court found an implied covenant of continuous operation because the tenant was required to "use its best efforts to obtain and maintain the highest volume of business on the

154. Jerrico, Inc. v. Wash. Nat'l Ins. Co., 400 So.2d 1316, 1317 (Fla. Dist. Ct. App. 1981) (citing Mayfair Operating Corp. v. Bessemer Properties, 7 So.2d 342 (Fla. 1942)).
155. *See Jerrico*, 400 So.2d 1316.
156. *See id.*
157. *See id.*
158. *Id.* at 1317 (citing Floste Corp. v. Marlemes, 53 So.2d 538 (Fla.1951)).
159. *See Jerrico,* 400 So.2d at 1318.
160. *See* Mayfair Operating Corp. v. Bessemer Properties, 7 So.2d 342, 343 (Fla. 1942).
161. 7 So.2d 342, 343 (Fla. 1942).
162. *Id.*

premises."[163] In *Diltz v. J & M Corp.*,[164] the court did not find an implied covenant of continuous operation precisely because the lease lacked the type of language found in *Mayfair Operating Corp.*[165] Similarly, in *Stemmler*, the court did not find the covenant because the lease lacked language similar to that found in *Mayfair.*[166]

Florida may also find the right of the tenant to remove fixtures from the premises weighs against finding a covenant of continuous operation.[167] The *Stemmler* court held that

> [t]he right 'at any time' to remove 'all' fixtures, counters, shelving, show cases, etc., from the leased premises is entirely inconsistent with the idea that there is an implied agreement to continue to operate a jewelry business, to which such items are essential, in the leased premises.[168]

Moreover, Florida also has an interesting case that discusses a tenant trying to impose an implied covenant on the landlord to have the rest of the shopping center built and to continuously operate it to support the tenant's business.[169] In that case, the court rejected the tenant's argument because the lease was sufficiently detailed and there was opportunity to have included such a clause if it had been truly important to the tenant.[170]

G. Georgia

Georgia follows a three-part test when determining whether a lease contains an implied covenant of continuous operation.[171] The factors are as follows:

> (1) whether the lease provides the tenant can use the premises in any other lawful manner; (2) whether the lease is freely assignable;

163. *Id*.
164. 381 So.2d 272 (Fla. Dist. Ct. App. 1980).
165. *Id.* at 273.
166. Stemmler v. Moon Jewelry Co., 139 So.2d 150, 152–53 (Fla. Dist. Ct. App. 1962) (quoting Ridgefield Investors v. Mae Ellen, Inc., 57 So.2d 842, 844 (Fla.1952)).
167. *See Stemmler*, 139 So.2d at 152.
168. *Id*.
169. *See* S. H. Kress & Co. v. Dresse & Garfield, Inc., 193 So. 2d 192, 194 (Fla. Dist. Ct. App. 1966).
170. *Id.* at 195.
171. *See* DPLM, Ltd. v. J.H. Harvey Co., 526 S.E.2d 409, 414 (1999).

> and (3) whether the lease contains a provision that the tenant pays a percentage of revenue as rent.[172]

Georgia examines the permitted uses under the lease.[173] Specifically, if the lease allows the premises to be used for any lawful purpose, then the court is unlikely to find an implied covenant of continuous operation.[174] Georgia's rationale is that "the language of the agreement expressly negates a requirement of continuous operation."[175]

Georgia also examines the discrepancy between the amount of fixed rent and percentage rent. In Georgia,

> [a]s a general rule, courts will not infer a covenant of continuous operation where the lease provides for the payment of both a percentage of gross receipts and a "substantial minimum" rent.[176]

Georgia looks at the ratio of percentage rent as compared to fixed rent to determine if the fixed rent is "substantial" instead of whether the dollar amount appears to be large.[177] For instance, in *DPLM, Ltd. v. J.H. Harvey Co*.[178] the Georgia Court of Appeals found that the fixed rent was substantial when the fixed rent constituted between 50% to 54% of the total rental during the life of the lease.[179] The *DPLM* court also noted another case where the fixed rent constituted 47% of the total rent and that court deemed it substantial.[180]

Georgia also places substantial weight on whether the lease is freely assignable. The Georgia Supreme Court stated that:

> [an] agreement's provision for free assignability by the tenant, without consent of the lessor, weighs strongly against a construction

172. DPLM, Ltd. v. J.H. Harvey Co., 526 S.E.2d 409, 414 (Ga. Ct. App. 1999).
173. *See id.*
174. *See* Piggly Wiggly S., Inc. v. Heard, 405 S.E.2d 478 (Ga. 1991).
175. *Id*. at 479.
176. *DPLM*, 526 S.E.2d at 415 (citing Kroger Co. v. Bonny Corp., 216 S.E.2d 341, 344 (Ga. Ct. App. 1975)).
177. *See DPLM*, 526 S.E.2d at 415; *Cf.* William L. Patton Jr., Family Ltd. P'ship, LLLP v. Simon Prop. Group, Inc., 370 F. Supp.2d 846, 852 (E.D. Ark. 2005).
178. 526 S.E.2d 409 (Ga. Ct. App. 1999).
179. *Id.* at 415.
180. *Id*. The *DPLM* court cited *Piggly Wiggly Southern Inc. v. Heard*, 405 S.E.2d 478 (Ga. 1991) at pages 479–80 for this proposition but noted that this case does not state the rent percentage, but the court stated that it knew the percentage in that case from the time that it was at the Court of Appeals before being appealed to the Georgia Supreme Court.

> of the contract which would require the tenant to continue its business throughout the term of the lease.[181]

Further, Georgia does not find the presence of a noncompetitive restriction on the landlord persuasive.[182] In *Kroger Co. v. Bonny Corp.*,[183] the tenant had the exclusive right to place a grocery store in the mall.[184] The court, however, did not find this noncompetitive restriction as weighing in favor of an implied covenant of continuous operation.[185]

H. Idaho

Idaho examines several factors when determining whether to imply a covenant of continuous operation, but it does not appear to have a formal list of factors.[186] Idaho considers the following factors: (i) whether the landlord constructed a building for the tenant's use (this could be interpreted as looking at the amount spent by the landlord on the tenant's behalf, such as a tenant buildout allowance); (ii) whether the lease has percentage rent; (iii) whether the fixed rent is substantial compared to the percentage rent; and (iv) whether the lease imposes a noncompetition covenant on the landlord to protect the tenant from competitors.[187] In Idaho, an implied covenant of continuous operation cannot be found if the lease allows the tenant to sublease the premises and remove its fixtures from the premises.[188]

Idaho will consider the presence of a merger clause.[189] A merger clause, also called an integration clause, is a term in a contract that states that the contract constitutes and contains the entire agreement between the parties.[190] In Idaho, however, the merger clause must clearly exclude implied covenants to effectively inoculate the lease from

181. *Piggly Wiggly*, 405 S.E.2d at 479–80 (citing Kroger Co. v. Bonny Corp., 216 S.E.2d 341 (Ga. Ct. App. 1975).

182. *See Kroger*, 216 S.E.2d 341 (Ga. Ct. App. 1975).

183. *Id.*

184. *See id.* at 343.

185. *Id*.

186. *See* Bastian v. Albertson's, Inc., 643 P.2d 1079 (Idaho Ct. App. 1982) (*superceded on other grounds by statute*, IDAHO CODE ANN. § 12-120, *as recognized in* Herrick v. Leuzinger, 900 P.2d 201 (Idaho Ct. App. 1995)).

187. *Id.* at 1082.

188. *See Bastian*, 643 P.2d at 1082.

189. *See id.* at 1081–82.

190. BLACK'S LAW DICTIONARY 824 (8th ed. 2004) (defining an integration clause as "[a] contractual provision stating that the contract represents the parties' complete and final agreement and supersedes all informal understandings and oral agreements relating to the subject matter of the contract").

a finding an implied covenant of continuous operation.[191] In *Bastian*, the court found a merger clause insufficient that "merely provides that the contract governing the rights of the parties . . . 'shall merge into this instrument and this lease agreement shall govern as the sole agreement between the parties . . . .'"[192]

Idaho will also consider the intensity of the negotiations concerning the lease.[193] Idaho, however, does not believe that the intensity of the negotiations will preclude finding an implied covenant of continuous operation.[194]

I. Illinois

Illinois uses several factors when evaluating implied covenants of continuous operation, although there does not appear to be a specific list, at least not in a recent case.[195]

> Where a lease specifies a particular use of the property and rent is to be computed on a percentage of profit basis, there is an implied covenant to occupy and use the premises for the specified purpose and in a manner which will generate the amount of rent contemplated by the parties.[196]

Illinois also holds that allowing the tenant to sublet or assign the lease prohibits finding an implied covenant of continuous operation.[197] Furthermore, allowing the tenant to use the premises "for any other lawful purpose" can be fatal to finding an implied covenant of continuous operation.[198]

J. Indiana

Like Illinois, Indiana seems to lack a standard list of factors for analyzing implied covenants of continuous operation.[199] Indiana, however, looks at several factors.[200] First, Indiana courts note that implied

191. *See Bastian*, 643 P.2d at 1081–82.
192. *Id.* at 1082 (citation omitted).
193. *See id*.
194. *See id*.
195. *See* Stein v. Spainhour, 521 N.E.2d 641 (Ill. App. Ct. 1988).
196. *Id.* at 643 (citations omitted).
197. *Id*.
198. *Id*. (citation omitted).
199. *See* Keystone Square Shopping Ctr. Co., v Marsh Supermarkets, Inc., 459 N.E.2d 420 (Ind. Ct. App. 1989).
200. *See id.*

covenants in general are disfavored.[201] Indiana considers the relative bargaining power of the parties, the sophistication of the parties, and the sophistication and comprehensiveness of the lease.[202] Indiana also seems to adopt the position that having a general assignment or subletting right prohibits finding an implied covenant of continuous operation.[203]

K. Iowa

Iowa looks at several factors when determining whether to imply a covenant of continuous operation but, like many states, does not appear to have a formal list.[204] The factors considered in Iowa include the following: (i) whether the fixed rent is substantial in comparison to the percentage rent; (ii) whether the landlord built the building for the tenant (i.e., whether the landlord expended funds upfront for the tenant's benefit); (iii) whether the lease imposes a noncompetition covenant on the landlord to protect the tenant from competitors;[205] and (iv) whether there is an economic interdependence between the landlord and the tenant.[206] A general right of assignment will negate finding an implied covenant of continuous operation, but a restricted right of assignment or subletting that requires the landlord's consent will not prohibit the implied covenant.[207] Also, the existence of a merger clause is fatal to finding an implied covenant of continuous operation.[208]

L. Kansas

Kansas has an interesting case that is similar to an implied covenant of continuous operation.[209] In *Williams v. Safeway Stores, Inc.*,[210] the tenant attempted to abandon the premises and sublease it to a shoe store.[211] The landlord alleged that there was an implied covenant re-

201. *See id.* at 423.
202. *See id*. *Cf.* Bastian v. Albertson's, Inc., 643 P.2d 1079 (Idaho Ct. App. 1982). (holding that the intensity of the negotiations concerning the lease is irrelevant to finding an implied covenant).
203. *See Keystone*, 459 N.E.2d at 423.
204. *See* E. Broadway Corp. v. Taco Bell Corp., 542 N.W.2d 816, 820 (Iowa 1996); Fashion Fabrics of Iowa, Inc. v. Retail Investors Corp., 266 N.W.2d 22, 29 (Iowa 1978).
205. *Broadway* , 542 N.W.2d at 820.
206. *Fashion Fabrics*, 266 N.W.2d at 29.
207. *See Broadway*, 542 N.W.2d at 820.
208. *See Fashion Fabrics*, 266 N.W.2d at 28. *See also Broadway*, 542 N.W.2d at 819.
209. *See* Williams v. Safeway Stores, Inc., 424 P.2d 541 (Kan. 1967).
210. *Id.*
211. *Id.* at 543.

stricting assignment by the tenant to purposes which would yield a percentage rental comparable to that paid by the tenant.[212] Kansas did not announce a factor test for examining these situations.[213] The court, however, did not imply a restriction requiring the tenant to operate a business.[214]

In this case, the main concern of the Kansas Supreme Court was whether the existence of a percentage rent clause compelled the tenant to maintain the percentage rent at a certain level. The court stated:

> [i]f this court determines an implied covenant in the lease existed which required payment of comparable rentals [following an assignment] we say, in effect, it was intended as a fixed rental requiring comparable sales. This effect would be to change the percentage of income rental into a fixed rental based on past sales experience.[215]

The Kansas Supreme Court also found that the existence of a provision allowing full rights to assign and sublet the premises destroyed the landlord's argument.[216] Further, the court found it persuasive that the existence of fixed rent designed to compensate the landlord for its investment in the property after acquiring the property in a sale-leaseback transaction with the tenant.[217]

M. Kentucky

Kentucky has one of the leading cases on implied covenants of continuous operation.[218] Although not always followed, the *Lagrew*[219] case has been discussed in numerous other decisions including: Indiana's *Rothe* case, Utah's *Oakwood Village* case, Oklahoma's *Oklahoma Plaza* case, Tennessee's *BVT* case, Arkansas' *Patton* case and Connecticut's *Pequot* case.[220]

212. *Id*.
213. *Id.* at 548.
214. *Id*.
215. *Williams*, 424 P.2d at 549.
216. *Id*.
217. *Id.* at 551.
218. Rothe v. Milwaukee, etc., Co., 21 Wis. 256 (1866).
219. Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401 (E.D. Ky. 1995).
220. In relative order, see *Rothe v. Revco D.S., Inc.*, 976 F. Supp 784 (S.D. Ind. 1997); *Oakwood Vill. LLC v. Albertsons, Inc*., 104 P.3d 1226 (Utah 2004); *Okla. Plaza Investors v. Wal-Mart Stores, Inc*., 155 F.3d 1179 (10th Cir. 1998); *BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc.*, 48 S.W.3d 132 (Tenn. Ct. App. 2001); *William L. Patton Jr., Family Ltd. P'ship, LLLP v. Simon Prop. Group, Inc*., 370 F. Supp.2d 846 (E.D. Ark. 2005); and *Pequot Spring Water Co. v. Brunelle*, 698 A.2d 920 (Conn. App. Ct. 1997).

Kentucky begins with the following basic proposition:

> The courts will declare implied covenants to exist only when there is a satisfactory basis in the express contract of the parties which makes it necessary to imply certain duties and obligations in order to effect the purposes of the parties to the contract made. Such covenants can be justified only upon ground of legal necessity arising from the terms of the contract or the substance thereof. The implication from the words must be such as will clearly authorize the inference or an imputation in law of the creation of a covenant. It is not enough to say that it is necessary to make the contract fair, that it ought to have contained a stipulation which is not found in it, or that without such covenant it would be improvident, unwise, or operate unjustly. The covenants raised by law from the use of particular words in an instrument are only intended to be operative when the parties themselves have omitted to insert the covenants. But when a party clearly indicated to what extent he intends to warrant or obligate himself, that is the limit of his covenant, and the law will not hold him beyond it…. .[221]

Kentucky originated and uses the same six factors as listed above under the Connecticut heading. The Kentucky court recognized that "shopping centers are designed for going concerns, not empty store fronts."[222] The court even went so far to say:

> [t]hus, when an entity in the business of operating a retail drug store negotiates a lease with a shopping center absent a showing of unusual circumstances, it is implicit that the lessor [sic—should read "lessee"] intends to operate a store and that the lessor is leasing the space for that purpose.[223]

Considering the hesitancy to find implied covenants of continuous operation found in many other states, this statement is somewhat radical. It essentially switches the burden from the landlord proving that there should be an implied covenant of continuous operation to the tenant to prove what "unusual circumstances" should prohibit such a finding.[224]

The Kentucky court also has a different approach to the sufficiency of fixed rent in *Lagrew*.[225] The court recognized that fixed rent alone

221. *Lagrew*, 905 F. Supp. at 405 (citation omitted).
222. *Id*.
223. *Id.* at 405–06.
224. *Cf.* Stop & Shop, Inc. v. Ganem, 200 N.E.2d 248, 252 (Mass. 1964); Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 729 (Minn. Ct. App. 1994).
225. *See Lagrew*, 905 F. Supp. 401.

does not provide the landlord a hedge against inflation.[226] Based on this, the Kentucky court determined that merely having substantial base rent is insignificant if the lease has a long term and the landlord's only protection from inflation is the percentage rent.[227]

Like Arizona, Kentucky does not believe that the tenant having the right to assign or sublet is fatal to finding an implied covenant of continuous operation.[228] Essentially, Kentucky holds that this right is not fatal because an assignment to a similar business entity should generate percentage rent similar to what the landlord is accustomed to receiving.[229]

Kentucky also considers which party has the right to retain the fixtures at the end of the lease.[230] If the landlord is entitled to the fixtures, then that is strong evidence that the parties intended the tenant to continuously operate the premises.[231] The reverse, however, is not true and does not prohibit finding an implied covenant of continuous operation.[232]

The *Lagrew* court also addressed a clause in the lease that said: "[n]o obligation not stated herein shall be imposed by either party hereto."[233] The court held that this merger clause was insufficient to disclaim an implied covenant of continuous operation.[234] The court stated:

> The defendant must recognize, when dealing with "implied" covenants, such provision will never be written into an agreement and a failure to specify a provision is not necessarily "evidence that there was no such understanding." The courts look to the terms and circumstances of the parties [sic] agreement to see if the law must necessarily imply a provision to effectuate the true intent of the agreement. Under such circumstances, an oblique reference to the situation, like Paragraph 27 [the merger clause], is not always given full force and effect. For example, in every contract, there is an implied covenant of good faith and fair dealing to impose on the parties "a duty to do everything necessary to carry out" the intent of the contract. Likewise, when a contract contains a clause disclaiming im-

226. *Id*. at 406. I suppose this would be different if the lease periodically adjusted the fixed rent for inflation, which is often the case.
227. *Id*.
228. *See id*.
229. *Id.* at 407.
230. *See Lagrew*, 905 F. Supp. 401.
231. *See id*. at 407.
232. *See id*.
233. *Id*.
234. *Id.*

> plied warranties, the law requires the clause be "conspicuous" so as to draw the readers [sic] attention to the clause. Such exclusionary language disclaiming implied warranties in a contract will not always be upheld by the Court.[235]

This language highlights a possible distinction between the Kentucky situation and that found in other states. Kentucky imposes a covenant of good faith and fair dealing in leases.[236] Although this is a common approach,[237] not all states recognize a cause of action for breach of this covenant.[238] For instance, Arkansas specifically does not recognize a tort for breach of the covenant of good faith and fair dealing except in the context of insurance cases; even though Arkansas recognizes that every contract imposes an obligation to act in good faith.[239] Arkansas has not decided whether a cause of action for breach of the covenant of good faith and fair dealing can arise from a contract.[240]

N. Louisiana

Not too surprisingly, the analysis in Louisiana is somewhat different. In *Slidell Investment Co. v. City Products Corp.*,[241] the tenant leased a one story building for a term of approximately ten years with the fixed rent being $6,412 per year and the percentage rent being four percent of gross sales in excess of $142,500.[242] The lease contained a provision allowing the premises to be used "for the sale, storage Or [sic] display of goods, wares and merchandise."[243] The lease also contained a non-competition clause restricting the landlord's right to lease nearby property to competitors of the tenant.[244]

The tenant raised several arguments to avoid finding an implied covenant of continuous operation but cited cases from common law

235. *Id.* (citations omitted).
236. *See Lagrew*, 905 F. Supp. at 407. *See also* Iroquois Manor v. Walgreen Co., No. 3:99CV-27-S, 2000 WL 33975410, at *1 (W.D. Ky. May 12, 2000); Ranier v. Mount Sterling Nat'l Bank, 812 S.W.2d 154, 156 (Ky. 1991).
237. *See, e.g.*, Ferrara v. Walters, 919 So. 2d 876, 883 (Miss. 2005); Wallace v. Nat'l Bank of Commerce, 938 S.W.2d 684, 686 (Tenn.1996) (alphabetical by state).
238. *See, e.g., Plaza Associates*, 524 N.W.2d at 730-31 (noting the argument that the covenant of good faith does not apply to landlord tenant law but not ruling on the issue).
239. *See* Preston v. Stoops, No. 07-805, 2008 WL 2287217, at *1 (Ark. June 5, 2008).
240. *See id*.
241. 202 So. 2d 323 (La. Ct. App. 1967).
242. *Id.* at 324.
243. *Id*.
244. *Id.* at 325.

jurisdictions to support its position, which the Louisiana court rejected as inconsistent with Louisiana's civil law system.[245] The Louisiana court found an implied covenant of continuous operation despite the language in the lease that theoretically allowed the tenant to use the premises for non-retail purposes (i.e., the storage of goods) because the court, relying on other Louisiana decisions, found "that it was the intention that plaintiff [the landlord] be paid a basic and percentage rental on the premises. It is the opinion of this court that the record amply shows that this lease agreement would not have been entered into had plaintiff not anticipated receipt of percentage rental."[246]

O. Massachusetts

The leading case in Massachusetts has a somewhat different fact pattern than the typical scenario found in other states. In *Stop & Shop, Inc. v. Ganem*[247] the tenant leased a building for a term of approximately thirteen years with fixed rent of $22,000 per year and percentage rent of 1.25% of gross sales above $1,269,230, but only if the tenant's total sales at this location and another location in the City of Lawrence exceeded $3,000,000 per year.[248] The tenant planned to close the store because it was apparently not profitable.[249] The landlord filed a claim against the tenant because the tenant had opened two other stores near the leased premises, one store about a mile and a half away and the other store about one mile away, which pulled business from the original store.[250]

In analyzing the case, the Massachusetts court stated that,

> even if there is a more than nominal minimum rent [i.e., fixed rent], other circumstances such as that the fixed rent is significantly below the fair rental value of the property might justify the conclusion that the parties intended that the lessor have the benefit of the percentage rent throughout the term.[251]

245. *Id.* at 327.
246. *Slidell Inv. Co.*, 202 So. 2d at 325.
247. 200 N.E.2d 248 (Mass. 1964).
248. *Id.* at 250.
249. *Id*.
250. *Id*.
251. *Id* at 251.

The court held that the landlord had the burden of proving a disparity between the fixed rent and the fair rental value that was sufficient grounds for implying a covenant to operate.[252]

Ultimately, the *Stop & Shop* court did not analyze a list of factors, but it felt that the landlord did not meet its burden of proving the necessity of implying a covenant of continuous operation.[253] The court concluded that the mere presence of a percentage rent clause does not give rise to an implied covenant of continuous operation unless there are some other facts justifying such a finding.[254] For instance, the court stated that "[w]e assume, without deciding, that such interest [a landlord's interest in receiving percentage rent] could be protected against certain acts of the lessee, as for example, discontinuance of operations for spite or to inflict harm."[255]

P. Michigan

Michigan's analysis makes it rather difficult to imply a covenant of continuous operation. Michigan courts start with the axiom that leases are construed against the landlord unless drafted by the tenant.[256] Even when drafted by the tenant, however, courts still construe even express restrictive covenants strictly and in favor of the free alienability of land.[257] Michigan's position is that,

> [g]enerally . . . the lessee is under no obligation, in the absence of a specific provision therefor, to occupy or use, or continue to use, the leased premises, even though one of the parties, or both, expected or intended that they would be used for the particular purpose to which they seemed to be adapted or which they seemed to be constructed.[258]

This general presumption against implied covenants of continuous operation can be overcome, however, when the lease provides for percentage rent.[259] When the lease has a percentage rent clause, Michigan will consider a variety of factors.[260] First, Michigan considers whether

252. *Id.* at 252.
253. *Id.* at 252–53.
254. *Stop & Shop,* 200 N.E.2d at 253.
255. *Id*.
256. *See* Carl A. Schuberg, Inc. v. Kroger Co., 317 N.W.2d 606, 607 (Mich. Ct. App. 1982).
257. *See id.* at 607.
258. *Id.* (internal citations omitted).
259. *See id*.
260. *See id.*

the fixed rent provides a substantial return on the landlord's investment.[261] "In the absence of evidence that the minimum rent is unsubstantial, courts generally do not infer a covenant to continue operations."[262]

Second, the Michigan court holds that having a thoroughly negotiated lease weighs against finding an implied covenant.[263] The court stated: "where the parties have deliberately and extensively negotiated a contract, as a Court we should decline to rewrite an agreement to include a continuous occupancy clause."[264]

Third, the court holds that the presence of express continuous operating clauses in other leases executed by the landlord weighs against finding an implied covenant of continuous operation.[265] The *Schuberg* court noted;

> [p]laintiff [the landlord] negotiated several contracts during the period with other tenants in the shopping center. Some of those contracts specifically included continuous occupancy clauses. Under these circumstances, we find the parties' intent did not encompass Kroger's [the tenant] being bound by a continuous occupancy clause.[266]

Michigan does not believe the presence of a noncompetition covenant on the landlord weighs in favor of finding an implied covenant of continuous operation.[267] This position conflicts with the approach of Kentucky's *Lagrew* decision and the cases in other states that follow *Lagrew*.[268]

Q. Minnesota

Minnesota considers several factors to determine if there should be an implied covenant of continuous operation and follows Michigan in many respects.[269] The Minnesota court considers the following fac-

261. *Id.* at 609.
262. *Schuberg*, 317 N.W.2d at 609 (citation omitted).
263. *See id.* at 610.
264. *Id*.
265. *Id*.
266. *Id*.
267. *See id*.
268. *See* Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401 (E.D. Ky. 1995). *See also* Okla. Plaza Investors v. Wal-Mart Stores, Inc., 155 F.3d 1179 (10th Cir. 1998); Rothe v. Revco D.S., Inc., 976 F. Supp 784 (S.D. Ind. 1997); Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226 (Utah 2004).
269. *See* Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 729 (Minn. Ct. App.

tors: (i) whether the fixed rent is substantial and a smaller part of the total rent than the percentage rent; (ii) whether the parties were sophisticated and actively negotiated the lease; (iii) whether the landlord included an express covenant of continuous operation in leases with third-parties; (iv) whether the lease gives the tenant broad assignment or sublease rights; and (v) whether the lease has language detailing the scope of the business operation or the identity of the operator.[270]

First, the Minnesota court examines whether the fixed rent is substantial and a smaller part of the total rent than the percentage rent.[271] Minnesota holds that "the implication of an operating covenant is less likely where the tenant is paying 'substantial' base rent [i.e., fixed rent] and a relatively smaller part of the rent as a percentage of gross receipts."[272] In *Plaza Associates*, the court found the fixed rent substantial when the fixed rent was $6,666 per month and the percentage rent ranged from 0% percent to 46% during the life of the lease.[273] The court held that fixed rent is "substantial" if there is a correlation between the base rent and the fair market value of the lease at the time of the execution, which makes an implied covenant less likely.[274]

Second, Minnesota considers whether the parties were sophisticated and actively negotiated the lease.[275] The *Plaza Associates* court held that the "active and extensive negotiation of a lease by sophisticated parties also weights against finding an implied covenant in a lease 'since the parties were free to include whatever provisions they wished.'"[276]

Third, Minnesota considers whether the landlord included an express covenant of continuous operation in leases with third-parties.[277] The *Plaza Associates* court further held that the "failure of a landlord to use an express operating covenant where it has included the covenant in the lease of other tenants further weights against finding an implied operating covenant because it makes clear that the landlord know how to employ such a clause."[278]

1994).

270. *Id.* at 729–30.
271. *See id.*
272. *Id.* at 729.
273. *Id*.
274. *Id*.
275. *See Plaza Associates*, 524 N.W.2d at 727.
276. *Id.* at 729 (internal citations omitted).
277. *See id.* at 727.
278. *Id.* at 729–30.

Fourth, Minnesota considers whether the lease gives the tenant broad assignment or sublease rights.[279] With this factor, the *Plaza Associates* court held that "provisions in a lease giving a tenant broad assignment or sublease rights is another factor preventing the implication of an operating covenant. The express right of a tenant to assign or sublet and vacate the premises is inconsistent with an implied obligation to remain and do business."[280]

Fifth, Minnesota considers whether the lease has language detailing the scope of the business operation or the identity of the operator.[281] Here, the court held that "an operating covenant is less likely to be implied where, as here, there is no language detailing the scope of the business operation or the identity of the operator."[282] In analyzing this factor, the court was not persuaded by Walgreen's promise to use the premises as a "drugstore only."[283] The court interpreted this as giving the tenant two options under the lease: "(1) refrain from using the premises; or (2) use the premises [as specified]."[284]

Like Michigan, Minnesota does not believe the presence of a noncompetition covenant on the landlord weighs in favor of finding an implied covenant of continuous operation.[285] In *Plaza Associates*, the tenant had the exclusive right to operate a drugstore in the mall.[286] The court stated: "[t]he fact that appellant [landlord] agreed not to allow any other drugstores in the mall does not indicate an implied covenant by Walgreen [tenant] to use the space for the full term of the lease."[287]

R. Mississippi

Mississippi courts do not seem to have a factor test to apply to implied covenants of continuous operation.[288] Mississippi, however, looks at the terms of the lease to determine if there is some language in the lease that could be interpreted as essentially containing a covenant of continuous operation.[289]

279. *See id.* at 727.
280. *Plaza Associates*, 524 N.W.2d at 730.
281. *See id.* at 727.
282. *Id.* at 730.
283. *Id*.
284. *Id.* (internal citations omitted).
285. *See id.* at 730.
286. *Plaza Associates*, 524 N.W.2d at 730.
287. *Id*.
288. *See* Kroger Co. v. Chimneyville Props., Ltd., 784 F. Supp. 331 (S.D. Miss. 1991).
289. *See id.* 346–47. *See also* TOC Retail, Inc. v. Gulf Coast Oil Co., 886 F. Supp. 1306, 1313 (E.D. La. 1995) (interpreting Mississippi law).

For instance, in *Kroger Co. v. Chimneyville Props., Ltd.*,[290] the lease stated: "[n]otwithstanding any assignment or sublease, or any vacating of the demised premises by Tenant, Tenant shall remain fully liable on this Lease."[291] The court found that this language implied the opposite of a covenant of continuous operation, in other words, that the tenant had the express right to vacate the premises.[292] The *Chimneyville* court also focused on a term in the lease that said that the landlord's covenant not to lease to competitors of the tenant expired if the tenant ceased conducting a business on the premises for a period of 180 days or longer.[293]

S. Missouri

Missouri has an interesting set of case law highlighted by an Eighth Circuit Court of Appeals case interpreting Missouri law that has been criticized by a Missouri state court.[294] Though Missouri has case law on implied covenants of continuous operation, Missouri does not appear to have developed a formulaic approach to analyzing these cases.[295]

In *EMRO Marketing Co. v. Plemmons*,[296] the Eighth Circuit Court of Appeals interpreted Missouri law to find an implied covenant of continuous operation.[297] In reaching its conclusion, the *EMRO* court relied on several terms in the lease at issue.[298] First, the court found the presence of a restriction in the lease limiting the tenant's use of the premises for a Nickerson Farms store to be persuasive for implying a covenant.[299] Second, the court was persuaded by the fact that the lease relied primarily upon percentage rent (the monthly fixed rent was $100).[300] The court did not find the tenant's right to sublease or assign the lease to be persuasive in the analysis.[301] The court was also not persuaded by a clause in the lease allowing the tenant to remove buildings, fixtures and other improvements, though the court's dismissal of this term may have specifically related to the fact that the landlord might

290. 784 F. Supp. 331 (S.D. Miss. 1991).
291. *Id.* at 347 (emphasis omitted).
292. *Id*.
293. *Id*.
294. *See* EMRO Mktg. Co. v. Plemmons, 855 F.2d 528 (8th Cir. 1988).
295. *See id.*
296. *Id.*
297. *Id.* at 530.
298. *Id.*
299. *Id*.
300. *EMRO*, 855 F.2d at 530.
301. *Id*.

perceive the improvements in question as a burden because they were components of a retail gasoline station.[302]

In *Giessow Restaurants, Inc. v. Richmond Restaurants, Inc.*,[303] the Missouri Court of Appeals criticized the *EMRO* decision and stated that it ignored applicable Missouri law.[304] The Missouri Court of Appeals stated "the mere fact that a rental provision of a lease was based upon a combination of fixed rent and a percentage rent is insufficient to find an implied covenant of continued use."[305] The court stated that "[i]n fact, Missouri courts consistently refuse to find implied covenants in clearly drafted leases."[306] The court held that the mere presence of a term restricting the tenant's use of the premises does not give rise to an implied covenant of continuous operation.[307] The court also distinguished the *EMRO* decision by pointing out that the case at bar had fixed rent of $25,000 per year with percentage rent of 7% of gross sales between $357,142 and $962,391 and an additional 7% of gross sales in excess of $962,391, not to exceed $20,000.[308] The Missouri Court of Appeals found this amount of fixed rent to be "substantial."[309]

Missouri also finds the presence of a merger clause in a contract to weigh heavily against finding an implied covenant of continuous operation.[310] According to Missouri, "[t]he existence of a merger clause is a strong indication on the face of the contract that the writing is intended to be complete."[311]

T. Nevada

Nevada primarily relies on Arizona's approach to covenants of continuous operation.[312] A federal district court interpreting Nevada law pointed out the reliance on Arizona law and also added that,

302. *Id*.
303. 232 S.W.3d 576 (Mo. Ct. App. 2007).
304. *Id.* at 579–80.
305. *Id.* at 580 (citing Crestwood Plaza, Inc. v. Kroger, 520 S.W.2d 93, 97 (Mo. Ct. App. 1974)).
306. *Giessow*, 232 S.W.3d at 580.
307. *Id*.
308. *Id*.
309. *Id*.
310. *See* Adbar Co., L.C. v. PCAA Mo., LLC, No. 4:06-CV-1689, 2008 WL 68858, at *4 (E.D. Mo. Jan. 4, 2008).
311. *Id.* at *4.
312. *Supra* Part IV.B. *See* Hornwood v. Smith's Food King No. 1, 772 P.2d 1284, 1285 (Nev., 1989). *See also* Interface Group – Nevada, Inc. v. Men's Apparel Guild in Cal. Inc., No. 2:04-CV-00351-BES-GWF, 2007 WL 923952, at *6 (D. Nev. March 23, 2007).

> [u]nder Nevada state law, the Court may conclude that an implied provision to use space for a particular purpose exists where (1) the implied duty arises from the language used; (2) where the implied duty appears from that language that it was so clearly within the contemplation of the parties that they deemed it unnecessary to express it; (3) where the implied duty is justified on the grounds of legal necessity; and (4) where it can be rightfully assumed that it would have been made if attention had been called to it.[313]

This last quoted portion is essentially the Standard Factors.[314]

U. New Jersey

New Jersey implies a covenant of continuous operation when the lease contains a percentage rent clause or "where there are other circumstances sufficiently evidencing the intention of the parties that the lessee will be under a mandate to operate reasonably within the terms of the lease."[315] New Jersey cited (with approval) a Texas court when it said:

> [w]e think it is common knowledge that the volume of pedestrian traffic at the site of a retail merchandising business is a factor which affects the gross sales potential of the business. That being so the purpose and the importance to appellants of the lease provisions with reference to a supermarket are obvious. Plainly the parties intended that a supermarket should be in operation during the term of the lease. We find it impossible to believe that when the parties entered into this lease agreement it was intended that the particular lease provision in question would be satisfied if A. C. F. Wrigley Stores should continue to pay rent on an idle store building after discontinuing operation of the supermarket.[316]

New Jersey does not have a formal set of factors but looks at the terms of the lease.[317] For instance, in *Ingannamorte v. Kings Super Mar-*

313. *Interface Group*, 2007 WL 923952, at *6.

314. *See generally* Lippman v. Sears Roebuck & Co., 280 P.2d at 779 (Cal. 1955). Notably, the Nevada District Court left off the last of the five factors but included the rest. However, from the context of the court's decision in *Interface Group*, it is difficult to conclude that the court meant to limit or modify the Standard Factors with this omission.

315. Ingannamorte v. Kings Super Mkts., Inc., 260 A.2d 841, 843–44 (N.J. 1970). *See* Tooley's Truck Stop, Inc. v. Chrisanthopouls, 260 A.2d 845, 848 (N.J. 1970).

316. *Ingannamorte*, 260 A.2d at 844 (citing Lilac Variety, Inc. v. Dallas Tex. Co., 383 S.W.2d 193, 196 (Tex. App. 1964).

317. *See Ingannamorte*, 260 A.2d 841.

kets., Inc.,[318] the court considered the following factors: (i) that the lease specified was for a supermarket; (ii) that the landlord had to enforce a noncompetitive restriction to protect the tenant in the remainder of the shopping center; and (iii) that the landlord was required to maintain parking for the tenant.[319] The court determined that those provisions implied that the parties did not intend for the tenant's building to be an "idle store building."[320]

V. New York

New York may find an implied covenant of continuous operation under certain circumstances.[321] New York takes the following stance on contracts:

> [t]hat a particular provision has not been expressly stated in a contract does not necessarily mean that no such covenant exists. As was eloquently stated by Judge Cardozo, "[t]he law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal. It takes a broader view today. A promise may be lacking, and yet the whole writing may be 'instinct with an obligation,' imperfectly expressed."[322]

New York examines the rental provisions when analyzing implied covenants of continuous operation.[323] If there is a percentage rent clause, New York may find the percentage rent clause to be "a promise to use reasonable efforts to bring profits into existence."[324] The party asserting the existence of an implied covenant, however, "bears a heavy burden, for it is not the function of the courts to remake the contract agreed to by the parties, but rather to enforce it as it exists."[325] New York will probably not imply a covenant unless the lease places "unusual restrictions upon the uses of the premises."[326] New York also looks at the sophistication of the parties negotiating the lease and the comprehensiveness of the lease.[327]

318. *Id.*
319. *Id.* at 844.
320. *Id*.
321. *See* Rowe v. Great Atl. & Pac. Tea Co., Inc., 46 N.Y.2d 62, 69 (N.Y. 1978).
322. *Id.*
323. *See* Goldberg, 168-05 Corp. v. Levy, 9 N.Y.S.2d 304, 306 (N.Y. App. Div. 1938).
324. *Id*. (citations omitted).
325. *Rowe*, 46 N.Y.2d at 69.
326. *Id.* at 70.
327. *See id.* at 72.

W. North Carolina

North Carolina does not appear to have a formal set of factors for determining when to imply a covenant of continuous operation.[328] North Carolina, however, will not find an implied covenant of continuous operation when the lease (i) contains sufficient fixed rent to compensate the landlord for its investment in the property;[329] or (ii) contains no, or limited, restrictions on use of the leased premises.[330]

If the lease contains a provision allowing the premises to be used for any lawful purpose, then the tenant is not required to conduct business on the premises for the full term of the lease.[331] Also, if the lease allows unfettered subletting or assignment, the tenant probably does not have an implied obligation to continuously operate the premises.[332]

X. Ohio

Ohio starts its analysis of implied covenants of continuous operation with the Standard Factors.[333] Ohio also looks at the sufficiency of fixed rent as compared to the percentage rent.[334] Ohio courts hold that,

> [w]here a lease provides for rental based on a percentage of sales with a *fixed substantial adequate minimum*, and there is no express covenant or agreement to occupy and use the premises, no implied covenant or agreement will be inferred that the lessee is bound to occupy and use the premises for the purpose expressed in the lease.[335]

Furthermore, Ohio examines whether the parties "industriously" negotiated and drafted the lease to cover all terms.[336] A federal court interpreting Ohio law noted several factors that might be considered in the analysis: (i) whether the issue was discussed during lease negotiations;

328. *See* Lowe's of Shelby, Inc. v. Hunt, 226 S.E.2d 232, 234 (N.C. Ct. App. 1976); Jenkins v. Rose's 5, 10 and 25 cent Stores, 197 S.E. 174, 175 (N.C. 1938).

329. *Jenkins*, 197 S.E. at 175; *Lowe's*, 226 S.E.2d at 234.

330. Forrest Drive Assocs. v. Wal-Mart Stores, Inc., 72 F. Supp. 2d 576 584–85 (M.D.N.C. 1999).

331. *See Lowe's*, 226 S.E.2d at 234.

332. *See id*.

333. *See* Kretch v. Stark, 193 N.E.2d 307, 315 (Ohio Misc. 1962).

334. *See id* at 315–16.

335. *Id.* at 316.

336. *See id*.

(ii) whether the fixed rent is substantial; and (iii) whether the parties in the transaction were sophisticated. [337]

Oklahoma courts are reluctant to imply a covenant of continuous operation in the absence of express language.[338] Oklahoma does not appear to have a formal set of factors to consider and the case law is limited.[339] Oklahoma starts with the general rule that

> (1) the [implied] obligation must arise from the presumed intention of the parties as gathered from the language used in the written instrument itself or it must appear from the contract as a whole that the obligation is indispensible in order to give effect to the intent of the parties; and (2) it must have been so clearly within the contemplation of the parties that they deemed it unnecessary to express it.[340]

In *United Associates, Inc. v. Wal-Mart Stores, Inc.*,[341] the Tenth Circuit Court of Appeals interpreted Oklahoma law and refused to find a covenant of continuous operation when: (i) the lease had fixed rent of $104,595 per year in addition to the percentage rent; (ii) the tenant had the right to assign or sublet without the consent of the landlord; (iii) the lease had a use clause stating, "'[i]t is understood and agreed that the Demised Premises will be used by Lessee in the operation of a discount department store, but Lessor agrees the Demised Premises may be used for any lawful purpose' except as a supermarket or grocery store;" (iv) the tenant had the right to remove any and all fixtures at any time; (v) the tenant, including its assignees and sublessees, had the right to make alterations to the premises for business purposes; (vi) the lease's default clause was triggered if the premises were deserted for more than 30 days; and (vii) when the lease contained an merger clause.[342] The court did not apportion weight to the factors or state whether any of the factors were irrelevant.[343] The court noted, however, that the clause prohibiting the tenant from deserting the premises for more than thirty days seemed to weigh in favor of finding an implied covenant of continuous operation.[344] Nevertheless, the court stated that the

337. Hamilton W. Dev., Ltd. v. Hills Stores Co., 959 F. Supp. 434, 440–41 (N.D. Ohio 1997).

338. *See* In re Okla. Plaza Investors, Inc., 203 B.R. 479, 484 (N.D. Okla. 1994) (interpreting Oklahoma law and overturning a decision by the bankruptcy court).

339. *See* Mercury Inv. Co. v. F.W. Woolworth Co.,706 P.2d 523, 530 (Okla. 1985).

340. *Id.* at 530.

341. 133 F.3d 1296 (10th Cir. 1997).

342. *United Associates*, 133 F.3d at 1297.

343. *See id.*

344. *Id.* at 1298.

lease "'must be considered as a whole so as to give effect to all its provisions without narrowly concentrating upon some clause or language taken out of context.'"[345] Therefore, the court found that this clause alone did not change the balance of the other facts.[346]

Oklahoma courts also seem to focus on whether the tenant has the right to assign or sublease and the breadth of the permitted uses under the lease.[347] Oklahoma courts will probably not find an implied covenant of continuous operation if the tenant has broad assignment and use rights.[348] Furthermore, Oklahoma courts will not find the implied covenant if the fixed rent is "substantial" and "adequate."[349] Also, in Oklahoma, the existence of a merger clause could negate finding an implied covenant of continuous operation.[350]

Furthermore, Oklahoma will not imply a covenant of continuous operation if the lease is comprehensive. As the court in *Mercury Inv. Co. v. F.W. Woolworth Co.*[351] pointed out:

> [t]he lease is cast in the form of a highly sophisticated document employing clear, precise and unambiguous language that covers a myriad of details regarding the parties' relationship as landlord vis-a-vis tenant. In the fact of its comprehensive terms, this court is powerless to add a covenant requiring Woolworth [the tenant] to generate sales that would subject it to liability for percentage rentals.[352]

Z. Pennsylvania

Pennsylvania also appears not to have a formal set of factors for analyzing implied covenants of continuous operations.[353] In analyzing these cases, even when the terms are not ambiguous, Pennsylvania starts with

345. *Id.* (quoting Mercury Inv. Co. v. F.W. Woolworth Co., 706 P.2d 523, 529 (Okla. 1985)).
346. *United Associates*, 133 F.3d at 1298.
347. *See* Okla. Plaza Investors v. Wal-Mart Stores, Inc., 155 F.3d 1179, 1180 (10th Cir. 1998).
348. *See id*.
349. *See* Monte Corp. v. Stephens, 324 P.2d 538, 538 (Okla. 1958). *See also Mercury*, 706 P.2d at 531.
350. *See United Associates*, 133 F.3d at 1297–98.
351. 706 P.2d 523 (Okla. 1985).
352. *Id.* at 532.
353. *See* Slater v. Pearle Vision Ctr., Inc., 546 A.2d 676, 679 (Pa. Super. Ct. 1988).

> [T]he doctrine of necessary implication, which has been described as follows: In the absence of an express provision, the law will imply an agreement by the parties to a contract to do and perform those things that according to reason and justice they should do in order to carry out the purpose for which the contract was made and to refrain from doing anything that would destroy or injure the other party's right to receive the fruits of the contract.[354]

Pennsylvania recognizes the concept that a clause in a lease requiring a specific use may imply a covenant of continuous operation because such a clause does not contemplate a permanently idle store front.[355] Pennsylvania noted with approval a landlord's argument that courts should recognize the "economic interdependence" among a "key tenant" and the other tenants of a shopping center.[356] Pennsylvania may also interpret a lease clause limiting the amount of time that the premises can be vacant as implying a covenant of continuous operation.[357]

AA. Rhode Island

Rhode Island does not appear to have a formal set of factors for analyzing implied covenants of continuous operation.[358] Rhode Island seems to take the approach that a ground lease where the tenant has the right to remove improvements (i.e., fixtures) prohibits finding an implied covenant of continuous operation.[359] Also, Rhode Island may not find the implied covenant when the lease has substantial fixed rent.[360] Rhode Island takes the general approach to implied covenants expressed by Oklahoma in *Monte* and *Mercury.*[361]

354. *Id*. (citations omitted).

355. *See id.* at 678–79.

356. McKnight-Seibert Shopping Ctr., Inc. v. Nat'l Tea Co., 397 A.2d 1214, 1217 (Pa. Super. Ct. 1979).

357. *See Slater*, 546 A.2d at 680. *Cf.* United Associates, Inc. v. Wal-Mart Stores, Inc., 133 F.3d 1296, 1298 (10th Cir. 1997) (finding that a clause prohibiting the tenant from deserting the leased premises for more than thirty days as weighing in favor of finding an implied covenant of continuous operation).

358. *See* Aneluca Assocs. v. Lombardi, 620 A.2d 88, 91 (R.I. 1993).

359. *See id*.

360. *See id.* (noting the fixed rent was $8,400 with percentage rent at 3% of gross income in excess of $280,000 per year).

361. *Id.* at 91–92 (following the holdings in *Monte Corp. v. Stephens*, 324 P.2d 538 (Okla. 1958) and *Mercury Inv. Co. v. F.W. Woolworth Co.*, 706 P.2d 523 (Okla. 1985)).

BB. South Carolina

South Carolina starts its analysis by trying to "determine the situation of the parties, as well as their purposes, at the time the contract was entered."[362] South Carolina will imply a covenant in a lease "that according to reason and justice should be done to carry out the purpose for which the contract was made."[363]

South Carolina recognizes the role that anchor tenants play to draw customers into a shopping center and note that the "use of one or more anchor tenants to bring customers to the smaller shops in a shopping center is a common practice."[364] South Carolina noted that "[i]f the anchor tenant were permitted to leave the premises vacant, the landlord's purpose for signing the lease would be defeated."[365] Thus, South Carolina may take a different approach to implied covenants of continuous operation for anchor tenants than smaller tenants.[366] This is similar to the approach of Pennsylvania and New Jersey, which look at the economic role of the lease and the landlord's intention that the property not be left "idle."[367]

CC. Tennessee

Tennessee begins its analysis of implied covenants of continuous operation by examining the Standard Factors.[368] According to Tennessee,

> "[c]ontracts implied in law, or more properly quasi or constructive contracts, are a class of obligations which are imposed or created by law without the assent of the party bound, on the ground that they are dictated by reason and justice and which are allowed to be enforced by an action ex contractu."[369]

362. Columbia E. Assocs. v. Bi-Lo, Inc., 386 S.E.2d 259, 261 (S.C. Ct. App. 1989). *See also* United Dominion Realty Trust, Inc. v. Wal-Mart Stores, Inc., 413 S.E.2d 866, 868 (S.C. Ct. App. 1992) (interpreting an express covenant of continuous operation).

363. *Columbia*,386 S.E.2d at 262.

364. *Id*.

365. *Id*.

366. *See id.*

367. *Cf.* Ingannamorte v. Kings Super Mkts., Inc., 260 A.2d 841, 843–44 (N.J. 1970); Slater v. Pearle Vision Ctr., Inc., 546 A.2d 676, 679 (Pa. Super. Ct.1988).

368. *See* BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *11 (Tenn. Ct. App. Apr. 23, 1999) (*rev'd on other grounds by* BVT Lebanon Shopping Ctr., Inc. v Wal-Mart Stores, Inc., 48 S.W.3d 132 (Tenn. 2001)).

369. *BVT*, 1999 WL 236273, at *6 (citations omitted).

Further, before courts will imply a term in a contract, "it must appear therefrom that it was so clearly in the contemplation of the parties that they deemed it unnecessary to express it, or that it is necessary to imply such covenant in order to give effect to the purpose of the contract as a whole."[370] In addition, "[t]he decision whether to imply a covenant of continuous operation must be evaluated at the time the parties signed the agreement."[371] Furthermore, Tennessee utilizes the six factors from the *Lagrew* case.[372]

A percentage rent clause is not required to find an implied covenant of continuous operation, but a lease with a percentage rent clause is more likely to contain the implied covenant.[373] "[T]he major prerequisite for a finding of an implied covenant in a percentage rental agreement is that the stipulated minimum rental must not be substantial consideration."[374] The landlord has the burden of proving that the disparity between the fixed rent and the fair rental value is so great as to justify an implied covenant of continuous operation.[375]According to Tennessee, "[t]he 'substantial-insubstantial' question is tied closely to market value in the law governing implied covenants of continuous operation."[376] The fixed rent, however, has to be more than just nominal.[377] Furthermore, "even if there is a more than nominal minimum rent, other circumstances such as that the fixed rent is significantly below the fair market value of the property might justify the conclusion that the parties intended that the lessor have the benefit of the percentage rent throughout the term."[378]

Like some other states, Tennessee holds that "[t]he presence of a right to assign or sublet is not necessarily inconsistent with an implied covenant of continuous operation. The two covenants can be harmonized to permit subletting or assignment to a business of the same character."[379]

370. *Id.* at *7.

371. *Id.* at *8 (quoting Nalle v. Taco Bell Corp., 914 S.W.2d 685, 688 (Tex. Ct. App. 1996)).

372. *See BVT*, 1999 WL 236273, at *12–13. *Cf.* Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995)).

373. *See BVT.*, 1999 WL 236273, at *7.

374. *Id.* at *8 (citation omitted).

375. *See id.* at *7. *See also* Kroger Co. v. Chem. Sec. Co., 526 S.W.2d 468, 471 (Tenn. 1975) (stating the landlord "bears a heavy burden in proving the lease contains an implied covenant of continuous occupancy." *Id.*).

376. *BVT*, 1999 WL 236273, at *9.

377. *See id.* at *9–10.

378. *Id.* at *10.

379. *Id.* at *11.

Tennessee does not find the presence of a noncompetitive restriction on the landlord persuasive in the analysis. In *Kroger Co. v. Chemical Securities Co.*,[380] the landlord was prohibited from leasing any other property in the shopping center to another grocery store.[381] The court held that the "restriction on competition written into the lease is not broad enough to give birth to implied covenants of continuous occupancy and operation of a grocery business . . . . "[382]

DD. Texas

Texas starts with the general rule that implied covenants are disfavored.[383] Such a covenant will only be implied if it is "necessary in order to make the contract fair, or that without such a covenant it would be improvident or unwise, or that the contract would operate unjustly."[384] In another case, however, a lower court said Texas "will not imply a covenant simply because it is needed to make the contract fair, wise, or just."[385] Texas also considers whether the lease agreement is comprehensive and covers a variety of terms.[386] The decision whether to imply the covenant is evaluated at the time the parties signed the lease.[387]

Texas will typically only find an implied covenant of continuous operation if the percentage rent is the only (or nearly only) source of rent for the landlord.[388] It is unclear, however, whether the fixed rent has to be "adequate," as Texas has not decided whether to apply the California rule that the fixed rent must be adequate.[389]

In addition, Texas will not find an implied covenant of continuous operation just because the lease says the tenant "shall" operate a certain business.[390] The "shall" language does not create an implied covenant of continuous operation under Texas law.[391]

380. 526 S.W.2d 468 (Tenn. 1975).
381. *Id.* at 472.
382. *Id*.
383. *See* Nalle v.Taco Bell Corp., 914 S.W.2d 685, 687 (Tex. App. 1996).
384. Danciger Oil & Ref. Co. of Tex. v. Powell, 154 S.W.2d 632, 635 (Tex. 1941).
385. *Nalle*, 914 S.W.2d at 687.
386. *See id.* at 688.
387. *See id*.
388. *See id*. *See also* Marvin Drug Co. v. Couch, 134 S.W.2d 356, 358 (Tex. Civ. App. 1939).
389. *See Nalle*, 914 S.W.2d at 688–89.
390. *See* Daniel G. Kamin Kilgore Enters. v. Brookshire Grocery Co., 81 Fed. Appx. 827, 830 (5th Cir. 2003).
391. *See id.* at 830–31

Texas also considers the economic interdependence of the parties. In *Lilac Variety, Inc. v. Dallas Tex. Co.*,[392] the court found an implied covenant of continuous operation when the court determined that the landlord was depending on the pedestrian traffic generated by a grocery store to help the entire shopping center.[393] Based on this decision, it appears that Texas is more likely to find an implied covenant of continuous operation if the landlord is an anchor for the shopping center.[394]

EE. Utah

Utah will find an implied covenant of continuous operation only under "extreme circumstances" when supported by "substantial evidence."[395] There are two circumstances where Utah may find an implied covenant of continuous operation: "(1) where there is 'plain and unmistakeable language in the relevant contracts which would support the restrictive covenant'; and (2) where there is a 'legal necessity' to imply a restrictive covenant 'to effectuate the intent of the parties.'"[396] Utah considers several factors to determine if there is an implied covenant of continuous operation.[397]

The first factor is whether the lease contains a percentage rent clause.[398] Like Texas, a percentage rent clause is not absolutely required to find an implied covenant of continuous operation, but the absence of such a clause will make it difficult to imply the covenant.[399]

The second factor is whether the lease contains a restrictive "use of premises" clause.[400] If the "use of premises" clause is broad, then it indicates the parties did not contemplate requiring the tenant to remain continuously open.[401]

The third factor is whether the tenant can sublet or assign the lease without the landlord's consent and without restriction on the type of sublessees or assigns.[402] If the tenant has broad subletting or as-

392. 383 S.W. 2d 193 (Tex. Civ. App. 1964).
393. *Id.* at 196.
394. *See id.*
395. *See* Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226, 1233 (Utah 2004).
396. *Id.* (internal citations omitted).
397. *See id.*
398. *See id*.
399. *See id.* at 1233–34.
400. *See id.* at 1234.
401. *See Oakwood Village*, 104 P.3d at 1234.
402. *See id*.

signment rights, then Utah is less likely to imply a covenant of continuous operation.[403]

The fourth factor is whether the tenant owns the fixtures and has the right to remove them at any time.[404] According to Utah, the right to remove the fixtures during the lease is not consistent with an implied covenant of continuous operation.[405]

The fifth factor is whether the landlord has the right to reenter and relet the premises in the event the tenant vacates the premises.[406] If the landlord has such a right, then Utah believes it is inconsistent with finding an implied covenant of continuous operation.[407]

The sixth factor, which likely would not apply to many cases, is whether the tenant had an obligation to construct the leased building.[408] In *Oakwood Village LLC v. Albertsons, Inc.*,[409] the tenant leased vacant land but did not have a contractual obligation to build a building on the land.[410] This lack of a requirement helped the court determine that there was not an implied covenant of continuous operation.[411]

The seventh factor is whether the lease is a ground lease.[412] According to the court in *Oakwood Village*, "[a] ground lease . . . is different from an ordinary commercial lease."[413] The court further stated that "[t]he law has clearly established that a tenant has significantly more flexibility and control over the premises under a ground lease than it has under a building lease. Indeed, 'a ground lease is best considered as a financing device for developing unimproved land.'"[414]

FF. Washington

Washington courts start with the proposition that

> implied covenants are not favored in the law; and courts will declare the same to exist only when there is a satisfactory basis in the express contract of the parties which makes it necessary to imply cer-

403. *See id.* at 1234–35.
404. *See id.* at 1235.
405. *See id*.
406. *See id*.
407. *See Oakwood Village*, 104 P.3d at 1235.
408. *See id*.
409. 104 P.3d 1226 (Utah 2004).
410. *Id.* at 1235.
411. *Id.* at 1236.
412. *See id.* at 1238.
413. *Id*.
414. *Oakwood Village LLC*, 104 P.3d at 1239.

> tain duties and obligations in order to effect the purposes of the parties to the contract made.[415]

Courts will only find implied covenants if there is a "legal necessity arising from the terms of the contract, or the substance thereof, and the circumstances attending its execution; and the implication from the words must be such as will clearly authorize the inference of an imputation in law of the creation of a covenant."[416] Washington then applies the Standard Factors.[417]

In cases with percentage rent clauses, Washington courts ask "whether the parties regarded the amount of the stipulated minimum rental [i.e., fixed rent] as an adequate reflection of the full rental value of the premises, or whether they contemplated the full value would be realized only through the percentage provision."[418] If the fixed rent was "adequate," then the court is unlikely to imply a covenant of continuous operation.[419] Also, the existence of a merger clause could hurt finding an implied covenant of continuous operation.[420]

GG. West Virginia

West Virginia uses a well-defined set of factors for analyzing implied covenants of continuous operation that are synthesized from West Virginia's review of the disparate factors used in other states.[421] West Virginia courts hold that the following factors should be reviewed:

> 1) whether the lease contains an inconsistent express term or a provision for a substantial fixed base rent; 2) whether the lease contains a provision giving the tenant free assignability of the lease; 3) whether the lease was actively negotiated by all parties involved; and, 4) whether the lease contains a noncompetitive provision.[422]

For the first factor, West Virginia looks at whether the fixed rent is substantial and, if it is, then the factor weighs against finding the implied covenant.[423] West Virginia also looks for conflicting terms.[424] In

415. Fuller Mkt. Basket, Inc. v. Gillingham & Jones, Inc., 539 P.2d 868, 872 (Wa. Ct. App. 1975).
416. *Id*.
417. *Id*.
418. Brown v. Safeway Stores, Inc., 617 P.2d 704 (Wash. 1980).
419. *See id.* at 711.
420. *See Fuller*, 539 P.2d. at 872.
421. *See* Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 140–41 (W. Va. 1991).
422. *Id.* at 141.
423. *See id.* (finding $6,438.17 fixed rent substantial compared to a smaller amount

Thompson Development, Inc .v Kroger Co.,[425] the court examined the provision in the lease that said: "No obligation not stated herein shall be imposed on either party hereto."[426] The court found that this merger clause conflicted with finding the implied covenant.[427] Other examples in West Virginia of terms that are inconsistent with finding an implied covenant of continuous operation are: (i) a term allowing the tenant to remove fixtures at will; and (ii) a term stating that the tenant makes no representations or warranties regarding the sales it expects to make in the leased premises.[428]

Arguably, West Virginia should divide this first factor into two separate factors because the court is really looking for two different things. Even though having substantial rent could be considered an inconsistent express term, there are other inconsistent terms that the court will consider.

For the second factor, West Virginia examines assignment rights.[429] In *Thompson Development, Inc. v. Kroger Co.*,[430] the court determined that this factor weighed against finding an implied covenant because the tenant had the right to assign the premises without landlord consent; the assignment provision did not obligate the tenant to sublet only to another supermarket, and the lease only mandated that the premises be used for a lawful purpose and not be in conflict with exclusive rights granted to other tenants in the shopping center.[431]

For the third factor, if the lease is actively negotiated, then this factor will weigh against finding an implied covenant of continuous operation.[432] In *Thompson*, the court noted that a lawyer, an accountant, and a real estate broker assisted in the lease negotiations.[433] This heavy involvement by sophisticated advisors weighed against the landlord.

For the fourth factor, the court examines whether the landlord is restricted from leasing to competitors, with the lack of such restrictions weighing against finding the implied covenant.[434] In *Thompson*, a non-

of percentage rent).

424. *See id.*

425. 413 S.E.2d 137 (W. Va. 1991).

426. *Id.* at 141.

427. *Id. See also* Frederick Bus. Props. Co. v. Peoples Drug Stores, Inc., 445 S.E.2d 176, 181 (W. Va. 1994).

428. *See Frederick*, 445 S.E.2d at 181–82.

429. *See* Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 141 (W. Va. 1991).

430. *Id.*

431. *Id*.

432. *See id.* at 141–42.

433. *Id.* at 142.

434. *See id*.

competitive restriction burdened the landlord, but the tenant released the landlord from the obligation.[435] By releasing the landlord, the court found that this factor was "of slight import" in deciding the issue.[436] Even if the restriction remained, however, it may not have changed the outcome of the factor test. According to West Virginia, "[t]he mere existence of a noncompetition clause, in and of itself, does not require a court to find an implied covenant of continuous operation in a lease."[437]

HH. Wisconsin

Wisconsin is one of the most conservative states when it comes to finding implied covenants of continuous operation.[438] Wisconsin holds "that a commercial lessee cannot be forced to continuously operate a business in the absence of a clear, express provision in the lease requiring continuous operation."[439]

Even if the lease restricts the property to only one specific use, Wisconsin will still not find a continuous use obligation.[440] For instance, in *Brugman v. Noyes*,[441] a Wisconsin court said that a restriction limiting a leased property to use as cabinet warerooms did not compel the tenant to stay continuously open.[442] In *Henry Rahr's Sons Co. v Buckley*,[443] a Wisconsin court similarly refused to find a covenant to stay continuously open just because the property was restricted to use as a hotel and salon.[444] Wisconsin is very unlikely to find an implied covenant of continuous operation in most instances because "the burden that these clauses place on the lessee is so great as to require a clear statement of intent before imposing continuous operation."[445]

Although a Wisconsin court is unlikely to ever find an implied covenant of continuous use, the court will also look for terms that it believes should usually be in a lease where the parties intended a con-

435. *Thompson*, 413 S.E.2d at 142.
436. *Id*.
437. Frederick Bus. Props. Co. v. Peoples Drug Stores, Inc., 445 S.E.2d 176, 181 (W. Va. 1994).
438. *See* Sampson Invs. by Sampson v. Jondex Corp., 499 N.W.2d 177, 183 (Wis. 1993).
439. *Id*. *See also* Rapids Assos. v. Shopko Stores, Inc., 292 N.W.2d 668, 670–71 (Wis. Ct. App. 1980).
440. *See Sampson*, 499 N.W.2d at 180.
441. 6 Wis. 1 (Wis. 1857).
442. *Id.* at 6.
443. 150 N.W. 994 (Wis. 1915).
444. *Id.* at 996.
445. *Sampson*, 499 N.W.2d at 181.

tinuous operating covenant.[446] For example, courts look for provisions that set forth the required days and hours of operation, the required level of staffing, the required stock of merchandise and the conditions under which the tenant might justifiably cease operations.[447]

II. Wyoming

Wyoming takes an approach that is nearly the opposite of Wisconsin. Whereas Wisconsin does not equate a use restriction with a covenant of continuous operation, Wyoming looks heavily at the use restrictions in the lease.[448] According to a Wyoming court:

> A paramount purpose, from a lessor's standpoint, is said to be the amount of rent to be received, and when that amount is variable and conditioned upon the use to be made of the leased premises, words relating to the use intended are of primary importance and must be construed and interpreted to have been intended as an express covenant that the occupancy specified shall be continued during the entire lease period so as to provide a constant base upon which the agreed rent formula may be applied and the rent computed.[449]

In *Ayres Jewelry Co. v O & S Building*,[450] the tenant was restricted to using the property "for a jewelry shop, and for no other purpose whatsoever unless the written consent of Lessor is first and obtained thereto."[451] Based on this restriction, the court found an implied covenant of continuous operation.[452] The court stated that:

> The evident and plain intention of the parties is that the lessor would receive for its store a rental computed upon the gross sales of a jewelry shop conducted therein. That intention furnishes unmistakable guideline [sic] justifying the interpretation of the words used in the leasehold as being an express covenant that the leased premises be continuously used during the lease period as and for the conduct of a jewelry shop.[453]

446. *See id.* at 182.
447. *See id.* at 182–83.
448. *See id. Cf.* Ayres Jewelry Co. v. O & S Bldg., 419 P.2d 628, 632 (Wyo. 1966).
449. *Ayres Jewelry*, 419 P.2d at 632.
450. 419 P.2d 628 (Wyo. 1966).
451. *Id.* at 629 (citing a contract provision between the parties).
452. *Id.*
453. *Id.* at 632.

V. TRENDS IN ANALYZING IMPLIED COVENANTS OF CONTINUOUS OPERATION

There are trends that can be discerned from the cases examined in the foregoing section. It appears that there are four different formal factor tests applied by the states (five if you count the Standard Factors that several states use as a starting point for the analysis). Although the majority of states have not adopted one of the formal factor tests, states consider many of the same factors, even though there is significant disagreement on how to weigh some of the factors. Even the states that have formal factor tests tend to look at a variety of other issues in their analysis. This section will first consider the available formal factor tests then discuss the other factors frequently examined by courts.

A. The Factor Tests

Some states use more formal factor tests than others. Several states use the Standard Factors plus some additional factors to analyze implied covenants of continuous operation. Four relatively well-defined factor tests specific to implied covenants of continuous operation have emerged. For purposes of this article, I am calling the four formal factor tests the Kentucky Test, the Georgia Test, the Minnesota Test, and the West Virginia Test.[454]

The Standard Factors are discussed at the beginning of this article, so I will not repeat the discussion in this section.[455] There appear, however, to be six states that begin their analysis with the Standard Factors: Arizona, California, Nevada, Ohio, Tennessee, and Washington.[456]

1. *The Kentucky Test*

The Kentucky Test is the most landlord-friendly test.[457] The Kentucky Test looks at the following factors:

---

454. *See supra* Part IV.M (Kentucky Test); Part IV.G (Georgia Test); Part IV.Q (Minnesota Test); Part IV.GG (West Virginia Test).

455. *See supra* Part II.

456. *See* First Am. Bank & Trust Co., 729 P.2d 938, 940 (Ariz. Ct. App. 1986); Brentwood Investors v. Wal-Mart Stores, Inc., No. 98-16387, 2000 WL 734384, at *1 (9th Cir. June 7, 2000); Interface Group – Nevada, Inc. v. Men's Apparel Guild in Cal. Inc., No. 2:04-CV-00351-BES-GWF, 2007 WL 923952, at *6 (D. Nev. March 23, 2007); BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *11 (Tenn. Ct. App. Apr. 23, 1999); Fuller Mkt. Basket, Inc. v. Gillingham & Jones, Inc., 539 P.2d 868, 872 (Wa. Ct. App. 1975).

457. *See*, *e.g.* , Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 407 (E.D. Ky. 1995) (finding an implied covenant of continuous operation using the Kentucky Test); Pequot

1. Whether the base rent is below market value;

2. Whether percentage payments are substantial in relation to base rent;

3. Whether the term of the lease is lengthy;

4. Whether the tenant may sublet;

5. Whether the tenant has rights to fixtures; and

6. Whether the lease contains a noncompetitive provision.[458]

Under the Kentucky Test, the first factor weighs in favor of implying the covenant if the base rent is below market value.[459] The second factor weighs in favor of finding the implied covenant if the percentage payments are substantial in relation to base rent.[460] The third factor weighs in favor of finding an implied covenant of continuous operation if the term of the lease is lengthy.[461] The fourth factor weighs in favor of implying the covenant of continuous operation if the right to sublet or assign is somehow limited (either by requiring the landlord's consent or limiting the range of permitted transferees).[462] The fifth factor weighs in favor of implying the covenant if the tenant does not have the right to remove the fixtures at will.[463] The sixth factor weighs in favor of implying the covenant if the lease imposes a noncompetitive use restriction on the landlord.[464]

Both Connecticut and Tennessee follow the Kentucky Test.[465] The Kentucky Test was also listed (but not exactly followed) in Arkansas' *Patton* decision.[466] The Kentucky Test is not, however, universally fol-

Spring Water Co. v. Brunelle, 698 A.2d 920, 925 (Conn. App. Ct. 1997) (finding an implied covenant of continuous operation using the Kentucky Test); BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *11 (Tenn. Ct. App. Apr. 23, 1999) (finding an implied covenant of continuous operation using the Kentucky Test).

458. *See Lagrew*, 905 F. Supp. at 405. *See also Pequot*, 698 A.2d at 923–24.

459. *See Lagrew*, 905 F. Supp. at 406.

460. *See id*.

461. *See Pequot*, 698 A.2d at 924.

462. *See id*. *See also BVT*, 1999 WL 236273, at *13.

463. *See Pequot*, 698 A.2d at 924.

464. *See Lagrew*, 905 F. Supp. at 407.

465. *See Pequot*, 698 A.2d at 923–24; *BVT*, 1999 WL 236273, at *12–13.

466. *See* William L. Patton, Jr. Family Ltd. P'ship., LLLP v. Simon Prop. Group, Inc., 370 F. Supp.2d 846, 849 (E.D. Ark. 2005).

lowed. For instance, Utah strongly criticized the Kentucky Test in *Oakwood Village*.[467] The Utah court stated:

> [C]ontrary to the trial court's decision in *Lagrew* [which announced the Kentucky Test], appellate courts throughout the United States have almost universally held that "a lease provision granting the tenant the right to assign his lease or sublet the premises is inconsistent with an obligation on the part of the tenant to continuously operate his business on the premises." The decision in *Lagrew*, therefore, is an anomaly and fails to persuade us to follow its lead toward a conclusion that almost every other court would reject.[468]

2. *The Georgia Test*

Unlike the Kentucky Test, the Georgia Test is more tenant-friendly. The Georgia Test factors are as follows:

> 1. Whether the lease provides the tenant can use the premises in any other lawful manner;
>
> 2. Whether the lease is freely assignable;
>
> 3. Whether the lease contains a provision that the tenant pays a percentage of revenue as rent.[469]

Under the Georgia Test, the first factor weighs against implying the covenant of continuous operation if the lease permits the tenant to use the premises in any lawful manner.[470] The second factor weighs against implying the covenant if the lease is freely assignable.[471] The third factor weighs against implying the covenant if the lease does not contain a provision that the tenant owes percentage rent.[472]

Unfortunately for Georgia, no other state appears to be expressly following the Georgia Test. There does not appear to be any case law outside of Georgia discussing the Georgia Test or its application. Moreover, the Georgia Test is rather weak because it only considers three factors and omits many issues that are deemed important in other states. For instance, the Georgia Test does not address the meaning of a noncompetitive use restriction on the landlord, the disposition of

467. Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226, 1237 (Utah 2004).
468. *Id.* (internal citations omitted).
469. DPLM, Ltd. v. J.H. Harvey Co., 526 S.E.2d 409, 414 (1999).
470. *See id*.
471. *See id*.
472. *See id*.

of fixtures, the economic interdependence of the parties, or the comprehensiveness of the lease.

3. *The Minnesota Test*

The Minnesota Test is more tenant-friendly than the Kentucky Test but more comprehensive than the Georgia Test.[473] Minnesota does not provide a numbered list of factors, but it has a clearly defined set of factors that it considers.[474] The Minnesota factors are:

> 1. Whether the fixed rent is substantial and a smaller part of the total rent than the percentage rent;
>
> 2. Whether the parties were sophisticated and actively negotiated the lease;
>
> 3. Whether the landlord included an express covenant of continuous operation in leases with third-parties;
>
> 4. Whether the lease gives the tenant broad assignment or sublease rights; and
>
> 5. Whether the lease has language detailing the scope of the tenant's business operation or the identity of the operator.[475]

Under the Minnesota Test, the first factor weighs against implying a covenant of continuous operation if the rent includes substantial fixed rent and the percentage rent is a relatively small part of the total rent.[476] The second factor weighs against implying the covenant if the parties were sophisticated and actively negotiated the lease.[477] The third factor weighs against implying the covenant if the landlord included express covenants of continuous operation in leases with third parties.[478] The fourth factor weighs against implying the covenant if the lease gives the tenant broad assignment or sublease rights.[479] Finally, the fifth factor weighs against implying the covenant if the lease does

473. *See supra* Part IV.Q (Minnesota); Part IV.M (Kentucky); Part IV.G (Georgia).
474. *See* Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 729–30 (Minn. Ct. App. 1994).
475. *Id*.
476. *See id.* at 729.
477. *See id*.
478. *See id.* at 729–30.
479. *See id.* at 730.

not have language detailing the scope of the business operation or the identity of the operator.[480]

Although not exactly followed in any other state, the Minnesota Test is heavily influenced by Michigan.[481] The Michigan court analyzes whether the base rent provided a substantial return on the landlord's investment;[482] whether the parties "deliberately and extensively" negotiated the lease;[483] and whether there are express continuous operating clauses in other leases executed between the landlord and third-parties.[484] Also, though not included in the factor test, neither Michigan nor Minnesota finds the presence of a noncompetitive restriction on the landlord relevant.[485]

Although the Minnesota Test covers more factors than the Georgia Test, the question is whether the Minnesota Test covers enough issues to be sufficiently comprehensive. Like the Georgia Test, the Minnesota Test seems to overlook issues important in other states such as whether there is economic interdependence of the parties or whether the tenant has rights to remove fixtures.

4. *The West Virginia Test*

West Virginia uses a four factor test. The factors are:

> 1. Whether the lease contains an inconsistent express term or a provision for a substantial fixed base rent;
>
> 2. Whether the lease contains a provision giving the tenant free assignability of the lease;
>
> 3. Whether the lease was actively negotiated by all parties involved; and
>
> 4. Whether the lease contains a noncompetitive provision.[486]

As noted in the general analysis of West Virginia's law, the first factor would be better expressed as two separate factors. West Virginia's analysis examines the lease for inconsistent factors, and then looks for

480. *See Plaza Associates*, 524 N.W.2d at 730.
481. *See* Carl A. Schuberg, Inc. v. Kroger Co., 317 N.W.2d 606, 607 (Mich. Ct. App. 1982).
482. *See id.* at 609.
483. *See id.* at 610.
484. *See id*.
485. *See Plaza Associates*, 524 N.W.2d at 730; *Schuberg*, 317 N.W.2d at 610.
486. Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 141 (W. Va. 1991).

provisions regarding how substantial the fixed rent is.[487] This factor (or factors) weighs against implying a covenant of continuous operation if there are inconsistent terms, or if the fixed rent is substantial.[488]

The second factor weighs against finding a covenant of continuous operation if the lease contains a provision giving the tenant free assignability of the lease.[489] The third factor weighs against implying the covenant if the lease was actively negotiated by all parties involved.[490] The fourth factor weighs against finding the implied covenant if the lease does not contain a noncompetitive provision.[491]

Like the Minnesota Test, the West Virginia Test is well-developed and considers a variety of factors deemed important in many states. Like Minnesota and Georgia, however, the West Virginia Test ignores some possibly important factors. For instance, the test does not consider the economic interdependence of the parties. The test also does not consider whether the tenant can remove the fixtures or whether an "any lawful use" clause is fatal to implying the covenant.

5. *Other Factors*

As noted, most states do not use an established factor test. There seem to be common themes, however, that states look for, though there is significant disagreement on how to interpret some factors. This section will briefly examine the frequently recurring factors and discuss how states approach the issue.

a. Whether there is sufficient fixed rent to compensate the landlord

Many states examine the adequacy or sufficiency of the fixed rent. This is a somewhat different concept than the question of whether the fixed rent is significant in relation to the base rent. When examining the adequacy of the fixed rent, the question is typically whether the rent is sufficient to compensate the landlord for its investment in the property.[492] If the fixed rent is sufficient to compensate the landlord, then

487. *See* Frederick Bus. Props. Co. v. Peoples Drug Stores, Inc., 445 S.E.2d 176, 181–82 (W. Va. 1994).

488. *See id*.

489. *See Thompson*, 413 S.E.2d at 141.

490. *See id.* at 141–42.

491. *See id.* at 142.

492. *See* Lowe's of Shelby, Inc. v. Hunt, 226 S.E.2d 232, 234 (N.C. Ct. App. 1976); Jenkins v. Rose's 5, 10 and 25 cent Stores, 197 S.E. 174, 175 (N.C. 1938). *See also* Stop & Shop, Inc. v. Ganem, 200 N.E.2d 248, 252 (Mass. 1964).

this factor weighs against implying a covenant of continuous operation.[493] Numerous states apply this factor including Connecticut,[494] Kansas,[495] Kentucky,[496] Massachusetts,[497] Michigan,[498] North Carolina,[499] Oklahoma[500] and Tennessee.[501]

b. Whether the Fixed Rent Is Significant Compared to Percentage Rent

Some states look at the significance of the fixed rent compared to the percentage rent. The question is usually whether the lease relies heavily on percentage rent or has better than nominal fixed rent. If the lease has only nominal fixed rent, so that the landlord only profits from the percentage rent, then courts are more likely to imply a covenant of continuous operation. This approach is followed in Alabama,[502] Arizona,[503] California,[504] Connecticut,[505] Georgia,[506] Idaho,[507] Iowa,[508] Kansas,[509] Minnesota,[510] Missouri,[511] Ohio,[512] Rhode Island,[513] Tennessee,[514] Texas,[515]Washington,[516] and West Virginia.[517]

493. *See id.*
494. *See Pequot Spring Water Co.*, 46 Conn. App. at 192, 698 A2d at 924.
495. *See Williams*, 198 Kan. at 342, 424 P.2d at 551.
496. *See Lagrew*, 905 F. Supp. at 405.
497. *See Stop & Shop, Inc.*, 347 Mass. at 702, 200 N.E.2d at 251.
498. *See Carl A. Schuberg*, 113 Mich. App. at 318, 317 N.W.2d at 609.
499. *See Lowe's of Shelby, Inc.*, 30 N.C. App. at 87, 226 S.E.2d at 234.
500. *See Oklahoma Plaza Investors*, 155 F.3d at 1180 and *BVT Lebanon Shopping Center, Ltd.*, 1999 WL 236273 at *7
501. *See Hamilton West Development, Ltd.*, 959 F. Supp. at 440-41.
502. *See* Percoff v. Solomon, 67 So.2d 31, 39 (Ala. 1953).
503. *See* First Am. Bank & Trust Co. v. Safeway Stores, Inc., 729 P.2d 938, 940 (Ariz. Ct. App. 1986).
504. *See* Brentwood Investors v. Wal-Mart Stores, Inc., No. 98-16387, 2000 WL 734384, at *1 (9th Cir. June 7, 2000). *See also* Brentwood Investors v. Wal-Mart Stores, Inc., No. C-95-0856, 1998 WL 337968, at *8 (N.D. Cal. June 19, 1998).
505. *See* Pequot Spring Water Co. v. Brunelle, 698 A.2d 920, 924 (Conn. App. Ct. 1997).
506. *See* DPLM, Ltd. v. J.H. Harvey Co., 526 S.E.2d 409, 415 (1999).
507. *See* Bastian v. Albertson's, Inc., 643 P.2d 1079, 1082 (Idaho Ct. App. 1982).
508. *See* E. Broadway Corp. v. Taco Bell Corp., 542 N.W.2d 816, 820 (Iowa 1996).
509. *See* Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995).
510. *See* Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 729 (Minn. Ct. App. 1994).
511. *See* EMRO Mktg. Co. v. Plemmons, 855 F.2d 528 (8th Cir. 1988).
512. *See* Kretch v. Stark, 193 N.E.2d 307, 315–16 (Ohio Misc. 1962).
513. *See* Aneluca Assocs. v. Lombardi, 620 A.2d 88, 91 (R.I. 1993).
514. *See* BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *12–13 (Tenn. Ct. App. Apr. 23, 1999) (*rev'd on other*

c. Whether the tenant has an unfettered right of assignment or subletting

Many states examine whether the tenant has an unfettered right to assign or sublease the property to a third party. There is, however, division among the states on how to interpret this factor. Some states take the position that the tenant's right to assign or sublease the property is inconsistent with implying a covenant of continuous operation. Other states believe the tenant's right to sublease the property is irrelevant, or at least not fatal to the implied covenant.

The majority position is that having an assignment right weighs against implying a covenant of continuous operation. Georgia's holding is fairly representative of the majority approach, which provides: "[an] agreement's provision for free assignability by the tenant, without consent of the lessor, weighs strongly against a construction of the contract which would require the tenant to continue its business throughout the term of the lease."[518] This concept is repeated in Idaho,[519] Illinois,[520] Indiana,[521] Kansas,[522] Minnesota,[523] North Carolina,[524] Oklahoma,[525] Utah,[526] and West Virginia.[527]

Arizona, and the states that follow its approach, believes that the right to assign or sublease is irrelevant, or at least not fatal, to finding an implied covenant of continuous operation: "The presence of a right to assign or sublet is not necessarily inconsistent with an implied covenant of continuous operation. The two covenants can be harmonized to

grounds by BVT Lebanon Shopping Ctr., Inc. v Wal-Mart Stores, Inc., 48 S.W.3d 132 (Tenn. 2001))..

515. *See* Nalle v. Taco Bell Corp., 914 S.W.2d 685, 688 (Tex. Ct. App. 1996)).

516. *See* Brown v. Safeway Stores, Inc., 617 P.2d 704, 711 (Wash. 1980).

517. *See* Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 141 (W. Va. 1991).

518. Piggly Wiggly S., Inc. v. Heard, 405 S.E.2d 478, 479–80 (Ga. 1991).

519. *See* Bastian v. Albertson's, Inc., 643 P.2d 1079, 1082 (Idaho Ct. App. 1982).

520. *See* Stein v. Spainhour, 521 N.E.2d 641, 643 (Ill. App. Ct. 1988).

521. *See* Keystone Square Shopping Ctr. Co. v. Marsh Supermarkets, Inc., 459 N.E.2d 420, 423 (Ind. App. 1984)).

522. *See* Williams v. Safeway Stores, Inc., 424 P.2d 541, 549 (Kan. 1967).

523. *See* Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 730 (Minn. Ct. App. 1994).

524. *See* Lowe's of Shelby, Inc. v. Hunt, 226 S.E.2d 232, 234 (N.C. Ct. App. 1976).

525. *See* Okla. Plaza Investors v. Wal-Mart Stores, Inc., 155 F.3d 1179 (10th Cir. 1998).

526. *See* Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226, 1234–35 (Utah 2004).

527. *See* Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 141 (W. Va. 1991).

permit subletting or assignment to a business of the same character."[528] This same approach is followed by Tennessee,[529] and Kentucky.[530]

Iowa takes an approach between the two positions. Iowa holds that a general right of assignment will negate finding an implied covenant of continuous operation, but a restricted right of assignment or subletting that requires the landlord's consent will not prohibit the implied covenant.[531]

d. Whether the lease contains a restriction on the tenant's permitted uses of the leased property

Another common factor examined by courts is whether the lease contains a restriction on the tenant's permitted uses of the leased property. This is another factor that does not have consensus among the states. Some states believe that a use-restriction on the tenant implies that the parties intended that the tenant continuously operate during the term of the lease. Other states believe that a use-restriction has no bearing on whether to imply a covenant of continuous operation.

The majority position is that a narrow use-restriction will weigh in favor of implying a covenant of continuous operation. Utah's holding summarizes this position. According to Utah, if the "use of premises" clause is broad, then it indicates that the parties did not contemplate requiring the tenant to remain continuously open.[532] Conversely, if the use of premises is very limited, then it indicates that the parties intended for the tenant to remain continuously open. This approach is generally the same in Georgia,[533] Illinois,[534] New Jersey,[535] New York,[536] North Carolina,[537] Oklahoma,[538] and Pennsylvania.[539]

528. *See* First Am. Bank & Trust Co. v. Safeway Stores, Inc., 729 P.2d 938, 941 (Ariz. Ct. App. 1986) (quoting with approval the finding of the trial court).

529. *See* BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *11 (Tenn. Ct. App. Apr. 23, 1999) (*rev'd on other grounds by* BVT Lebanon Shopping Ctr., Inc. v Wal-Mart Stores, Inc., 48 S.W.3d 132 (Tenn. 2001))..

530. *See* Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 406 (E.D. Ky. 1995).

531. *See* E. Broadway Corp. v. Taco Bell Corp., 542 N.W.2d 816, 820 (Iowa 1996).

532. *See* Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226, 1234 (Utah 2004).

533. *See* DPLM, Ltd. v. J.H. Harvey Co., 526 S.E.2d 409, 414 (1999).

534. *See* Stein v. Spainhour, 521 N.E.2d 641, 643 (Ill. App. Ct. 1988).

535. *See* Ingannamorte v. Kings Super Mkts., Inc., 260 A.2d 841, 844 (N.J. 1970).

536. *See* Rowe v. Great Atl. & Pac. Tea Co., Inc., 46 N.Y.2d 62, 70 (N.Y. 1978).

537. *See* Forrest Drive Assoc. v. Wal-Mart Stores, Inc., 72 F. Supp. 2d 576, 584–85 (M.D.N.C. 1999).

538. *See* United Assocs., Inc. v. Wal-Mart Stores, Inc., 133 F.3d 1296, 1297 (10th Cir. 1997).

Some states find the presence of a tenant use-restriction irrelevant. The District of Columbia holds that, "[t]he law does not say that by accepting the grant of premises for a particular purpose, with a prohibition against its use for any other purpose, a lessee becomes affirmatively obligated to use it continually for such purpose."[540] Similarly, Missouri holds that the mere presence of a term restricting the tenant's use of the premises does not give rise to an implied covenant of continuous operation.[541] This view is also held by Texas[542] and Wisconsin.[543]

e. Whether the lease contains an "any lawful use" clause

Although similar to the previous factor, which examined the permitted use of the leased property, some states give special significance to the inclusion of an "any lawful use" clause. An "any lawful use" clause is a provision in a lease that allows the tenant to use the premises for any lawful use. A typical clause in a lease might read: "[t]enant shall use the leased premises for the operation of a grocery store, or any other lawful use." In states that examine this factor, it can lead automatically to a court finding no implied covenant of continuous operation. The idea is that any lawful use includes no use at all (or use as an empty storefront).

Courts that view the inclusion of an "any lawful use" clause as automatically meaning that there is no implied covenant of continuous operation are those in Georgia,[544] Illinois,[545] and North Carolina.[546] In Oklahoma[547] and West Virginia,[548] an "any lawful use" clause weighs against finding an implied covenant of continuous operation.

539. *See* Slater v. Pearle Vision Ctr., Inc., 546 A.2d 676, 678–79 (Pa. Super. Ct. 1988).
540. Cong. Amusement Corp. v. Weltman, 55 A.2d 95, 96 (D.C. 1947).
541. *See* Giessow Rests., Inc. v. Richmond Rests., Inc., 232 S.W.3d 576, 580 (Mo. Ct. App. 2007).
542. *See* Daniel G. Kamin Kilgore Enters. v. Brookshire Grocery Co., 81 Fed. Appx. 827, 830–31 (5th Cir. 2003).
543. *See* Sampson Invs. by Sampson v. Jondex Corp., 499 N.W.2d 177, 180 (Wis. 1993).
544. *See* Piggly Wiggly S., Inc. v. Heard, 405 S.E.2d 478, 479 (Ga. 1991).
545. Stein v. Spainhour, 521 N.E.2d 641 (Ill. App. Ct. 1988).
546. *See* Lowe's of Shelby, Inc. v. Hunt, 226 S.E.2d 232, 234 (N.C. Ct. App. 1976).
547. *See* United Associates, Inc. v. Wal-Mart Stores, Inc., 133 F.3d 1296 (10th Cir. 1997).
548. *See* Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 141 (W. Va. 1991).

f. Whether the lease contains a merger clause

Some states consider whether the lease contains a merger clause (i.e., a clause that expressly states that the lease contains the entire agreement between the parties). If the lease contains a merger clause, courts will generally interpret this factor as weighing against finding an implied covenant of continuous operation. A merger clause weighs heavily against finding the covenant in Iowa,[549] Missouri,[550] Oklahoma,[551] Washington[552] and West Virginia.[553] Idaho and Kentucky will also consider this factor but are willing to overlook the clause if it is not specific enough.[554] Kentucky would probably require the merger clause to specifically disclaim implied covenants of any sort. Kentucky might even require a specific disclaimer of the implied covenant of continuous operation.

g. Whether the landlord is subject to a noncompetitive restriction

Some commercial leases restrict the landlord from leasing other space in the vicinity to competitors of the tenant. When this type of noncompetitive restriction is present, some states interpret it as a factor weighing in favor of implying a covenant of continuous operation. There are some states, however, that do not follow this approach.

California,[555] Connecticut,[556] Idaho,[557] Iowa,[558] Kentucky,[559] New Jersey,[560] Tennessee,[561] and West Virginia[562] believe that the presence

549. *See* Fashion Fabrics of Iowa, Inc. v. Retail Investors Corp., 266 N.W.2d 22, 28 (Iowa 1978). *See also* E. Broadway Corp. v. Taco Bell Corp., 542 N.W.2d 816, 819 (Iowa 1996).

550. *See* Adbar Co., L.C. v. PCAA Mo., LLC, No. 4:06-CV-1689, 2008 WL 68858, at *4 (E.D. Mo. Jan. 4, 2008).

551. *See United Associates, Inc.*, 133 F.3d at 1298 (stating that "as a general rule, implied covenants are disfavored." *Id*.).

552. *See* Fuller Mkt. Basket, Inc. v. Gillingham & Jones, Inc., 539 P.2d 868, 873 (Wa. Ct. App. 1975).

553. *See* Frederick Bus. Props. Co. v. Peoples Drug Stores, Inc., 445 S.E.2d 176, 181 (W. Va. 1994).

554. *See* Bastian v. Albertson's, Inc., 643 P.2d 1079, 1081–82 (Idaho Ct. App. 1982) (*superceded on other grounds by statute*, IDAHO CODE ANN. § 12-120, *as recognized in* Herrick v. Leuzinger, 900 P.2d 201 (Idaho Ct. App. 1995)); Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995).

555. *See* College Block v. Atl. Richfield Co., 254 Cal. Rptr. 179, 183 (Cal. Ct. App. 1988).

556. *See* Pequot Spring Water Co. v. Brunelle, 698 A.2d 920, 925 (Conn. App. Ct. 1997).

of a noncompetitive restriction weighs in favor of finding an implied covenant of continuous operation. These states believe that the parties must have intended the tenant to operate its business continuously if the landlord is restricted from leasing to a similar business. In other words, if a tenant has the exclusive right to operate a grocery store in a shopping center, but the grocery store closes, the landlord is prohibited from replacing the tenant with another grocery store in the same shopping center. Therefore, the parties must have intended that the tenant stay open.

Georgia,[563] Michigan,[564] Minnesota,[565] and Tennessee[566] do not believe that a noncompetitive restriction weighs in favor of implying a covenant of continuous operation. For instance, a Tennessee court said that, "[t]his restriction on competition written into the lease is not broad enough to give birth to implied covenants of continuous occupancy and operation of a grocery business . . . ."[567] In other words, Tennessee and the like-minded courts do not see a restriction on the landlord as being significant to imply a covenant of continuous operation.

h. Whether the tenant has the right to remove the fixtures

Several states examine whether the tenant has the right to remove fixtures from the leased property during the term of the lease. The typical rationale is that the lease probably does not contain an implied covenant of continuous operation if the tenant has the right to remove fixtures from the leased property during the lease.[568] In other words, if the tenant can take its fixtures out of the building, then the tenant must not have an obligation to keep its business open.

557. *See Bastian*, 643 P.2d at 1082.
558. *See* E. Broadway Corp. v. Taco Bell Corp., 542 N.W.2d 816, 820 (Iowa 1996).
559. *See Lagrew*, 905 F. Supp. at 405.
560. *See* Ingannamorte v.Kings Super Mkts., Inc., 260 A.2d 841, 844 (N.J. 1970).
561. *See* BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *11 (Tenn. Ct. App. Apr. 23, 1999) (*rev'd on other grounds by* BVT Lebanon Shopping Ctr., Inc. v Wal-Mart Stores, Inc., 48 S.W.3d 132 (Tenn. 2001)).
562. *See* Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 142 (W. Va. 1991).
563. *See* Kroger Co. v. Bonny Corp., 216 S.E.2d 341, 343 (Ga. Ct. App. 1975).
564. *See* Carl A. Schuberg, Inc. v. Kroger Co., 317 N.W.2d 606, 610 (Mich. Ct. App. 1982).
565. *See* Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 730 (Minn. Ct. App. 1994).
566. *See* Kroger Co. v Chem. Sec. Co., 526 S.W.2d 468, 472 (Tenn. 1975).
567. *Id*.
568. *See* Stemmler v. Moon Jewelry Co., 139 So.2d 150, 152 (Fla. Dist. Ct. App. 1962).

Most states that have addressed this factor agree that the right to remove fixtures is inconsistent with an implied covenant of continuous operation. As stated by Florida: "[t]he right 'at any time' to remove 'all' fixtures, counters, shelving, show cases, etc., from the leased premises is entirely inconsistent with the idea that there is an implied agreement to continue to operate a jewelry business, to which such items are essential, in the leased premises."[569] This result is generally followed by Connecticut,[570] Idaho,[571] Oklahoma,[572] Rhode Island,[573] Tennessee,[574] Utah,[575] and West Virginia.[576]

Kentucky is the odd state when it comes to analyzing this factor. Under the Kentucky Test, if the landlord is entitled to the fixtures, then that is strong evidence that the parties intended the tenant to continuously operate the premises.[577] Tenant's right to remove fixtures, however, does not prohibit finding an implied covenant of continuous operation.[578]

Missouri may also have a different approach to this issue. In *EMRO Marketing Co. v Plemmons*,[579] the federal court interpreting Missouri law did not believe that the tenant's right to remove fixtures was persuasive to finding an implied covenant of continuous operation.[580] This, however, may not be the law in Missouri because the *EMRO* case was subsequently, heavily criticized and expressly overruled in some respects by the Missouri Court of Appeals.[581]

569. *Id*.

570. *See* Pequot Spring Water Co. v. Brunelle, 698 A.2d 920, 924 (Conn. App. Ct. 1997).

571. *See* Bastian v. Albertson's, Inc., 643 P.2d 1079, 1081–82 (Idaho Ct. App. 1982) (*superceded on other grounds by statute*, IDAHO CODE ANN. § 12-120, *as recognized in* Herrick v. Leuzinger, 900 P.2d 201 (Idaho Ct. App. 1995)).

572. *See* United Associates, Inc. v. Wal-Mart Stores, Inc., 133 F.3d 1296, 1297 (10th Cir. 1997).

573. *See* Aneluca Assocs. v. Lombardi, 620 A.2d 88, 91 (R.I. 1993).

574. *See* BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *12 (Tenn. Ct. App. Apr. 23, 1999) (*rev'd on other grounds by* BVT Lebanon Shopping Ctr., Inc. v Wal-Mart Stores, Inc., 48 S.W.3d 132 (Tenn. 2001)).

575. *See* Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226 (Utah 2004).

576. *See* Frederick Bus. Props. Co. v. Peoples Drug Stores, Inc., 445 S.E.2d 176, 181–82 (W. Va. 1994).

577. *See* Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 407 (E.D. Ky. 1995).

578. *See id*.

579. 855 F.2d 528 (8th Cir. 1988).

580. *See id.* at 530.

581. *See* Giessow Rests., Inc. v. Richmond Rests., Inc., 232 S.W.3d 576, 580 (Mo. Ct. App. 2007).

.

i. Whether the lease is comprehensive

Some states look at the comprehensiveness of the lease agreement. If the lease is a comprehensive and detailed agreement, then it is less likely that the parties omitted an intended term such as a covenant of continuous operation. Also, if the lease was heavily negotiated, then it is less likely that the parties accidentally omitted a term. Therefore, a comprehensive, detailed, and thoroughly negotiated lease agreement weighs against finding an implied covenant. This approach is followed by Idaho,[582] Indiana,[583] Michigan,[584] Missouri,[585] New York,[586] Oklahoma,[587] and Texas.[588]

j. Whether the parties were sophisticated

Some courts consider whether the parties to the lease were sophisticated. Often, this factor is considered along with the comprehensiveness of the lease factor. They are two different concepts, however, and would best be treated separately since it is possible to have a comprehensive lease with unsophisticated parties, or vice versa.

States that consider the sophistication of the parties typically hold that an implied covenant of continuous operation is less likely between sophisticated parties. Sophisticated parties are less likely to omit an intended term, such as a covenant of continuous operation. Sophisticated parties also have the opportunity to hire advisors, such as attorneys or commercial real estate brokers, who know or should know about a covenant of continuous operation and can assure that the issue is addressed expressly. This approach is followed by Indiana,[589] Minnesota,[590] New York,[591] Ohio,[592] and West Virginia.[593]

582. *See* Bastian v. Albertson's, Inc., 643 P.2d 1079, 1082 (Idaho Ct. App. 1982) (*superceded on other grounds by statute*, IDAHO CODE ANN. § 12-120, *as recognized in* Herrick v. Leuzinger, 900 P.2d 201 (Idaho Ct. App. 1995)).

583. *See* Keystone Square Shopping Ctr. Co. v. Marsh Supermarkets, Inc., 459 N.E.2d 420, 423 (Ind. App. 1984)).

584. *See* Carl A. Schuberg, Inc. v. Kroger Co., 317 N.W.2d 606, 607 (Mich. Ct. App. 1982).

585. *See Giessow Restaurants, Inc.*, 232 S.W.3d at 580.

586. *See* Rowe v. Great Atl. & Pac. Tea Co., Inc., 46 N.Y.2d 62, 72 (N.Y. 1978).

587. *See* Mercury Inv. Co. v F.W. Woolworth Co., 706 P.2d 523, 532 (Okla. 1995).

588. *See* Nalle v Taco Bell Corp., 914 S.W.2d 685, 688 (Tex. App. 1996).

589. *See* Keystone Square Shopping Ctr. Co. v. Marsh Supermarkets, Inc., 459 N.E.2d 420, 423 (Ind. App. 1984)).

590. *See* Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 729 (Minn. Ct. App. 1994).

591. *See* Rowe v. Great Atl. & Pac. Tea Co., Inc., 46 N.Y.2d 62, 72 (N.Y. 1978).

k. Whether the parties included an express covenant of continuous operation in unrelated agreements with third parties

Michigan[594] and Minnesota[595] examine whether the parties included an express covenant of continuous operation in unrelated agreements with third parties. These states rationalize that the presence of an express covenant in other leases indicates that the parties knew how to draft a covenant of continuous operation and include it when desired. Therefore, if there is an express covenant in third-party leases, then this factor weighs against finding an implied covenant of continuous operation. As stated by Minnesota, "[f]ailure of a landlord to use an express operating covenant where it has included the covenant in the lease of other tenants further weighs against finding an implied operating covenant because it makes clear that the landlord knew how to employ such a clause."[596]

l. Whether the landlord made a substantial investment in the leased property for the tenant

Some states consider whether the landlord made a substantial investment in the leased property for the tenant. This substantial investment usually takes the form of the landlord custom-building a structure or a facility for the tenant or performing major build-out or renovation work for the tenant. If the landlord expended considerable funds for the tenant's benefit, then the rationale is that the parties intended for the tenant to remain in business. In other words, why would a landlord spend considerable money for the benefit of a tenant who is just going to close shop? Therefore, this factor weighs against implying a covenant of continuous operation if the landlord expended considerable funds for the tenant's benefit. This factor is only considered by Idaho[597] and Iowa.[598]

592. *See* Hamilton W. Dev., Ltd. v. Hills Stores Co., 959 F. Supp. 434, 440–41 (N.D. Ohio 1997).

593. *See* Thompson Dev., Inc. v. Kroger Co., 413 S.E.2d 137, 142 (W. Va. 1991).

594. *See* Carl A. Schuberg, Inc. v. Kroger Co., 317 N.W.2d 606, 607 (Mich. Ct. App. 1982).

595. *See Plaza Associates*, 524 N.W.2d at 729–30.

596. *Id.*

597. *See* Bastian v. Albertson's, Inc., 643 P.2d 1079, 1082 (Idaho Ct. App. 1982) (*superceded on other grounds by statute*, IDAHO CODE ANN. § 12-120, *as recognized in* Herrick v. Leuzinger, 900 P.2d 201 (Idaho Ct. App. 1995)).

598. *See* E. Broadway Corp. v. Taco Bell Corp., 542 N.W.2d 816, 820 (Iowa 1996).

m. Whether the tenant is an anchor in the shopping center

Some courts consider the role of the tenant in the shopping center. If the tenant is the anchor in the shopping center or there is some other strong economic dependence on the tenant (other than just receiving rent), then courts are more likely to imply a covenant of continuous operation. As stated by South Carolina:, "[i]f the anchor tenant were permitted to leave the premises vacant, the landlord's purpose for signing the lease would be defeated."[599] As stated by New Jersey, the parties did not intend the tenant's building to be "an 'idle store building.'"[600] This factor is considered by Iowa,[601] Kentucky,[602] New Jersey,[603] Pennsylvania,[604] South Carolina,[605] and Texas.[606]

Some states, however, specifically reject this factor. Arizona does not provide weight to this factor and criticizes New Jersey's analysis of the economic interdependence theory.[607] The Arizona court stated:

> New Jersey seems to stand alone for this proposition [*i.e.*, that economic interdependence weighs in favor of finding an implied covenant of continuous operation] . . . . Also, the fact that a lessor may have a myriad of reasons why he desires the continued active operation by the lessee, unrelated to rent, should not relieve the lessor from the responsibility, if this is important, of specifically expressing his desires on the subject, so that the lessee may properly consider such an arrangement in determining the advisability of entering into the lease. In short, we find the New Jersey court's "integrated" reasoning to be unpersuasive.[608]

Minnesota also rejects this approach. Minnesota stated

> Moreover, we do not find the economic interdependence theory advanced by [the landlord] compelling because economic interde-

599. Columbia E. Assocs. v. Bi-Lo, Inc., 386 S.E.2d 259, 262 (S.C. Ct. App. 1989).
600. Ingannamorte v. Kings Super Mkts., Inc., 260 A.2d 841, 844 (N.J. 1970).
601. *See* Fashion Fabrics of Iowa, Inc. v. Retail Investors Corp., 266 N.W.2d 22, 29 (Iowa 1978).
602. *See* Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995).
603. *See Ingannamorte*, 260 A.2d at 844.
604. *See* McKnight-Seibert Shopping Ctr., Inc. v. Nat'l Tea Co., 397 A.2d 1214, 1217 (Pa. Super. Ct. 1979).
605. *See* Columbia E. Assocs. v. Bi-Lo, Inc., 386 S.E.2d 259, 262 (S.C. Ct. App. 1989).
606. *See* Lilac Variety, Inc. v. Dallas Tex. Co., 383 S.W. 2d 193, 196 (Tex. Civ. App. 1964).
607. *See* Walgreen Ariz. Drug Co. v. Plaza Ctr. Corp., 647 P.2d 643, 648 (Ariz. Ct. App.1982).
608. *Id*.

> pendence in cases of large tenants in shopping malls inevitably exists. Parties entering into such leases are well aware of this interdependence and capable of specifically expressing their desires on the subject so that it can be fully considered by both parties."[609]

n. Whether the lease is lengthy

Several states examine whether the lease is lengthy. The states, however, each weigh this factor differently. Some states weigh this factor against implying a covenant of continuous operation, especially when the lease is a ground lease. In other words, if the lease is for a large number of years, then it is more likely that the tenant's business interests or plans may change during the lease and necessitate a shutdown. This approach is followed by Rhode Island[610] and Utah.[611]

Other states, however, view this factor differently. Connecticut interprets a long-term lease as meaning that the parties intended the tenant to remain in business the entire time.[612] Kentucky[613] and Tennessee[614] take the same approach on this issue as Connecticut.

o. Appropriate factors for Arkansas

The question remains, which factors should Arkansas consider when faced with the question of whether to imply a covenant of continuous operation? The factors can generally be classified into landlord-friendly factors and tenant-friendly factors. So the ultimate issue is whether Arkansas should take a landlord-friendly approach or a tenant-friendly approach. Either option presents a fundamental challenge to established principals in Arkansas.

From one perspective, Arkansas tends to be a very landlord-friendly state. Arkansas has a series of cases that tend to find in favor of the landlord.[615] This position is further illustrated by looking at Ar-

609. Plaza Assocs. v. Unified Dev., Inc., 524 N.W.2d 725, 730 (Minn. Ct. App. 1994).

610. *See* Aneluca Assocs. v. Lombardi, 620 A.2d 88, 91 (R.I. 1993).

611. *See* Oakwood Vill. LLC v. Albertsons, Inc., 104 P.3d 1226, 1238 (Utah 2004).

612. *See* Pequot Spring Water Co. v. Brunelle, 698 A.2d 920, 924 (Conn. App. Ct. 1997).

613. Lagrew v. Hooks-SupeRx, Inc., 905 F. Supp. 401, 405 (E.D. Ky. 1995).

614. BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc., No. 01-A-01-9710-CV00607, 1999 WL 236273, at *12–13 (Tenn. Ct. App. Apr. 23, 1999) (*rev'd on other grounds by* BVT Lebanon Shopping Ctr., Inc. v Wal-Mart Stores, Inc., 48 S.W.3d 132 (Tenn. 2001)).

615. *See generally* .Lacy v. Flake & Kelley Mgmt., Inc., 366 Ark. 365, 370–71, 235 S.W.3d 894, 898 (2006) (holding that a landlord does not owe a duty of ordinary care to

kansas' version of the Uniform Residential Landlord and Tenant Act ("URLTA"). In 2007, Arkansas adopted the Arkansas Residential Landlord-Tenant Act of 2007, which is Arkansas' version of URLTA.[616] Arkansas, however, deleted the portion of URLTA titled "Tenant Remedies" and modified the article titled "Landlord Obligations" from five sections to one.[617]

From another perspective, Arkansas is traditional in its interpretation of contracts and not inclined to read terms into a contract. Arkansas holds that "[i]t is the duty of the court to construe a contract according to its unambiguous language without enlarging or extending its terms."[618] According to the Arkansas court: "[t]he first rule of interpretation is to give the language employed by the parties to a contract the meaning they intended. It is the duty of the court to do this from the language used where it is plan and unambiguous."[619] Moreover,

> [o]ne of the basic precepts of contract interpretation is that the different clauses of a contract must be read together so that all of the parts harmonize, and one provision should not be given effect to the exclusion of another, nor an interpretation be adopted which neutralizes a provision in if the various provisions can be reconciled."[620]

tenants and tenants are not an invitee of a landlord); Stewart v. McDonald, 330 Ark. 837, 843, 958 S.W.2d 297, 300 (1997) (holding that there is no common-law duty for landlords to provide a safe workplace for the employees of a tenant); Wheeler v. Phillips Dev. Corp., 329 Ark. 354, 357, 947 S.W.2d 380, 382 (1997) (holding that a landlord has no duty to a tenant to remove hazards from common areas); Bartley v. Sweetser, 319 Ark. 117, 121, 890 S.W.2d 250, 251 (1994) (refusing to find a duty on the part of the landlord to provide protection for tenants); Hall v. Rental Mgmt., Inc., 323 Ark. 143, 149–50, 913 S.W.2d 293, 297 (1996) (refusing to find that a landlord had assumed a duty to protect tenants by providing some security services); Weingarten/Ark., Inc. v. ABC Interstate Theatres, Inc., 306 Ark. 64, 67, 811 S.W.2d 295, 2971 (1991) (holding that a landlord can disclaim its obligation to mitigate damages upon a tenant's default); Nash v. Landmark Storage, LLC, 102 Ark. App. 182, ___ S.W.3d ___ (2008) (holding that a landlord does not owe a duty to protect a tenant from criminal acts); Denton v. Pennington, 82 Ark. App. 179, 182, 119 S.W.3d 519, 521 (2003) (holding that a landlord owes no duty to his tenant to repair the premises).

616. *See* ARK. CODE ANN. §§ 18-17-101 *et seq.* (LEXIS Supp. 2007).

617. *See* Lynn Foster, *The Arkansas Residential Landlord—Tenant Act of 2007*, ARK. REAL EST. REV., Vol. 1, No.1 (Spring 2008). *See also* ARK. CODE ANN. § 18-17-501 (LEXIS Supp. 2007) (listing the landlord obligations).

618. North v. Phillliber, 269 Ark. 403, 406, 602 S.W.2d 643, 645 (1980).

619. Stoops v. Bank of Brinkley, 146 Ark. 127, 135, 225 S.W.593, 595 (1920). *See also* Lee Wilson & Co. v. Fleming, 203 Ark. 417, 156 S.W.2d 893, 894 (1941).

620. Byme, Inc. v. Ivy, 367 Ark. 451, 465, 241 S.W.3d 229, 240 (2006) (Imber, J., dissenting).

So the question again becomes, which approach is right for Arkansas? Is it a landlord-friendly approach like the Kentucky Test or a tenant-friendly approach like the Minnesota Test? Should Arkansas adopt one of the established approaches or create a new one by picking from a variety of factors? Obviously, only the Arkansas Supreme Court can make this decision, but what are the options?

One of Arkansas' options is to adopt one of the formula approaches, such as the Kentucky Test, the Georgia Test, the Minnesota Test, or the West Virginia Test. The Kentucky Test is the obvious choice if Arkansas decides to take a landlord-friendly approach. The Minnesota Test or West Virginia Test is probably best if Arkansas wants an approach that is more tenant-friendly or a test that is less likely to imply a covenant of continuous operation.

Arkansas' other option is to create its own factor test. Arkansas may choose to start with the Standard Factors to determine if it is appropriate to imply any type of covenant. Arkansas could then move into an analysis of numerous factors specific to covenants of continuous operation including the following:

1. Whether there is sufficient fixed rent to compensate the landlord;

2. Whether the fixed rent is significant compared to percentage rent;

3. Whether the tenant has an unfettered right of assignment or subletting;

4. Whether the lease contains a restriction on the tenant's permitted uses of the leased property;

5. Whether the lease contains an "any lawful use" clause;

6. Whether the lease contains a merger clause;

7. Whether the landlord is subject to a noncompetitive restriction;

8. Whether the tenant has the right to remove the fixtures;

9. Whether the lease is comprehensive;

10. Whether the parties were sophisticated;

11. Whether the parties included an express covenant of continuous operation in unrelated agreements with third parties;

12. Whether the landlord made a substantial investment in the leased property for the tenant;

13. Whether the tenant is an anchor in the shopping center; and

14. Whether the lease is lengthy.

All of these factors have merit and are worthy of consideration. A fourteen factor test, however, is probably too unwieldy to be effective. Some of the factors are more important than others. The following are arguably the least probative:

> 1. The fifth factor: whether the lease contains an "any lawful use" clause. This factor may be overreaching because many commercial leases use this type of language almost as boilerplate. If there is a thorough analysis of the permitted uses, it may not be necessary to include this analysis as well.
>
> 2. The sixth factor: whether the lease contains a merger clause. This factor also may be overreaching since a merger clause is common boilerplate that the parties may not really consider.
>
> 3. The eighth factor: whether the tenant has the right to remove the fixtures. This factor may be a little too complicated to effectively analyze and may not add much to the analysis that is not already provided by analyzing the use restrictions on the parties.
>
> 4. The ninth factor: whether the lease is comprehensive. This factor could be skipped because many leases simply use forms and the comprehensiveness of the form may not be a true reflection of the parties' intent. Of all the factors on this list, it may be the most worthy of being included in an analysis.
>
> 5. The eleventh factor: whether the parties included an express covenant of continuous operation in unrelated agreements with third parties. This factor could be eliminated because the presence of an express covenant of continuous operation in a third-party lease may be the result of many causes, including a different attorney drafting the agreement. Also, including this factor could make the discovery process more difficult and invasive than it needs to be by causing the parties to subpoena each other's third-party leases.
>
> 6. The fourteenth factor: whether the lease is lengthy. This factor could be left out because there is not sufficient consensus among the states whether the length of the lease should weigh for or against finding an implied covenant of continuous operation.

If these factors are omitted, it would leave the following list of factors:

> 1. Whether there is sufficient fixed rent to compensate the landlord;
>
> 2. Whether the fixed rent is significant compared to percentage rent;

3. Whether the tenant has an unfettered right of assignment or subletting;

4. Whether the lease contains a restriction on the tenant's permitted uses of the leased property;

5. Whether the landlord is subject to a noncompetitive restriction;

6. Whether the parties were sophisticated;

7. Whether the landlord made a substantial investment in the leased property for the tenant; and

8. Whether the tenant is an anchor in the shopping center.

Of course, the Arkansas Supreme Court will ultimately decide what to consider, but this list of factors would keep Arkansas consistent with the majority of states. This list would also balance economic considerations and the integrity of contracts.

p. Avoiding the analysis through contractual terms

The implied covenant of continuous operation exists for situations where the lease does not address the tenant's obligation to continuously operate. It is, however, best for all parties if the lease expressly addresses the tenant's obligations rather than leaving it to the courts to interpret. So what should a lease include if the parties want to disclaim an obligation to continuously operate? A possible lease term may read as follows:

> **No Covenant of Continuous Operation**. Nothing in this Lease shall be interpreted or construed as either an express or implied covenant of continuous operation or covenant against going dark. The parties recognize and agree that Tenant, in its sole discretion, shall have the absolute right to cease operations at the premises at any time prior to the expiration of the lease so long as Tenant fulfills all obligations contained in this Lease, including without limitation paying the fixed rent and maintaining the premises in good order and repair. Landlord hereby waives any right or claim for damages or equitable relief related to Tenant ceasing business operations at the leased premises. Tenant's cessation of business shall not be deemed an abandonment or surrender of the leases premises so long as Tenant continuous to fulfill its obligations under this Lease. Neither the existence of percentage rent nor Tenant's role as a so-called "anchor" (as that term is used in the shopping center industry) in the shopping center shall imply a covenant of continuous operation.

VI. CONCLUSION

Arkansas' law on the implied covenant of continuous operation is sparse at best. Landlords and tenants in Arkansas have very little guidance to help them understand the legal rights of the parties if the lease does not expressly address the tenant's obligation to operate. Arkansas' only guidance comes from the *Patton* case.

The *Patton* case, however, has many weaknesses. First, the *Patton* case is a federal case interpreting Arkansas law and is, therefore, merely persuasive. Second, the *Patton* case failed to provide a clear structure for analyzing implied covenants of continuous operation. The *Patton* case cites the Kentucky Test for the implied covenant. The Kentucky Test, however, is very landlord-friendly, has been criticized by other states, and takes an approach that is followed by only two other states. Furthermore, even though the court described the Kentucky Test, the court failed to fully analyze the factors or follow the spirit of the test based on its application in Kentucky, Tennessee, and Connecticut. Instead, the *Patton* court drifted between several different factors to conclude the lease in the case at bar did not contain a covenant of continuous operation. The result is that the *Patton* case provides little guidance and, perhaps, more confusion.

Arkansas would be well-advised to distinguish the *Patton* case and avoid applying its rationale in future cases. The *Patton* case is not, however, all bad and probably ultimately reaches a result that Arkansas would concur with. Even though Arkansas tends to be very landlord-friendly, Arkansas is also reluctant to burden parties in a contract with obligations that are not expressly stated. While the Kentucky Test is likely to imply a covenant of continuous operation, the Kentucky Test stands as a minority position. The majority of states apply an analysis that is reluctant to find an implied covenant of continuous operation. Arkansas should follow the majority approach and adopt a test that would not imply a covenant of continuous operation except in special and unique circumstances.

Instead of relying on the courts, parties are better off if they directly address the tenant's obligations and expressly state whether the tenant has an obligation to continuously operate during the lease. Without expressing the obligation, the parties are left to the discretion of the court and both may be left with a result they did not desire. If the landlord is counting on the tenant to continuously operate, either to collect percentage rent or to anchor a shopping center, then the landlord should expressly state the tenant's obligation. Likewise, if the tenant is counting on the flexibility to close its operations during the term

of the lease, then the tenant should expressly state that it has the right to close.