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Lease Disclaimers and Landlord Fraud
McClain v Octagon Plaza, LLC (2008)
159 CA4th 784, 71 CR3d 885

Lease disclaimers do not insulate landlord from liability for fraud

McClain's lease with Octagon contained disclaimers that any statement of size was an approximation and that the lessee should satisfy itself with respect to the premises. Later, McClain claimed that Octagon had, among other misdeeds, negligently or intentionally misrepresented the size of the premises in order to induce her to pay excessive rent. The trial court sustained Octagon's demurrer to claims relating to size of the premises on the ground that they were barred by the lease disclaimers. Following a bench trial, the trial court also ruled against McClain's remaining claims. McClain appealed.

The court of appeal reversed in part and remanded for further proceedings. The disclaimer in McClain's lease that asserted that McClain had an adequate opportunity to examine the leased unit did not insulate Octagon from liability for fraud or prevent McClain from demonstrating justified reliance on Octagon's representations. Likewise, the purported disclaimer regarding the estimates of size was not exculpatory. The fact that Octagon claimed that the representations as to the size of the premises and the shopping center were approximations did not preclude McClain from showing that they were in fact, materially and unreasonably inaccurate. Moreover, the court held that McClain also stated a claim for declaratory relief because she had adequately alleged a fraud claim based on misrepresentations about the proper base rent and share of common expenses under the lease. She could not, however, state a claim for breach of the covenant of good faith and fair dealing based on precontract negotiations. Nor was she entitled to an accounting of Octagon's expenses. Rather, McClain was entitled only to disclosure of the documents supporting the "reasonably detailed statement" of common expenses, specified by the lease, for the limited purpose of verifying that the expenses were incurred and the amounts accurate. McClain was not entitled to dispute the need for expenses or to audit the landlord's records.

THE EDITOR'S TAKE: It is unclear to me what the trial judge is supposed to do on remand. The demurrer initially sustained was to a complaint that included two counts alleging that the landlord had (1) intentionally and/or (2) negligently misstated the size of the tenant's unit in its shopping center. Insofar as the misrepresentation was alleged to have been intentional, it seems clear that a statement in the lease that the measurements were approximate would have no greater protective effect than would an "as is" clause in a sales contract. Exculpatory clauses just do not protect against fraud. So, the intentional misrepresentation count should get to trial notwithstanding the lease provision. (Although the tenant is going to have to prove not only that there were misrepresentations, but that they were intentional. The fact that different numbers appeared in an insurance application may show that there was a discrepancy, but I do not think that it also proves the discrepancy was intended.)

The other count in the complaint alleged a negligent misrepresentation as to size, and the appellate opinion overturned the demurrer to that claim as well, seeming to say that the lease clause did not protect against it, either. That should be much more worrisome because, unless the landlord can show that the lease footage was right and the insurance footage was wrong, it looks like the landlord might be per se guilty of negligent misrepresentation. How else can one explain the 2600 square feet on one form and 2400 on another, except that somebody was probably careless? People often make errors when measuring things and try to deal with that by saying "more or less" or "approximately." Now, it appears that if that number turns out later on to be incorrect, the error may be actionable despite those admonitory phrases and despite the absence of any intent to deceive. If this landlord cannot successfully explain away the overage, it may find that not only could it not hide behind a demurrer to the negligent misrepresentation cause of action against it, it may indeed be at risk of exposure to a summary judgment.

Although the opinion says nothing about the matter, I would have been interested in knowing who profited from the miscalculation. The tenant was allegedly charged 23 percent of common area

expenses rather than 19 percent. Does that mean that the other tenants paid 4 percent less than they should have paid? Or did the landlord collect 104 percent of common area charges from the tenants (or possibly even more if it was doing the same to all of them)? If the error amounted to a windfall to the other tenants rather than to the landlord, can this landlord now correct its other leases? Or will those other tenants be able to hide behind the same approximation clause in their leases? After all, they have the additional argument that they were not the ones who came up with the number in the first place.—*Roger Bernhardt*