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Security Deposits Under Leases

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the value of property of a plaintiff, who has come into equity seeking a mandatory injunction against the defendant, where such defendant has the right to condemn such property.

The decision in the present case is a valid exercise of the powers of equity, and the plaintiff's constitutional rights have not been infringed upon.

J. CYRIL O'CONNOR.

SECURITY DEPOSITS UNDER LEASES.

In the case of *Senz, Inc.* v. *Hammer*[1] the tenant sought to recover a deposit under a lease, afer having removed from the premises pursuant to a ten-day notice, served upon him by the landlord, to pay or move. The lease contained a provision that a continued default in the payment of rent, for ten days after said notice was served, shall terminate the lease without any entry or further act on the part of the landlord. It was also provided that the foregoing provision is intended as a conditional limitation. The court held that where from the provisions of a lease, though obscure, an inference must be drawn that the parties contemplated a deposit as security for the performance of all the covenants, and that the landlord's agreement to repay it after the expiration of the lease was conditioned on the tenant's full performance, a removal of the tenant from the premises, and acceptance by the landlord of possession after a default by the tenant, does not warrant the recovery of the deposit by the tenant. Following the rulings of *International Publications* v. *Matchabelli*,[2] and *Hand* v. *Rifkin*,[3] the court held that, under such circumstances, the liability of the tenant survives the severance of the relationship of landlord and tenant.

The general question underlying these cases is, whether the termination of the lease destroys all obligations thereunder, or whether a proper covenant concerning the continued liability of the tenant survives the termination so as to allow the landlord to hold the deposit until such time when all the damages are ascertainable and to apply same in satisfaction of such damages.

The cases of *International Publications* v. *Matchabelli* and *Hand* v. *Rifkin* hold that the parties may contract for a continuing liability on the part of the tenant, beyond the termination of the lease. While these two cases refer to termination because of summary proceedings,[4] the principle is the same whether the termination occurs by

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[1] 265 N. Y. 344, 193 N. E. 168 (1934).
[2] 260 N. Y. 451, 184 N. E. 51 (1933).
[3] 263 N. Y. 416, 189 N. E. 476 (1934).
[4] Section 1434 of the New York Civil Practice Act expressly provides that the issuance of a warrant for the removal of a tenant cancels the lease

operation of law or by contract of the parties, provided, of course, that the tenant has properly covenanted in substance for full performance of all the terms, covenants and conditions of the lease or that he will be liable in damages for deficiency covering such contingency.

These covenants of continued liability are legal under the common law, and they are not prohibited by statute; nor are they against public policy.[5] As was said in *Michaels* v. *Fishel,*[6] "The right to enter into engagements of this character exists at common law, and, since there is no statute to prevent, as was said in an early case, such a contract 'certainly is not an illegal agreement, nor is there anything unreasonable in the lessee agreeing to completely indemnify his lessor for any injury which may arise to him by the lessee's breach of his own agreement.' "

Although the relationship of landlord and tenant has ceased and the lease itself is annulled, the tenant's liability survives since the contractual relationship between the parties is not terminated.[7] The covenant is deemed a separate and distinct agreement despite the fact that it is part of the lease which itself is destroyed. What survives, however, is a liability, not for rent, but for damages,[8] because a lease is an instrument of dual legal effect; it is both a contract and a conveyance.

That such a covenant should survive the termination of the lease seems reasonable, otherwise the very purpose for which it was inserted becomes futile. Concerning this we find the following in *Baylies* v. *Ingram:* [9] "It is evident that the covenant itself could not come into operation until there was a breach of its conditions. Its purpose was to provide a remedy in favor of the landlord, should the defendants be guilty of a breach of the terms and conditions of the lease. Manifestly, a provision which gave a remedy for the tenant's default ought not to be held to fail the moment the relation of landlord and tenant ceased in consequence of a breach by the tenant. The covenant was aimed at just such a contingency, and was utterly valueless unless it can be made to serve the purpose of its creation,

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and annuls accordingly the relation of landlord and tenant, except that rent payable or a claim for use and occupation is not thereby discharged. This was the old Section 2253 of the Code of Civil Procedure. A similar statute was in effect since 1820, when the first law for the recovery of demised premises by summary proceedings was enacted in New York, although an English statute on the subject was in force while we were a colony of Great Britain. (Laws of 1820, c. 194, §3, amending Laws of 1813, c. 202; 2 R. S. 515, §43; 11 Geo. II, §19.)

[5] See Slater v. Von Chorus, 120 App. Div. 16, 17, 104 N. Y. Supp. 996, 997 (1st Dept. 1907).

[6] 169 N. Y. 381, 387, 62 N. E. 425, 426 (1902).

[7] Halpern v. Manhattan, 173 App. Div. 610, 160 N. Y. Supp. 616 (1st Dept. 1916), *aff'd,* 220 N. Y. 655, 115 N. E. 718 (1917).

[8] Hermitage Co. v. Levine, 248 N. Y. 333, 337, 162 N. E. 97, 97 (1928); see Kottler v. N. Y. Bargain House, 242 N. Y. 28, 150 N. E. 591 (1926).

[9] 84 App. Div. 360, 363, 364, 82 N. Y. Supp. 891, 894 (1st Dept. 1903).

otherwise it would be a mere dead letter without any vitality whatever."

Under such circumstances, then, where a tenant defaults in the payment of rent, with the resultant cancellation or termination of the lease, and, relying on such termination, he sues the landlord to recover the deposit, the courts hold that the tenant must abide the liquidation of the loss. In other words, where a tenant is obligated for damages under such a covenant he will not be allowed to recover his deposit, despite the termination of the lease, until such time when the damages are ascertainable. And until such time, such actions will be dismissed for being premature.[10] So, in *Hand* v. *Rifkin,* it is said: "We think that under these covenants the tenant's liability survives the severance of the conventional relationship created by the lease, but that the loss, if any, which the landlord may suffer through the tenant's default has not been, and cannot be, ascertained until the end of the term denominated in the lease." [11]

Thus it is that, despite an old writer who said,[12] "a tenant can make no return for a thing he has not," a tenant can, although out of possession, be held liable for the premises he does not occupy, and, in effect, be compelled to make a return for the very thing he has not.

The security deposit is very commonly used in New York for it is only by this contractual method that the landlord has some security out of which to satisfy the damages or deficiencies in such cases. Many states allow to the landlord a security right, without such provisions in a lease, as, for example, the right of distraint or a statutory landlord's lien on goods or property of his tenant. Formerly New York also had a distress for rent but in 1846 this was abolished. And for this reason the security deposit is so widely used here, although in those states which allow the statutory security, the security deposit provisions are also included in leases, since this is a simpler method of obtaining the security than the enforcing of the statutory security right.[13]

In regards to security deposits, however, it should be noted that the non-performance by the depositor does not vest title to the deposit in the secured party. It merely allows him to resort to the deposit only in the event that there are damages sustained by the secured party and then, only to the extent of actual indemnification for his loss or damage.[14] And it is in this respect that deposits on leases differ with moneys paid on a contract of purchase. In such a case the vendee paying the deposit cannot recover it back.[15] For, as said

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[10] Lenco v. Hirshfield, 247 N. Y. 488, 159 N. E. 718 (1928).
[11] 263 N. Y. 416, 420, 421, 189 N. E. 476, 477 (1934).
[12] 7 BACON'S ABR. (7th ed.) 57.
[13] Wilson, *Lease Security Deposits* (1934) 34 COL. L. REV. 426.
[14] Peirson v. Lloyds, 260 N. Y. 214, 183 N. E. 368 (1932).
[15] Haynes v. Hart, 42 Barb. 58 (N. Y. 1864); see Page v. McDonell, 55 N. Y. 299, 303, 304 (1873); Lawrence v. Miller, 86 N. Y. 131, 139 (1881); Saperstein v. Mechanics, 228 N. Y. 257, 126 N. E. 708 (1920); Friedland v. Argentor, 214 App. Div. 242, 211 N. Y. Supp. 896 (1st Dept. 1925).

in *Chaude* v. *Shepard,*[16] "In such a case the party so paying, who afterwards by reason of his default is deprived of or denied the benefits of his contract, cannot recover back the money so paid by him upon it." But where a tenant deposits money, he may recover the deposit back; even though he be in default, if the damages which the landlord sustained are satisfied therefrom. "This may seem anomalous," says McAdam,[17] "but it is because the equitable principle of avoiding forfeitures has been applied to the one case, but not to the other." So, where there was money deposited under a lease (which lease did not contain a covenant of continuing liability) and the tenant is dispossessed in summary proceedings for non-payment of rent, the courts will make the landlord return the deposit for security, after deducting therefrom the amount apportioned for rent due *prior* to the removal.[18] "For there can be no recovery for damages accruing after the termination of the lease by summary proceedings in the absence of an express agreement to the contrary."[19]

There are, however, some cases in which a landlord may retain the amount of deposit on the default of the tenant as outright damages and not as a security. These are the "liquidated damage" cases.[20] Here a provision is inserted in the lease to the effect that since the damages are not ascertainable the landlord may retain the amount on deposit as liquidated damages. But the general tendency of the courts is to treat such deposits as penalties and to allow the landlord to keep only so much as would indemnify him for his actual loss or damage.[21] Concerning this is the following quotation from *Seidlitz* v. *Auerbach:*[22] "The great weight of authority is to the effect that where a contract contains a number of covenants of different degree of importance and the loss resulting from the breach of some of

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[16] 122 N. Y. 397, 402, 25 N. E. 358, 360 (1890).

[17] 2 McADAM, LANDLORD AND TENANT (5th ed. 1934) 1123.

[18] Kelly v. Miles, 48 Hun 6 (N. Y. 1888), *aff'd,* 122 N. Y. 645, 25 N. E. 957 (1890).

[19] 8 CARMODY'S N. Y. PRACTICE (2d ed. 1933) pt. 1, 317; see Crausmann v. Graham, 95 Misc. 608, 159 N. Y. Supp. 709 (1916).

[20] J. & H. Garage v. Flow, 225 App. Div. 65, 232 N. Y. Supp. 242 (1st Dept. 1928), *aff'd,* 251 N. Y. 553, 168 N. E. 424 (1929). (In the Appellate Division, Finch, J., said: "The general principles of law governing the construction of a lease providing for liquidated damages are as follows: Equity, in order to do justice at a time when justice has become over-ridden by legal formalism and love of logic, established the principle of granting relief from penalties and forfeitures. This principle, as applied to an agreement in a lease for a sum certain to become liquidated damages, does not raise a presumption that such a sum is a penalty. On the contrary, when the parties to such a lease are competent to contract, their intention will be carried out unless the Court can see that the liquidated sum, although denominated 'liquidated damages,' is but a cloak of language to attempt to hide a sum which is out of proportion to, and differs greatly from, the actual damages which would in the course be suffered," at pp. 66, 67.)

[21] Chaude v. Shepard, 122 N. Y. 397, 25 N. E. 358 (1890); see Seidlitz v. Auerbach, 230 N. Y. 167, 129 N. E. 461 (1920).

[22] 230 N. Y. 167, 173, 129 N. E. 461, 463 (1920).

them will be clearly disproportionate to the sum sought to be fixed as liquidated damages, especially where the loss in some cases is readily ascertainable, the sum so fixed will be treated as a penalty. The strength of a chain is that of its weakest link." So too, in *City of New York* v. *Brooklyn & Manhattan Ferry Co.:* [23] "The tendency of the courts in doubtful cases is to favor the construction which makes the sum payable for breach of contract a penalty rather than liquidated damages, even where the parties have styled it liquidated damages rather than a penalty."

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[23] 238 N. Y. 52, 56, 143 N. E. 788, 790 (1924).