

# Unlawful Lease Provision

## Iowa Supreme Court Hands Down Decisions in Two Iowa City Residential Landlord Tenant Cases – June 1, 2017

Jodie Clark McDougal

On May 19, 2017, the Iowa Supreme Court handed down decisions in two highly publicized Iowa City cases in which tenants had brought suit against their landlords - *Kline v. Southgate Property Management* and *Walton v. Gaffey*. Both sides have appeared to claim victory from the decisions, and, while Iowa landlords can glean more clarity from the decisions in many respects, landlords are necessarily left with some uncertainty in other respects.

### Prior Cases Leading Up to the *Kline* and *Walton* Decisions:

In 2013, the Iowa Court of Appeals entered an unpublished decision in the *Staley v Barkalow* landlord-tenant case, in which the Court entered a decision in favor of the tenants, concluding that (1) under the Uniform Residential Landlord and Tenant Law set forth in Iowa Code Chapter 562A (the “Act”), a landlord is liable for the inclusion of prohibited provisions in a rental agreement, even without enforcement, if the landlord's inclusion was willful and knowing (note: a similar provision can be found within Iowa Code Chapter 562B); and (2) in such event, the tenant may recover from landlord the “actual damages sustained by the tenant and not more than three months' periodic rent and reasonable attorney fees” (note: under Chapter 562B, a tenant's recoverable damages are less robust than in Chapter 562A). In the years following, other decisions were rendered by various district courts, the Iowa Court of Appeals (such as *Amor v. Houser*), and the Iowa Supreme Court (*Elyse De Stefano v. Apts. Downtown, Inc.*, and *Lenora Caruso v. Apts. Downtown, Inc.*, a summary of these cases is available [here](#)), which dealt with some, but not all, of the issues pertinent to the *Kline* and *Walton* cases.

### Summary of the *Kline* and *Walton* Decisions:

In both cases, tenants sued their landlords over the content of their lease agreements and argued that the landlord was liable for damages and attorney's fees under the Act because the landlords' leases included several provisions known by the landlord to be prohibited provisions. The district court granted summary judgment in favor of the tenants, and the landlord appealed. On appeal, the Iowa Supreme Court affirmed in part, and reversed and remanded in part, both of the district courts' decisions. The questions answered and issues discussed in the Supreme Court's two decisions are summarized below, but landlords are well-advised to read the entirety of both decisions.

## Can a Landlord be Liable for the Mere Inclusion of Unlawful Lease Provisions?

Yes. The Iowa Supreme Court affirmed the district courts' decisions in this regard, concluding that a landlord is liable for the landlord's mere inclusion of prohibited provisions in a rental agreement, even without enforcement of those provisions against the tenant, if the landlord's inclusion was willful and knowing.

Are Flat Fees, Fines/Charges, and Liquidated Damages Lease Provisions, Set Without Consideration of a Landlord's Actual Damages, Categorically Prohibited?

No. The Iowa Supreme Court reversed the district courts' decisions in this regard. The Iowa Supreme Court held that certain fees, charges, and liquidated damages included within the leases at issue were not "categorically prohibited" merely "because they were set without any consideration of what the landlord's actual damages and fees would be in each situation," contrary to the district courts' opinions.

Though, the Iowa Supreme Court emphasized that the lawfulness of any such fees, charges, and liquidated damages are to be determined on a case-by-case basis and are unlawful if they are contrary to the Act or Iowa law, unconscionable, or otherwise unenforceable penalties under the Act or Iowa law. Concerning the specific provisions in the two leases at issue, the Supreme Court agreed that some of those provisions were unlawful as a matter of law, while consideration of the remaining provisions was remanded back down to the district courts to be decided upon at a later date.

## What Types of Lease Provisions Are Categorically Prohibited Under the Act?

Consistent with previous decisions, the Iowa Supreme Court held that the Act imposes certain specific categories of lease provisions that are prohibited as a matter of law. The Supreme Court held that, among others, the following categories of lease provisions are unlawful and categorically prohibited under the Act:

1. A waiver of a tenant's rights and/or remedies otherwise established under the Act;
2. Exculpation, limitation, or indemnification of a landlord's duty or liability under the Act or law;
3. An agreement by a tenant to pay the landlord's attorney fees;
4. An agreement by a tenant to confess judgment in a certain regard; and
5. An unconscionable provision, or unenforceable penalty, under Iowa law.

The Supreme Court held that, "[b]eyond these express prohibitions, however, landlords and tenants are free to form residential rental contracts consistent with Chapter 562A and the principles of law and equity supplementing it." This is good news for Iowa landlords.

However, for Iowa landlords, the devil is in the details in following the guidance by the Iowa Supreme Court. In particular, a landlord must remember that under Iowa law, and as confirmed by the Kline and Walton decisions, a landlord owes tenants the duty to keep the leased premises in a fit and habitable condition and to otherwise repair and maintain in good and safe working order all electrical, plumbing, HVAC, and other facilities/appliances and to pay for such repair and maintenance work (with a limited exception for single-family residences in which the parties may agree that the tenant shall perform certain repairs/work, but a landlord still cannot charge the tenant for such repairs/work). Thus, as noted in Kline, a lease provision is unlawful if it purports to limit the aforementioned repair and maintenance duties imposed upon landlords, or in any other way limits or extinguishes a landlord's other duties or liability under the Act or Iowa law. In Kline and Walton, the Iowa Supreme Court also affirmed that a landlord can only deduct from a security deposit amounts for damages to the premises if the landlord proves such damages are "beyond normal wear and tear" resulting from a deliberate or negligent act of a tenant, or tenant knowingly permitting it, thereby invalidating any lease provision to the contrary. Perhaps the most difficult task for landlords in following the guidance of these cases is landlords attempting to answer the question of whether a proposed flat fee, fine, charge, or liquidated damages provision within a lease is unlawful because it is unconscionable or otherwise an unenforceable penalty, which is discussed in the last section below.

## What Conclusions did the Iowa Supreme Court Reach Regarding the Specific Lease Provisions?

In the two decisions, the Iowa Supreme Court affirmed the district courts' rulings that the following provisions were unlawful:

1. in the Walton case, an automatic carpet cleaning provision in which a landlord automatically imposed a carpet cleaning fee and automatically deducted that fee from the security deposit at the end of every lease term,

regardless of whether such cleaning was necessary to restore the premises to the condition at the outset of the tenancy beyond ordinary wear and tear;

2. in Kline, a delayed possession provision in which the tenant's sole remedy for delayed possession was rent being rebated on a pro rata basis, as such provision constituted an unlawful exculpation and limitation of the landlord's liability arising under law;
3. in Walton, a provision limiting the landlord's liability for any loss of use or consequential damages arising from appliance failure, as such provision also constituted an unlawful exculpation provision; and
4. in Walton, a provision providing that the landlord was not liable for any damage or loss of any of the tenant's personal property for any cause whatsoever, as such provision was an unlawful exculpation provision.

Conversely, in the Kline case, the Supreme Court held that an apartment-inspection checklist provision was not categorically prohibited because the Court viewed the provision as a "procedural device to promote documentation of the condition of the dwelling at the outset of the landlord-tenant relationship," and concluded that, while such prohibition creates a presumption that may have some "evidentiary significance in the event [the landlord] claims the tenant caused damage to the dwelling," such provision was not a black-and-white unlawful exculpation provision.

Finally, the Iowa Supreme Court concluded that numerous other fees, charges, and liquidated damages provisions in the leases at issue – including a charge for returned checks, maintenance call charge, liquidated damages provision for unauthorized pets, fee for subletting, per diem fee for holdover tenants, charge for lockout service calls, charge for replacement keys, and charges/fines for certain lease violations – were not "categorically prohibited" as a matter of law. Instead, the Court remanded those issues back to the district courts to consider on a case-by-case basis within the confines of the principles set forth within the decisions and otherwise by the Act and Iowa law. If the district courts enter decisions on the aforementioned remanded issues, I will provide another update, however, there is certainly a possibility that the parties in the two cases will settle their remaining disputes and eliminate the need for any further district court proceedings.

### Are There Any Unanswered Questions?

Yes. The Iowa Supreme Court necessarily left open questions to be answered by future courts on a case-by-case basis. Specifically, the question of what fines, flat fees, charges, and liquidated damages provisions are lawful and what ones are not? Future courts will have to consider, on a case-by-case basis, any challenged lease provisions and, pursuant to the Supreme Court's guidance, will strike down as unlawful any such provisions that are unconscionable, unenforceable penalties, or otherwise prohibited under the Act or Iowa law. Below is a very brief summary of further Iowa law in this regard.

Regarding unconscionability, in prior cases, the Iowa Supreme Court has emphasized that "[b]ecause of its equitable purpose, neither the courts nor the legislature have attempted to give [unconscionability] a precise definition." Generally, "[a] bargain is said to be unconscionable at law if it is such as no man in his senses and not under delusion would make on the one hand, and no honest and fair man would accept on the other . . . We look at the factors of assent, unfair surprise, notice, disparity of bargaining power, and subjective unfairness." Regarding liquidated damages provisions being deemed to be unenforceable penalties, the Iowa Supreme Court has held in prior cases that liquidated damages provisions are enforceable and lawful when both the "anticipated amount of actual damages resulting from a breach of the lease were uncertain" and the "amount fixed in a liquidated damages provision is reasonable to the extent that it approximates the loss anticipated at the time of the making of the contract, even though it may not approximate the actual loss." On prior occasions, the Iowa Supreme Court has struck down fines and liquidated damages provisions, on public policy grounds, when the contractual provision provided for "unreasonably large liquidated damages" or an amount that was "out of reasonable proportion to the loss or injury actually sustained or reasonably to be anticipated."

We will all keep an eye on future court decisions in which these issues are analyzed in more detail.

# Iowa's Highest Court Enters First Decision on Certain Landlord-Tenant Issues Raised in 2013 Staley Case: Landlords Must Take Note of De Stefano v. Apts. Downtown - May 13, 2016

Jodie Clark McDougal

**Please be advised that this area of law has been affected by certain recent Iowa Supreme Court opinions. An update as to the current law in this area is available in Iowa Supreme Court Hands Down Decisions in Two Residential Landlord-Tenant Cases**

As most landlords are aware, in 2013, the Iowa Court of Appeals entered a decision in the Staley v Barkalow case, which involved a group of tenants who sued their landlord over the content of their lease agreements. Ultimately, the Court of Appeals entered a ruling in favor of the tenants and, among other things, concluded that under the Uniform Residential Landlord and Tenant Law set forth in Iowa Code Chapter 562A, "a landlord is liable for the inclusion of prohibited provisions in a rental agreement, even without enforcement, if the landlord's inclusion was willful and knowing" and, in such event, the tenant may recover from landlord the "actual damages sustained by the tenant and not more than three months' periodic rent and reasonable attorney fees." Thereafter, in 2014 and 2015, the Iowa Court of Appeals (in Amor v. Houser), as well as several district courts, rendered similar decisions. Such courts ruled that certain landlords had violated Iowa law by their mere inclusion of various unenforceable provisions within their leases, and, in those cases, the district courts ruled that various commonly used lease provisions were unlawful for various reasons.

Prior to this month, the Iowa Supreme Court had not rendered any decisions on the landlord-tenant issues raised in the aforementioned Court of Appeals and district court decisions. Then, on May 6, 2016, the Iowa Supreme Court entered two decisions that addressed some of those landlord-tenant issues. Importantly, it should be noted that while the aforementioned cases are ones in which the courts were interpreting Iowa Code Chapter 562A, the prevailing opinion is that the courts' various holdings are equally applicable to Iowa Code Chapter 562B and manufactured housing communities, as the relevant statutory provisions in Chapter 562B regarding lease agreements and landlord responsibilities are essentially the same as in Chapter 562A. Notably, the statutory provisions regarding a tenant's recoverable damages in 562B are more favorable to landlords than the provisions in Chapter 562A.

On May 6, 2016, the Iowa Supreme Court issued its decision in the case of Elyse De Stefano v. Apts. Downtown, Inc., and similar case of Lenora Caruso v. Apts. Downtown, Inc. This article contains a summary of the Court's conclusions in these cases, but landlords should review these two decisions in their entirety. In the De Stefano case, a tenant sued her landlord in small claims court over the content of her lease agreement and based upon her claim that the landlord had improperly withheld certain portions of her rental deposit, thereby entitling her to money damages, plus attorney's fees. After the case was heard, first, by the small claims court and, second, by the district court, it was heard by the Iowa Supreme Court.

Importantly, the Iowa Supreme Court concluded that multiple lease provisions and actions by the landlord were unlawful based upon various points, including the following legal principles and conclusions set forth within the decisions:

1. Generally speaking, a landlord owes tenants the duty to keep the leased premises in a fit and habitable condition and to otherwise maintain in good and safe working order all electrical, plumbing, HVAC, and other facilities/appliances therein.
2. A lease provision cannot extinguish or limit, in any way, the landlord's legal duties noted above or any other statutory landlord duties (except under a very limited statutory exception for single-family residences in which the parties may agree that the tenant shall perform certain repairs/work, but a landlord still cannot charge the tenant for such repairs/work).
3. Based upon principles (1) and (2) above, a provision in a lease agreement that extinguishes or limits those landlord duties or otherwise forces a tenant to pay for repairs or maintenance for which the landlord is legally responsible is an unlawful provision.
4. A landlord can only deduct amounts from a rental deposit for damages to the premises if the landlord proves such damages are "beyond normal wear and tear" resulting from a deliberate or negligent act of a tenant, or tenant knowingly permitting it.

5. Even when a landlord may have a legal right to pass along certain costs/fees to a tenant, a landlord cannot simply withhold from the tenant's rental deposit an automatically-imposed charge, even if pursuant to an explicit lease provision.

In addition, the Supreme Court also held that certain lease provisions were unlawful.

Specifically, in *De Stefano*, the Court struck down a lease provision that stated as follows and under which the landlord had charged the tenant for repair of a damaged door (due to third-party vandalism): "Unless the Landlord is negligent, Tenants are responsible for the costs of all damages/repairs to windows, doors, carpet, and walls, regardless of whether such damages is caused by residents, guests, or others." (*De Stefano* at p. 4). The Court concluded that such provision was unlawful because it was inconsistent with the landlord's unwaivable duty to "make all repairs and do whatever is necessary to put and keep the premises in a fit and habitable condition." (*Id.* at p. 41).

Further, the Court ruled that the landlord had unlawfully deducted from the rental deposit, certain fees pursuant to an automatic carpet cleaning fee provision within the lease, which provided as follows: "The carpets throughout the building are professionally cleaned each time apartments turn over occupancy. Tenants agree to a charge starting at \$95, not to exceed \$225, being deducted from the deposit for professional cleaning at the expiration of the lease agreement." (*Id.* at p. 5). Specifically, the Court reasoned that the landlord had unlawfully charged fees pursuant to such provision because a cleaning charge is lawful if, and only if, the landlord proves that such cleaning was necessary to restore the premises to the condition at the outset of the tenancy beyond ordinary wear and tear, and, further, the Court expressly noted that the "rental deposit is not designed to serve as an advance payment of amounts that will always be due under the lease," such as amounts due under an automatic carpet cleaning fee provision.

The Iowa Supreme Court set forth similar conclusions in the accompanying decision of *Lenora Caruso v. Apts. Downtown, Inc.* Therein, the Court confirmed, among other things, that "a landlord cannot shift the financial costs of repairs necessary to comply with its duty of fitness and habitability to the tenant." (*Caruso*, at p. 12).

In addition, in the *De Stefano* case, the tenant raised arguments surrounding her request to sublease the premises. In this regard, the Court held that, even when a landlord reserves in its lease agreement the right to pre-approve subleases, the landlord can only refuse a requested subleasing when such refusal is reasonable. Moreover, the Court concluded that in this specific situation, the landlord's refusal to allow the requested subleasing was unreasonable and, thus, unlawful because the basis for such refusal was the tenant's failure to abide by an otherwise unlawful lease provision.

Lastly, there were a few upsides to these two decisions for Iowa landlords. First, the Iowa Supreme Court, in *Caruso*, reversed the lower court's finding that the tenant was entitled to certain additional damages and attorney's fees for the landlord's "knowing" inclusion of unlawful provisions in its lease agreement, concluding that the tenant had not submitted sufficient proof of the landlord's actual knowledge and noting that "actual knowledge is a very high standard." (*Caruso*, at p. 15). Though, the Court went on to note that actual knowledge may be established through circumstantial evidence and made the following statements, which appear to be a word of warning to landlords:

We have now unambiguously held in *De Stefano* and in this case that such [unlawful repair and carpet cleaning] lease provisions violated Iowa Code section 562A.12(3). The existence of our precedent alone, however, will not prove actual knowledge of illegality in a future case, but it will be a circumstance to be considered by the fact finder making that determination. (*Caruso*, at pp. 13, 15)

Second, the Court in *De Stefano* held that a tenant is only allowed to recover punitive damages from the landlord for improper retention of deposit amounts when the landlord's actions were "dishonest," and not merely intentional or deliberate and, therefore, reversed the lower court's finding in this regard. (*De Stefano* at pp. 58, 63). Finally, the Court ruled upon a question regarding recovery of attorney's fees in small claims matters, which works to benefit both landlords and tenants who prevail in small claims matters. The Court held that the \$5,000 maximum recovery cap in small claims matters does not apply to attorney's fees, thereby meaning that a landlord (or a tenant) can recover from the other party up to \$5,000 in damages, plus its incurred reasonable attorney's fees, as awarded by the Court.

The clear implication for all Iowa landlords is that, in light of these precedential decisions, landlords must carefully review their leases and Rules and Regulations, remove any unlawful provisions, and otherwise ensure their leases and other documents contain no unlawful provisions. Please feel free to contact me if you have any questions.

## Questionable Provisions Included in Residential Leases: Landlords Must be on Alert After the Staley v. Barkalow Case - January 13, 2014

Jodie Clark McDougal

**Please be advised that this area of law has been affected by certain recent Iowa Supreme Court opinions. An update as to the current law in this area is available in Iowa Supreme Court Hands Down Decisions in Two Residential Landlord-Tenant Cases**

In May of 2013, the Iowa Court of Appeals entered a decision in the Staley v. Barkalow case, which involved a group of various tenants who affirmatively sued their landlord over the content of their lease agreements. It should be noted that while the Court was interpreting Iowa Code Chapter 562A, most attorneys believe the Court's holding is equally applicable to 562B and manufacturing housing communities.

In the case, the plaintiff, Brooke Staley, and other tenants filed a petition against their landlord, alleging that a large number of provisions within their leases were unlawful, i.e., violated the Iowa Code and sought damages. In short, the landlord argued that she had not enforced any of the allegedly unlawful provisions against the tenants, and thus, the tenants had not been harmed or damaged by such provisions. Conversely, the tenants argued that a landlord's (knowing) inclusion of unlawful provisions within a lease agreement does constitute "use" of such rental agreement under the statute and, therefore, a landlord has violated the law notwithstanding any lack of enforcement, thereby entitling the tenants to damages and payment of their attorney's fees.

The district court ruled in the landlord's favor, but on appeal, the decision was reversed by the Iowa Court of Appeals. The appellate court held as follows: "[w]e decide 'willfully uses', in Iowa Code section 562A.11(2) does not require 'willful enforcement', but encompasses a landlord's 'willful inclusion' of prohibited provisions." Accordingly, the Court concluded that the relevant sections of 562A, when read together "make a landlord liable for the [knowing] inclusion of prohibited provisions in a rental agreement, even without enforcement, if the landlord's inclusion was willful and knowing." Under the statute, a tenant may recover "actual damages sustained by the tenant and not more than three months' periodic rent and reasonable attorney fees."

The clear implication to all residential Iowa landlords is that they should carefully review their leases and Rules and Regulations to ensure they contain no unlawful provisions.