Asanuma v. Koo Soon Park, 11 ROP 53 (2004)

KAZUO ASANUMA and
HIROMI ASANUMA,
Appellants,

v.

KOO SOON PARK,
Appellee.

CIVIL APPEAL NO. 02-034
Civil Action No. 00-133

Supreme Court, Appellate Division
Republic of Palau

Argued: November 10, 2003
Decided: January 23, 2004
⊥54
Counsel for Appellants: Mark P. Doran

Counsel for Appellee: J. Roman Bedor, T.C.[1]

BEFORE: R. BARRIE MICHELSEN, Associate Justice; KATHLEEN M. SALII, Associate Justice; ROSE MARY SKEBONG, Associate Justice Pro Tem.

Appeal from the Supreme Court, Trial Division, the Honorable LARRY W. MILLER, Associate Justice, presiding.

MICHELSEN, Justice:

The question presented by this appeal is whether a landlord can invoke the "no illegal activities" clause in a lease to evict a tenant who is violating the Foreign Investment Act, 28 PNC § 101 *et seq.* (sometimes hereinafter, "the Act"). The Trial Division concluded that the tenant's activities did not violate the Act, and therefore did not reach this issue. Although we conclude that the tenant was in violation of the Act, we affirm the Trial Division's ultimate judgment in favor of the tenant, because a landlord cannot use a general "no illegal activities" clause in a lease to evict a tenant for non-compliance with foreign investment laws.

[1]Mr. Bedor appeared at oral argument and informed us that he had not been instructed to file a brief in this case, and he did not request permission from the Court to present oral argument pursuant to ROP R. App. Pro. 31 (c).

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BACKGROUND

In August 1999, Plaintiff-Appellee Koo Soon Park ["Park"] who is not a citizen of Palau, signed a 10-year lease for a parcel of land owned by Appellants Kazuo and Hiromi Asanuma ["the Asanumas"]. A $6000 payment was due upon execution of the lease and another $4000 was due on October 1. There was also due additional monthly rental payments, with step increases, over the term of the lease. Ten days later, Park struck a separate deal with one Franky Borja. Park planned to ship a prefabricated building from Korea to be constructed on the parcel. Borja was hired to build it. Park's payment for Borja's work was an assignment of a right to use the building for commercial purposes for six months, after which it would be Park's building for all purposes. The building was completed in May 2000, and a karaoke bar was opened as "the Blue Corner Lounge." The applicable licenses were in the name of Borja, (d/b/a High Profile Enterprises), but all equipment and furnishings in the building were bought and owned by Park. Park was also the general manager of the bar and was to be paid a "salary." The amount of the salary is not of record. Borja was to supply the liquor.

That same month, the Asanumas delivered a notice of default. The Asanumas considered the Park-Borja understanding as both a violation of the Foreign Investment Act and an unauthorized sublease. After some letter writing back and forth in May and June, with the Asanumas asserting the arrangement violated the lease and Park and his counsel insisting that the use was permissible and legal, the Asanumas put a chain on the front door and then nailed the back door shut. They later blocked the entrance to the building, and, according to Borja and Park, took $15,000 worth of electric equipment as well as ⊥55 significant amounts of personal property owned by the employees. The building also suffered damage.

In July, Park filed a complaint and a request for a temporary restraining order to prevent the Asanumas from interfering with the property. The Asanumas' answer asserted that Park was in violation of the lease, entitling them to a forceable eviction. Specifically, the Asanumas reiterated their position that, because Park did not posses a foreign investment approval certificate, the Park-Borja arrangement for operating the Blue Corner Lounge was in violation of the Act. As a consequence of this alleged foreign investment violation, the Asanumas claimed Park was in violation of Section 7(a) of the lease, which prohibits the use of the premises "for any illegal activities."[2] Furthermore, the Park-Borja transaction, they argued, was an unauthorized sublease in any event. Therefore, they argued they were entitled to evict both Park and Borja, keep the $10,000 initial rental payment as well as the additional $10,000 in monthly rents paid to date, assume possession and title of the newly constructed building, and also take all of Mr. Park's other property that happened to be on the premises of the time of the takeover.[3]

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[2]Section 7 of the lease reads:

> Tenant may use the premises for office space, residence, or for any other purposes as deemed appropriate by Tenant, provided that (a) Tenant shall not use the premises for any illegal activities, and (b) Tenant shall not use the premises in any manner that will constitute waste, nuisance, or unreasonable annoyance to owner or occupants of adjacent properties.

[3]In what appears to be a clear example of over-reaching on the part of the landlord, the lease provided that, upon eviction, the tenant would forfeit all personal property then on the premises to the landlord.

The Trial Division granted a temporary restraining order as requested by Park, finding that the agreement between Park and Borja constituted a license, which was permissible, and not a prohibited sublease. Secondly, the court found that Park's involvement in the Blue Corner Lounge did not violate foreign investment laws.

In the meantime, still attempting to recover his building expenses because of the business closure, Borja wrote Park to request an extension of their agreement. On December 1, Borja and Park signed a new agreement allowing Borja use of the building for the bar indefinitely until he earned enough money to cover the $30,000 billing owed by Park. The Asanumas objected to the second agreement as well, which then became part of the on-going litigation, although they did not formally make the agreement a separate basis for termination.

After trial, the Trial Division found the second agreement did not affect the result and held: "(1) that the lease was not validly terminated before the events giving rise to the complaint; (2) that, as a result, defendants are liable to plaintiff and the other claimants for damage caused by their wrongful use of self-help; and (3) that the lease remains in effect."

The Asanumas' appeal focuses solely ⊥56 on their assertion that the lease was properly and justifiably terminated because Park violated the Act. We review the trial court's legal conclusions *de novo*. *See Skebong v. EQPB*, 8 ROP Intrm. 80, 82 (1999); *Fanna Mun. Gov't v. Sonsorol State Gov't*, 8 ROP Intrm. 9 (1999).

ANALYSIS

The Asanumas claim two lease provisions gave them the right to terminate. As already noted, Section 7, which is entitled "Use of Premises," provides: "Tenant shall not use the premises for any illegal activities." Consistent with Section 7, Section 12, under the heading "Default by Tenant," states: "The occurrence of any of the following shall constitute a default by Tenant . . . (3) Violations of law." Therefore, to justify an eviction of Park as lessee, the Asanumas, as lessors, must prove that Park is in violation of the Act, and that a violation of the Act is the type of "illegal activity" or "[v]iolation[] of law" that allows a landlord to evict a tenant.

The Asanumas suggest that Park violated § 103 of the Act. Section 103(a) provides that "[n]o non-citizen shall carry on a business enterprise in the Republic, either directly or indirectly, without first obtaining a foreign investment approval certificate." "'Carrying on a business' means engaging in any kind of business enterprise, profession or trade, as an owner or part-owner, for the purpose, in whole or in part, of commercial gain or profit." 28 PNC § 102(d).

Under § 103(b), "[n]o non-citizen shall acquire any ownership interest or make any investment in an existing business enterprise in the Republic owned wholly by citizens until that business enterprise obtains a foreign investment approval certificate approving such acquisition."

See Section 12(b)(ii) (providing that the owner has right to "full possession and ownership of the premises and [can] take full possession and ownership of the premises, including all properties and items of tenant therein").

"Investment" is defined as "cash or the value of tangible assets subscribed or contributed to the equity capital or ownership interest in a business enterprise." 28 PNC § 102(j).

The trial court saw the "core question" as "whether there is a non-citizen who is truly reaping the benefits of ownership." The trial court held that the Park-Borja arrangement did not fall within the purview of the Act. We disagree, even though High Profile Enterprises (Borja's business) is listed on the licenses for the bar as the owner of Blue Corner Lounge, and, for now, Borja is assigned the revenue from the bar until he is compensated for construction of Park's building. Notwithstanding those facts, a closer examination is required because substance, not form, governs issues relating to the Act. *Micronesian Yachts Co. v. Palau Foreign Inv. Bd*., 7 ROP Intrm. 128, 129 (1998). *See generally Wenty v. ROP*, 8 ROP Intrm. 188, 189 (2000) ("Statutes should be interpreted so that the manifest purpose or object can be accomplished.").

Looking past the surface elements of the transaction, Park violated both § 103 (a) and § 103 (b). In addition to owning the building and being responsible for the costs of its construction, Park supplied the bar with all of the furniture and electronic equipment, without which there could not have been business. In addition, Park stood to profit from the bar's success, even though he assigned the initial revenue to Borja to finance building construction costs. If the business had done well, Park could have continued the arrangement with Borja or some other licensee by further assignment of revenue or profits in exchange for other consideration. And, of course, he immediately got the benefit of a "salary" as the bar's "general manager." In summary, a non-citizen cannot on the one hand, lease realty, contract for the ⊥57 construction of a building on that property, buy all of the fixtures and furniture for a business, assign its revenue for valuable consideration, and generally control the business as "general manager," yet on the other hand successfully assert his involvement was not an investment. Therefore, we find that Park's activities constitute a foreign investment under the Act.

Nonetheless, the fact that Park was violating the Act does not necessarily mean that the Asanumas had the right to terminate the lease. As noted by the trial court, "there is an initial question in the Court's mind as to whether the alleged Foreign Investment Act violation asserted by defendants, even if proven, fits within this lease language."

The Asanumas argue that the Restatement (Second) of Property, specifically § 12.5, applies to these facts. The Section provides in pertinent part:

> If the tenant uses the leased property for a purpose that is illegal and the landlord is not a party to that illegal use, the landlord may:
>
> (1) terminate the lease, if he does so while the use is continuing, or if he does so within a reasonable time after the use is stopped by public authorities, and recover damages; or
>
> (2) hold the tenant to the lease and obtain appropriate equitable and legal relief including recovery of damages.

Restatement (Second) of Prop.: Landlord & Tenant § 12.5 (1977).

Comment (b) explains that lease provisions prohibiting "illegal activities" are intended to put the landlord "in the position to resist such conduct on his leased property to protect its reputation." *Id*. cmt. b. Several United States courts have construed the rule to mean that a landlord cannot terminate a lease because of an illegal act that does not affect the property or its reputation. For example, in *Deutsch v. Phillips Petroleum*, 56 Cal. App. 3d 586 (1976), the Court found that a landlord could not terminate a lease pursuant to a generic provision prohibiting illegal activities because the tenant allegedly violated the Sherman Antitrust Act. *See also Rowe v. Wells Fargo Realty, Inc.,* 166 Cal. App. 3d 310 (1985) (holding that lessee's alleged violation of Department of Energy regulations did not trigger termination provision); *Sherwood Med. Indus. v. Bldg. Leasing Corp.*, 527 S.W.2d 407 (Mo. App. 1975) (finding that attempt to alter leased property without a valid city permit does not trigger termination provision).

The common thread seen in such cases is that the alleged illegal activity did not affect the subsequent economic value of the landlord's property. This factor seems to be underlying the statutory provisions of many states that list specific illegal activities that justify termination of a lease. *See, e.g.*, Ill. Ann. Stat. ch. 100 § 10 (mandating that landlord has option to terminate lease if premises are used for prostitution, assignation, or lewdness); Kan. Stat. Ann. § 41-805 (1973) (providing that lease is automatically terminated and landlord has right to immediate entry if premises used to unlawfully manufacture, possess, or sell intoxicating liquor); Mass. Gen. Laws Ann. ch. 139, § 19 (1974) (giving landlord option to terminate lease if premises are used for ⊥58 prostitution, illegal gaming, or illegal possession or sale of intoxicating liquor); Or. Rev. Stat. § 91.410(3) (discussing gambling). In this case, it was not the activity that was illegal. It was Park's involvement that was illegal. His violation of the Act is personal to him and does not stigmatize the Asanumas' property so as to lessen its value to future tenants or buyers. Hence, any violations of the Act by Park did not trigger the termination provisions in Sections 7 and 12 of the lease.[4]

Finally, the Asanumas alternatively assert that the lease should have been considered terminated because of untimely payment of rent for the months of August, September, and October 2000. Given the uproar and confusion created by the Asanuma's initial efforts at self-help, and their subsequent refusal to initially accept the August payment when it was tendered, and considering Park's resumption of payments after the hearings that clarified matters in September and October, we agree with the trial court that "[t]he fair result is to declare that the lease was not terminated but also to declare that defendants did not waive their right to payment for those three months and to apply the amounts due as an offset against the amounts due plaintiff."

CONCLUSION

[4]This ruling should not be read to suggest that a landlord could never terminate a lease for violations of the Act or other technically illegal activities. A landlord is free to include provisions prohibiting any disapproved uses. Our analysis here applies only to the general "illegal activities" clause which, as the Restatement shows, has a specific and limited reach.

For the foregoing reasons, we affirm the judgment of the Trial Division.