REVISION OF UNIFORM COMMERCIAL CODE
ARTICLE 2A – LEASES

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ON UNIFORM STATE LAWS

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REVISION OF UNIFORM COMMERCIAL CODE
ARTICLE 2A – LEASES
WITH PREFATORY NOTE AND COMMENTS

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# REVISION OF UNIFORM COMMERCIAL CODE ARTICLE 2A – LEASES

## TABLE OF CONTENTS

### PART 1. GENERAL PROVISIONS

<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>2A-101</td>
<td>SHORT TITLE</td>
<td>8</td>
</tr>
<tr>
<td>2A-102</td>
<td>DEFINITIONS AND INDEX OF DEFINITIONS</td>
<td>8</td>
</tr>
<tr>
<td>2A-104</td>
<td>TRANSACTIONS SUBJECT TO OTHER LAW</td>
<td>20</td>
</tr>
<tr>
<td>2A-105</td>
<td>TERRITORIAL APPLICATION OF ARTICLE TO GOODS COVERED BY CERTIFICATE OF TITLE</td>
<td>22</td>
</tr>
<tr>
<td>2A-106</td>
<td>LIMITATION ON POWER OF PARTIES TO CONSUMER LEASE TO CHOOSE APPLICABLE LAW [OR JUDICIAL FORUM] (CHOICE OF FORUM)</td>
<td>23</td>
</tr>
<tr>
<td>2A-107</td>
<td>UNCONSCIONABILITY</td>
<td>24</td>
</tr>
<tr>
<td>2A-108</td>
<td>OPTION TO ACCELERATE AT WILL</td>
<td>25</td>
</tr>
<tr>
<td>2A-109</td>
<td>EFFECT OF AGREEMENT</td>
<td>26</td>
</tr>
</tbody>
</table>

### PART 2. FORMATION, TERMS, AND READJUSTMENT OF LEASE CONTRACT

<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>2A-201</td>
<td>FORMAL REQUIREMENTS</td>
<td>27</td>
</tr>
<tr>
<td>2A-201</td>
<td>FORMAL REQUIREMENTS; STATUTE OF FRAUDS</td>
<td>29</td>
</tr>
<tr>
<td>2A-202</td>
<td>PAROL OR EXTRINSIC EVIDENCE</td>
<td>31</td>
</tr>
<tr>
<td>2A-203</td>
<td>FORMATION IN GENERAL</td>
<td>32</td>
</tr>
<tr>
<td>2A-204</td>
<td>FIRM OFFERS: SEALED INSTRUMENTS</td>
<td>32</td>
</tr>
<tr>
<td>2A-205</td>
<td>OFFER AND ACCEPTANCE</td>
<td>33</td>
</tr>
<tr>
<td>2A-206</td>
<td>CONSUMER CONTRACTS, RECORDS</td>
<td>34</td>
</tr>
<tr>
<td>2A-207</td>
<td>ATTRIBUTION PROCEDURE</td>
<td>35</td>
</tr>
<tr>
<td>2A-208</td>
<td>ATTRIBUTION OF ELECTRONIC RECORD, MESSAGE, OR PERFORMANCE</td>
<td>36</td>
</tr>
<tr>
<td>2A-209</td>
<td>AUTHENTICATION EFFECT AND PROOF; ELECTRONIC AGENT AUTHENTICATION</td>
<td>38</td>
</tr>
<tr>
<td>2A-210</td>
<td>PROOF OF AUTHENTICATION</td>
<td>39</td>
</tr>
<tr>
<td>2A-211</td>
<td>ELECTRONIC TRANSACTIONS AND MESSAGES: TIMING OF CONTRACT AND EFFECTIVENESS OF MESSAGE</td>
<td>39</td>
</tr>
<tr>
<td>2A-212</td>
<td>ACKNOWLEDGMENT OF ELECTRONIC MESSAGE</td>
<td>40</td>
</tr>
</tbody>
</table>

### PART 3. CONSTRUCTION OF LEASE CONTRACT

<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>2A-301</td>
<td>COURSE OF PERFORMANCE OR PRACTICAL CONSTRUCTION</td>
<td>42</td>
</tr>
<tr>
<td>2A-302</td>
<td>MODIFICATION, RESCISSION, AND WAIVER</td>
<td>43</td>
</tr>
<tr>
<td>2A-303</td>
<td>CONTINUING CONTRACTUAL TERMS</td>
<td>44</td>
</tr>
<tr>
<td>2A-304</td>
<td>LESSEE UNDER FINANCE LEASE AS BENEFICIARY OF SUPPLY CONTRACT</td>
<td>45</td>
</tr>
<tr>
<td>2A-305</td>
<td>ELECTRONIC VIRUSES</td>
<td>46</td>
</tr>
<tr>
<td>2A-306</td>
<td>ELECTRONIC REGULATION OF PERFORMANCE</td>
<td>48</td>
</tr>
<tr>
<td>2A-307</td>
<td>IDENTIFICATION</td>
<td>49</td>
</tr>
<tr>
<td>2A-308</td>
<td>INSURANCE AND PROCEEDS</td>
<td>50</td>
</tr>
<tr>
<td>2A-309</td>
<td>RISK OF LOSS</td>
<td>50</td>
</tr>
<tr>
<td>2A-310</td>
<td>CASUALTY TO IDENTIFIED GOODS</td>
<td>52</td>
</tr>
<tr>
<td>2A-311</td>
<td>TERMINATION; SURVIVAL OF OBLIGATIONS</td>
<td>54</td>
</tr>
</tbody>
</table>

### PART 4. EFFECT OF LEASE CONTRACT

<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>2A-401</td>
<td>ENFORCEABILITY OF LEASE CONTRACT</td>
<td>56</td>
</tr>
<tr>
<td>2A-402</td>
<td>TITLE TO AND POSSESSION OF GOODS</td>
<td>56</td>
</tr>
<tr>
<td>2A-403</td>
<td>ALIENABILITY OF PARTY’S INTEREST UNDER LEASE CONTRACT OR OF LESSOR’S RESIDUAL INTEREST IN GOODS; DELEGATION OF PERFORMANCE; TRANSFER OF RIGHTS</td>
<td>56</td>
</tr>
<tr>
<td>2A-404</td>
<td>SUBSEQUENT LEASE OF GOODS BY LESSOR</td>
<td>59</td>
</tr>
<tr>
<td>2A-405</td>
<td>SALE OR SUBLEASE OF GOODS BY LESSEE</td>
<td>61</td>
</tr>
<tr>
<td>2A-406</td>
<td>PRIORITY OF CERTAIN LIENS ARISING BY OPERATION OF LAW</td>
<td>62</td>
</tr>
<tr>
<td>2A-407</td>
<td>PRIORITY OF LIENS ARISING BY ATTACHMENT OR LEVY ON, SECURITY INTERESTS IN, AND OTHER CLAIMS TO GOODS</td>
<td>63</td>
</tr>
<tr>
<td>Section</td>
<td>Title</td>
<td>Page</td>
</tr>
<tr>
<td>---------</td>
<td>--------------------------------------------</td>
<td>------</td>
</tr>
<tr>
<td>2A-408.</td>
<td>SPECIAL RIGHTS OF CREDITORS</td>
<td>64</td>
</tr>
<tr>
<td>2A-409.</td>
<td>RIGHTS OF LESSOR AND LESSEE WHEN GOODS BECOME FIXTURES</td>
<td>65</td>
</tr>
<tr>
<td>2A-410.</td>
<td>LESSOR'S AND LESSEE'S RIGHTS WHEN GOODS BECOME ACCESSIONS</td>
<td>69</td>
</tr>
<tr>
<td>2A-411.</td>
<td>PRIORITY SUBJECT TO SUBORDINATION</td>
<td>71</td>
</tr>
<tr>
<td></td>
<td><strong>PART 5. WARRANTIES</strong></td>
<td></td>
</tr>
<tr>
<td>2A-501.</td>
<td>DEFINITIONS</td>
<td>72</td>
</tr>
<tr>
<td>2A-502.</td>
<td>WARRANTY AGAINST INTERFERENCE AND AGAINST INFRINGEMENT; LESSEE'S OBLIGATION AGAINST INFRINGEMENT</td>
<td>73</td>
</tr>
<tr>
<td>2A-503.</td>
<td>EXPRESS WARRANTIES TO IMMEDIATE LESSEE</td>
<td>75</td>
</tr>
<tr>
<td>2A-504.</td>
<td>IMPLIED WARRANTY OF MERCHANTABILITY; USAGE OF TRADE</td>
<td>76</td>
</tr>
<tr>
<td>2A-505.</td>
<td>IMPLIED WARRANTY OF FITNESS FOR PARTICULAR PURPOSE</td>
<td>77</td>
</tr>
<tr>
<td>2A-506.</td>
<td>DISCLAIMER OR MODIFICATION OF WARRANTY</td>
<td>77</td>
</tr>
<tr>
<td>2A-507.</td>
<td>CUMULATION AND CONFLICT OF WARRANTIES</td>
<td>79</td>
</tr>
<tr>
<td>2A-508.</td>
<td>EXTENSION OF EXPRESS OR IMPLIED WARRANTY</td>
<td>80</td>
</tr>
<tr>
<td></td>
<td><strong>PART 6. PERFORMANCE OF LEASE CONTRACT:</strong> REPUDIATED, SUBSTITUTED, AND EXCUSED</td>
<td></td>
</tr>
<tr>
<td>2A-601.</td>
<td>RIGHT TO ADEQUATE ASSURANCE OF PERFORMANCE</td>
<td>82</td>
</tr>
<tr>
<td>2A-602.</td>
<td>ANTICIPATORY REPUDIATION</td>
<td>83</td>
</tr>
<tr>
<td>2A-603.</td>
<td>RETRACTION OF ANTICIPATORY REPUDIATION</td>
<td>84</td>
</tr>
<tr>
<td>2A-604.</td>
<td>SUBSTITUTED PERFORMANCE</td>
<td>84</td>
</tr>
<tr>
<td>2A-605.</td>
<td>EXCUSE BY FAILURE OF PRESUPPOSED CONDITIONS</td>
<td>85</td>
</tr>
<tr>
<td>2A-606.</td>
<td>PROCEDURE ON NOTIFICATION CLAIMING EXCUSE</td>
<td>86</td>
</tr>
<tr>
<td>2A-607.</td>
<td>IRREVOCABLE PROMISES: FINANCE LEASES</td>
<td>87</td>
</tr>
<tr>
<td></td>
<td><strong>PART 7. DEFAULT</strong></td>
<td></td>
</tr>
<tr>
<td>A. GENERAL</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2A-701.</td>
<td>SUBJECT TO GENERAL LIMITATIONS</td>
<td>88</td>
</tr>
<tr>
<td>2A-702.</td>
<td>DEFAULT: PROCEDURE</td>
<td>88</td>
</tr>
<tr>
<td>2A-703.</td>
<td>WAIVER OF DEFAULT; PARTICULARIZATION OF NONCONFORMITY</td>
<td>90</td>
</tr>
<tr>
<td>2A-704.</td>
<td>NOTICE AFTER DEFAULT</td>
<td>91</td>
</tr>
<tr>
<td>2A-705.</td>
<td>REMEDIES IN GENERAL</td>
<td>92</td>
</tr>
<tr>
<td>2A-706.</td>
<td>MEASUREMENT OF DAMAGES IN GENERAL</td>
<td>92</td>
</tr>
<tr>
<td>2A-707.</td>
<td>INCIDENTAL DAMAGES</td>
<td>93</td>
</tr>
<tr>
<td>2A-708.</td>
<td>CONSEQUENTIAL DAMAGES</td>
<td>93</td>
</tr>
<tr>
<td>2A-709.</td>
<td>SPECIFIC PERFORMANCE</td>
<td>94</td>
</tr>
<tr>
<td>2A-710.</td>
<td>CANCELLATION; EFFECT</td>
<td>95</td>
</tr>
<tr>
<td>2A-711.</td>
<td>LIQUIDATION OF DAMAGES; DEPOSITS</td>
<td>97</td>
</tr>
<tr>
<td>2A-713.</td>
<td>REMEDIES FOR MISREPRESENTATION OR FRAUD</td>
<td>101</td>
</tr>
<tr>
<td>2A-714.</td>
<td>PROOF OF MARKET RENT</td>
<td>101</td>
</tr>
<tr>
<td>2A-715.</td>
<td>LIABILITY OF THIRD PARTIES FOR INJURY TO GOODS</td>
<td>102</td>
</tr>
<tr>
<td>2A-716.</td>
<td>STATUTE OF LIMITATIONS</td>
<td>103</td>
</tr>
<tr>
<td>B. LESSOR'S REMEDIES</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2A-717.</td>
<td>LESSOR'S REMEDIES IN GENERAL</td>
<td>104</td>
</tr>
<tr>
<td>2A-718.</td>
<td>LESSOR'S RIGHT TO POSSESSION OF GOODS</td>
<td>106</td>
</tr>
<tr>
<td>2A-719.</td>
<td>LESSOR'S RIGHT TO IDENTIFY GOODS TO LEASE CONTRACT DESPITE DEFAULT OR TO SALVAGE UNFINISHED GOODS</td>
<td>107</td>
</tr>
<tr>
<td>2A-720.</td>
<td>LESSOR'S REFUSAL TO DELIVER BECAUSE OF LESSEE'S INSOLVENCY; STOPPAGE IN TRANSIT OR OTHERWISE</td>
<td>108</td>
</tr>
<tr>
<td>2A-721.</td>
<td>LESSOR'S RIGHTS TO DISPOSE OF GOODS</td>
<td>109</td>
</tr>
<tr>
<td>2A-722.</td>
<td>LESSOR'S DAMAGES FOR NONACCEPTANCE, FAILURE TO PAY, OR REPUDIATION</td>
<td>111</td>
</tr>
<tr>
<td>2A-723.</td>
<td>LESSOR'S ACTION FOR THE RENT</td>
<td>113</td>
</tr>
<tr>
<td>2A-724.</td>
<td>LESSOR'S RIGHTS TO RESIDUAL INTEREST</td>
<td>115</td>
</tr>
</tbody>
</table>
C. LESSEE'S REMEDIES

SECTION 2A-725. LESSEE'S REMEDIES IN GENERAL; LESSEE'S SECURITY INTEREST IN REJECTED GOODS ........................................ 115
SECTION 2A-726. LESSEE'S RIGHTS ON NONCONFORMING DELIVERY; RIGHTFUL REJECTION ...................................................... 117
SECTION 2A-727. INSTALLMENT LEASE CONTRACT: DEFAULT ........................... 119
SECTION 2A-728. MERCHANT LESSEE'S DUTIES; LESSEE'S OPTIONS AS TO SALVAGE ......................................................... 119
SECTION 2A-729. LESSEE'S DUTIES AS TO RIGHTFULLY REJECTED GOODS ............. 120
SECTION 2A-730. CURE ........................................................................ 121
SECTION 2A-731. ACCEPTANCE OF GOODS ............................................. 122
SECTION 2A-732. EFFECT OF ACCEPTANCE OF GOODS; NOTICE OF DEFAULT; BURDEN OF ESTABLISHING DEFAULT AFTER ACCEPTANCE; NOTICE OF CLAIM OR LITIGATION TO PERSON ANSWERABLE OVER ........................................................................ 123
SECTION 2A-733. REVOCATION OF ACCEPTANCE OF GOODS ....................... 125
SECTION 2A-734. COVER; LESSEE'S ACQUISITION OF SUBSTITUTE GOODS ........ 126
SECTION 2A-735. LESSEE'S DAMAGES FOR NON-DELIVERY, REPUDIATION, DEFAULT, AND BREACH OF WARRANTY IN REGARD TO ACCEPTED GOODS ......................................................... 127
SECTION 2A-736. LESSEE'S DAMAGES FOR DEFAULT REGARDING ACCEPTED GOODS ...................................................................... 129
SECTION 2A-737. PREPAYING LESSEE'S RIGHT TO GOODS ............................ 130
Article 2A is being revised to take account of the amendments to Articles 2 and 9 (primarily Article 2) and the promulgation of Article 2B. Article 2A is based largely on Article 2 and in general follows the Article 2 sequence of sections. However, many present Article 2 sections were not adopted in Article 2A because the Article 2 sections dealt with issues which were not significant in the leasing context or stated rules which were inappropriate in leases. Other Article 2 sections were followed exactly or very closely in the analogous Article 2A section. Some Article 2A sections follow the policy of present Article 2, but the specific rules are different because of the differences between sales and leases. Article 2A also contains a few provisions, such as the sections on lessors of fixtures or accessions, which are based on the similar provisions of Article 9.

The revision of Article 2 and the prospective promulgation of Article 2B raise the issue of the extent to which Article 2A should be revised to follow changes in policy or language in Article 2 or to adopt rules similar to some of those in new Article 2B. The Article 2A Drafting Committee was appointed to examine that question. The charge to the Committee is to review Article 2 changes to sections used as the basis for Article 2A sections and adopt those Article 2 changes in Article 2A unless differences between leases and sales justify a different rule for leases. Similarly new sections in Article 2 and the provisions of new Article 2B are being reviewed for possible addition to Article 2A. Also, changes made by the Article 9 Committee are being considered for possible adoption in the relevant Article 2A sections. The Article 2A Committee charge is not to second-guess the Article 2 Committee nor to decline to accept Article 2 changes in Article 2A merely because the Article 2A Committee disagrees with the Article 2 Committee decision.

The Article 2A Committee does not have authority to make substantive changes to Article 2A which are not related to changes in Articles 2 or 9 or to provisions of new Article 2B. If the Article 2A Drafting Committee discovers a need for substantive change in Article 2A not related to other articles, it must seek authorization from the Scope and Program and Executive Committees to make those changes.

The Article 2A Committee has met three times, the last time in February of this year. At each meeting the Article 2A Committee has reviewed the draft of revised Article 2 current at that time. A planned late May meeting of the Article 2A Committee was cancelled to await a more final version of revised Article 2, therefore the Article 2A Committee has not reviewed changes made since January of this year in the Article 2 draft. However, the Article 2A draft submitted to the Conference is based on the Article 2 draft, including changes made after last January, which is also being presented to the Conference this summer. Therefore, we are in the unusual position of presenting to the Conference a draft of Article 2A which contains many language changes and some new sections that have not been reviewed by the Drafting Committee.
However, many of the changes in revised Article 2 as it appears now were made by the time of the January, 1997, draft. The Article 2A Committee has considered those changes and concluded that a number of them should not be followed in Article 2A because of differences between leases and sales. The Committee has also identified one area of possible substantive changed unrelated to revisions in other articles.

As noted above, the instruction to the Article 2A Drafting Committee is to conform Article 2A to revised Article 2 unless there is a reason for a different rule in leases because of differences between sales and leases, including differences in relevant practice. Therefore, adoption of a revised Article 2 section in Article 2A doesn’t necessarily indicate that the Article 2A Committee believes that the provision is desirable in leases or in sales. It may mean merely that the Article 2A Committee cannot see a reason for a different rule in leases than in sales. In one case the Article 2A Committee has rejected a revision in Article 2 where it may be difficult to argue that there is a reason for a different rule in lease transactions.

A discussion follows of (1) matters on which Article 2A has failed to follow revised Article 2 and (2) the one substantive amendment to Article 2A that the Article 2A Committee is considering that is not related to changes in other articles.

As a preliminary matter, it should be noted that draft revised Article 2A looks very different than present Article 2A. Language in almost every section, following similar changes in Article 2, has been changed, and the sections have been rearranged. Many of the language changes are not intended to be substantive. The new language usually merely tries to clarify the meaning of present sections or conform to the current style rules of the Conference. The section reordering is a result of the addition of a number of new sections from Articles 2B and 2 and reorganization, particularly, in the remedies parts of the Act.

A. Special rule for determining whether terms in a record are binding on consumers (no Article 2A section)

Section 2-206 of revised Article 2 provides that in a consumer transaction, “any non-negotiated term [in a record] that a reasonable consumer in a transaction of this type would not reasonably expect to be in the record is excluded from the contract, unless the consumer had knowledge of the term before agreeing to the record.

Lessors, particularly of automobiles for short terms, have strongly objected to incorporating such a provision in Article 2A. The Article 2A Committee has previously expressed opposition to earlier similar Article 2 provisions. There is some likelihood that the Article 2A Committee will be inclined to reject Section 2-206 for Article 2A. The issue is, as noted, particularly acute in short term auto rentals. In such cases, the renter is usually in a hurry, other people are standing in line, and the renter often doesn’t want to take time to read or indicate awareness of particular provisions of the contract. But, when, for example, an unexpected accident occurs and the lessor asserts that the renter has thousands of dollars of liability, the renter deny liability on the ground that a reasonable consumer would not have expected to incur such a large liability. What is the appropriate policy regarding the binding effect of unknown terms in a form contract in such a
situation? Should a distinction be drawn between short term leases and leases for longer terms? Can a distinction between leases and sales be justified?

B. The battle of the forms (no Article 2A section)

Present Article 2A does not contain a section analogous to present Section 2-207. That section deals with formation of contract through the exchange of forms, typically a purchase order and an acknowledgment. The provision was omitted from Article 2A because leasing contracts are seldom, if ever, made through such an exchange of forms. The typical leasing pattern is the execution of a single writing (now “record”) by both parties.

The Article 2 Drafting Committee has tried a number of different approaches to the battle of forms problem in revised Article 2. The present provisions in the revision are Sections 2-203(d), 2-205(a)(1), and 2-207. Under Sections 2-203(d) and 2-205(a)(1), a definite expression of acceptance in a record is an acceptance even though the record contains terms different from those of the offer, unless the record of one of the parties conspicuously states that the party intends contract only if the other party agrees to all terms in that record. Section 2-207 then states rules for determining the terms of a contract created by an exchange of forms which contain differing terms.

The Article 2A Committee has decided to adhere to the original Article 2A decision and not include “battle of the forms provisions in Article 2A.

C. Statute of frauds (Section 2A-201)

Present Article 2A has a statute of frauds provision modeled closely on the present Article 2 statute of frauds. Until early this year, the Article 2 Drafting Committee proposed repeal of the statute of frauds. The Article 2A Committee had rejected repeal of the statute in Article 2A. The Committee received strong representations from lessor representatives that the present Article 2A statute of frauds should be preserved. Now that Article 2 has adopted a statute of frauds very similar to the present Article 2 statute, the Article 2A Committee must decide whether to conform Section 2A-201 to the revised Article 2 provision or retain the present Article 2A version. There are two major differences between the revised Article 2 draft and present Article 2A. First, Article 2A requires a writing if the lease price is $1,000 or more while revised Article 2 sets the threshold at $10,000. Second, revised Article 2 includes a statutory estoppel provision which adopts the holdings of some courts that a party’s conduct may estop it from asserting the statute of frauds as a defense.

The Article 2A Committee’s decision to reject repeal of the statute of frauds was strongly influenced by a memorandum prepared by Edwin Huddleson, III on behalf of the Equipment Leasing Association of America. Mr. Huddleson spoke for 26 lawyers who represent companies engaged in leasing activity. Following is a brief reprise of those arguments which persuaded the Drafting Committee to retain the statute of frauds. The arguments may be relevant to whether the present Article 2 version of the statute of frauds should be included in Article 2A.

The typical leasing transaction is more complex than the typical sale. Most commercially important leases create a long term continuing relationship between
the parties which often involves multiple duties on each side. Therefore, it is more
important than in a sales transaction that the terms of the agreement be in writing.
In fact, even small value leases are essentially always represented by a single
written contract signed by both parties.

Retaining the statute of frauds creates some additional incentive for parties
to get the deal in writing. And this is a good thing. Deleting the statute might lead
to an undesirable casualness in making leasing deals. On the other hand, since
leases are essentially always put in writing today, retaining the statute of frauds will
not interfere with any significant practice of entering into oral leases. Therefore, a
statute of frauds for leasing transactions, in any event, does less harm through
allowing welshers to defeat deals actually made than may be true in sales.

D. Extension of express warranties to remote lessees (no Article 2A
section)

Section 2-408 of the Article 2 draft gives remote buyers and lessees rights
against sellers who make promises or representations in advertising or in materials
distributed with products. The Article 2A Committee has decided not to include a
similar provision in Article 2A because we know of no instances in which lessors
advertise or make representations in material to be delivered to remote lessees.
Industry advisors have argued that Article 2A should not contain a warranty
provision which deals with a situation which does not exist in the industry. (The
Article 2 provision itself extends seller advertised, or with-the-goods, warranties to
remote lessees.) It should be noted that revised Section 2A-508 does extend lessor
warranties, made to an immediate lessee, to transferees who may be expected to use
or be affected by the goods.)

E. Contractual modification of remedy (Section 2A-712)

Article 2A adopted unchanged Section 2-719 of present Article 2. The
Article 2 Drafting Committee has changed that section (now Section 2-810) in two
substantive ways. First the revised section states that an agreed remedy “may not
be applied to deprive the aggrieved party of a minimum adequate remedy”. Second,
it makes limitations on consequential damages unenforceable in consumer contracts
if the “agreed remedy fails to substantially achieve the intended purposes of the
parties. The Article 2A Committee rejected these changes to the section.

On the first point, the revised Article 2 section retains the present rule that
an agreed remedy is not effective if the agreed remedy fails to achieve its purpose.
(The revised language is that the agreed remedy is ineffective if it “fails
substantially to achieve the intended purpose of the parties.) The section also adds
a second statutory limitation on the effectiveness of an agreed remedy; it must not
“deprive the aggrieved party of a minimum adequate remedy under the
circumstances. In present Article 2, there is a reference to “adequate minimum
remedy in the Comments to Section 2-719 which explains the intent of the “failure
of essential purpose” test. The Article 2A Committee rejected the incorporation of
the adequate minimum remedy language in the statute because it creates uncertainty
as to the relationship between the two stated tests and suggests increased
restrictions on the effectiveness of agreed remedies.
On the second point, the Article 2A Committee does not believe that the failure of a repair or replacement warranty, for example, should automatically invalidate a disclaimer of liability for consequential damages, even in a consumer transaction. Most cases under present Article 2 hold that a limitation on consequential damages may be effective even if the seller is unable to provide the agreed limited remedy. (The usual agreed remedy is a repair or replacement promise. Therefore, the issue is whether, if the lessor is unable to repair or replace, a consumer lessee is, in all cases, entitled to recover consequential damages even though the contract also separately excludes liability for consequential damages.

It is fair to say that it is difficult to argue for a difference between sales and leases on these points, but perhaps the argument can be successfully made.

F. Unconscionability and consumers (Section 2A-107 (continues existing variation)

Present Article 2A expanded the unconscionability provisions of Article 2 in three ways as to consumer lessees. First, Article 2A gives a court power to grant “appropriate relief” if it finds unconscionable conduct in the collection of a claim arising from a lease contract. Second, courts are given power to grant relief if agreement to the lease contract or to a term thereof was induced by unconscionable conduct. Third, attorney’s fees are given to consumers who prevail on an unconscionability claim (and attorney’s fees are given to the other party if the court finds that the consumer lessee knew an asserted unconscionability claim to be groundless).

The Article 2 Drafting Committee chose to adopt the unconscionable inducement concept and apply it to all sales, not just sales to consumers, but did not adopt the other Article 2A expansions of unconscionability protections in consumer transactions. The Article 2A Committee voted to retain the present Article 2A unconscionability provisions which give greater protection to consumers than does the Article 2 provision. The Article 2A Committee also decided not to extend the unconscionable inducement concept to business transactions.

G. Limitation on choice of law and choice of forum in consumer transactions (Section 2A-107) (continues existing variation)

Present Article 2A restricts the power of the parties to a consumer lease to chose the applicable law or applicable forum. The law chosen must be that of jurisdiction in which the lessee resides or the jurisdiction in which the goods will be used. A choice of forum is effective only if that jurisdiction would otherwise have jurisdiction over the lessee. Present Article 2 has no such provisions and the Article 2 Drafting Committee has chosen not to adopt similar provisions in Article 2. The Article 2A Committee, adopting the principle that it would not reduce consumer protections in present Article 2A, has voted to retain those provisions.

H. Statute of limitations, accrual of cause of action (Section 2A-708) (continues existing variation)

In present Article 2 a cause of action accrues when the breach occurs whether or not the other party knows of the breach, and breach of warranty occurs when goods are delivered unless the warranty expressly extends to future
The original Article 2A Drafting Committee rejected the time-of-breach rule and instead adopted the rule that the time the other party learned, or should have learned, of the breach is the time of the accrual of the cause of action. (Article 2A adopted the Article 2 four year period for bringing action after accrual of the cause of action.) The Article 2 revision has slightly modified the original statute by extending the statute for an additional year, to five years maximum, if the aggrieved party does not discover the breach until after it has occurred.

The Article 2A Committee decided to adhere to the present Article 2A position as to time of accrual of the cause of action. The Committee believes that generally the time the injured party learned, or should have learned, of the breach is a fairer rule and works even handedly between lessors and lessees. In sales, using the time the injured party learned, or should have learned, of the breach would create the possibility of a warranty claim against a seller ten or twenty or more years after the sale and long after the seller had any contact with the buyer or the goods. In leases that problem for lessors exists only to a small degree, if at all. In any event, the lessor business community is willing to accept that small additional risk in order to also gain the advantage of not having the statute of limitations run against lessors until the lessor discovers or should have discovered the breach.

I. Proposed amendment of Article 2A title warranties not related to changes in Article 2 (Section 2A-502)

Under present Section 2A-211 non-finance lessors warrant only “that no person holds a claim to or interest in the goods “that arose from an act or omission of the lessor” that will interfere with the leasehold estate. Finance lessors make no warranty of quiet enjoyment at all. The Article 2A Committee proposes to modify those warranties so that a non-finance lessor makes a general warranty of quite enjoyment (which protects against title defects even though not caused by an act or omission of the lessor) and a finance lessor warranties against its own acts which cause interference with the leasehold interest. The warranty also covers unfounded but colorable claims which interfere with the leasehold interest.
REVISION OF UNIFORM COMMERCIAL CODE
ARTICLE 2A – LEASES

PART 1
GENERAL PROVISIONS

SECTION 2A-101. SHORT TITLE. This article may be cited as Uniform
Commercial Code – Leases.

SECTION 2A-102. DEFINITIONS AND INDEX OF DEFINITIONS.
(a) Unless the context otherwise requires, in this article
(1) “Authenticate” means to sign or to execute or adopt a symbol, or
encrypt a record in whole or part, with present intent to identify the authenticating
party or to adopt, or accept a record or term, or to establish the authenticity of a
record or term that contains the authentication or to which a record containing the
authentication refers.
(2) “Buyer in ordinary course of business” means a person that buys
goods in good faith, without knowledge that the sale to violates the rights of
another person in the goods, and in the ordinary course from a person, other than a
pawnbroker, in the business of selling goods of that kind. A person buys in the
ordinary course if the sale to the person comports with the usual or customary
practices in the kind of business in which the seller is engaged or with the seller’s
own usual or customary practices. A person that sells minerals or the like,
including oil and gas, at the wellhead or minehead is a person in the business of
selling goods of that kind. A buyer in the ordinary course of business may buy for
cash, by exchange of other property, or on secured or unsecured credit, and may
acquire goods or documents of title under a pre-existing contract for sale. Only a
buyer that takes possession of the goods or has a right to recover the goods from the
seller (Section 2-807, 2-822, or 2-824) may be a buyer in ordinary course of
business. A person that acquires goods in a transfer in bulk or in total or partial or
total satisfaction of a money debt is not a buyer in ordinary course of business.

(3) “Cancellation” means an act by either party which ends a lease
contract because of a default by the other party. “Cancel” has a corresponding
meaning.

(4) “Commercial unit” means a unit of goods which by commercial
usage is a single whole for purposes of lease and whose division materially impairs
its character or value in the relevant market or in use. A commercial unit may be a
single article, such as a machine; a set of articles, such as a suite of furniture or a
line of machinery; a quantity, such as a gross or carload; or any other unit treated in
use or in the relevant market as a single whole.

(5) “Conspicuous” means so displayed or presented that a reasonable
person against whom it operates ought to have noticed it or, in the case of an
electronic message intended to evoke a response without the need for review by an
individual, in a form that would enable a reasonably configured electronic agent to
take it into account or react to it without the review of the message by an
individual. A term is conspicuous if it is:

(A) a heading in capitals (e.g., NON-NEGOTIABLE BILL OF
LADING) equal or greater in size to the surrounding text;

(B) language in the body or text of a record or display in larger or
other contrasting type or color than other language;

(C) a term prominently referenced in the body or text of an
electronic record or display that can be readily accessed from the record or display
(D) language so positioned in a record or display that a party cannot proceed without taking some additional action with respect to the term or the reference thereto; or

(E) language readily distinguishable in another manner.

Drafting Comment

The definition of conspicuous is from Article 2B.

(6) “Conforming goods or performance under a lease contract means goods or performance that are in accordance with the obligations under the contract.

(7) “Consumer means an individual who leases or contracts to lease goods that, at the time of contracting, are intended by the individual to be used primarily for personal, family, or household use. The term does not include an individual who leases or contracts to lease goods that, at the time of contracting are intended by the individual to be used primarily for professional or commercial purposes.

[(8) “Consumer lease means a lease between a lessor regularly engaged in the business of leasing or selling and a consumer.]"

Drafting Comment

Revised Article 2 defines “consumer goods and does not include a dollar cap in the definition. Some States have not included a dollar cap in present Article 2A and States which have adopted a dollar cap have stated varying amounts. If a State wishes to include a dollar cap, the cap should be inserted here. Any cap probably should be set high enough to bring within the definition most automobile leasing transactions for personal, family, or household use.

(9) “Delivery means the transfer of physical possession or control of goods.

(10) “Electronic agent means a computer program or other automated means used, selected, or programmed by a party to initiate or respond to electronic messages or performances in whole or in part without review by an individual.
(11) “Electronic” means electrical, digital, magnetic, optical, electromagnetic, or any other form of wave propagation, or by any other technology that entails capabilities similar to those technologies.

(12) “Electronic message” means a record that, for purposes of communication to another person, is stored, generated, or transmitted by electronic, optical, or similar means. The term includes electronic data interchange, electronic or voice mail, facsimile, telex, telecopying, scanning and similar communications.

(13) “Electronic transaction” means a transaction formed by electronic messages in which the messages of one or both parties will not be reviewed by an individual as an expected step in forming the contract.

(14) “Finance lease” means a lease with respect to which:

(A) the lessor does not select, manufacture, or supply the goods;

(B) the lessor acquires the goods or the right to possession and use of the goods in connection with the lease; and

(C) one of the following occurs:

(i) the lessee receives a copy of the agreement by which the lessor acquired, or proposes to acquire, the goods or the right to possession and use of the goods before authenticating the lease agreement;

(ii) the lessee’s approval of the agreement or of the general contractual terms under which the lessor acquired or proposes to acquire the goods or the right to possession and use of the goods is a condition to the effectiveness of the lease contract;

(iii) the lessee, before authenticating the lease agreement, receives an accurate and complete statement designating the promises and warranties, and any disclaimers of warranties, limitations or modifications of remedies, or liquidated damages, including those of a third party, such as the
manufacturer of the goods, provided to the lessor by the person supplying the goods
in connection with or as part of the contract by which the lessor acquired the goods
or the right to possession and use of the goods; or

(iv) if the lease is not a consumer lease, before the lessee
authenticates the lease agreement, the lessor informs the lessee in writing:

(I) of the identity of the person supplying the goods to the
lessor, unless the lessee has selected that person and directed the lessor to acquire
the goods or the right to possession and use of the goods from that person;

(II) that the lessee is entitled under this article to the
promises and warranties, including those of any third party, provided to the lessor
by the person supplying the goods in connection with or as part of the contract by
which the lessor acquired the goods or the right to possession and use of the goods;

and

(III) that the lessee may communicate with the person
supplying the goods to the lessor and receive an accurate and complete statement of
those promises and warranties, including any disclaimers and limitations of them,
or a statement of remedies.

Drafting Comment

The stricken language in the definition of finance lease was suggested by
Jim White. Several people had noted that finance lessors perhaps should be able to
have that status as to goods which come back from the original lessee either
because of default by the lessee, or at the end of the lease term. However, at a
discussion with about 20 members of the Leasing Subcommittee of the UCC
Committee of the Business Law Section at the ABA meeting in Atlanta, there was
no support for giving finance lease status to the second lease. Incidentally, no one
there, apparently, structures deals to fit the definition of finance lease.

However, the Ed Huddleson-Equipment Leasing Association memorandum
(ELA memorandum) urges the White revision, plus some additional revisions
discussed on page 8 of the ELA memorandum.

Also, the Stephen Whelan letter from the ABA group urges the White
amendment. However, at the February meeting, the Committee voted 4-2 to delete
the language.
(15) “Good faith” means honesty in fact and the observance of reasonable commercial standards of fair dealing.

(16) “Goods” means all things that are movable at the time of identification to a lease contract, or which are fixtures. The term includes the unborn young of animals. The term does not include money in which the rent is to be paid, the subject of foreign exchange transactions, documents, letters of credit, instruments, investment property, accounts, chattel paper, general intangibles, payment intangibles, or minerals, or the like, including oil and gas, before extraction.

Drafting Comment

The final Comments should state that Article 2A does not apply to oil and gas leases.

Drafting Comment

Definition of “installment lease” is moved to Section 2A-726, following Article 2.

(17) “Lease” means a transfer of the right to possession and use of goods for a period in return for consideration. The term includes a sublease unless the context clearly indicates otherwise. The term does not include a sale, including a sale on approval or a sale or return, or retention or creation of a security interest.

(18) “Lease agreement” means the bargain, with respect to the lease, of the lessor and the lessee in fact as found in their language or inferred from other circumstances, including course of performance, course of dealing, or usage of trade as provided in this article. The term includes a sublease agreement unless the context clearly indicates otherwise.

(19) “Lease contract” means the total legal obligation resulting from the lease agreement as affected by this article and other applicable law. The term includes a sublease contract unless the context clearly indicates otherwise.
At the coordinating meeting, it was suggested that the two above definitions be moved to Article 1. It is probably not necessary that those two definitions specifically refer to subleases; the definition of lease does so, and is probably sufficient to bring subleases fully within the Act. When Article 1 is revised, the definitions will probably be deleted here.

(20) “Leasehold interest” means the interest of the lessor or the lessee under a lease contract.

(21) “Lessee” means a person that acquires the right to possession and use of goods under a lease. The term includes a sublessee unless the context clearly indicates otherwise.

(22) “Lessee in ordinary course of business” means a person that, in good faith and without knowledge that its lease is in violation of ownership rights, security interest, or leasehold interest of a third party in the goods, leases in the ordinary course from a person in the business of selling or leasing goods of that kind for cash or by exchange of other property or on secured or unsecured credit, including receiving goods or documents of title under a preexisting lease contract but not including a transfer in bulk or as security for or in total or partial satisfaction of a money debt. The term does not include a pawnbroker.

Drafting Comment
Definition (22) will be moved to Article 1 when that Article is revised to conform to the Article 9 rules.

(23) “Lessor” means a person that transfers the right to possession and use of goods under a lease. The term includes a sublessor unless the context clearly indicates otherwise.

(24) “Lessor’s residual interest” means the lessor’s interest in goods after expiration, termination, or cancellation of a lease contract.
(25) “Lien” means a charge against or interest in goods to secure payment of a debt or performance of an obligation, but the term does not include a security interest.

(26) “Lot” means a parcel or single article that is the subject matter of a separate lease or delivery, whether or not it is sufficient to perform the lease contract.

(27) “Merchant lessee” means a lessee that is a merchant with respect to goods of the kind subject to the lease.

(28) Present value means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. In determining present value, the discount is determined by the interest rate specified by the parties if the rate was not manifestly unreasonable at the time the transaction was entered into. Otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into.

(29) “Receipt”

(A) with respect to goods, means taking delivery; and

(B) with respect to an electronic record, means when it enters an information processing system in a form capable of being processed by a system of that type and the recipient uses or has designed that system for the purpose of receiving such records or information. “Receive” has an analogous meaning.

(30) “Record” means information that is inscribed on a tangible medium, or that is stored in an electronic or other medium and is retrievable in perceivable form.

(31) “Sublease” means a lease of goods whose right to possession and use is acquired by the lessor as a lessee under an existing lease.
“Supplier” means a person from which a lessor buys or leases goods to be leased under a finance lease.

“Supply contract” means a contract under which a lessor buys or leases goods to be leased.

“Terminate” means to end a contract or a part thereof by an act by a party under a power created by agreement or law, or by operation of the terms of the agreement for a reason other than for a breach by the other party.

(b) The following definitions in other articles apply to this article:

“Account”. Section 9-103(a).

“Between merchants”. Section 2-102(2).

“Buyer”. Section 2-102(3).

“Chattel paper”. Section 9-102(a)(4).

“Consumer goods”. Section 9-106(a).


“Entrusting”. Section 2-504(e).

“General intangibles”. Section 9-103(b).


“Merchant”. Section 2-102(23).

“Mortgage”. Section 9-102(a)(24).

“Pursuant to commitment”. Section 9-102(a)(29).

“Sale”. Section 2-102(27).

“Sale on approval”. Section 2-506(a)(1)

“Sale or return”. Section 2-506(a)(2)

“Seller”. Section 2-102(a)(28).

Drafting Comment

The citations to other articles have been corrected to the revised articles.
(c) In addition, Article 1 contains general definitions and principles of construction that apply throughout this article.

SECTION 2A-103. SCOPE.

(a) This article applies to any transaction regardless of form which creates a lease.

(b) If a transaction involves both information and goods, this article applies to the aspects of the transaction which involve the goods and their performance and rights in the goods other than the physical medium containing the information, its packaging, and its documentation. However, this article applies to a lease of a computer program which was not developed specifically for a particular transaction and that is embedded in goods other than a copy of the program or an information processing machine, if the program is not the subject of a separate license with the lessor. (Section 2-103)

Drafting Comment – January, 1997

The January, 1997 version of Section 2-103 states that except as provided in subsection (b) if another article applies to a transaction governed by Article 2, Article 2 does not apply to the part of the transaction governed by the other Article. I assume that we do not wish to adopt that rule. We state some rules which are different that the Article 9 rules – arguably they don’t overlap with Article 9, but it may be better no to create the argument.

Notes

Article 2A covers leases of goods. A pure services contract is not covered by Article 2A, but a court, as in Article 2, could apply Article 2A to a mixed transaction of goods and services if the lease of goods predominates. Also, courts have applied Article 2 to disputes over the quality of goods furnished in transactions in which services predominate. Such results under Article 2A are not precluded by this section.

Subsection (b) deals with transactions in which both goods and information licensed under Article 2B are involved. See Section 2B-103 on the scope of Article 2B. Presumably, Article 2B governs all disputes over “licenses of information and software contracts and “related support and maintenance agreements. Section 2B-103(a). Article 2A, however, may apply to transactions excluded from Article 2B under Section 2B-103(d). Under Section 2B-103(d) “a sale or lease of a copy of a computer program that was not developed specifically for a particular transaction
and that is embedded in goods other than a copy of the program or an information
processing machine, if the program was not the subject of a separate license with
the buyer or lease. Therefore all aspects of such a transaction would be governed
by Article 2A if the underlying transaction is a lease of the goods in which the
computer program is embedded.

SECTION 2A-104. TRANSACTIONS SUBJECT TO OTHER LAW.

(a) A transaction subject to this article is also subject to:

   (1) [list any certificate of title statutes covering automobiles, trailers,
       mobile homes, boats, farm tractors, or the like]; except as to the rights of a lessee in
       the ordinary course of business under Sections 2A-404(d) and 2A-405(d) whose
       rights arise before a certificate of title covering the goods is effective in the name of
       the [competing?] [purchaser].

        [(2) any applicable certificate-of-title statute of another jurisdiction; ]

        (3) any applicable law which establishes a different rule for consumer
            leases.

        (4) any other law of this State to which the subject matter of this article
            is subject, such as laws dealing with sale or lease of agricultural products, the
            consignment or transfer by artists of works of art or fine prints, distribution
            agreements, franchises and other relationships through which goods are leased,
            liability for products which cause injury to person or property, the making and
            disclaimer of warranties, and dealers in particular products, such as automobiles,
            motorized wheelchairs, agricultural equipment, and hearing aids.

(b) [Except for the rights of a lessee in the ordinary course of business, ]in
    case of conflict between this article, other than Sections 2A-105, 2A-401(c), and
    2A-402(c), and a statute or decision referred to in subsection (a), the statute or
decision controls.

(c) If a law referred to in subsection (a) existing on the effective date of this
    article applies to a transaction governed by this article, the following rules apply:
(1) A requirement that a contractual obligation, waiver, notice, or disclaimer be in writing is satisfied by a record.

(2) A requirement that a record or a contractual term be signed is satisfied by an authentication.

(3) A requirement that a contractual term be conspicuous or the like is satisfied by a term that is conspicuous in accordance with that article.

(d) With respect to this article, failure to comply with a statute or decision referred to in subsection (a) has only the effect specified therein. (Section 2-104)

Drafting Comment – May, 1997

The latest version of Section 2-104 raises a number of issues for Article 2A. First, Section 2-104(a)(1) overrides certificate of title legislation as to rights of buyers in ordinary course under Section 2-504(d) if their rights arose before “a certificate of title covering the goods is effective in the name of the buyer.” The “buyer here is probably meant to be a competing buyer. If the last reference to “buyer” is to the protected buyer in ordinary course, I don’t understand the subsection. Section 2-504(d) is the entrusting provision of Article 2. Perhaps we should include a similar rule in Article 2A, but Article 2A presently is subject to both in state and other state certificate of title laws with no exception for lessee in ordinary course situations. Note that subsection (e) of Section 2A-404 and Section 2A-405 seems to state a rule contrary to that now being proposed in Article 2 and set out above. The Article 2A Committee must decide what position Article 2A should take. Apparently, a few western States require that lessees in leases longer than a few month by noted on certificates of title as owners with the lessor appearing as “lienholder”. In most States, apparently, the practice is not to note the lessee’s interest on the certificate of title.

What do you think of the specific listing which is now in subsection (a)(4)? Look at the listing in Section 2-104. I have omitted items, such as blood products, which I thought could not be leased.

The reference to certificate of title laws of other States is probably not necessary both because they are already covered under subsection (a)(1) and because of Section 2A-105.

SECTION 2A-105. TERRITORIAL APPLICATION OF ARTICLE TO GOODS COVERED BY CERTIFICATE OF TITLE. Subject to Sections 2A-401(c) and 2A-402(c), with respect to goods covered by a certificate of title issued under a statute of this State or of another jurisdiction, compliance and the
effect of compliance or noncompliance with a certificate-of-title statute are
governed by the law, including the conflict-of-laws rules, of the jurisdiction issuing
the certificate until the earlier of the time the certificate ceases to be effective under
the law of that jurisdiction or the time the goods subsequently become covered by
another certificate of title from another jurisdiction.

Drafting Comment – May 1997

Section 2A-105 is conformed to the new rules of Article 9. See Section 9-303 in the April, 1997 draft.

SECTION 2A-106. LIMITATION ON POWER OF PARTIES TO
CONSUMER LEASE TO CHOOSE APPLICABLE LAW [OR JUDICIAL
FORUM] [: CHOICE OF FORUM].

[(a)] A choice-of-law term in a consumer lease contract is not enforceable
if the law chosen is that of a jurisdiction other than one in which the lessee resides
at the time the lease agreement becomes enforceable or within 30 days thereafter or
in which the goods are to be used.

[(b) The parties may choose an exclusive judicial form. However, in a
consumer lease the choice is not enforceable if the chosen jurisdiction would not
otherwise have jurisdiction over the consumer and the choice unfairly
disadvantages the consumer. A choice of forum in a term of an agreement is not
exclusive unless the agreement expressly so provides.]

Drafting Comment

The ELA memorandum, page 10, asks that this section specifically state that
choice of law/forum selection clauses are valid in commercial leases. Choice of
law is dealt with in 1-105, and probably should not be separately addressed in
Article 2A. Since Article 2B presently does state specifically that, except in
consumer transactions, the parties may choose the forum, perhaps we should also.
SECTION 2A-107. UNCONSCIONABILITY.

(a) If a court finds as a matter of law that a lease contract or a term of the contract was unconscionable at the time the contract was made, the court may refuse to enforce the contract, enforce the remainder of the contract without the term, or so limit the application of the term to avoid an unconscionable result.

(b) With respect to a consumer lease, if the court finds as a matter of law that a lease contract or a term of the contract was induced by unconscionable conduct or that unconscionable conduct has occurred in the collection of a claim arising from the lease contract, the court may grant appropriate relief.

(c) Before making a finding of unconscionability under subsection (a) or (b), the court, on motion of a party or its own motion, shall afford the parties a reasonable opportunity to present evidence as to the setting, purpose, and effect of the lease contract or term thereof or of the conduct.

(d) In an action in which a lessee claims unconscionability with respect to a consumer lease the following rules apply:

(1) If the court finds unconscionability under subsection (a) or (b), the court shall award reasonable attorney’s fees to the lessee.

(2) If the court does not find unconscionability and the lessee claiming unconscionability has brought or maintained an action the lessee knew to be groundless, the court shall award reasonable attorney’s fees to the party against which the claim is made.

(3) In determining attorney’s fees, the amount of the recovery on behalf of the claimant under subsections (a) and (b) is not controlling. (Section 2-105)

Drafting Comment

In the October, 1996 meeting, the Drafting Committee voted to retain present Section 2A-108 (new Section 2A-107) with the slight word change in subsection (c). At the February, 1997 meeting, the Committee rejected a proposal to delete the reference to unconscionable conduct in collection.
The final version of Article 2A will contain a Comment modeled on a U3C comment of unconscionable inducement.

SECTION 2A-108. OPTION TO ACCELERATE AT WILL.

(a) A term in a lease agreement providing that one party or that party’s successor in interest may accelerate payment or performance or require collateral or additional collateral “at will” or when the party “deems itself insecure” or in words of similar import must be construed to mean that the party has power to do so only if it in good faith believes that the prospect of payment or performance is impaired.

(b) In a consumer lease, the burden of establishing good faith under subsection (a) is on the party that exercised the power. In all other leases, the burden of establishing lack of good faith is on the party against which the power has been exercised.

SECTION 2A-109. EFFECT OF AGREEMENT.

(a) Except as otherwise expressly provided in Section 1-102 and this article, the effect of any provision may be varied by agreement.

(b) The absence of a phrase such as “unless otherwise agreed” does not by itself preclude the parties from varying the provision by agreement.

(c) Whenever this article allocates a risk or imposes a burden as between the parties, an agreement may shift the allocation and apportion the risk or burden,

Drafting Comment

Should Article 2A adopt this provision? Do we create an undesirable negative implication if we do not, and Article 2 does?
[SECTION 2A-201. FORMAL REQUIREMENTS.]

(a) Except as otherwise provided in this section, a lease contract is not enforceable by way of action or defense unless:

   (1) the total payments to be made under the lease contract, excluding payments for options to renew or buy, are less than $1,000; or

   (2) there is a record, authenticated by the party against which enforcement is sought or by the party’s agent, sufficient to indicate that a lease contract has been made between the parties and to describe the goods leased and the duration of the lease.

(b) Any description of the leased goods or of the duration of the lease is sufficient and satisfies subsection (a)(2), whether or not it is specific, if it reasonably identifies what is described.

(c) A record is not insufficient because it omits or incorrectly states a term agreed upon, but a lease contract is not enforceable under subsection (a)(2) beyond the duration of the lease and the quantity of goods agreed to in the authenticated record.

(d) An otherwise valid lease contract that does not satisfy the requirements of subsection (a) is enforceable:

   (1) if the goods are to be specially manufactured or obtained for the less and are not suitable for lease or sale by the lessor to others in the ordinary course of business, and the lessor, before notice of repudiation is received and under circumstances that reasonably indicate that the goods are for the lessee, has made
either a substantial beginning of their manufacture or commitments for their procurement;

(2) if the party against which enforcement is sought admits in its pleading, testimony, or otherwise in court that a lease contract was made, but the lease contract is not enforceable under this provision beyond the quantity of goods admitted; or

(3) with respect to goods that have been received and accepted by the lessee.

(e) The duration of a lease under a contract referred to in subsection (d) is:

(1) if there is a record authenticated by the party against which enforcement is sought or by that party’s authorized agent specifying the duration of the lease, the period so specified;

(2) if the party against which enforcement is sought admits in that party’s pleading, testimony, or otherwise in court, the duration of the lease, the period so admitted; or

(3) a reasonable duration.

(f) The affixing of a seal to a record evidencing a contract or offer does not make the record a sealed instrument. The law with respect to sealed instruments does not apply to the contract or offer.]

[SECTION 2A-201. FORMAL REQUIREMENTS; STATUTE OF FRAUDS.

(a) Except as otherwise provided in this section, a claim for default under a lease contract in which the total payments are $10,000 or more is not enforceable by way of action or defense against a person that denies that an agreement was made unless there is a record authenticated by the person against which the claim is
asserted as the record of that person and which is sufficient to indicate that a contract was made. A record is not insufficient merely because it omits or incorrectly states a term, including a quantity term. If the record contains a quantity term, the claim is not enforceable beyond that quantity.

(b) If an authenticated record in confirmation of a contract is sufficient against the sender and is sent within a reasonable time to the other party, the record is sufficient against the other party who is a merchant, unless the merchant sends a notice of objection to the record within 10 days after the record is received.

(c) A claim for default under an otherwise valid lease contract which is barred under subsection (a) is enforceable if:

(1) the goods are to be specially manufactured or processed for the lessee, and the lessor substantially manufacturers, processes the goods, or makes commitments for the procurement of the goods in performance of a contract believed in good faith to exist, and the lessor cannot relet or sell the goods at a reasonable price;

(2) the conduct of both parties in performing the agreement recognizes that a contract was formed;

(3) reliance by one party on representations or an agreement under law outside of this [Act] estops the other party from raising the lack of a sufficient authenticated record as a defense; or

(4) the party against which enforcement is sought, in pleading or testimony in court or otherwise under oath, admits facts from which lease contract can be found.

(d) A claim for breach of a lease contract enforceable under this section is not enforceable on the ground that it is not capable of being performed within one year or any other applicable period after its making.] (Section 2-201)
At the February meeting of the Article 2A Committee, the Committee decided to return to present Section 2A-201 with style changes. It also decided that it would return to the statute of frauds issue after seeing the new Section 2-201 added by the Article 2 Drafting Committee. Therefore, both present Section 2-201, restyled, and the new Article 2 statute of frauds sections are set out above.

To what extent should Article 2A follow new Section 2-201. Among the issues are:

(1) Should the dollar threshold be raised?

(2) Should a party pleading the statute be forced to deny that a contract was made?

(3) Should estoppel principles be stated in the statute?

(6) Should the admission which makes the contract enforceable be extended to an admission under oath not make in the pleading or testimony.

SECTION 2A-202. PAROL OR EXTRINSIC EVIDENCE. Terms with respect to which confirmatory records of the parties agree, or which are otherwise set forth in a record intended by the parties as a final expression of their agreement with respect to the included terms, may not be contradicted by evidence of a previous agreement or contemporaneous oral agreement. However, terms in a record may be explained by any relevant evidence and may be supplemented by evidence of:

(1) course of performance, usage of trade, or course of dealing; and

(2) noncontradictory additional terms, unless

(A) the terms if agreed upon would certainly have been included in the record, or

(B) the court finds that the record was intended as a complete and exclusive statement of the terms of the agreement. (Section 2-202)
SECTION 2A-203. FORMATION IN GENERAL.

(a) A lease contract may be formed in any manner sufficient to show agreement, including by offer and acceptance, conduct of both parties or the operations of an electronic agent which recognizes the existence of a contract.

(b) A lease contract may be found if the parties intend to form a contract, even if the time that the agreement was made cannot be determined, one or more terms are left open or to be agreed upon, or one party reserves the right to modify terms.

(c) Even if one or more terms are left open, a lease contract does not fail for indefiniteness if the parties intended to form a contract and there is a reasonably certain basis for giving an appropriate remedy. (Section 2-203)

Drafting Comment – May, 1997

The above draft includes changes made in the March and May Article 2 drafts. See Section 2-203(d) in the July Article 2 draft. That is, apparently, a small remnant of the form contract material in Article 2. It is not included in the above version of Section 2A-203. The Article 1 Committee, in its coordination mode, suggests that the Article 2 Committee again consider whether to retain Section 2-203(d).

SECTION 2A-204. FIRM OFFERS: SEALED INSTRUMENTS.

(a) An offer by a merchant to enter into a lease contract made in an authenticated record that by its terms gives assurance that the offer will be held open is not revocable for lack of consideration during the time stated. If a time is not stated, the offer is irrevocable for a reasonable time not exceeding 90 days. A term of assurance in a record supplied by the offeree is ineffective unless the term is conspicuous.

(b) Affixing a seal to a writing evidencing a lease contract or an offer to enter into a lease contract does not render the record a sealed instrument. The law
with respect to sealed instruments does not apply to the lease contract or offer.

(Section 2-204)

**SECTION 2A-205. OFFER AND ACCEPTANCE.**

(a) Unless otherwise unambiguously indicated by the language or circumstances, an offer to make a lease contract invites acceptance in any manner and by any medium reasonable in the circumstances.

(b) If the beginning of a requested performance is a reasonable mode of acceptance, an offeror that is not notified of acceptance within a reasonable time may treat the offer as having lapsed before acceptance.

(c) Subject to subsection (d), actions taken by one or more electronic agents which confirm the existence of a contract are effective to form a contract even if no individual representing either party was aware of or reviewed the action or its results.

(d) In an electronic transaction, the following rules apply:

(1) An agreement is formed by the interaction of two electronic agents if the interaction results in both agents each engaging in operations that signify agreement, such as by engaging in performing the agreement, ordering or instructing performance, accepting performance, or making a record of the existence of an agreement.

(2) An agreement may be formed by the interaction of an electronic agent and an individual. An agreement is formed if an individual has reason to know that the individual is dealing with an electronic agent and performs actions the person should know will cause the agent to perform or to permit further use, or that are clearly indicated as constituting acceptance regardless of other
contemporaneous expressions by the individual to which the electronic agent cannot react.

(3) The terms of the contract include terms on which the parties have previously agreed, terms which the electronic agents could take into account, and, to the extent not covered by the foregoing, terms provided by this article or other law. (Sections 2-205, 2B-307(e) and (f))

[SECTION 2A-206. CONSUMER CONTRACTS; RECORDS.

(a) In a consumer lease, if a consumer agrees to a record by authentication or affirmative conduct, any non-negotiated term that a reasonable consumer in a transaction of this type would not reasonably expect to be in the record is excluded from the lease, unless the consumer had knowledge of the term before agreeing to the record.

(b) Before deciding whether to exclude a term under subsection (a), the court, on motion of a party or its own motion, after affording the parties a reasonable and expeditious opportunity to present evidence on whether the term should be included or excluded from the lease, shall decide whether the contract should be interpreted to exclude the term.

(c) This section shall not operate to exclude an otherwise effective term disclaiming or modifying an implied warranty.] (Section 2-206)

Drafting Comment – May 1997

In the February meeting, the Article 2A Committee decided to examine the latest Article 2 draft dealing with consumer contracting through use of forms.

Also note the latest version of Section 2-207, the battle of the forms section. Do we still regard that section as unnecessary in Article 2A?

SECTION 2A-207. ATTRIBUTION PROCEDURE.
(a) An attribution procedure is a procedure established by agreement or mutually adopted by the parties for the purpose of verifying that electronic records, messages, or performances are those of the respective parties or for detecting errors in the transmission or informational content of an electronic message, record, or performance, if the procedure is commercially reasonable.

(b) The commercial reasonableness of an attribution procedure is a question of law to be determined by the court in light of the purposes of the procedure and the commercial circumstances at the time of the agreement, including the nature of the transaction, sophistication of the parties, volume of similar transactions engaged in by either or both of the parties, availability of alternatives offered to but rejected by the party, cost of alternative procedures, and procedures in general use for similar types of transactions. An attribution procedure may require the use of algorithms or other codes, identifying words or numbers, encryption, callback procedures, key escrow, or any security devices that are reasonable under the circumstances.

SECTION 2A-208. ATTRIBUTION OF ELECTRONIC RECORD, MESSAGE, OR PERFORMANCE.

(a) As between the parties, an electronic message, record, or performance received by a party is attributable to the party indicated as the sender if:

(1) it was sent by that party, its agent, or its electronic agent;

(2) the receiving party, in good faith and in compliance with an attribution procedure concluded that it was sent by the other party; or

(3) subject to subsection (b), the message or performance:
(A) resulted from acts of a person that obtained access to access numbers, codes, computer programs, or the like from a source under the control of the alleged sender creating the appearance that it came from the alleged sender; (B) the access occurred under circumstances constituting a failure to exercise reasonable care by the alleged sender; and (C) the receiving party reasonably relied to its detriment on the apparent source of the message or performance.

(b) In a case governed by subsection (a)(3), the following rules apply:

(1) The receiving party has the burden of proving reasonable reliance, and the alleged sender has the burden of proving reasonable care.

(2) Reliance on an electronic record or performance that does not comply with an agreed authentication procedure is not reasonable unless authorized by an individual representing the alleged sender.

(c) If an electronic message was transmitted pursuant to an attribution procedure for the detection of error and the message contained an error the following rules apply:

(1) If the sender complied with the attribution procedure and the error would have been detected had the receiving party also complied with the attribution procedure, the sender is not bound if the error relates to a material element of the message or performance.

(2) If the sender receives a notice required by the attribution procedure of the content of the message or performance as received, the sender has a duty to in a commercially reasonable manner review the notice and report any error detected by it.

(d) Except as otherwise provided in subsection (a)(1) and (c), if a loss occurs because a party complies with a procedure for attribution that was not
commercially reasonable, the party that required use of the procedure bears the loss unless it disclosed the nature of the risk to the other party or offered commercially reasonable alternatives that the party rejected. The party’s liability under this section is limited to losses that could not have been prevented by the exercise of reasonable care by the other party. (Section 2B-111)

SECTION 2A-209. AUTHENTICATION EFFECT AND PROOF;
ELECTRONIC AGENT AUTHENTICATION.

(a) An authentication is intended to establish the party’s identity, its adoption and acceptance of a record or a term, and the authenticity of the record or term.

(b) Operations of an electronic agent constitute the authentication of a party if the party designed, programmed, or selected the electronic agent for the purpose of achieving results of that type.

(c) A record or message is authenticated as a matter of law if party complied with an attribution procedure for authentication. Otherwise, authentication may be proven in any manner including by showing that a procedure existed by which a party necessarily must have executed or adopted a symbol in order to proceed further in the use or processing of the information, or adopted a symbol in order to proceed further in the use or processing of the information.

(Section 2B-114)

SECTION 2A-210. PROOF OF AUTHENTICATION.

(a) Actions by an electronic agent constitute the authentication of a party if the party designed, programmed, or selected the electronic agent for the purpose of achieving results of that type.
(b) A record or message is authenticated as a matter of law if a party complied with an attribution procedure for authentication. Otherwise, authentication may be proven in any manner including by showing that a procedure existed by which a party necessarily must have executed.

SECTION 2A-211. ELECTRONIC TRANSACTIONS AND MESSAGES:
TIMING OF CONTRACT AND EFFECTIVENESS OF MESSAGE.

(a) If an electronic message initiated by a party or an electronic agent evokes an electronic message in response and the messages reflect an intent to be bound, a contract exists when:

   (1) the response signifying acceptance is received; or

   (2) if the response consists of electronically furnishing the requested information or notice of access to the information when the information or notice is received unless the originating message prohibited that form of response.

(b) Subject to Section 2B-212, an electronic message is effective when received, even if no individual is aware of its receipt.

SECTION 2A-212. ACKNOWLEDGMENT OF ELECTRONIC MESSAGE.

(a) If the originator of an electronic message requests or has agreed with the addressee of the message that receipt of the message must be acknowledged electronically, the following rules apply:

   (1) If the originator indicated in the message or otherwise that the message was conditional on receipt of an acknowledgment, the message does not bind the originator until acknowledgment is received and lapses if acknowledgment is not received in a reasonable time.
(2) If the originator requested acknowledgment but did not state that the
message was conditional on acknowledgment and acknowledgment has not been
received within a reasonable time after the message was sent, on notice to the
other party, the originator may either retract the message or specify a further
reasonable time within which acknowledgment must be received or the message
will be treated as not having binding effect. If acknowledgment is not received
within that additional time, the originator may treat the message as not having
binding effect.

(3) If the originator requested acknowledgment and specified a time for
receipt, the originator may exercise the options in subsection (a)(2) if receipt does
not occur within that time.

(b) Receipt of acknowledgment establishes that the message was received
but does not in itself establish that the content sent corresponds to the content
received. (Section 2B-205)
PART 3
CONSTRUCTION OF LEASE CONTRACT

SECTION 2A-301. COURSE OF PERFORMANCE OR PRACTICAL CONSTRUCTION.

(a) A “course of performance” is a sequence of conduct between the parties to a particular lease transaction that exists if:

(1) the agreement of the parties with respect to the transaction involves repeated occasions for performance by a party;

(2) that party performs on one or more occasions; and

(3) the other party, with knowledge of the nature of the performance and opportunity for objection to it, accepts the performance or acquiesces in it without objection.

(b) A course of performance between the parties is relevant to ascertaining the meaning of the parties’ agreement, may give particular meaning to specific terms of the agreement, and may supplement or qualify the terms of the agreement.

(c) Except as otherwise provided in subsection (d), the express terms of an agreement and any applicable course of performance, course of dealing, or usage of trade must be construed, whenever reasonable, as consistent with each other. If such construction is unreasonable:

(1) express terms prevail over course of performance, course of dealing, and usage of trade;

(2) course of performance prevails over course of dealing and usage of trade, and

(3) course of dealing prevails over usage of trade.
(d) Subject to Section 2A-302, course of performance is relevant to show a waiver or modification of a term inconsistent with the course of performance.

(Section 2-209)

Drafting Comment

This section will probably be moved to Article 1.

SECTION 2A-302. MODIFICATION, RESCISSION, AND WAIVER.

(a) An agreement made in good faith which modifies a lease contract is binding without consideration.

(b) Except in a consumer lease contract, a lease contract that contains a term that excludes modification or rescission except by an authenticated record may not be otherwise modified or rescinded. However, a party whose language or conduct is inconsistent with the term requiring an authenticated record may not assert that term if the language or conduct induced the other party to change its position reasonably and in good faith.

(c) Subject to subsection (b), a term in a contract may be waived by the party for whose benefit it was included. Language, conduct, or a course of performance between the parties may be relevant to show a waiver. The waiver of an executory portion of a contract, however, may be retracted by seasonable notification received by the other party that strict performance is required of any term waived unless the waiver induced the other party to change its position reasonably and in good faith. (Section 2-210)

Drafting Comment – May, 1997

At the October, 1996, meeting, the Committee expressed displeasure with the failure of revised Section 2-210 to retain the rule that a waiver can be retracted unless retraction would be unjust because of a material change of position by the other party. The Article 2 draft still refers merely to “change of position reasonably and in good faith.” There is no reference to the materially of the change of position. Such we return to the present Code language under which a waiver can be retracted “unless the retraction would be unjust in view of a material change of position in reliance on the waiver:?”
[SECTION 2A-303. CONTINUING CONTRACTUAL TERMS.

(a) Terms of a lease agreement involving repeated performances apply to all later performances unless modified pursuant to this article, even if the terms are not subsequently displayed or otherwise brought to the attention of the parties or electronic agents in the context of the later performance.

(b) A modification in good faith of a continuing lease contract made pursuant to a term in a contract providing that the contract may be modified as to future performances by compliance with a described contractual procedure is effective if:

(1) compliance with the procedure reasonably notifies the other party of the change; and

(2) in a consumer lease, the procedure permits the lessee to terminate the lease contract if the modified term is material and is in good faith unacceptable to the lessee.

(c) A contractual term that specifies standards for reasonable modification is enforceable unless the standards are manifestly unreasonable in light of the commercial circumstances.] (Section 2B-304)

Drafting Comment – June, 1997

The coordination group, at its May, 1997, meeting suggested that the Article 2A Committee consider adding this section

SECTION 2A-304. LESSEE UNDER FINANCE LEASE AS BENEFICIARY OF SUPPLY CONTRACT.

(a) The benefit of the supplier’s promises to the lessor under a supply contract and of all warranties, whether express or implied, including those of any third party provided in connection with or as part of the supply contract, extends to the lessee to the extent of the lessee’s leasehold interest under a finance lease
related to the supply contract but is subject to the terms of the warranty and supply contract and all defenses or claims arising therefrom.

(b) The extension of the benefit of a supplier’s promises and of warranties to the lessee does not modify the rights and obligations of the parties to the supply contract, whether arising therefrom or otherwise, or impose any duty or liability under the supply contract on the lessee.

(c) A modification or rescission of a supply contract by the supplier and the lessor is effective between the supplier and the lessee unless, before the modification or rescission, the supplier has received notice that the lessee has entered into a finance lease related to the supply contract. If the modification or rescission is effective between the supplier and the lessee, the lessor assumes by, in addition to the obligations of the lessor to the lessee under the lease contract, the promises of the supplier to the lessor and warranties that were so modified or rescinded as they existed and were available to the lessee before modification or rescission.

(d) In addition to the extension of the benefit of the supplier’s promises and of warranties to the lessee under subsection (a), the lessee retains all rights that the lessee may have against the supplier which arise from a contract between the lessee and the supplier or under other law.

[SECTION 2A-305. ELECTRONIC VIRUSES.]

(a) In this section “virus” means computer instructions intended to disrupt, damage, destroy, or interfere with use of a communications facility or a computer without the consent or permission of the owner.
(b) Unless the circumstances clearly indicate that a duty of care could not be expected, a party shall exercise reasonable care to ensure that its performance or message when completed by it does not contain an undisclosed virus.

(c) The duty described in subsection (b) is owed solely to the other party to the lease contract and is satisfied if:

   (1) the party exercised reasonable care; or

   (2) except with respect to a consumer lease involving delivery of a copy of information on a physical medium by a merchant dealing in information of the kind, language in a contract states that no action was taken to ensure exclusion of a virus or that a risk exists that viruses have not been excluded.

(d) A party is not liable if the virus was introduced by a third party after the party completed its performance or if the party injured by the virus failed to exercise reasonable care to prevent or avoid loss.

(e) In determining whether reasonable care has been exercised, the court shall consider the nature of the party, type and value of the transaction, consideration exchanged, circumstances of the transaction, language on packaging or in a display, and general standards of practice prevailing among persons of a similar type for similar transactions at the time of the performance or message. A party is deemed to have exercised reasonable care if it or its agent searches for known viruses using any commercially reasonable virus checking software at or before the time the licensor completes its performance or, as to the licensee, the time the licensee first uses the information.

(f) A party’s obligations with respect to the existence of a virus are determined by this section and the express terms of the contract and not implied warranty.]
Addition of this section to Article 2A was recommended by the coordination group at its May, 1997, meeting. The section, if retained, probably should be moved to Part 5.

[SECTION 2A-306. ELECTRONIC REGULATION OF PERFORMANCE.]

(a) A party entitled to enforce a limitation or restriction may include in the information and utilize a program, code, or device that restricts use in a manner consistent with the agreement if:

(1) a term in the contract authorizes use of the program, code, or device;

(2) the program, code, or device merely prevents uses of the information that are not consistent with the agreement but does not destroy or alter the information;

(3) the program, code, or device merely prevents uses of the information that are not consistent with a licensor’s rights under copyright or patent law and that were not granted to the licensee but does not destroy or alter the information.

(4) the information is obtained for a stated period of time not more than 30 days or a stated number of uses and the program, code, or device merely enforces that limitation; or

(5) the program, code, or device prevents further use at the expiration of the term of the license and the program, code or device or the licensor gives reasonable notice to the licensee before further use is prevented.

(b) Operation of a program, code, or device that restricts use consistent with the agreement is not a breach of contract, and the party that included the program, code, or device is not liable for any loss created by its operation. Operation of a program, code, or device that prevents use permitted by the agreement is a breach of contract.]
(c) This section does not preclude electronic replacement or disabling of an earlier version of information by the licensor with a new version of the information pursuant to an agreement with the licensee.

(d) A program, code or device included in information pursuant to this section or as authorized under other law does not constitute a virus for purposes of Section 2B-313.

SECTION 2A-307. IDENTIFICATION. Identification of goods as goods to which a lease contract refers may be made at any time and in any manner expressly agreed to by the parties. In the absence of express agreement, identification occurs when:

(1) the lease contract is made, if the contract is for the lease of existing and described goods;

(2) goods are shipped, marked, or otherwise designated by the lessor as goods to which the lease contract refers, if the lease contract is for a lease of goods that are not existing and identified; or

(3) young are conceived, if the lease contract is for a lease of unborn young of animals. (Section 2-502)

SECTION 2A-308. INSURANCE AND PROCEEDS.

(a) A lessee obtains an insurable interest in existing goods identified to the lease contract even if the goods are nonconforming and the lessee has an option to return or reject them.

(b) If a lessee has an insurable interest only by reason of the lessor’s identification of the goods, the lessor may substitute other goods for those
identified until default or insolvency or notification to the lessee that the
identification is final.

(c) The lessor also retains an insurable interest until an option to buy has
been exercised by the lessee and risk of loss has passed to the lessee.

(d) This section does not affect any insurable interest recognized under any
other law.

(e) The parties, by agreement, may determine that one or more parties have
an obligation to obtain and pay for insurance covering the goods and determine the
beneficiary of the proceeds of the insurance. (Section 2-502)

SECTION 2A-309. RISK OF LOSS.

(a) Except in the case of a finance lease, risk of loss is retained by the lessor
and does not pass to the lessee. In the case of a finance lease, risk of loss passes to
the lessee.

(b) If under the lease contract risk of loss will pass to the lessee but the
agreement does not specify when the risk passes, except as otherwise provided in
subsection

(c) Risk of loss passes to the lessee regardless of the conformity of the
goods to the contract, as follows:

(1) Subject to this subsection, the risk of loss passes to a lessee upon
receipt of the goods. If the lessee does not intend to take possession, risk of loss
passes to the lessee when the lessee receives control of the goods.

(2) If a lease contract requires or authorizes a lessor to ship goods by
carrier, the following rules apply:
(A) If the contract does not require delivery at a particular
destination, risk of loss passes to the lessee when the goods are duly delivered to
the carrier.

(B) If the contract requires delivery at a particular destination and
the goods arrive there in the possession of the carrier, risk of loss passes to the
lessee when the goods are so tendered as to enable the lessee to take delivery.

(3) If goods are held by a bailee to be delivered without being moved,
risk of loss passes to the lessee on acknowledgment by the bailee to the lessee of
the lessee’s right to possession of the goods.

(d) A default under the lease contract by either party affects risk of loss
only in the following cases:

(1) If the lessee rightfully and effective rejects the goods or revokes
acceptance of the goods, the lessor has the risk of loss from the time when the
rejection or revocation is effective.

(2) If the lessor has tendered nonconforming goods, the risk of loss has
passed to the lessee, and the goods are damaged or lost before the lessee effectively
rejects or revokes acceptance, the seller has the risk of loss to the extent the
nonconformity of the goods caused the damage or loss.

(3) If conforming goods are identified to the lease contract when the
lessee repudiates or is otherwise in breach and the risk of loss has not otherwise
passed to the lessee, the lessee has the risk of loss for those goods for a
commercially reasonable time after the breach or repudiation. (Section 2-612)

Drafting Comment – January, 1997

At the October, 1996, Committee meeting, the Committee asked that
subsection (b) contain some language referring to the failure of the agreement to
specify when risk passes if under the agreement risk is to pass to the lessee.
SECTION 2A-310. CASUALTY TO IDENTIFIED GOODS. If the parties to a lease contract assume the continued existence and eventual delivery to the lessee of goods identified when the lease contract is made and the goods suffer casualty without fault of the lessee, the lessor, or the supplier before delivery, or if the goods suffer casualty before risk of loss passes to the lessee under the lease agreement or Section 2A-309, and no commercially reasonable substitute is available, the following rules apply:

(1) If the loss occurs before the goods are delivered to the lessee, the lessor or supplier shall seasonably notify the lessee of the nature and extent of the loss.

(2) If the loss is total, the lease contract is avoided.

(3) If the loss is partial or the goods no longer conform to the lease contract, the lessee may nevertheless demand inspection and may treat the lease contract as avoided or, except in a finance lease that is not a consumer lease, accept or retain the goods with due allowance from the rent payable for the balance of the duration of the lease for the nonconformity but without further right against the lessor.

(Section 2-714)

Drafting Comment – May, 1997

Addition of the words “or retain” in subdivision (3) is not required for conformity to Article 2.

The Comments to the May draft of Section 2-714 speak to the new language as follows:

“The language regarding commercially reasonable substitution is inserted for discussion to address the following scenario. Seller agrees to sell stock goods, those goods are identified and then destroyed. If the seller had other stock that was the commercially reasonable substitute for the identified goods, this section would not excuse the delivery. In part this narrows the excuse provided by this section back toward the original version of Section 6-613 which allowed an excuse only when the “contract required for its performance goods identified when the contract was made.”
SECTION 2A-311. TERMINATION; SURVIVAL OF OBLIGATIONS.

(a) Except as otherwise provided in subsection (b), on termination of a lease contract, all obligations that are still executory on both sides are discharged.

(b) The following survive termination of a lease contract:

1. a right based on a previous default or performance of the contract

2. a term limiting the scope, manner, method, or location of the exercise of rights in the goods;

3. an obligation of confidentiality, nondisclosure, or noncompetition;

4. an obligation to return or dispose of goods;

5. a choice of law or forum;

6. an obligation to arbitrate or otherwise resolve disputes through alternative dispute resolution procedures;

7. a term limiting the time for commencing an action or for providing notice;

8. an indemnity term;

9. a limitation of remedy or disclaimer of warranty;

10. any term limiting disclosure of information;

11. any right, remedy, or obligation stated in the agreement as surviving; and

12. other rights, remedies, or limitations if in the circumstances such survival is necessary to achieve the purposes of the parties.

(c) The obligation under subsection (b)(3) must be promptly performed.

(Section 2-310).

Drafting Comment – May 1997

Present Article 2A addresses termination in the section on Termination and Cancellation (present Section 2A-505(2)). That section merely says: On termination of the lease contract, all obligations that are still executory on both sides are discharged, but any right based on prior default or performance survives.
The revised version of present Section 2A-505 (Section 2A-709) deals only with cancellation.

The changes in this draft, other than subsection (b)(8), come from decisions of the Article 1 Drafting Committee serving as a coordination committee. Subsection (b)(8) was added by decision of the Article 2A Drafting Committee in February. (Section 2-311)
PART 4
EFFECT OF LEASE CONTRACT

SECTION 2A-401. ENFORCEABILITY OF LEASE CONTRACT.
Except as otherwise provided in this article, a lease contract is effective and enforceable according to its terms between the parties, against purchasers of the goods, and against creditors.

SECTION 2A-402. TITLE TO AND POSSESSION OF GOODS. Except as otherwise provided in this article, the application of this article is not affected by whether the lessor or a third party has title to the goods, or the lessor, the lessee, or a third party has possession of the goods, or by any statute or rule of law that possession or the absence of possession is fraudulent. (Section 2-501)

SECTION 2A-403. ALIENABILITY OF PARTY’S INTEREST UNDER LEASE CONTRACT OR OF LESSOR’S RESIDUAL INTEREST IN GOODS; DELEGATION OF PERFORMANCE; TRANSFER OF RIGHTS.
(a) In this section, “creation of a security interest” includes the sale of a lease contract that is subject to Article 9 by reason of Section 9-102(1)(b).
(b) Except as otherwise provided in subsections (c) and (d), a term in a lease agreement which prohibits the voluntary or involuntary transfer, including a transfer by sale, sublease, creation or enforcement of a security interest, or attachment, levy, or other judicial process, of an interest of a party under the lease contract or of the lessor’s residual interest in the goods, or which makes such a transfer an event of default, gives rise to the rights and remedies provided in subsection (e). However, a transfer that is prohibited or is an event of default under the lease agreement is otherwise effective.
(c) In a consumer lease, to prohibit the transfer of an interest of a party under the lease contract or to make a transfer an event of default, the language must be specific, be in a record, and be conspicuous.

(d) A term of a lease agreement which prohibits the creation or enforcement of a security interest in an interest of a party under the lease contract or in the lessor’s residual interest in the goods, or which makes such a transfer an event of default, is enforceable only to the extent that there is a transfer by the lessee of the lessee’s right of possession or use of the goods in violation of the provision or a delegation of a material performance of either party to the lease contract in violation of the provision. Neither the granting nor the enforcement of a security interest in the lessor’s interest under the lease contract, or the lessor’s residual interest in the goods, is a transfer that materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on, the lessee within the meaning of subsection (e) unless, and only to the extent that, there is a delegation of a material performance of the lessor.

(e) A term of a lease agreement which prohibits a transfer of a right to damages for default with respect to the whole lease contract or of a right to payment arising out of the transferor’s due performance of the transferor’s entire obligation, or which makes such a transfer an event of default, is not enforceable. Such a transfer is not a transfer that materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on, the other party to the lease contract within the meaning of subsection (f).

(f) Subject to subsections (d) and (e):
(1) if a transfer is made that is an event of default under a lease agreement, the other party to the lease contract has the rights and remedies described in Section 2A-702(b) unless that party waives the default or otherwise agrees; and

(2) if paragraph (1) does not apply and a transfer is made that is prohibited under a lease agreement or materially impairs the prospect of obtaining return performance by, materially changes the duty of, or materially increases the burden or risk imposed on, the other party to the lease contract, unless the party not making the transfer agrees at any time to the transfer in the lease contract or otherwise or unless limited by contract:

(A) the transferor is liable to the party not making the transfer for damages caused by the transfer to the extent that the damages could not reasonably be prevented by the party not making the transfer; and

(B) a court having jurisdiction may grant other appropriate relief, including cancellation of the lease contract or an injunction against the transfer.

(g) A transfer of “the lease” or of “all my rights under the lease,” or a transfer in similar general terms, is a transfer of rights and, unless the language or the circumstances indicate the contrary, as in a transfer for security, the transfer is a delegation of duties by the transferor to the transferee. Acceptance by the transferee constitutes a promise by the transferee to perform those duties. The promise is enforceable by either the transferor or the other party to the lease contract.

(h) Unless otherwise agreed by the lessor and the lessee, a delegation of performance does not relieve the transferor as against the other party of any duty to perform or liability for default. (Section 2-503)

SECTION 2A-404. SUBSEQUENT LEASE OF GOODS BY LESSOR.
(a) Subject to Section 2A-403, a subsequent lessee from a lessor of goods under an existing lease contract obtains, to the extent of the leasehold interest transferred, the leasehold interest which the lessor had or had power to transfer, and except as otherwise provided in subsections (b) and (c) and Section 2A-720(d), takes subject to the existing lease contract.

(b) A lessor with voidable rights or title acquired in purchase of goods from a transferor that has relinquished possession or control has power to transfer a good leasehold interest to a good-faith, subsequent lessee for value until the transferror regains possession or control, but only to the extent provided in subsection (a).

(c) For purposes of this section, a purchase includes a transaction in which:

1. the transferor was deceived as to the identity of the lessor;
2. the delivery was in exchange for a check later dishonored;
3. it was agreed that the transaction was to be a cash sale; or
4. the delivery was procured through fraud punishable under criminal law.

(d) A subsequent lessee in the ordinary course of business from a lessor that is a merchant dealing in goods of that kind to which the goods were entrusted by the existing lessee of that lessor before the interest of the subsequent lessee became enforceable against that lessor obtains, to the extent of the leasehold interest transferred, all rights to the goods of that lessor and the existing lessee, and takes free of the existing lease contract.

(e) A subsequent lessee from the lessor of goods that are subject to an existing lease contract and are covered by a certificate of title issued under a statute of this State or of another jurisdiction takes no greater rights than those provided both by this section and by the certificate-of-title statute. (Section 2-504)

Drafting Comment – June, 1997
Section 2-504 provides that “entrusting of goods to a merchant . . . gives the
merchant and a buyer from that merchant power to transfer all rights and title of the
entruster . . . Should Article 2A similarly extend the entrusting protection to a
lessee from a first lessee that was not itself a lessee in ordinary course?

If lessee A entrusts goods to lessor who leases to lessee B who is not a
lessee in the ordinary course of business, and lessee B then subleases to lessee C,
should lessee C take free of lessee A’s interest? If lessee B is a lessee in ordinary
course, the shelter principle would protect lessee C. If that is the correct rule, is it
worth five more words in the statute?

SECTION 2A-405. SALE OR SUBLEASE OF GOODS BY LESSEE.

(a) Subject to Section 2A-403, a buyer or sublessee from the lessee of
goods under an existing lease contract obtains, to the extent of the interest
transferred, the leasehold interest in the goods that the lessee had or had power to
transfer, and except as otherwise provided in subsection (b) and Section 2A-727(e),
takes subject to the existing lease contract.

(b) A lessee with a voidable leasehold interest acquired in a lease
transaction from a lessor that has relinquished possession or control has power to
transfer a good leasehold interest to a good faith buyer for value or a good faith
sublessee for value unless the lessor regains possession or control, but only to the
extent provided in subsection (a).

(c) For purposes of this section, a purchase includes a lease in which:

(1) the lessor was deceived as to the identity of the lessee;

(2) the delivery was in exchange for a check later dishonored; or

(3) the delivery was procured through fraud punishable under criminal
law.

(d) A buyer in the ordinary course of business or a sublessee in the ordinary
course of business from a lessee that is a merchant dealing in goods of that kind to
which the goods were entrusted by the lessor obtains, to the extent of the interest
transferred, all of the rights of the lessor and lessee to the goods and takes free of the existing lease contract.

(e) A buyer or sublessee from the lessee of goods that are subject to an existing lease contract and are covered by a certificate of title issued under a statute of this State or of another jurisdiction takes no greater rights than those provided both by this section and by the certificate-of-title statute. (Section 2-504)

SECTION 2A-406. PRIORITY OF CERTAIN LIENS ARISING BY OPERATION OF LAW. If a person in the ordinary course of its business furnishes services or materials with respect to goods subject to a lease contract, a lien upon those goods in the possession of that person given by statute or rule of law for those materials or services has priority over any interest of the lessor or lessee under the lease contract or this article unless the lien is created by statute and the statute provides otherwise, or the lien is created by rule of law and the rule of law provides otherwise.

SECTION 2A-407. PRIORITY OF LIENS ARISING BY ATTACHMENT OR LEVY ON, SECURITY INTERESTS IN, AND OTHER CLAIMS TO GOODS.

(a) Except as otherwise provided in Section 2A-406, a creditor of a lessee takes subject to the lease contract.

(b) Except as otherwise provided in subsections (c) and (d) and Sections 2A-406 and 2A-408, a creditor of a lessor takes subject to the lease contract unless:

(1) the creditor holds a lien that attached to the goods before the lease contract became enforceable;
(2) the creditor holds a security interest in the goods and the lessee did
not give value and receive delivery of the goods without knowledge of the security
interest; or

(3) the creditor holds a security interest in the goods which was
perfected under Article 9 before the lease contract became enforceable.

(c) A lessee in the ordinary course of business takes the leasehold interest
free of a security interest in the goods created by the lessor even if the security
interest is perfected under Article 9 and the lessee knows of its existence.

(d) A lessee other than a lessee in the ordinary course of business takes a
leasehold interest free of a security interest to the extent that it secures future
advances made after the secured party acquires knowledge of the lease or more than
45 days after the lease contract becomes enforceable, whichever first occurs, unless
the future advances are made pursuant to a commitment entered into without
knowledge of the lease and before the expiration of the 45-day period.

Drafting Comment – January, 1997

Subsections (b)(2), (b)(3), (c), and (d) of Section 2A-407 will be included in
Article 9 when the Article 9 revision is complete. The Article 9 package of
amendments should include repeal of those parts of Section 2A-407. The Article 9
Drafting Committee will be told that the Article 2A Committee is happy with the
substance of the rules be transferred to Article 9.

SECTION 2A-408. SPECIAL RIGHTS OF CREDITORS.

(a) Except as otherwise provided in subsections (b) and (c), the rights of
creditors of the lessor with respect to goods identified to a lease contract and
retained by the lessor are subject to the lessee’s rights under Sections 2A-709,
2A-723(d), and 2A-738 if the lessee’s rights vest before a creditor’s claim in rem
attaches to the goods.

(b) A creditor of a lessor which has retained possession of goods subject to
a lease contract may treat the lease contract as void or voidable if, as against the
creditor, retention of possession by the lessor is fraudulent or void or voidable under any statute or rule of law. However, it is not fraudulent for a lessor, for a commercially reasonable time after the goods are identified to the lease to retain possession in good faith and current course of trade.

(c) Except as otherwise provided in subsection (a), this article does not impair the rights of a creditor of the lessor in a case in which identification to the lease contract or delivery is made other than in current course of trade but in satisfaction of or as security for a preexisting claim for money, security, or the like and under circumstances such that the transaction would constitute a fraudulent transfer or voidable preference under a statute or rule of law other than this section.

(d) A creditor of a seller may treat a sale or an identification of goods to a contract for sale as void or voidable if, as against the creditor, retention of possession by the seller is fraudulent or void or voidable under any statute or rule of law. However, it is not fraudulent for a seller to retain possession of the goods pursuant to a lease contract entered into by the seller as lessee and the buyer as lessor in connection with the sale or identification of the goods if the buyer bought for value and in good faith. (Section 2-505)

Drafting Comment – June, 1997

The coordination group, at its May, 1997, meeting, suggested that the reference to Article 9 is not necessary. In present Section 2A-308 there is no reference to Article 9.

SECTION 2A-409. RIGHTS OF LESSOR AND LESSEE WHEN GOODS BECOME FIXTURES.

(a) In this section:

(1) “Encumbrance includes a real estate mortgage, other lien on real estate, and any other right in real estate which is not an ownership interest.
(1) “fixtures” means goods that have become so related to particular real estate that an interest in them arises under real estate law;

(2) “fixture filing” means a filing, in the office where a mortgage on the real estate would be filed or recorded, of a financing statement covering goods that are or are to become fixtures and conforming to the requirements of Section 9-502(a);

(3) “purchase money lease” means a lease in which the lessee does not have possession or use of the goods or the right to possession or use of the goods [before] [until] the lease agreement is enforceable;

(4) A mortgage is a “construction mortgage to” the extent that it secures an obligation incurred for the construction of an improvement on land including the acquisition cost of the land, if the recorded record so indicates.

(b) A lease under this article may be of goods that are fixtures or may continue in goods that become fixtures, but there may be no lease under this article of ordinary building materials incorporated into an improvement on land.

(c) This article does not prevent creation of a lease of fixtures under real estate law.

(d) The perfected interest of a lessor of fixtures has priority over a conflicting interest of an encumbrancer or owner of the real estate if:

(1) except as otherwise provided in subsection (f), the lease is a purchase money lease, the interest of the encumbrancer or owner arises before the goods become fixtures, the interest of the lessor is perfected by a fixture filing before the goods become fixtures or within 10 days thereafter, and the lessee has an interest of record in the real estate or is in possession of the real estate; or

(2) the interest of the lessor is perfected by a fixture filing before the interest of the encumbrancer or owner is of record, the lessor’s interest has priority
over any conflicting interest of a predecessor in title of the encumbrancer or owner,
and the lessee has an interest of record in the real estate or is in possession of the
real estate.

(e) The interest of a lessor of fixtures, whether or not perfected, has priority
over the conflicting interest of an encumbrancer or owner of the real estate if:

(1) the fixtures are readily removable factory or office machines, readily
removable equipment that is not primarily used or leased for use in the operation of
the real estate, or readily removable replacements of domestic appliances that are
goods subject to a consumer lease, and before the goods become fixtures the lease
contract is enforceable; or

(2) the conflicting interest is a lien on the real estate obtained by legal or
equitable proceedings after the lease contract is enforceable; or

(3) the encumbrancer or owner has, in a [signed] [authenticated] record,
consented to the lease or has disclaimed an interest in the goods as fixtures; or

(4) the lessee has a right to remove the goods as against the
encumbrancer or owner. If the lessee’s right to remove terminates, the priority of
the interest of the lessor continues for a reasonable time.

(f) Subject to subsections (d) and (e), the interest of a lessor of fixtures,
including the lessor’s residual interest, is subordinate to the conflicting interest of
an encumbrancer of the real estate under a construction mortgage recorded before
the goods become fixtures if the goods become fixtures before the completion of
the construction. To the extent that it is given to refinance a construction mortgage,
a mortgage has this priority to the same extent as the construction mortgage.

(g) In cases not within subsections (c) through (g), priority between the
interest of a lessor of fixtures, including the lessor’s residual interest, and the
conflicting interest of an encumbrancer or owner of the real estate who is not the
lessee is determined by the priority rules governing conflicting interests in real estate.

(h) If the interest of a lessor of fixtures, including the lessor’s residual interest, has priority over all owners and encumbrancers of the real estate, the lessor or the lessee may on default, expiration, termination, or cancellation of the lease contract but subject to the lease agreement and this article, or if necessary to enforce other rights of the lessor or lessee under this article, remove the goods from the real estate, free and clear of all conflicting interests of all owners and encumbrancers of the real estate. However, the lessor or lessee shall reimburse any encumbrancer or owner of the real estate that is not the lessee and who has not otherwise agreed for the cost of repair of any physical injury, but not for any diminution in value of the real estate caused by the absence of the goods removed or by any necessity of replacing them. A person entitled to reimbursement may refuse permission to remove until the party seeking removal gives adequate security for the performance of this obligation.

(i) Even if the lease agreement does not create a security interest, the interest of a lessor of fixtures, including the lessor’s residual interest, is perfected by filing a financing statement as a fixture filing for leased goods that are or are to become fixtures in accordance with the relevant provisions of Article 9.

SECTION 2A-410. LESSOR’S AND LESSEE’S RIGHTS WHEN GOODS BECOME ACCESSIONS.

(a) “Accession” mean goods that [are [installed in or affixed to other goods] [physically united with other goods in a manner such that the identity of the original goods is lost].
(b) Except as provided in subsection (d), the interest of a lessor or a lessee under a lease contract entered into before the goods an accession is superior to all interests in the whole.

(c) Except as provided in subsection (d) the interest of a lessor or a lessee under a lease contract entered into at the time or after the goods became accessions is valid against all persons subsequently acquiring interests in the whole but is invalid against any person with an interest in the whole which has not, in a record consented to the lease or disclaimed an interest in the goods as part of the whole.

(d) The interest of a lessor or a lessee under a lease contract described in subsection (b) or (c) is subordinate to the interest of

(1) a buyer in the ordinary course of business or a lessee in the ordinary course of business of any interest in the whole acquired after the goods became accessions; or

(2) a creditor with a security interest in the whole perfected before the lease contract was made to the extent that the creditor makes subsequent advances without knowledge of the lease contract.

(e) If under this section a lessor or lessee holds an interest in accessions which has priority over the claims of all persons that have interests in the whole, the lessor or lessee may on default, expiration, termination, or cancellation of the lease contract by the other party but subject to the provisions of the lease contract and this article or, if necessary to enforce other rights under this article, remove the goods from the whole. However, the lessor or lessee shall reimburse any holder of an interest in the whole which is not the lessee and which has not otherwise agreed for the cost of repair of any physical injury but not for any diminution in value of the whole caused by the absence of the goods removed or by any necessity for replacing them. A person entitled to reimbursement may refuse permission to
remove the goods until the party seeking removal gives adequate security for the
performance of this obligation.

Drafting Note – May, 1997

The April 14, 1997 draft of Article 9 has completely rewritten and
substantially changed the substance of its accessions section (Section 9-332). The
new draft treats all parts of the whole as separate accessions when a new part
subject to a separate security interest is added. If, for example, SP-1 has a security
interest in a tractor and SP-2 has a security interest in a new engine added to the
tractor, both SP-1 and SP-2 now have an accession interest. Carrying out that line
of thought, the accessions section states that other provisions of Article 9 determine
priorities between the two parties. The new section also provides that a security
interest in an accession loses to a security interest in the whole that is perfected by
compliance with a certificate of title law.

Since Article 2A cannot leave priority issues to other provisions of Article
2A, Article 2A probably should continue its present accession rules. If so, the
Committee should reject the alternative underlined definition of accession se out
above.

The Committee should consider whether it wishes to permit persons who
deal with the whole through certificates of title to take priority over a lessor’s
interest in accessions to the certificate of title goods.

A copy of new Section 9-332 is attached to the notes accompanying this
draft.

SECTION 2A-411. PRIORITY SUBJECT TO SUBORDINATION.

Nothing in this article prevents subordination by agreement by any person entitled
to priority.
PART 5
WARRANTIES

SECTION 2A-501. DEFINITIONS. In this part:

(1) “Damage” means all loss resulting in the ordinary course from a breach of warranty, including injury to a person or property as permitted in Section 2A-707.

(2) “Goods” includes a component incorporated in substantially the same condition in other goods.

(3) “Immediate lessee” means a lessee in privity of contract with the lessor.

(4) “Remote lessee” means a lessee from a lessor other than the lessor or seller against which a claim for breach of warranty is asserted.

(5) “Representation” means a description, demonstration, or depiction of the goods, an affirmation of fact relating to the goods, or a sample or model of the goods.

Drafting Comment – June, 1997

The definition of representation is moved from Section 2A-503.

(Section 2-401)

SECTION 2A-502. WARRANTY AGAINST INTERFERENCE AND AGAINST INFRINGEMENT; LESSEE’S OBLIGATION AGAINST INFRINGEMENT.

(a) Except in a finance lease, a lessor in a lease contract warrants that, except for claims by any person by way of infringement or the like, for the duration of the lease no person holds a:

(1) claim to or interest in the goods which will interfere with the lessee’s enjoyment of its leasehold interest, or
(2) colorable claim to or interest in the goods which will unreasonably expose the lessee to litigation.

(b) A finance lessor warrants that, except for claims by way of infringement or the like, for the duration of the lease no person holds a:

(1) claim or interest in the goods that arose from an act or omission of the lessor which will interfere with the lessee’s enjoyment of its leasehold interest, or

(2) colorable claim to or interest in the goods that arose from an act or omission of the lessor which will unreasonably expose the lessee to litigation.

(c) Except in a finance lease, a lessor that is a merchant regularly dealing in goods of the kind warrants that the goods will be delivered free of the rightful claim of a third party by way of infringement or the like. However, a lessee that furnishes specifications to the lessor holds the lessor harmless against any claim of infringement or the like that arises out of compliance with the specifications.

(d) A warranty under subsections (a) through (c) may be disclaimed or modified only by express language or by circumstances giving the lessee reason to know that the lessor purports to transfer only such right as the lessor or a third party may have. In an electronic transaction that does not involve review of the record by an individual, language is sufficient if it is conspicuous and related to the warranty against third party claims. Otherwise, language in a record is sufficient to disclaim warranties under this section if it is conspicuous and states “There is no warranty against third-party claims that may interfere with lessee’s enjoyment of his leasehold interest or against infringement in this lease”, or words of similar import.

(e) A lessor’s warranty under this section, made to an immediate lessee, extends to any remote lessee that may be reasonably expected to lease the goods and which suffers damage from breach of the warranty. The rights and remedies of
a remote lessee against the lessor for breach of the warranty are determined by the
terms of the contract between the lessor and the immediate lessee and this article.

(Section 2-402)

Drafting Comment

The warranties under present Section 2A-211 are too narrow. A non-
finance lessor presently warrants only against its own conduct which affects
lessee’s quite enjoyment of the lease, and finance lessors seem to make no warranty
even against their own acts, though a court could probably deal with that. Present
Section 2A-214(4) states the rules for disclaimer of warranties under this section.

At the February meeting, the Committee recommended that “colorable
claims be dealt with in a separate sentence. Is the above draft satisfactory?

SECTION 2A-503. EXPRESS WARRANTIES TO IMMEDIATE
LESSEE.

(a) If a lessor makes a representation or promise relating to the goods to an
immediate lessee the representation or the promise becomes part of the agreement,
unless a reasonable person in the position of the immediate lessee would not
believe that the representation or promise became part of the agreement or would
believe that the representation was merely of the value of the goods or purported to
be merely the seller’s opinion or commendation of the goods. An obligation may
be created under this section even though the lessor does not use formal words such
as “warranty or “guaranty.

(b) A representation or a promise that becomes part of the agreement is an
express warranty and the lessor has an obligation to the immediate lessee that the
goods will conform to the representation, or, if a sample is involved, that the whole
of the goods will conform to the sample, or that the promise will be performed.
The obligation is breached if the goods do not conform to any representation at the
time when tender of delivery was completed or if the promise was not performed
when due.
(c) A lessor’s obligation to the immediate lessee under this section may be created by representations and promises made in a medium for communication to the public, including advertising, if the immediate lessee has knowledge of them at the time of the agreement. (Section 2-403)

SECTION 2A-504. IMPLIED WARRANTY OF MERCHANTABILITY; USAGE OF TRADE.

(a) Except in a finance lease and subject to Section 2A-506, a lessor that is a merchant with respect to goods of that kind makes in a lease contract an implied warranty that the goods are merchantable.

(b) To be merchantable, goods at a minimum must:

(1) pass without objection in the trade under the contract description;

(2) in the case of fungible goods, be of fair, average quality within the description;

(3) be fit for the ordinary purposes for which goods of that description are used;

(4) run, within the variation permitted by the lease agreement, of even kind, quality, and quantity within each unit and among all units involved;

(5) be adequately contained, packaged, and labeled as the lease agreement or circumstances may require; and

(6) conform to promises or affirmations of fact made on the container or label, if any.

(c) Subject to 2A-506, implied warranties other than those described in this section may arise from course of dealing or usage of trade. (Section 2-404)
SECTION 2A-505. IMPLIED WARRANTY OF FITNESS FOR
PARTICULAR PURPOSE. Except in a finance lease and subject to Section
2A-506, if a lessor at the time of contracting has reason to know any particular
purpose for which the goods are required and that the lessee is relying on the
lessor’s skill or judgment to select or furnish suitable goods, there is an implied
warranty that the goods are fit for that purpose. (Section 2-405)

Drafting Comment – June, 1997

Section 2B-405 contains a special fitness warranty that components of an
integrated system will work together. See Section 2B-405(b). Should Article 2A
contain that warranty in addition to the general fitness warranty?

SECTION 2A-506. DISCLAIMER OR MODIFICATION OF
WARRANTY.

(a) Language or conduct relevant to the creation of an express warranty and
language or conduct tending to disclaim or modify an express warranty must be
construed wherever reasonable as consistent with each other. Subject to Section
2A-202 with regard to parol or extrinsic evidence, language or conduct disclaiming
or modifying an express warranty is ineffective to the extent that this construction is
unreasonable.

(b) Except as otherwise provided in subsection (c) or (e), an implied
warranty is disclaimed or modified by language or an expression that, under the
circumstances, makes it clear that the implied warranty has been disclaimed or
modified. An implied warranty may also be disclaimed or modified by course of
performance, course of dealing, or usage of trade.

(c) Except as otherwise provided in Section 2A-502(d) and subsection (e),
language in a record is sufficient to disclaim or modify an implied warranty if the
language is conspicuous and:
(1) in the case of the implied warranty of merchantability, mentions merchantability;

(2) in the case of the implied warranty of fitness, states that “the goods are not warranted to be fit for any particular purpose or words of similar import;

(3) unless the circumstances indicate otherwise, states that the goods are leased “as is” or “with all faults” or words of similar import.

(d) If a lessee before entering into a contract, has examined the goods, sample, or model as fully as desired or has declined to examine them, there is no implied warranty with regard to conditions that an examination in the circumstances would have revealed to the lessee.

(e) Language in a consumer lease contract is sufficient to disclaim or modify an implied warranty only if:

(1) At the time of contracting, a lessor in good faith passes through to a lessee an express warranty obligation created by a seller under Section 2-408(a) that is reasonable in scope, duration and remedies and there is conspicuous language in a record stating, for example, “You are receiving an express warranty obligation from the [manufacturer] instead of any implied warranty of merchantability or fitness from us;” or

(2) Conspicuous language is in a record which language the consumer lessee has separately authenticated [expressly agreed] states: “Unless we say otherwise in the contract, we make no promises about the quality or usefulness of what you are leasing. They may not work. They may not be fit for any specific purpose you may have in mind.

(f) Remedies for breach of warranty may be limited in accordance with this article with respect to liquidation or limitation of damages and contractual modification of remedy. (Section 2-406)
SECTION 2A-507. CUMULATION AND CONFLICT OF WARRANTIES. Warranties, whether express or implied, must be construed as consistent with each other and as cumulative. However, if that construction is unreasonable, the intention of the parties determines which warranty prevails. In ascertaining that intention, the following rules apply:

(1) Exact or technical specifications prevail over an inconsistent sample, model or demonstration or general language of description.

(2) A sample, model or demonstration prevails over inconsistent general language of description.

(3) Except in a consumer lease, an express warranty prevails over inconsistent implied warranties other than an implied warranty of fitness for a particular purpose. (Section 2-407)

SECTION 2A-508. EXTENSION OF EXPRESS OR IMPLIED WARRANTY.

(a) A lessor’s express warranty under Section 2A-503 or implied warranty under Section 2A-504 made to an immediate lessee extends to any transferee, and in the case of a consumer transferee, to anyone in the family or household of the remote transferee, that may reasonably be expected to use or be affected by the goods and is damaged breach of warranty. The rights and remedies of the transferee or members of the transferees family or household against the lessor for breach of a warranty extended under this subsection are determined by the terms of the contract between the lessor and the immediate lessee. However, the lessor is not be liable for consequential loss profits for breach of warranty under this section.

(b) This section and Section 2A-502 do not:
(1) diminish the rights and remedies of a third-party beneficiary or
assignee under the law of contracts or of persons to which goods are transferred by
operation of law; or
(2) displace principles of law and equity that extend an express or
implied warranty to or for the benefit of a remote transferee, or other person.
(c) The operation of this section may not be excluded, modified, or limited
unless the lessor has a substantial interest based on the nature of the goods in
having a warranty extend only to the immediate lessee.

Drafting Note
At the February, 1997, meeting, the Article 2A Committee voted to delete
references to remote lessees in this section. (Section 2-409)

See May, 1997 Draft of Article 2, pages 74-76 for a discussion of the above
provision.
PART 6
PERFORMANCE OF LEASE CONTRACT:
REPUDIATED, SUBSTITUTED, AND EXCUSED

SECTION 2A-601. RIGHT TO ADEQUATE ASSURANCE OF
PERFORMANCE.

(a) A lease contract imposes an obligation on each party not to impair the
other’s expectation of receiving due performance. If reasonable grounds for
insecurity arise with respect to the performance of either party, the other party may
demand in a record adequate assurance of due performance and, until that assurance
is received, if commercially reasonable, may suspend any performance for which
the agreed return has not already been received.

(b) Between merchants, the reasonableness of grounds for insecurity and
the adequacy of any assurance offered is determined according to commercial
standards.

(c) Acceptance of improper delivery or payment does not prejudice an
aggrieved party’s right to demand adequate assurance of future performance.

(d) After receipt of a demand under subsection (a), failure to provide within
a reasonable time, not exceeding 30 days, assurance of due performance which is
adequate under the circumstances of the particular case is a repudiation of the
contract under Section 2A-602. (Section 2-711)

SECTION 2A-602. ANTICIPATORY REPUDIATION.

(a) If either party to a lease contract repudiates a performance not yet due
and the loss of performance will substantially impair the value of the lease contract
to the other, the aggrieved party may:
(1) await performance by the repudiating party for a commercially reasonable time, or resort to any remedy for default under the lease contract or this article, even if it has urged the repudiating party to retract the repudiation or has notified the repudiating party that it would await the agreed performance; and

(2) in either case, suspend its own performance or, if a lessor, proceed in accordance with Section 2A-719.

(b) Repudiation includes language that one party will not or cannot make a performance still due under the contract or voluntary affirmative conduct that reasonably appears to the other party to make a future performance impossible.

(Section 2-712)

Drafting Comment – January, 1997

The final text will contain a Comment noting that a failure to give assurances under Section 2A-402 is a repudiation giving the other party the rights given by this section. Note the added language in Section 2A-601 which also makes the point.

SECTION 2A-603. RETRACTION OF ANTICIPATORY REPUDIATION.

(a) A repudiating party may retract a repudiation until its next performance is due unless the aggrieved party, after the repudiation, has canceled the lease contract, materially changed its position, or otherwise indicated that the repudiation is considered to be final.

(b) Retraction may be by any method that clearly indicates to the aggrieved party that the repudiating party intends to perform the contract. However, a retraction must include any assurance justifiably demanded under Section 2A-601.

(c) Retraction reinstates a repudiating party’s rights under the lease contract with due excuse and allowance to the aggrieved party for any delay caused by the repudiation. (Section 2-713)
SECTION 2A-604. SUBSTITUTED PERFORMANCE.

(a) If, without the fault of the lessee, lessor, or supplier, agreed berthing, loading, or unloading facilities, or an agreed type of carrier becomes unavailable, or an agreed manner of delivery otherwise becomes commercially impracticable, an aggrieved party [the lessor or supplier] may claim excuse under Section 2A-605 unless a commercially reasonable substitute is available. In that case, reasonable substitute performance must be tendered and accepted.

(b) If an agreed means or manner of payment fails because of domestic or foreign governmental regulation, the lessor may withhold or stop delivery or cause the supplier to withhold or stop delivery until the lessee provides a means or manner of payment which is commercially a substantial equivalent. If delivery has already been made, payment by the means or in the manner provided by the regulation discharges the lessee’s obligation unless the regulation is discriminatory, oppressive, or predatory. (Section 2-715)

SECTION 2A-605. EXCUSE BY FAILURE OF PRESUPPOSED CONDITIONS.

(a) Subject to Section 2A-604 and subsection (b), delay in performance or nonperformance by the lessor or supplier is not a default under the lease contract if performance as agreed has been made impracticable by:

(1) the occurrence of a contingency whose nonoccurrence was a basic assumption on which the lease contract was made; or

(2) compliance in good faith with any applicable foreign or domestic governmental regulation, statute, or order, whether or not it later proves to be invalid.
(b) A party claiming excuse under subsection (a) shall seasonably notify the other party that there will be delay in performance. If the claimed excuse affects only a part of the lessor’s or supplier’s capacity to perform, the lessor or supplier shall also allocate production and deliveries among its customers in a manner that is fair and reasonable and notify the lessee of the estimated quota made available. However, the lessor or supplier may include regular customers not them under contract as well as its own requirements for further manufacture. (Section 2-716)

Drafting Comment – May, 1997
This is the latest Article 2 version of Section 2-716.

SECTION 2A-606. PROCEDURE ON NOTIFICATION CLAIMING EXCUSE.

(a) A lessee that receives notification of a material or indefinite delay in performance or an allocation permitted under Section 2A-307 or 2A-605 as to any delivery concerned, or of there is a breach of the whole contract under Section 2A-726(c), by notification in a record may:

(1) terminate and thereby discharge any unexecuted portion of the lease contract; or

(2) except in a finance lease that is not a consumer lease, modify the contract by accepting the available allocation in substitution [with due allowance from the rent payable for the balance of the lease term for the deficiency but without further right against the lessor.]

(b) If, after receipt of a notification from a lessor under Section 2A-307 or 2A-605, the lessee fails to terminate or modify the lease contract within a reasonable time not exceeding 30 days, the contract lapses with respect to any performance affected.
(c) This section may be varied by agreement only to the extent that the parties have assumed a different obligation under Sections 2A-604 and 2A-605. (Section 2-717)

SECTION 2A-607. IRREVOCABLE PROMISES: FINANCE LEASES.

(a) In a finance lease that is not a consumer lease, the lessee’s promises under the lease contract become irrevocable and independent upon the lessee’s acceptance of the goods.

(b) A promise that has become irrevocable and independent under subsection (a):

(1) is effective and enforceable between the parties and by or against third parties including assignees of the parties; and

(2) is not subject to cancellation, termination, modification, repudiation, excuse, or substitution without the consent of the party to which the promise runs.

(c) This section does not affect the validity under any other law of a covenant in any lease agreement making the lessee’s promises irrevocable and independent upon the lessee’s acceptance of the goods.
PART 7
DEFAULT

[A. GENERAL]

SECTION 2A-701. SUBJECT TO GENERAL LIMITATIONS. The remedies of the lessee and lessor and other protected persons under this article are subject to the general limitations and principles stated in Sections 2A-702 through 2A-715. (Section 2-801)

SECTION 2A-702. DEFAULT: PROCEDURE.

(a) Whether the lessor or the lessee is in default under a lease contract is determined by the [lease agreement and this article] [the contract].

(b) If the lessor or the lessee is in default under the lease contract, the aggrieved party

(1) has the rights provided in this article and, except as limited by this article, as provided in the lease agreement.

(2) may reduce its claim to judgment, or otherwise enforce the lease contract by self-help or any available administrative or judicial procedure or the like, including, if agreed to by the parties, arbitration .

(c) If the lease agreement covers both real property and goods, the party seeking enforcement may proceed under this part as to the goods, or under other applicable law as to both the real property and the goods in accordance with that party’s rights and remedies in respect of the real property, in which case this part does not apply.
(d) To determine whether the value of an installment or the whole contract has been substantially impaired by a default under Section 2A-602, 2A-726, or 2A-733, the court may consider whether:

(1) the aggrieved party has been deprived of the benefit that it reasonably expected under the contract;

(2) cure of the default is permitted and likely;

(3) adequate assurance of due performance has been given; and

(4) the defaulting party acted in good faith.

(e) The cumulative effect of individual, insubstantial defaults may substantially impair the value of the whole contract to the other party. (Sections 2-70 and 2-802)

Drafting Comment – May, 1997

Subsections (c) and (d) come from Section 2-702(c) and (d) in the April Article 2 draft. We have not so far included subsection (c) in Article 2A. The cited sections in subsection (c) deal with repudiation, rejection in installment contracts, and revocation of acceptance. There is some reason to define substantial impairment in the context of those sections.

Article 2A has not so far included subsection (b) of Section 2-701 which reads:

“(b) A breach of contract occurs in the following circumstances, among others:

(1) A seller is in breach if it fails to deliver or perform an obligation, makes a nonconforming tender of performance, or repudiates the contract.

(2) A buyer is in breach if it wrongfully rejects a tender of delivery, wrongfully revokes acceptance, repudiates the contract, or fails to make a required payment or to perform an obligation.

It seems unnecessary to define the things mentioned in subsection (b) as breaches (or defaults).

Section 2-701 now says that whether a party is in breach is determined by the contract. Since contract is defined as the total legal obligation arising from agreement, saying that default is determined by the agreement and this article, as Article 2A does, is the same as saying is determined by the contract. But there may be reasons of emphasis to continue the present language.
SECTION 2A-703. WAIVER OF DEFAULT; PARTICULARIZATION OF NONCONFORMITY.

(a) Except as otherwise provided in subsections (b) and (c), a party that knows that the other party’s performance constitutes a default [or breach of warranty] but accepts that performance and fails within a reasonable time to object is precluded from relying on the default to cancel the contract. Except as provided in subsections (b) and (c), acceptance of that performance and failure to object do not preclude a claim for damages unless the party in breach has changed its position reasonably and in good faith in reliance of the aggrieved party’s inaction.

(b) A lessee’s failure to state, in connection with a rejection under Section 2A-725, a particular nonconformity that is ascertainable by reasonable inspection precludes reliance on the unstated nonconformity to justify rejection or to establish default if:

(1) the lessor, upon a seasonable particularization, had a right to cure under Section 2A-729 and would have cured the nonconformity; or

(2) between merchants, the lessor or the supplier after rejection has made a request in a record for a full and final statement in a record of all nonconformities on which the lessee proposes to rely.

(c) A lessee’s failure to state, in connection with a revocation of acceptance under Section 2A-7, the nonconformity that justifies the revocation precludes the lessee from relying on the nonconformity to justify the revocation or to establish default if the lessor had a right to cure the default under Section 2A-730 and [would] [could] have cured the breach. (Section 2-702)

Drafting Comment – May, 1997

Section 2A-703 was Section 2A-730 in the previous draft. The section has been moved here because subsection (a) now applies to lessors as well as lessees. Present Section 2A-514, which is based on present Section 2-605 deals only with lessee’s failure to state defects on rejection. Is Section 2A-703(a) inconsistent with
Section 2A-703 which states that a lessor or lessee in default is not entitled to notice of default? Should the section be combined with Section 2A-703?

SEC 2A-704. NOTICE AFTER DEFAULT. Except as otherwise provided in this article or the lease agreement, a lessor or lessee in default under a lease contract is not entitled to notice of default or notice of enforcement from the other party.

SEC 2A-705. REMEDIES IN GENERAL.

(a) Unless the lease contract provides for liquidated damages under Section 2A-710 or a limited remedy enforceable under Section 2A-711, an aggrieved party may not recover that part of a loss resulting from a default that could have been avoided by reasonable measures under the circumstances. The burden of establishing a failure to take reasonable measures under the circumstances is on the defaulting party.

(b) The rights and remedies provided in this article are cumulative, but a party may not recover more than once for the same injury. Unless the agreement provides for liquidated damages or a limited remedy enforceable under Section 2A-710 or 2A-711, a court may deny or limit a remedy if, under the circumstances, it would put the aggrieved party in a substantially better position than if the other party had fully performed.

(c) This article does not impair a remedy for breach of any obligation or promise collateral or ancillary to a lease contract. (Section 2-803)

SEC 2A-706. MEASUREMENT OF DAMAGES IN GENERAL. If there is a default, the aggrieved party may recover compensation as determined by Sections 2A-717 through 2A-737 or recover compensation for the loss resulting in
the ordinary course from the default as determined in any reasonable manner,
together with incidental damages and consequential damages, less expenses and
costs avoided as a result of the default. (Section 2-804)

Drafting Comment

The final version of Article 2A will contain a Comment discussing some
cases to which the rules of this section would be applicable and perhaps a reference
to DeKoven’s Article on Puritan Leasing.

SECTION 2A-707. INCIDENTAL DAMAGES. Incidental damages
resulting from a default under a lease contract include compensation for any
commercially reasonable charges, expenses, or commissions with respect to:

(1) inspection, receipt, transportation, care, or custody of identified goods
which are the subject of the lease contract;

(2) stopping delivery or shipment;

(3) effecting cover, return, or disposition of the goods;

(4) reasonable efforts otherwise to minimize or avoid the consequences of
default; and

(5) otherwise dealing with the goods or effectuating other remedies.
(Section 2-805)

SECTION 2A-708. CONSEQUENTIAL DAMAGES.

(a) Consequential damages resulting from a default include compensation
for:

(1) any loss, including loss to property other than the goods leased,
which the defaulting party at the time of contracting had reason to know would
probably result from the aggrieved party’s general or particular requirements and
needs and which could not have been avoided by reasonable measures under the
circumstances; and
(2) injury to person proximately resulting from any breach of warranty.

(b) The aggrieved party may not recover any consequential damages pursuant to subsection (a)(1) that result in disproportionate compensation to the aggrieved party. The breaching party has the burden of establishing that the consequential damages under subsection (a)(1) result in disproportionate compensation to the aggrieved party. (Section 2-806)

SECTION 2A-709. SPECIFIC PERFORMANCE.

(a) A court may enter a decree for specific performance if the parties have expressly agreed to that remedy the goods or the agreed performance of the defaulting party are unique or in other proper circumstances. Even if the parties expressly agree to specific performance, a court shall not enter a decree for specific performance where the breaching party’s sole remaining contractual obligation is the payment of money.

(b) A decree for specific performance may include terms and conditions as to payment of the rent, damages, or other relief the court considers just. (Section 2-807)

Drafting Comment

Article 2 has now adopted the rule that if the only remaining performance is the payment of money, specific performance is not available. Should Article 2A adopt the same rule? That rule probably would not prohibit specific performance actions for rent in most cases since lessees are likely to have obligations other than payment. Should we continue our earlier rule that specific performance actions for rent are not available unless the conditions of Section 2A-723 are satisfied. If we did that, specific performance actions would be available if the lessee does not return the goods, the goods have been damaged after risk of loss had passed to the lessee, or the lessor is unable to resell or relet. Perhaps we should have a flat rule that an obligation to pay money cannot be enforced by a decree for specific performance.

Following Article 2, subsection (c) has been moved to Section 2A-737 which covers lessee’s right to get the goods from lessor.
SECTION 2A-710. CANCELLATION; EFFECT.

(a) An aggrieved party may cancel a contract if the conditions of Section 2A-717 or 2A-725 are satisfied or the agreement so provides unless there is a waiver of the breach under Section 2A-302 or a right to cure the breach under Section 2A-730.

[(b) Cancellation is not effective until the canceling party sends notice of cancellation to the defaulting party.]

(c) Upon cancellation, the lessee is subject to the same obligations and duties with respect to goods in its possession or control as the lessee would be if it had rejected a nonconforming tender and remained in control of the goods of the lessor or if the lease contract had terminated according to its own terms.

(d) Except as otherwise provided in subsection (e), upon cancellation, all obligations that are still executory on both sides are discharged.

(e) The obligations surviving cancellation include:

(1) a right based on previous default or performance;

(2) any term limiting disclosure of information;

(3) a remedy for default on the whole contract or any unperformed balance;

(4) an obligation to return or dispose of goods

(5) a choice of law or forum;

(6) an obligation to arbitrate or otherwise resolve disputes through alternative dispute resolution procedures;

(7) a term limiting the time for commencing an action or for providing notice,

[(8) other rights, remedies, or limitations if in the circumstances such survival is necessary to achieve the purposes of the parties.]
(f) Unless a contrary intention clearly appears, language of cancellation, rescission, or avoidance of the lease contract, or similar language is not a renunciation or discharge of any claim in damages for an antecedent default.

(Section 2-808)

Drafting Comment – May, 1997

Subsection (a) does not follow exactly Article 2. Article 2 provides that there is a right to cancel if there is a breach under Section 2-701 or 2-710 (right to reject). It is probably better to refer to the basic remedies sections for lessor and lessee which include a reference to the right to cancel. Therefore, Article 2A refers to those sections, Sections 2A-718 and 2A-726 rather than to the rejection sections.

Subsection (e)(6) is an attempt to follow the direction of the Article 2A Drafting Committee that it be made clear that the specific listing is not exclusive. There is probably a better way to make the point. Possibly a Comment would be sufficient. The Article 2 Drafting Committee has not chosen to adopt subsection (e)(6). Subsection (e)(5) does not appear in Article 2, but it may be desirable in the lease context.

SECTION 2A-711. LIQUIDATION OF DAMAGES; DEPOSITS.

(a) Damages for default or any other act or omission, including indemnity for loss or diminution of anticipated tax benefits or loss or damage to lessor’s residual interest, may be liquidated but only at an amount or by a formula that is reasonable in light of either the actual loss or the then anticipated loss caused by the default or other act or omission. If a term liquidating damages is unenforceable under this subsection, the aggrieved party has the remedies provided in this article.

(b) If a lessor justifiably withholds or stops performance because of the lessee’s default or insolvency, the lessee is entitled to restitution of the amount by which the sum of payments exceeds the amount to which the lessor is entitled under a term liquidating damages in accordance with subsection (a).

(c) A lessee’s right to restitution under subsection (b) is subject to offset to the extent that the lessor establishes a right to recover damages under the provisions of this article other than subsection (a) and the amount or value of any benefits
received by the lessee directly or indirectly by reason of the lease contract. (Section 2-809)

Drafting Comment – May, 1997

The ELA memorandum, page 42, asks that this section specifically state that a deposit must be returned unless the lessor proves a right to retain under a liquidated damages clause or actual damages. Is the rule made clearer by changing “payments” to “deposit” or to “deposits and other payments? A Comment will make the point.

Article 2A continues to follow original Article 2A in not making enforceability of liquidated damages clauses dependent on actual damages being difficult to ascertain. The Comments to present Section 2A-504 speak at some length to the point. Does the Committee wish to adhere to that original position. Article 2 continues to include difficulty of ascertaining actual damages as a factor.

ALTERNATIVE A

SECTION 2A-712. CONTRACTUAL MODIFICATION OF REMEDY.

(a) Except as otherwise provided in this article, the lease agreement may include rights and remedies for default in addition to or in substitution for those provided in this article and may limit or alter the measure of damages recoverable under this article.

(b) Resort to a remedy provided under this article or in the lease agreement is optional unless the remedy is expressly agreed to be exclusive. If circumstances cause an exclusive or limited remedy to fail of its essential purpose, or provision for an exclusive remedy is unconscionable, remedy may be pursued as provided in this article.

(c) Consequential damages may be liquidated under Section 2A-710, or may otherwise be limited, altered, or excluded unless the limitation, alteration, or exclusion is unconscionable. Limitation, alteration, or exclusion of consequential damages for injury to the person in the case of consumer goods is presumed to be unconscionable, but limitation, alteration, or exclusion of damages where the loss is commercial is not presumed to be unconscionable.
(d) Rights and remedies on default by the lessor or the lessee with respect
to any obligation or promise collateral or ancillary to the lease contract are not
impaired by this article.

ALTERNATIVE B

[SECTION 2A-712. CONTRACTUAL MODIFICATION OF REMEDY.]

(a) Subject to Section 2A-710 [and except as otherwise provided in this article], the following rules apply:

(1) A lease agreement may add to, limit, or substitute for the remedies
provided in this article, such as by limiting or altering the measure of damages
recoverable for default or limiting the lessee’s remedies to return of the goods and
repayment by the lessor of any amounts paid by the lessee under the lease contract
or to repair and replacement of nonconforming goods or parts by the lessor or
supplier.

(2) An agreed remedy under paragraph (1) may not operate to deprive
the aggrieved party of a minimum adequate remedy under the circumstances[, such
as restitution for any benefits conferred on the party in breach].

(3) Resort to an agreed remedy under paragraph (1) is optional.

However, if the parties expressly agree that the agreed remedy is exclusive, it is the
sole remedy.

(b) Subject to subsection (a)(2) if, because of a default or other
circumstances, an exclusive, agreed remedy fails substantially to achieve the
intended purposes of the parties, the following rules apply:

(1) In a lease contract other than a consumer lease contract, the
aggrieved party may resort to all remedies provided in this article, but an agreement
expressly providing that incidental or consequential damages, including those
resulting from the failure to provide the limited remedy, are excluded is enforceable
to the extent permitted under subsection (c).

(2) In a consumer lease contract, an aggrieved party may reject the
goods or revoke acceptance and, to the extent of the failure, may resort to all
remedies provided in this article, including the right to recover consequential or
incidental damages despite any term purporting to exclude or limit such remedies.

(c) Subject to subsection (b), consequential damages and incidental
damages may be limited or excluded by agreement, unless the limitation or
exclusion is unconscionable. Limitation of consequential damages for injury to the
person in the case of a consumer is presumed to be unconscionable]. (Section
2-810)

Drafting Comment – May 1997
At the February, 1997, the Article 2A Drafting Committee voted to reinstate
the present Article 2A section on modification of remedy. That is done here. The
present Article 2A section is alternative A. The revised Article 2 provision is
alternative B.

SECTION 2A-713. REMEDIES FOR MISREPRESENTATION OR
FRAUD. Remedies for material misrepresentation or fraud include all remedies
available under this article for nonfraudulent default. Rescission or a claim for
rescission of a lease contract and rejection or return of the goods do not bar a claim
for damages or other consistent remedy. (Section 2-811)

Drafting Comment – May, 1997
In present Article 2A this section is a subsection of the section on
cancellation (see Section 2A-707(g) in the Nov. 24, 1996 draft).

SECTION 2A-714. PROOF OF MARKET RENT.

(a) Damages based on market rent are determined according to the rent for
the use of the goods concerned for a lease term identical to the remaining period of
the original lease agreement and prevailing at the times specified in Sections 2A-723 and 2A-736.

(b) If evidence of rent for the use of the goods concerned for a period identical to the remaining period of the original lease agreement and prevailing at the times or places described in this article is not readily available, the following rules apply:

(1) The rent prevailing within any reasonable time before or after the time described may be used.

(2) The rent prevailing at any other place or for a different lease period which in commercial judgment or usage of trade is a reasonable substitute may be used, making proper allowance for the difference, including the cost of transporting the goods to or from the other place.

(c) Evidence of a relevant rent prevailing at another time or place or for a lease period other than the one described in this section offered by one party is not admissible unless the party has given the other party notice that the court finds sufficient to prevent unfair surprise.

(d) If the prevailing rent or value of goods regularly leased in any established market is in dispute, reports in official publications or trade journals or in newspapers, periodicals, or other means of communication in general circulation and published as the reports of that market are admissible in evidence. The circumstances of the preparation of such a report may be affect the weight of the evidence but not its admissibility. (Section 2-812)

SECTION 2A-715. LIABILITY OF THIRD PARTIES FOR INJURY TO GOODS.
(a) If a third party deals with goods identified to a lease contract and causes actionable injury to the goods, the lessor has a right of action against the third party, and the lessee has a right of action against the third party, if the lessee:

1. has a security interest in the goods;
2. has an insurable interest in the goods; or
3. bears the risk of loss under the lease contract or has since the injury assumed that risk as against the lessor and the goods have been converted or destroyed.

(b) If at the time of the injury the plaintiff did not bear the risk of loss as against the other party to the lease contract and there is no arrangement between them for disposition of the recovery, any recovery or settlement is, subject to the plaintiff’s interest as fiduciary for the other party to the lease contract.

(c) Either party with the consent of the other may maintain an action for the benefit of an interested party. (Section 2-813)

Drafting Comment – January, 1997

The final text will contain a Comment that “injury to the goods” includes a breach which does not physically harm the goods, but which causes loss to one or more of the parties who have an interest in the goods.

SECTION 2A-716. STATUTE OF LIMITATIONS.

(a) An action for default under a lease contract, including breach of warranty or indemnity, must be commenced within four years after the right of action has accrued. Except in a consumer lease or an action for indemnity, the original lease agreement may reduce the period of limitations to not less than one.

(b) Except as otherwise provided in subsection (c), a right of action accrues when the act or omission on which the default or breach of warranty is based is or should have been discovered by the aggrieved party, or when the default occurs, whichever is later. A right of action for indemnity accrues when the act or
omission on which the claim for indemnity is based is or should have been
discovered by the indemnified party, whichever is later.

(c) If an action commenced within the applicable period of limitation is
terminated but a remedy by another action for the same default or breach of
warranty or indemnity is available, the other action may be commenced after the
expiration of the time limitation and within six months after the termination of the
first action unless the termination resulted from voluntary discontinuance or from
dismissal for failure to prosecute.

(d) This section does not alter the law on tolling of the statute of limitations
and does not apply to a right of action that accrued before this article took effect.
(Section 2-814)

Drafting Comment
Stricken subsection (c) does not appear in present Article 2A and has
disappeared from the Article 2 section.

[B. LESSOR’S REMEDIES]

SECTION 2A-717. LESSOR’S REMEDIES IN GENERAL.

(a) If a lessee wrongfully rejects or revokes acceptance of goods or fails to
make a payment when due or repudiates with respect to a part or the whole, the
lessee is in default under the lease contract with respect to any goods involved, and
with respect to all of the goods if under an installment lease contract the value of
the whole lease contract is substantially impaired, and the lessor may do one or
more of the following:

(1) withhold delivery of the goods and take possession of goods
previously delivered;
(2) stop delivery of the goods by any carrier or bailee pursuant to Section 2A-720(b);

(3) proceed under Section 2A-719 with respect to goods still unidentified to the lease contract;

(4) obtain specific performance under Section 2A-709 or recover the rent under Section 2A-723;

(5) dispose of the goods and recover damages under Section 2A-721 or retain the goods and recover damages under Section 2A-722;

(6) recover incidental and consequential damages under Sections 2A-707 and 2A-708;

(7) cancel the lease contract under Section 2A-710; or

(8) exercise any other rights or pursue any other remedies provided in the lease agreement.

(b) If a lessor does not fully exercise a right or obtain a remedy to which the lessor is entitled under subsection (a), the lessor may recover the loss resulting in the ordinary course of events from the lessee’s default as determined in any reasonable manner, together with incidental damages, less expenses avoided as a result of the lessee’s default.

(c) If a lessee is otherwise in default under a lease contract, the lessor may exercise the rights and pursue the remedies provided in the lease agreement, which may include a right to cancel the lease. In addition, except as otherwise provided in the lease agreement:

(1) if the default substantially impairs the value of the lease contract to the lessor, the lessor may exercise the rights and pursue the remedies under subsection (a) or (b); or
(2) if the default does not substantially impair the value of the lease contract to the lessor, the lessor may recover under subsection (b). (Section 2-815)

Drafting Comment – May, 1997

The expanded listing of rights on default follows the expanded listing in Article 2, but does not follow the sequence of Article 2 exactly.

SECTION 2A-718. LESSOR’S RIGHT TO POSSESSION OF GOODS.

(a) Upon a default by the lessee under a lease contract of the type described in Section 2A-717(a) or (c)(1) or, if agreed, upon other default by the lessee, the lessor may take possession of the goods. If the lease agreement so provides, the lessor may require the lessee to assemble the goods and make them available to the lessor at a place to be designated by the lessor which is reasonably convenient to both parties. Without removal, the lessor may render unusable any goods employed in trade or business and may dispose of goods on the lessee’s premises.

(b) A lessor may proceed under subsection (b) without judicial process if it can be done without breach of the peace, or the lessor may proceed by action. (Section 2-816)

Drafting Comment

In revised Article 2, subsection (a) is moved to the stoppage in transit section, should that be done here? I have done so.

SECTION 2A-719. LESSOR’S RIGHT TO IDENTIFY GOODS TO LEASE CONTRACT DESPITE DEFAULT OR TO SALVAGE UNFINISHED GOODS.

(a) Upon default by the lessee under the lease contract of the type described in Section 2A-717(a) or (c)(1) or, if agreed, after other default by the lessee, the lessor may:
(1) identify to the lease contract conforming goods not already identified if they are in the possession or control of the lessor or supplier at the time the lessor learned of the default; and

(2) dispose of goods that are shown to have been intended for the particular lease contract even if they are unfinished.

(b) If goods are unfinished at the time of default, an aggrieved lessor or the supplier, in the exercise of reasonable commercial judgment to minimize loss and for the purpose of effective realization, may complete the manufacture and wholly identify the goods to the lease contract, cease manufacture and lease, sell, or otherwise dispose of the goods for scrap or salvage value, or proceed in any other reasonable manner. (Section 2-817)

SECTION 2A-720. LESSOR'S REFUSAL TO DELIVER BECAUSE OF LESSEE’S INSOLVENCY; STOPPAGE IN TRANSIT OR OTHERWISE.

(a) A lessor that discovers that the lessee is insolvent may refuse to deliver the goods.

(b) Subject to subsection (d), a lessor may stop delivery of goods in the possession of a carrier or other bailee if the lessee is insolvent or repudiates or fails to make a payment due before delivery, whether for rent, security, or otherwise under the lease contract or if for any other reason the lessor has a right to withhold or reclaim the goods.

(c) As against a lessee under subsection (b), the lessor may stop delivery until:

(1) receipt of the goods by the lessee; or
(2) acknowledgment to the lessee by any bailee of the goods other than a carrier, or a carrier by reshipment or as a warehouseman, that the bailee holds the goods for the lessee.

(d) If notice to stop delivery has been given, the following rules apply:

(1) The notice must afford the carrier or bailee a reasonable opportunity to prevent delivery of the goods.

(2) After notification, the carrier or bailee shall hold and deliver the goods according to the directions of the lessor. The lessor is liable to the bailee or carrier for any resulting charges or damages. A carrier or bailee need not stop delivery if the lessor does not provide indemnity for charges or damages upon the carrier’s or bailee’s demand.

(3) A carrier or bailee that has issued a nonnegotiable document need not obey a notification to stop received from a person other than the person named in the document as the person from which the goods have been received for shipment or storage. (Section 2-818)

Drafting Comment – May, 1997

Article 2A omitted any reference to negotiable documents of title in this section because of an assumption that they would not be used in leasing transactions. I assume we will continue to do so.

SECTION 2A-721. LESSOR’S RIGHTS TO DISPOSE OF GOODS.

(a) Upon a default by a lessee under the lease contract of the type described in Section 2A-717(a) or (c)(1), or upon the lessor’s refusal to deliver or takes possession of goods under Section 2A-718 or 2A-720, or, if agreed, upon other default by a lessee, the lessor may dispose of the goods concerned or the undelivered balance thereof by lease, sale, or otherwise.

(b) Except as otherwise provided with respect to damages liquidated in the lease agreement or otherwise determined by agreement of the parties, if the
disposition is by lease agreement substantially similar to the original lease
agreement and the new lease agreement is made in good faith and in a
commercially reasonable manner, the lessor may recover from the lessee as
damages compensation for:

(1) accrued and unpaid rent as of the date of the commencement of the
period of the new lease agreement;

(2) the present value, as of the same date, of the total rent for the then
remaining lease period of the original lease agreement, minus the present value, as
of the same date, of the rent under the new lease agreement applicable to that part
of the new lease period which is comparable to the then remaining period of the
original lease agreement; and

(3) any incidental damages allowed under Section 2A-707, less expenses
avoided as a result of the lessee’s default.

(c) If the lessor’s disposition is by a lease agreement that for any reason
does not qualify for treatment under subsection (b), or is by sale or otherwise, the
lessee may recover from the lessee as if the lessor had elected not to dispose of the
goods, and Section 2A-722 governs.

(d) A person that subsequently buys or leases from the lessor in good faith
for value as a result of a disposition under this section takes the goods free of the
original lease contract and any rights of the original lessee even if the lessor fails to
comply with one or more of the requirements of this article.

(e) A lessor is not accountable to the lessee for any profit made on any
disposition. A lessee that has rightfully rejected or justifiably revoked acceptance
shall account to the lessor for any excess over the amount of the lessee’s security
interest. (Section 2-819)
SECTION 2A-722. LESSOR’S DAMAGES FOR NONACCEPTANCE, FAILURE TO PAY, OR REPUDIATION.

(a) Except as otherwise provided with respect to damages liquidated in the lease agreement under Section 2A-711 or otherwise determined by agreement of the parties under Sections 1-102(3) and 2A-712, if a lessor elects to retain the goods or elects to dispose of the goods and the disposition is by lease agreement that for any reason does not qualify for treatment under Section 2A-721(b) or is by sale or otherwise, the lessor may recover from the lessee as damages for a default of the type described in Section 2A-717(a) or 2A-717(c)(1), or if agreed for other default of the lessee:

(1) accrued and unpaid rent as of the date of default if the lessee has never taken possession of the goods, or, if the lessee has taken possession of the goods, as of the date the lessor repossesses the goods or an earlier date on which the lessee makes a tender of the goods to the lessor,

(2) the present value, as of the date determined under paragraph (i), of the total rent for the then remaining period of the original lease agreement, minus the present value as of the same date of the market rent at the place where the goods are located computed for the same lease term, and

(3) any incidental or consequential damages allowed under Section 2A-707 or 2A-708, less expenses saved in consequence of the lessee’s default.

(b) A lessor may recover damages measured by other than the market price, together with incidental and consequential damages, including:

(1) the present value of lost profits, including reasonable overhead, resulting from the default of the lessee determined in any reasonable manner; and
(2) reasonable expenditures made in preparing for or performing the
contract if, after the default, the lessor is unable to obtain reimbursement by
salvage, resale, or other reasonable measures.

Following is the version of Section 2A-721 which appeared in the January,
1997, Article 2A Draft.  (Section 2-821)

Drafting Comment – May, 1997

At the February, 1997, meeting, the Article 2A Committee voted to return to
the present language for Section 2A-712 (present Section 2A-528).  At that time,
the January, 1997, draft of Article 2, in cases of repudiation measured damages at a
different time depending on whether the action came to trial before or after the time
for performance under the contract. Duplicating that set of rules in Article 2A
resulted in a complex section.

Article 2 has now abandoned that distinction, but does contain a special rule
delaying the time for measuring contract market in repudiation cases until the end
of a commercially reasonable time after repudiation.

The above draft takes verbatim the first paragraph of present Section
2A-528 except that reference is now made to consequential damages which are now
allowed to lessors.

Subsection (b) is modified to follow subsection (b) of draft Section 2-821.
The change of substance is the right to lost profit damages is not limited to cases in
which a contract-market remedy is inadequate to put the lessor in as good a position
as performance would have done. Rather, the limitation is in Section 2A-705(c).
Under that section, a court may deny or limit a remedy if it would put the lessor in a
substantially better position that if the other party had fully performed.

SECTION 2A-723. LESSOR’S ACTION FOR THE RENT.

(a) Upon a default by the lessee under the lease contract of the type
described in Section 2A-717(a) or (c)(1) or if agreed upon another default by the
lessee, if the lessor complies with subsection (c), the lessor may recover from the
lessee the damages specified in subsection (b) for:

(1) goods accepted by the lessee and not repossessed by or tendered to
the lessor;
(2) goods identified to the lease contract if the lessor is unable after reasonable effort to dispose of them at a reasonable price or the circumstances reasonably indicate that effort will be unavailing; and

(3) conforming goods lost or damaged after risk of loss passes to the lessee, but if the lessor has retained or regained control of the goods, the loss or damage must occur within a commercially reasonable time after the risk of loss has passed to the lessee:

(b) The damages available under the circumstances described in subsection (a) are:

(1) accrued and unpaid rent as of the date of entry of judgment in favor of the lessor;

(2) the present value as of the same date of the rent for the then remaining lease term of the lease agreement; and

(3) any incidental or consequential damages allowed under Section 2A-707 or Section 2A-708, less expenses avoided as a result of the lessee’s default.

(c) Except as otherwise provided in subsection (d), a lessor shall hold for the lessee for the remaining period of the lease agreement any goods that have been identified to the lease contract and are in the lessor’s control.

(d) A lessor may dispose of the goods at any time before collection of the judgment for damages obtained pursuant to subsection (a). If the disposition is before the end of the remaining period of the lease agreement, the lessor’s recovery against the lessee for damages is governed by Section 2A-721 or 2A-722, and the lessor shall provide an appropriate credit against a judgment for damages to the extent that the amount of the judgment exceeds the recovery available under Section 2A-721 or 2A-722.
(e) Payment of the judgment for damages obtained under subsection (a) entitles the lessee to the use and possession of the goods not then disposed of for the remaining period of, and in accordance with, the lease agreement.

(f) Upon default by the lessee under the lease contract of the type described in Section 2A-717(a) or (c)(1) or if agreed upon other default by the lessee, a lessor that is not entitled to rent under this section is still entitled to damages for nonacceptance under Section 2A-721 or 2A-722. (Section 2-822)

SECTION 2A-724. LESSOR’S RIGHTS TO RESIDUAL INTEREST. In addition to any other recovery permitted by this article or other law, a lessor may recover from a lessee an amount that will fully compensate the lessor for any loss of or damage to the lessor’s residual interest in the goods caused by the lessee’s default.

[C. LESSEE’S REMEDIES]

SECTION 2A-725. LESSEE’S REMEDIES IN GENERAL; LESSEE’S SECURITY INTEREST IN REJECTED GOODS.

(a) If a lessor fails to deliver the goods in conformity to the lease contract or repudiates the contract, or a lessee rightfully rejects the goods or justifiably revokes acceptance of the goods, with respect to any goods involved and with respect to all of the goods if under an installment lease contract the value of the whole lease contract is substantially impaired, the lessor is in default under the lease contract, and the lessee may do one or more of the following:

(1) cancel the lease contract under Section 2A-710;

(2) recover so much of the rent and security as has been paid and is just under the circumstances;
(3) cover and obtain damages as to all goods affected, whether or not they have been identified to the lease contract under Sections 2A-734, 2A-707, and 2A-708;

(4) recover damages for nondelivery under Sections 2A-735, 2A-707, and 2A-708;

(5) if an acceptance of goods has not been justifiably revoked, recover damages for default with regard to accepted goods under Section 2A-736;

(6) enforce a security interest under subsection (e);

(7) exercise any other rights or pursue any other remedy provided in the lease contract.

(b) If a lessor fails to deliver or repudiates the lease contract, the lessee may also:

(1) recover identified goods under Section 2A-737; or

(2) in a proper case, obtain specific performance or replevy the goods under Section 2A-709.

(c) If a lessor is otherwise in default under a lease contract, the lessee may exercise the rights and pursue the remedies provided in the lease agreement, which may include a right to cancel the lease, and those in Section 2A-736(a).

(d) If a lessor has breached a warranty, whether express or implied, the lessee may recover damages under Section 2A-736(b).

(e) On rightful rejection or justifiable revocation of acceptance, a lessee has a security interest in goods in the lessee’s possession or control for any rent and security that has been paid and any expenses reasonably incurred in their inspection, receipt, transportation, care, and custody. In that case, the lessee may hold the goods and dispose of them in good faith and in a commercially reasonable manner. The disposition is subject to Section 2A-721(d) and (e).
(f) Subject to Section 2A-607, a lessee, on so notifying the lessor, may deduct all or any part of the damages resulting from any default under the lease contract from any part of the rent still due under the same contract. (Section 2-823)

Drafting Comment – May, 1997

The reference to Section 2A-721(d) in subsection (f) gives transferees after a lessee’s sale or lease to satisfy its security interest the same protection as transferees from a lessor under Section 2A-721.

SECTION 2A-726. LESSEE’S RIGHTS ON NONCONFORMING DELIVERY; RIGHTFUL REJECTION.

(a) Subject to Sections 2A-727, 2A-711, and 2A-712, if the goods or the tender or delivery fail in any respect to conform to the lease contract, a lessee may:

   (1) reject the whole;

   (2) accept the whole; or

   (3) accept any commercial unit or units and reject the rest.

(b) A rejection under subsection (a) is not effective unless the lessee notifies the lessor within a reasonable time after tender or delivery. (Section 2-703)

SECTION 2A-727. INSTALLMENT LEASE CONTRACT: DEFAULT.

(a) In this section, “installment lease contract” means a lease contract in which the terms require or the circumstances permit the delivery of goods in separate lots to be separately accepted, even if the lease agreement requires payment other than in installments or states “Each delivery is a separate lease” or words of similar import.

(b) A lessee may reject any nonconforming installment of delivery of goods in an installment lease if the nonconformity substantially impairs the value of that installment to the buyer. [However, if a nonconforming tender by the lessor [is not a breach of] [does not substantially impair the value of] the whole contract and the
lessor or the supplier gives adequate assurance of its cure, the lessee shall accept that installment].

(c) If a nonconformity or default with respect to one or more installments in an installment contract is a substantial impairment of the value of the whole contract, the aggrieved party may cancel the contract. However, the power to cancel the contract for default is waived, or a canceled contract is reinstated, if the aggrieved party accepts a nonconforming installment without seasonably giving notice of cancellation, brings an action with respect only to past installments, or demands performance as to future installments. (Section 2-710)

Drafting Comment – May, 1997

The bracketing of the last sentence of subsection (b) follows the April draft of Article 2. The Comments to Article 2 suggest that the sentence is no longer necessary now that the Act defines substantial impairment. (See new subsections (c) and (d) of Section 2A-702).

SECTION 2A-728. MERCHANT LESSEE’S DUTIES; LESSEE’S OPTIONS AS TO SALVAGE.

(a) Subject to a lessee’s security interest under Section 2A-725(e), if the lessor or supplier does not have an agent or place of business at the market where the goods were rejected or acceptance was revoked, a merchant lessee, upon an effective rightful rejection or justifiable revocation of acceptance, shall follow any reasonable instructions received from the lessor or supplier with respect to goods in the lessee’s possession or control and, in the absence of such instructions, shall make a reasonable effort to sell, lease, or otherwise dispose of the goods for the lessor’s account if they threaten to decline speedily in value. Instructions are not reasonable if on demand indemnity for expenses is not forthcoming.

(b) A merchant lessee that sells goods under subsection (a) is entitled to reimbursement from the lessor or supplier, or out of the proceeds, for the
reasonable expenses of caring for and disposing of them. If the expenses do not
include a disposition commission, the lessee is entitled to a commission usual in the
trade or, if there is none, to a reasonable sum not exceeding 10 percent of the gross
proceeds.

(c) Subject to subsection (a), unless a lessor or supplier gives instructions
within a reasonable time after notification of a rightful rejection or justifiable
revocation of acceptance, a lessee may store the rejected goods for the account of
the lessor or supplier, reship them to the lessor or supplier, or resell them for the
account of the lessor or supplier, with reimbursement as provided in subsection (b).

(d) In complying with this section or Section 2A-729, the lessee shall act in
good faith. Conduct in good faith under this section does not constitute acceptance
or conversion and may not be the basis of a claim for damages.

(e) A purchaser that purchases in good faith from a lessee under this section
or Section 2A-729 takes the goods free of any rights of the lessor and the supplier,
even if the lessee fails to comply with the requirements of this article. (Section
2-705)

Drafting Comment – May, 1997

Subsection (e) above comes from present Article 2A. A similar provision
does not appear in present Article 2, nor in revised Article 2. Should subsection (e)
be continued?

SECTION 2A-729. LESSEE’S DUTIES AS TO RIGHTFULLY
REJECTED GOODS.

(a) Subject to Section 2A-728, after an effective rightful rejection or
justifiable revocation of acceptance, a lessee that takes delivery of goods shall hold
the goods with reasonable care at the disposal of the lessor or supplier for a
sufficient time to permit the lessor or supplier to remove them. However, the lessee
has no further obligation with regard to the goods.
(b) An action by the lessee under subsection (a) is not acceptance or conversion.

(c) A lessee in possession which wrongfully but effectively rejects but does not accept goods is subsection to the duty of care in subsection (a). (Section 2-704)

Drafting Comment

The ELA memorandum, page 45, objects to including subsection (b)(1) in the statute. That group doesn’t want the statutory language to suggest that actual use by the lessee might not be a use “under the lease”, but rather a use to mitigate damages.

At the February meeting, the Drafting Committee voted to reject subsection (b) of Section 2-704. It is, therefore, stricken above. The Committee thought that whether use of rejected goods is inconsistent with the attempted rejection or is consistent with rejection as necessary mitigation of damages should be left to common law development, rather than codified. In leasing transactions, treated use as mitigation rather than as acceptance under the lease creates difficult fact issues regarded the obligations of the parties and the rent to be paid.

SECTION 2A-730. CURE.

(a) If a lessee effectively and rightfully rejects goods or a tender of delivery under Section 2A-726 or justifiably revokes an acceptance under Section 2A-733 and the agreed time for performance has not expired, the lessor or supplier, upon seasonable notice to the buyer and at its own expense, may cure any default by making a conforming tender of delivery within the agreed time and by compensating the lessee for all of the lessee’s reasonable and necessary expenses caused by the nonconforming tender and subsequent cure.

(b) If a lessee effectively and rightfully rejects goods or a tender of delivery under Section 2A-726 or justifiably revokes acceptance under Section 2A-733 and the agreed time for performance has expired, the lessor or supplier, upon seasonable notice to the lessee and at its own expense, may cure a default by making a tender of conforming goods and by compensation the lessee for all of the lessee’s reasonable and necessary expenses caused by the nonconforming tender and
subsequent cure, if the cure is [appropriate and] timely under the circumstances and
the buyer has no reasonable grounds to refuse the cure. (Section 2-709)

SECTION 2A-731. ACCEPTANCE OF GOODS.

(a) Acceptance of goods occurs when the lessee:

(1) states to the lessor or supplier at any time that the goods are accepted;

(2) after a reasonable opportunity to inspect the goods, signifies to the lessor or the supplier that the goods conform or will be taken or retained in spite of their nonconformity;

(3) after a reasonable opportunity to inspect the goods, fails to make an effective rejection; or

(4) either before or after rejection or after revocation of acceptance, does any unreasonable act inconsistent with the interest of the lessor or supplier in the goods or the lessor’s claim of rejection or revocation of acceptance and that act is ratified by the lessor or supplier as an acceptance.

(b) Acceptance of a part of a commercial unit is acceptance of the entire unit. (Section 2-706)

SECTION 2A-732. EFFECT OF ACCEPTANCE OF GOODS; NOTICE OF DEFAULT; BURDEN OF ESTABLISHING DEFAULT AFTER ACCEPTANCE; NOTICE OF CLAIM OR LITIGATION TO PERSON ANSWERABLE OVER.

(a) A lessee shall pay rent in accordance with the lease contract for any goods accepted.
(b) Acceptance of goods by a lessee precludes rejection of the goods accepted but does not by itself preclude any other remedy provided by this article or the lease agreement for nonconformity.

(c) If a tender has been accepted, the following rules apply:

(1) The lessee, within a reasonable time after the lessee discovers or should have discovered a default, shall notify the lessor and the supplier, if any, of the claimed default. However, a failure to give notice bars the lessee from a remedy only to the extent that the party entitled to notice establishes that it was prejudiced by the failure.

(2) Except in the case of a consumer lease, if a claim for infringement or the like is made against a lessee for which a lessor or supplier is answerable over, the lessee shall notify the lessor or supplier within a reasonable time after receiving notice of the litigation or be barred from any remedy over for liability established by the litigation.

(d) A lessee has the burden of establishing a default with respect to goods accepted.

(e) In a claim for breach of a warranty, indemnity, or other obligation against the lessee for which another party is answerable over, the following rules apply:

(1) The lessee may give notice of the litigation to the other party in a record, and the person notified may then give similar notice of the litigation to any other person that is answerable over. If the notice invites the person notified to intervene in the litigation and states that failure to do so will bind the person notified in any action later brought by the lessor as to any determination of fact common to the two actions, the person notified is so bound, unless, after seasonable receipt of the notice, the person notified intervenes in the litigation and defends.
(2) If the claim is one for infringement or the like, the original lessor or supplier may demand in a record that its lessee turn over control of the litigation, including settlement, or otherwise be barred from any remedy over. If the lessor or supplier also agrees to bear all expense and to satisfy any adverse judgment, the lessee is so barred unless, after seasonable receipt of the demand, control is turned over to the lessor or supplier.

(f) Subsections (c), (d), and (e) govern an obligation of a lessee to hold the lessor or the supplier harmless against infringement or the like. (Section 2-707)

SECTION 2A-733. REVOCATION OF ACCEPTANCE OF GOODS.

(a) A lessee may revoke acceptance of a lot or commercial unit whose nonconformity substantially impairs its value to the lessee if accepted:

(1) except in the case of a finance lease, on the reasonable assumption that its nonconformity would be cured and it has not been seasonably cured; or

(2) without discovery of the nonconformity if acceptance was reasonably induced by the lessor’s assurances or, except in the case of a finance lease, by the difficulty of discovery before acceptance.

(b) Except in the case of a finance lease that is not a consumer lease, a lessee may revoke acceptance of a lot or commercial unit if the lessor defaults under the lease contract and the default substantially impairs the value of that lot or commercial unit to the lessee.

(c) If the lease agreement so provides, the lessee may revoke acceptance of a lot or commercial unit because of other defaults by the lessor.

(d) To be effective, a lessee’s acceptance must be revoked within a reasonable time after the lessee discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused
by their own defects. The revocation is not effective until the lessee notifies the
lessor of it.

(e) A lessee that justifiably revokes acceptance has the same rights and
duties with regard to the goods involved under Sections 2A-728 and 2A-729 as if
they had been rejected. (Section 2-708)

Drafting Comment – May, 1997

The final text will contain a Comment on revocation of acceptance in
finance leases. It will point out that a lessee cannot revoke against a finance lessor
unless the lessee has been induced to accept by the finance lessor’s assurances.
However, the lessee may be able to get the agreement of the finance lessor to take
the goods back and revoke the finance lessor’s acceptance as against the supplier.

SECTION 2A-734. COVER; LESSEE’S ACQUISITION OF
SUBSTITUTE GOODS.

(a) Upon a default by a lessor under the lease contract of the type described
in Section 2A-725(a), or if agreed upon other default by the lessor, the lessee may
cover by making in good faith and without unreasonable delay any purchase or
lease of, or contract to purchase or lease, comparable goods to substitute for those
due from the lessor.

(b) Except as otherwise provided with respect to damages liquidated in the
lease agreement or determined by agreement of the parties, if a lessee’s cover is by
a lease contract substantially similar to the original lease contract and the new lease
contract is made in good faith and in a commercially reasonable manner, a lessee
that covers in the manner required by subsection (a); may recover damages
measured by the present value, as of the date of the commencement of the period of
the new lease contract, of the rent under the new lease contract applicable to that
part of the new lease period which is comparable to the then remaining period of
the original lease contract minus the present value as of the same date of the total
rent for the then remaining lease period of the original lease contract together with
any incidental or consequential damages, less expenses avoided as a result of the
lessor’s default.

(c) If a lessee’s cover is by a lease agreement that for any reason does not
qualify for treatment under subsection (b), or is by purchase or otherwise, the lessee
may recover from the lessor as if the lessee had elected not to cover, and Section
2A-735 governs. (Section 2-825)

Draft Comment – May, 1997

Stricken subsection (c) above in the January, 1997 draft of Article 2
contained the implication that a “bad faith cover” barred the lessee from any other
remedy. That implication has now been removed. Should Article 2A now adopt
the shorter, Article 2, version of subsection (c)?

SECTION 2A-735. LESSEE’S DAMAGES FOR NON-DELIVERY,
REPUDIATION, DEFAULT, AND BREACH OF WARRANTY IN REGARD
to accepted goods.

(a) Except as otherwise provided with respect to damages liquidated in the
lease agreement or otherwise determined by agreement of the parties (Sections
1-102(3) and 2A-711), if a lessee elects not to cover or a lessee elects to cover and
the cover is by lease agreement that for any reason does not qualify for treatment
under Section 2A-734, or is by purchase or otherwise, the measure of damages for
nondelivery or repudiation by the lessor or for rejection or revocation of acceptance
by the lessee is the present value, as of the date of the default, of the then market
rent minus the present value as of the same date of the original rent, computed for
the remaining period of the original lease agreement, together with incidental and
consequential damages, less expenses saved in consequence of the lessor’s default.

(b) Market rent is to be determined as of the place for tender or, in cases of
rejection after arrival or revocation of acceptance, as of the place of arrival.
(c) Except as otherwise agreed, if the lessee has accepted goods and given notification, the measure of damages for nonconforming tender or delivery or other default by a lessor is the loss resulting in the ordinary course of events from the lessor’s default as determined in any manner that is reasonable together with incidental and consequential damages, less expenses saved in consequence of the lessor’s default.

(d) Except as otherwise agreed, the measure of damages for breach of warranty is the present value at the time and place of acceptance of the difference between the value of the use of the goods accepted and the value if they had been as warranted for the lease period unless special circumstances show proximate damages of a different amount, together with incidental and consequential damages, less expenses saved in consequence of the lessor’s default or breach of warranty.

(Section 2-826)

Drafting Comment – May, 1997

At the February, 1997, meeting the Article 2A Committee voted to return Section 2A-735 to the language of present Section 2A-519. That has been done above.

SECTION 2A-736. LESSEE’S DAMAGES FOR DEFAULT REGARDING ACCEPTED GOODS.

(a) Except as otherwise agreed, a lessee that has accepted goods and given notice pursuant to Section 2A-732(c), may recover as damages for any nonconforming tender or other default by a lessor the loss resulting in the ordinary course of events from the lessor’s default as determined in any reasonable manner.

(b) Except as otherwise agreed, a measure of damages for breach of a warranty of quality is the present value at the time and place of acceptance of the difference between the value of the use of the goods accepted and the value if they
had been as warranted for the lease period, unless special circumstances show
proximate damages of a different amount.

(c) A lessee may also recover incidental and consequential damages.
(Section 2-827)

SECTION 2A-737. PREPAYING LESSEE’S RIGHT TO GOODS.

(a) A lessee that pays all or a part of the rent or security for goods identified
to the lease contract, whether or not they have been shipped, on making and
keeping good a tender of any unpaid portion of the rent and security due under the
lease contract, has a right to recover them from the lessor if the lessor repudiates or
fails to deliver as required by the contract.

(b) A lessee has a right of replevin, detinue, sequestration, claim and
delivery, or the like to recover goods identified to the lease contract if, after
reasonable efforts, the lessee is unable to effect cover for the goods or the
circumstances indicate that an effort to obtain cover would be unavailing.

(c) If the requirements of subsection (a) or (b) are satisfied, the lesser’s
right vests upon identification of the goods to the lease contract even if the lessor
has not then repudiated the contract or failed to deliver as required by the contract.
(Section 2-824)

Drafting Comment – May, 1997

My notes indicate that a Comment to this section should make it clear that
this section gives no rights to the lessee against a supplier.