



**ADVISORY BOARD FOR THE
PREPARATION OF A
MODEL LAW ON LEASING
Second session
Rome, 6-7 February 2006**

UNIDROIT 2006
Study LIXA–Doc. 4 add.
Original: English/French
January 2006

PRELIMINARY DRAFT MODEL LAW ON LEASING

*(prepared by the Reporter on the basis of the guidelines provided by the Advisory Board
at its first session (Rome, 17 October 2005)):*

ADDITIONAL COMMENTS

by Ms Ndonde and the Equipment Leasing Association of the United States of America, members of
the Advisory Board

COMMENTS OF MS NDONDE

CHAPTER II

Article 12 Other Laws

Suggestion: Add a conflict of laws provision. That is to say, in case of conflict with other laws this law shall take precedence over the subject matter of financial leasing.

CHAPTER III

Article 10(1)(b) Lessee under financial lease as beneficiary of supply agreement

Comment: Under article 10(1)(b), the extension of the benefit of a supplier's promises and warranties to the lessee does not modify the rights and duties of the parties to the supply agreement.

Doesn't this mean that the supplier could therefore be liable to both the lessor and lessee in respect of the same damage/defect in equipment covered by its promises and warranties?

Suggestion: Inclusion of a clause precluding the supplier from being liable to both the lessor and the lessee in respect of the same damage covered by its promises and warranties in respect of the equipment.

Article 19 Warranty of merchantability

Comment: Under Article 19, a warranty that the equipment will be merchantable is implied in a supply agreement if the supplier is a merchant with respect to equipment of that kind.

Given that an essential feature of a finance lease (as provided for under Article 2 – in definitions) is that the lessee specifies the equipment, should this warranty be implied even where the lessee has examined the goods and the examination ought to have revealed defects in the goods?

Suggestion: The warranty of merchantability should not apply where the goods have been examined by the lessee and the examinations ought to have revealed some defects in the goods.

CHAPTER V

Article 24 Damages

Comment: Under this Article, the aggrieved party is entitled to recover such damages as will exclusively, or in combination with other remedies provided by this law or the leasing agreement, place the aggrieved party in the position in which it would have been had the agreement been performed in accordance with its terms.

Loss of future rentals is a head of loss that causes a lot of problems because it is likely to be attacked as a penalty (at least from looking at British common law which a lot of countries in the developing world follow).

Suggestion: Loss of future rentals as a head of loss/damage should be provided for. The lessor should be able to receive a sum equal, at the time of the payment, to the then present value of the future rent stream.

OTHER COMMENTS

1. Special forms of financial lease transactions:

Comment: From my reading, special forms of financial lease transactions such as “sale and leaseback”, and “secondary leasing”, and their legal implications are not incorporated in the draft law.

Suggestion: The definition of “lease” should include “sale-leaseback” and “secondary lease” as special forms of financial lease transactions. The legal implications of such transactions such as the liability for defective equipment in these transactions should be addressed by the law.

2. Parties to financial lease transactions

Comment: It is implied by the definition of “finance lease” under Article 2 that a financial lease can only be a tripartite / three-party arrangement.

Suggestion: A financial lease transaction should include two -party arrangements, i.e., where the leased equipment is the lessor’s already owned equipment. The legal consequences of the two -party finance lease arrangement should be provided for in the law, i.e., regards liability for equipment leased.

COMMENTS OF THE EQUIPMENT LEASING ASSOCIATION OF THE UNITED STATES OF AMERICA

Article 2 Definitions

In this Law

Centre of main interests means the place where a ~~person~~ lessee conducts the administration of its interests on a regular basis. ~~In the absence of proof to the contrary, the person's registered office, or habitual residence in~~ The lessee's registered office, if any, is presumed to be lessee's centre of main interests. ~~If a lessee does not have a registered office its chief executive office is presumed to be lessee's centre of main interests.~~ In the case of an individual, as lessee, the individual's habitual residence is presumed to be the his centre of the person's main interests.

...

Equipment means all ~~personal property that is movable or that is a fixture~~ tangible personal property, regardless of whether such personal property is attached or affixed to real property, including future equipment, specially manufactured equipment, and the unborn young of animals. The term does not include information, money, investment securities, or software except to the extent that the software is so embedded in equipment as to become part of the equipment, ~~but no equipment shall cease to be equipment for the sole reason that it becomes attached or fixed to real estate.~~ The term does not include personal property that is leased by an individual primarily for personal, family or household purposes.

Financial lease means a lease that includes the following characteristics:

(a) the lessee specifies the ~~equipment without relying primarily on the skill and judgment of the lessor, supplier and the type and quantity of the equipment to be leased under the financial lease;~~

~~(b) the lessor~~

(b) the lessor is not the manufacturer or supplier of the equipment, and acquires the equipment or the right to possess and use the equipment in connection with the lease or a previous lease; ~~and the supplier is so notified;~~

(c) ~~the rentals or other funds payable under the leasing agreement are calculated so as to take into account the amortisation of the whole or a substantial part of the cost of the equipment; and~~

~~(d)~~ before the leasing agreement becomes effective, the lessee ~~either~~

(i) receives an accurate and complete statement designating the promises, warranties, disclaimers of warranties, and limitations on remedies, including those of a third party, such as the manufacturer of equipment, provided to the lessor by the supplier in connection with the supply agreement, or

(ii) is informed in a record that the lessee is entitled to all the promises and warranties provided in the supply agreement, is informed that the lessee may communicate with the supplier to receive an accurate and complete statement of those promises and warranties, and is informed of the supplier's identity unless the lessee selected the supplier, or

(iii) receives a copy of the supply agreement.

Lease means a transaction in which a person grants a right to possession ~~or control~~ and use of equipment to another person for use in trade or business for a ~~term~~ specified period of time in return for rentals or other funds payable. Unless the context indicates otherwise, the term includes a sub-lease.

...

Person means any natural person, business entity, non-profit entity, national or local governmental agency or instrumentality, or other entity.

Record means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in an understandable format. A record does not need to be permanent or indestructible. The term does not include human memory or oral communications.

Source: U.C.C. § 2A-103(1)(cc) (2003)

Supplier means a person from whom a lessor buys or leases equipment to be leased under a ~~financial lease-lease.~~

Supply Agreement means the contract under which the lessor buys or leases equipment from the supplier for lease to a lessee, whether such lessee or the related lease agreement has been identified at the time of such purchase or lease. A supply agreement may consist of one or more records.

Article 3 Freedom of contract

Except as otherwise ~~provided~~ expressly stated in this Law and the law of this State, the lessor ~~and~~, the lessee and the supplier are free to determine the content of and ~~create~~ vary the application of this Law to, a leasing agreement and a supply agreement.

CHAPTER II: FORMATION AND DOCUMENTATION OF LEASING AGREEMENT

Article 4 Formation

A leasing agreement ~~may~~ shall be created by the acceptance of an offer ~~or by conduct of the parties that is sufficient to show agreement.~~ An offer may be made and accepted in any manner sufficient to show the parties' agreement, including the use of electronic agents such as a computer program or electronic or other automated means used independently to initiate an action or respond to electronic records or performances without human intervention. Such leasing agreement shall be documented in accordance with Article 6.

...

Article 6 Documentation

1. A leasing agreement is not enforceable against a party unless there is a record, signed ~~by that~~ or otherwise authenticated by use of a symbol or other device by such party or that party's agent, sufficient to indicate that a leasing agreement has been made and identifying the parties thereto, the equipment to be leased, the rent and the duration of the lease.

2. A record is not insufficient because it omits ~~or incorrectly states~~ a provision that is important for a determination of the parties' rights and duties, provided there is a reasonable basis for determining the parties' intent with respect to such omission.

3. When a record omits ~~or incorrectly states~~ such a provision, a provision that is appropriate in the circumstances shall be supplied. In determining what provision to supply, factors to consider should include the intention of the parties, ~~good faith, fair dealing and reasonableness.~~ if ascertainable, the parties' prior course of dealing or, in the absence thereof, usage of trade in the leasing industry.

4. The terms of a leasing agreement agreed to by the parties which are set forth in a record intended by the parties as a final expression of their agreement may not be contradicted by evidence of any prior record or any oral agreement.

Article 7 Modification

A leasing agreement that contains a clause requiring modification or termination to be in a particular form may not be otherwise modified or terminated. A party agreeing to modification of a provision in some form other than the particular form designated in such clause may be precluded by its conduct from ~~asserting such a clause enforcing such provision absent such modification~~ to the extent that the other party has reasonably acted in reliance on that conduct. In such cases the party precluded by its conduct from asserting such provision absent such modification shall be deemed to have waived enforcement of such provision in such instance only and such conduct shall not result in amendment or permanent modification of the leasing agreement. A modification or termination of a leasing agreement requires no consideration to be binding.

CHAPTER III: EFFECT OF LEASING AGREEMENT

Article 8 Enforceability

Except as otherwise ~~provided~~ expressly stated in this Law or in any other law of the State, a leasing agreement is effective and enforceable according to its terms between the parties, ~~against and against all third parties, including assignees of the parties, sublessees and~~ purchasers of the equipment and against creditors of the parties, including an insolvency administrator.

Article 9 Transfer

1. The lessor's rights and duties under the leasing agreement may be ~~transferred freely~~ transferred by the lessor without the consent of or notice to the lessee, except when a transfer would materially impair the lessee's rights ~~in~~ under the leasing agreement with respect to the equipment.

2. The lessee's rights and duties under the leasing agreement may be transferred by lessee only (a) with the consent of the lessor, ~~which may not be unreasonably withheld~~, and (b) subject to the rights of third parties. The lessor and third parties may give their consent in advance. A transfer by the lessee shall include a change in the majority ownership or control of the lessee, unless the parties to the leasing agreement otherwise agree in writing.

3. A transfer that is prohibited by the leasing agreement is otherwise effective if ~~made to one who did not know and reasonably should not have known that the transfer was prohibited.:~~

(a) Such transfer is an assignment of the lessor's right to receive, and to enforce payment of, monies payable to it under the leasing agreement; or

(b) another statute of this State expressly authorizes a transfer of a lessor's or lessee's rights notwithstanding contractual prohibitions thereon.

4. An agreement by a lessee that the lessee will not assert against a transferee of lessor's interest any claim, defense, recoupment, setoff or right to cancel or terminate the leasing agreement that lessee may have against the lessor is enforceable by such transferee if such transferee (a) accepted such transfer in good faith, (b) gave lessor value for such transfer, and (c) did not at the time of such transfer have notice that the lessee had a defense, claim, recoupment, setoff or right to cancel or terminate the leasing agreement. "Good faith" means honesty in fact and the observance of reasonable commercial standards of fair dealing. A transferee takes for "value" (i) to the extent that the agreed consideration has been performed, or (ii) when such transferee accepts a transfer of the leasing agreement in payment of or as security for an antecedent claim, or (iii) when such transferee gives a negotiable instrument for such transfer.

Article 10 Lessee under financial lease as beneficiary of supply agreement; relationship of Lessor and Supplier

1. (a) The benefit of a supplier's promises to the lessor under the supply agreement and of all warranties, whether express or implied, including those of any third party provided in connection with or as part of the supply agreement, extends to the lessee to the extent of the lessee's leasehold interest under a ~~in the equipment subject to the~~ financial lease related to the supply agreement.

(b) The extension of the benefit of a supplier's promises and of warranties to the lessee does not (i) modify the rights and duties of the parties to the supply agreement, whether arising therefrom or otherwise, or (ii) impose any duty or liability under the supply agreement on the lessee, except to the extent that the duty or liability may only be performed by a person in possession of the equipment, or which are necessary or incident to the enforcement of ~~(c) Where the absence of privity of contract between the lessee and supplier creates a deficiency in the lessee's efforts to enforce the supplier's promises or warranties against the supplier, the lessor shall be bound to take commercially reasonable steps to assist the lessee. If the lessor does not take such steps, the lessor is deemed to have assumed such promises and warranties.~~

2. The lessee's rights under this Article shall not be affected by a variation, agreed to in writing by the lessor, of any term of the supply agreement made after the creation of the leasing agreement unless the lessee consented to that variation. If the lessee did not consent to such variation, then the lessor ~~is deemed to have assumed the promises and warranties of the supplier to the lessor that were so varied to the extent~~ shall be liable for damages to the extent suffered by the lessee as a result of the variation.

3. Nothing in this Article shall entitle the lessee to modify, terminate or rescind the supply agreement without the consent of the lessor.

4. A lessor shall not lose its status as lessor with respect to a leasing agreement and a finance lease shall not lose its status as a finance lease if the lessor is affiliated with or under common ownership or control with the supplier or manufacturer of the equipment to be leased under such leasing agreement, or because the lessor has a business relationship with the supplier or manufacturer of the equipment to be leased under such leasing agreement, including providing debt or lease financing for purchasers or lessees of equipment sold or leased by the supplier or manufactured by the manufacturer.

Article 11 Priority of liens

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3. If a person in the ordinary course of its business furnishes services or materials to the lessor or lessee in possession with respect to equipment subject to a leasing agreement, ~~that person shall have~~ a lien upon ~~that such~~ equipment in ~~the its~~ possession ~~of that person~~ for ~~the such~~ materials or services, which takes priority over any interest of the lessor or lessee in such equipment unless the law governing that lien provides otherwise.

Article 13 Liability for death, personal injury, or property damage caused to third parties

In a financial lease, the lessor shall not, in its capacity of lessor, be liable to ~~the~~ lessee or third parties for death, personal injury, or damage to property caused by the equipment or the use of the equipment, ~~unless the lessor was involved in selecting the supplier or the equipment, in which case the lessor shall be liable to the extent of that involvement.~~

Source: UNIDROIT Convention on International Financial Leasing Art. 8(1)(b), 28 May 1988, modified to include liability to lessee ~~and supplemented to reflect that while the lessee's selection of equipment in a financial lease will not "primarily" rely on the lessor's expertise, the lessor may play some role in selection~~

CHAPTER IV: PERFORMANCE OF LEASING AGREEMENT

Article 14 Risk of loss

1. Except in a financial lease or as provided in the lease agreement, risk of loss is retained by the lessor and does not pass to the lessee. In the case of a financial lease, risk of loss passes from the supplier to the lessee.

2. If risk of loss is to pass to the lessee and the time of passage is not stated in the leasing agreement in the case of a non-financial lease or in the supply agreement in the case of a financial lease, the risk of loss passes to the lessee ~~upon the lessee's acceptance of the equipment. when the specific equipment is identified to the leasing agreement.~~

3. If the lessee revokes acceptance of the equipment in accordance with ~~this Law or the leasing agreement, the lessee, to the extent of any deficiency in its insurance coverage, may treat the risk of loss as having remained with the lessor or, in a financial lease, the supplier, from the beginning.~~ Article 17, risk of loss shall remain with the lessee until redelivery of the equipment to the lessor or its designee.

Article 15 Damage to equipment

Except in a financial lease, when equipment subject to a leasing agreement is damaged without fault of the lessee or lessor before the equipment is delivered to the lessee,

(a) if the loss is total, the leasing agreement is terminated ~~÷~~ and if the lessor has purchased or is obligated to purchase the equipment, then the lessor's damages will be equal to the purchase price paid by lessor plus all costs and expenses incurred by lessor as a result of such loss; and

(b) if the loss is partial, the lessee may demand inspection and at the lessee's option either ~~treat demand delivery of conforming equipment within a reasonable time or terminate the leasing agreement as terminated or accept the equipment with due allowance from the rentals payable for the balance of the lease term for the loss in value but~~ upon reasonable notice to the lessor, and without further right against the lessor, but, if risk of loss has passed to the lessee, the lessor's damages shall be calculated in accordance with Article 15(a).

Article 16 Irrevocability

...

3. A leasing agreement that has become irrevocable and independent hereunder (a) is effective and enforceable between the parties and by or against third parties, including assignees of the parties, and (b) is not subject to cancellation, termination, modification, repudiation, excuse or substitution without the consent of the party to whom the agreement runs.

Article 17 Acceptance

...

2. ~~Once~~ Except in the case of a financial lease, once a lessee has accepted equipment, the lessee may still be entitled to damages for any non-conformity, ~~but and~~ the lessee may reject also revoke its acceptance of the equipment under Article 27 only if the non-conformity substantially impairs the value of the equipment and either (a) the lessee accepted the equipment without knowledge of the non-conformity, owing to the difficulty of discovering it, or (b) the lessee's acceptance was induced by the lessor's ~~or supplier's~~ assurances.

Sources: (1) U.C.C. §2A-515(1) (2003), modified to streamline language; (2) U.C.C. § 2A-517(1) (2003), modified ~~to remove limitations on revocation in financial leases and to remove option of revocation based on expectation of cure unless that expectation was induced by assurances~~

Article 18 Warranty of quiet possession

...

2. (a) In a lease other than a financial lease, the lessor warrants that the lessee's quiet possession will not be disturbed by a person who has a superior title or right, or who claims a superior title or right and acts under the authority of a court, ~~or who makes a claim by way of infringement, which claim arises from an act or omission of the lessor; and~~

(b) In a lease other than a financial lease, the supplier shall be liable to the lessee for any claim of infringement.

...

Article 20 Warranty of fitness for a particular purpose

1. ~~Except in a financial lease, if the lessor at the time the leasing agreement is created has reason to know of the particular purpose for which the equipment is required and that the lessee is relying on the lessor's skill or judgment to select or furnish suitable equipment, there is in the leasing agreement an implied warranty as to the equipment's fitness for a particular purpose. In leases other than financial leases, any implied warranty that the equipment will be fit for that purpose.~~ A lessor under a financial lease is not deemed to have made any implied warranties as to the equipment's fitness for a particular purpose. In leases other than financial leases, any implied warranty that the equipment will be fit for that purpose, a particular purpose shall arise only to the extent that the leasing agreement contains an express affirmation of fact or promise by the lessor to the lessee.

...

3. A warranty under this Article may be excluded or modified only by conspicuous and specific language contained in a record.

Article 21 Lessee's duty to maintain the equipment

...

2. To the extent the leasing agreement sets forth a duty to care for the equipment, compliance by the lessee therewith shall satisfy the lessee's duty of care under paragraph 1.

3. When the leasing agreement comes to an end the lessee, unless exercising a right to buy the equipment or to hold the equipment on lease for a further period, promptly shall return the equipment to the lessor or its designee in the condition specified in paragraph 1 and pursuant to the provisions of the leasing agreement.

CHAPTER V: DEFAULT

Article 22 Definition of default

1. The parties may ~~at any time~~ agree in ~~writing~~ the leasing agreement as to the events that constitute a default or otherwise give rise to the rights and remedies specified in this Chapter.

2. ~~In the absence of agreement, default~~ Default for the purpose of this Chapter occurs when ~~one party substantially deprives the other party of what it is entitled to expect under a party to a leasing agreement breaches a duty, obligation or liability arising thereunder or under this Law, including those set forth in paragraphs 3 and 4 of this Article.~~

3. ~~Except as otherwise provided in the leasing agreement and this Law,~~ default by the lessor includes (i) the failure by lessor to fund the purchase price for the equipment to the supplier pursuant to the terms of the supply contract upon acceptance of the equipment by lessee and lessee's satisfaction of any conditions precedent to lessor's obligation to so fund the purchase price, and (ii) breach of the warranty of quiet possession in Article 18.

4. ~~Except as otherwise provided in this Law or the leasing agreement,~~ default by the lessee includes any of the following: (i) lessee rejects the equipment; (ii) lessee attempts to revoke acceptance of the equipment; (iii) lessee fails to make any payment when due; or (iv) lessee repudiates the leasing agreement in whole or in part.

...

Article 24 Damages

Upon default, the aggrieved party is entitled to recover such compensatory damages as will, exclusively or in combination with other remedies provided by this Law or the leasing agreement, place the aggrieved party in the position in which it would have been had the leasing agreement been fully performed in accordance with its terms, plus incidental damages. The aggrieved party shall not be entitled to recover special, exemplary or punitive damages.

...

Article 26 Termination

1. Notwithstanding Article 16, a leasing agreement may be terminated by ~~operation of this Law,~~ by agreement of the parties, or by an aggrieved party upon the lessee's or lessor's default, after reasonable notice and opportunity to remedy the default. A lessee may terminate a financial lease upon lessor's default only if the leasing agreement so provides or if damages would not provide an adequate remedy.

2. On termination, all ~~duties~~ obligations under the leasing agreement that are executory on both sides are discharged, but any right based on prior default or performance survives and the party that terminated the leasing agreement retains any remedy for default of the leasing agreement (including the lessor's right to the unpaid balance of rental payments).

3. The right of a party to terminate the leasing agreement is exercised by notice to the other party identifying the breach and providing a reasonable time in which to remedy the breach.

Article 27 Rejection of non-conforming delivery

1. (a) ~~When~~ In a lease other than a financial lease, when the equipment is not delivered or is delivered ~~late~~ after any deadline set forth in the leasing agreement or fails to conform to the leasing agreement, the lessee has the right promptly to accept the equipment, to reject the equipment in whole ~~or (but not in part),~~ or, ~~in a lease other than a financial lease,~~ and subject to sub-paragraph 4(b) of this ~~Article, Article 22 paragraph 1,~~ and Article 26(1), to terminate the leasing agreement.

(b) Rejection of equipment or termination of the leasing agreement under the preceding sub-paragraph must be within a reasonable time after opportunity to inspect and notice to the lessor of the non-conforming delivery.

2. (a) ~~When~~ In a lease other than a financial lease, when a lessee rejects equipment in accordance with this Law or the leasing agreement while the lessee's duties are revocable, the lessee is entitled to ~~withhold~~ suspend payment of rentals until the non-conforming delivery has been remedied.

(b) When a lessee terminates a leasing agreement in accordance with the preceding paragraph or the leasing agreement while the lessee's duties are revocable, the lessee is entitled to recover any rentals and other funds paid in advance, less a reasonable sum for any benefit the lessee has derived ~~from~~ and any damages incurred by the lessor, from the lessee's possession or use of the equipment.

...

3. If the lessee rejects equipment or revokes acceptance of equipment in accordance with this Law or the leasing agreement and ~~the time for performance~~ any deadline for delivery set forth in the leasing agreement has not expired, the lessor ~~or and~~, in a financial lease, the supplier, has the right to ~~remedy its failure~~ deliver conforming equipment within the agreed time.

Article 28 Lessor's right to the equipment

1. Subject to the rights of a transferee under Article 9(3), upon termination of the leasing agreement ~~by the lessor~~, the lessor has the right to take possession of the equipment and to require the lessee, at its expense, to return the equipment to the lessor or its designee. The lessor may proceed without judicial process if it can be done without breach of the peace.

2. Upon termination of the leasing agreement by the lessor, the lessor has the right to dispose of the equipment, whether or not in its possession.