Introduction to Sales, Leases & Related Transactions

I. Foundations

A. Why Do People Buy and Lease Goods?: Division of labor and resources; benefits of specialization.

B. How Do People Buy and Lease Goods?

1. From Barter to Sale: Exchange of goods/services for goods/services vs. sale of goods/services for money the buyer earned by providing her own goods/services to a third party.

2. From Sales to Leases: Transfer of ownership vs. transfer of use.

C. How Do We Regulate Sales and Leases?

1. Formation Rules: Rules that specify the requisites of a valid sales contract (e.g., offer, acceptance, consideration). For example:

   a. §§ 2-204 & 2A-204: A contract to sell or lease goods may be

      i. made in any manner sufficient to show agreement, including conduct by both parties which recognizes the existence of such contract;

      ii. found even though the moment of its making is undetermined; and

      iii. formed even though one or more terms are left open, as long as the parties intended to make a contract and there is a reasonably certain basis for giving a remedy.

   b. § 2-207(1): A definite and seasonable expression of acceptance ... operates as an acceptance even though its states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.

♦ 2-207 has no counterpart in Article 2A.
c. **Firm Offers**: At common law, an enforceable option to accept requires separate consideration to support the option. Articles 2 and 2A require *no separate consideration* to hold a merchant to an offer that, in a signed writing, spelled out its irrevocability. §§ 2-205 & 2A-205.

2. **Validation Rules**: Rules that specify the requisites of a legally enforceable sales contract. Examples:
   
   a. Non-UCC “seal,” “attestation,” and similar requirements; and
   
   b. **Statutes of Frauds**: Subject to specific exceptions, the party against whom enforcement is sought must authenticate a record in order to be legally bound to certain types of contracts.
      
      i. § 2-201: Contracts for the sale of goods for $500 or more.
      
      ii. § 2A-201: Contracts for the lease of goods, with total lease payments of $1,000 or more.

3. **Suppletive Rules (“Gap Fillers”)**: Rules that supplement “incomplete” transactions, in the absence of contrary express language.
   
   a. Examples:
      
      1). **Payment Method**, § 2-304;
      
      2). **“Open Price” Term**, § 2-305;
      
      3). **Delivery in One or More Installments**, § 2-307;
      
      4). **Place of Delivery**, § 2-308;
      
      5). **Time for Performance**, § 2-309(a);
      
      6). **Contract Termination**, § 2-309(b)-(c);
      
      7). **Time for Payment**, § 2-310;
      
      8). **Implied Warranties**
         
         a). **Good Title/Noninfringement**, §§ 2-312 & 2A-211;
         
         b). **Merchantability**, §§ 2-314 & 2A-212;
         
         c). **Fitness for a Particular Purpose**, §§ 2-315 & 2A-213;
9). **Delivery Costs**, §§ 2-319 & 2-320; and


b. A significant difference between the UCC and common law is the extent to which the UCC **implies rights and obligations**

1). as if those implied terms were an explicit part of the parties’ agreement,

2). regardless of whether the contract is ambiguous or less than fully integrated as written.

c. However,

1). the parties may write implied terms “out” of the contract using contrary **express terms**, § 1-303(e);

2). a UCC “gap filler” will also yield to

   a). the parties’ **course of perform[ing]** the contract at issue, §§ 1-303(a) & (d);

   b). the parties’ **course of dealing** with respect to prior agreements, §§ 1-303(b) & (d); or

   c). a **usage of trade or custom** common to the particular industry and/or locale, §§ 1-303(c) & (d).

3). **Hierarchy of Terms** (see § 1-303(e)):

   a). **Express Terms** trump

   b). **Course of Performance**, which trumps

   c). **Course of Dealing**, which trumps

   d). **Usage of Trade**, which trumps

   e). **Terms Implied as a Matter of Law**, which trump

   f). **Consistent Additional Terms**.
4. **Interpretive Rules**: Rules that help resolve any apparent ambiguity in the terms of and/or the implementation of an agreement. Examples:


   b. **Course of Dealing**, §§ 1-303(b) & (d);

   c. **Usage of Trade**, §§ 1-303(c) & (d); and

   d. **Course of Performance**, §§ 1-303(a) & (d).

5. **Performance and Breach Rules**: Rules that dictate what will and will not constitute nonperformance by one party sufficient to give rise to a claim of breach by the other party, or that prescribe what actions the innocent party may or must take in order to be entitled to recover from the nonperforming party. Examples:

   a. **Duty of Good Faith**, § 1-304;

   b. **Duty of Best Efforts in Exclusive Dealing**, § 2-306;

   c. Buyer’s/Lessee’s **Right to Inspect**, §§ 2-513 & 2A-515(1);


   e. Seller’s/Lessor’s **Right to Cure**, §§ 2-508 & 2A-513;

   f. **Adequate Assurances of Performance**, §§ 2-609 & 2A-401;

   g. **Anticipatory Repudiation**, §§ 2-610 to -611 & 2A-402 to -403;

   h. **Destruction/Deterioration of Goods**, § 2-613;

   i. **Substituted Performance**, §§ 2-614 & 2A-404; and


6. **Remedial Rules**: Rules articulating (and allocating) the consequences of nonperformance by one party to a sales contract. Examples:

   a. **Seller’s Remedies**, §§ 2-702 to -710;

   b. **Buyer’s Remedies**, §§ 2-711 to -717;

   c. **Lessor’s Remedies**, §§ 2A-523 to -530;

7. **Rules of Disclaimer or Exclusion**: Rules describing how parties can contract “around” the foregoing default rules. Examples:

   a. § 1-302: All provisions of the UCC other than those requiring good faith, diligence, reasonableness (including, *inter alia*, the prohibition on unconscionability), and due care are subject to variation by agreement between the parties unless a provision specifically states otherwise.


   c. §§ 2-718 & 2A-504: Liquidated damages.

   d. §§ 2-719 & 2A-503: Other contractual limitations on remedies.

8. **Customs, Standards, and Practices**: In addition to the foregoing formal rules, many of which are “default” rules rather than “mandatory” ones, myriad informal customs, standards, and practices in an industry, a market, a place, or among parties may create additional rules or supplement, replace, or excuse adherence to existing rules.

D. **What Effects Do These Types of Rules Have?**

1. **Formation**: Bringing buyers/lessees and sellers/lessors together and enabling them to create legally enforceable transfers of ownership/use.

2. **Validation**: Memorializing the agreement between the buyer/lessee and the seller/lessor both to provide notice to the rest of the world and in the event of a subsequent dispute between the parties.

3. **Gap-Filling**: Providing standard terms that govern the transfer of ownership/use unless the buyer/lessee and seller/lessor chose to modify, replace, or disclaim the standard terms.
   - Extra-UCC “gap fillers” can be found in, *inter alia*, applicable common law, specific state or federal statutes, and industry-standard form contracts.

4. **Interpretation**: Providing standardized and predictable rules for construing and interpreting sales and lease contracts, both to facilitate proper performance by the parties and to resolve disputes that arise in the case of alleged non- or malperformance.

5. **Performance**: Facilitating the transfer of conforming goods for the agreed price.
6. **Enforcement**: Providing means to enforce sales and lease agreements and to remedy the breach of those agreements.

7. **Disclaimer/Exclusion**: Providing parties the maximum freedom of contract while also providing, at a minimum, good faith and fair dealing.

E. **Why Do We Regulate Sales and Leases?**

1. **Order**: “Rules specifying how to ‘make it legal’ are fundamental. *Without them, private ordering under law could not exist.*”

2. **Predictability**
   
   a. **Of the Rules Themselves**: Rules must be “clear, definite, accessible, and ascertainable, in advance of deals.”
   
   b. **Of the Outcome of Their Application**: Standardized rules are useless unless they are applied in a standard manner by the courts.
   
   c. **Of Their Use in Day-to-Day Business**: Once standardized, the rules can be embodied in the forms that businesses use to conduct sales and leasing transactions.

3. **Preventing and Resolving Disputes**: Predictable rules
   
   a. **guide parties** as they contemplate and enter into transactions;
   
   b. **facilitate counseling** of parties, both in anticipation of a transaction and in response to some perceived failure in the transaction;
   
   c. **enable parties to settle** their differences without resort to courts; and, if all else fails, and
   
   d. **guide courts** in resolving those disputes the parties are unable to resolve themselves.

4. **Protecting Parties with Inferior Bargaining Power**: One “core task” of commercial law may be “to stake out the necessary minimum area of protection for parties whose bargaining power is inferior.” Examples:
   
   ♦ **Duty of Good Faith**, § 1-304; and
   

5. **Protecting Third Parties**: Many commercial transactions affect the interests of third parties who are not privy to the transaction at hand.
II. Sources of Sales and Leases Law

A. Uniform Commercial Code (UCC) – primarily Articles 1, 2 & 2A, though Articles 5 & 7 occasionally come into play;


C. Uniform Electronic Transactions Act (UETA) – supplements UCC Articles 1, 2 & 2A (and perhaps the CISG) when the parties to a sales or lease contract have consented to deal with one another through electronic means;

D. Electronic Signatures in Global and National Commerce Act (E-SIGN) – supplements UCC Articles 1, 2 & 2A (and perhaps the CISG), whether or not the parties to a sales or lease contract have consented to deal with one another through electronic means, unless preempted by UETA or other state statute, regulation, or rule of law satisfying 15 U.S.C. § 7002(a)(2).

E. Common Law

1. Governing Law: The common law governs service transactions, sales of real property, and, except in states that have enacted Revised Article 1, sales of and other transactions in non-goods personal property and may govern a sale or lease of goods if it is part of a single transaction that also involves services, non-goods personal property, or real property.

   ♦ Federal and state non-UCC law may preempt, enhance, or even relax common law rules in certain transactions.

2. Roles of the Common Law in UCC Disputes

   a. Definitional Aid: In cases where the UCC is merely codifying existing law, common law can help define terms that the UCC has left undefined (e.g., “breach,” “offer,” “possession”).

   b. Explicit Supplement: Some UCC sections and Official Comments explicitly state that the provision in question is not intended to affect some related common-law doctrine (e.g., § 2-318 cmt. 3: “Alternative A is neutral and is not intended to enlarge or restrict the developing case law” regarding third party warranties).

   c. Implicit Supplement: Except where they are clearly superseded by the UCC, “the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.” § 1-103(b).
III. UCC Article 1

A. Scope: Revised Article 1 supplements the specific rules of the other UCC Articles for those transactions governed by another UCC Article. § 1-102.

♦ Pre-revised Article 1 also governed/governs sales of personal property not otherwise governed by another UCC Article.

B. Construction and Purpose

1. Construction: Parties and courts should construe and apply the UCC “to promote its underlying purposes and policies,” § 1-103(a), namely:

   a. simplifying, clarifying, and modernizing commercial law, § 1-103(a)(1);

   b. permitting the continued expansion of commercial practices through custom, usage, and agreement of the parties, §§ 1-103(a)(2) & 1-303; and

   c. making uniform the law among the various jurisdictions covered by the Code, § 1-103(a)(3).

2. Remedies: Courts shall “liberally administer” UCC remedies to

   i. put the aggrieved party in as good a position as if the other party had fully performed; provided that

   ii. a court may not aware consequential, special, or exemplary damages, unless specifically provided for by the parties’ contract, a specific UCC provision, or other rule of law. § 1-305.

C. Freedom of Contract

1. Power to Vary: Parties may vary the UCC’s provisions, as they apply to a particular transaction, except that

   a. parties may not disclaim their obligations of good faith, diligence, reasonableness, and care; but

   b. they may agree to the standards by which their performance of those obligations is judged, if the agreed standards are not manifestly unreasonable. § 1-302.

2. Contractual Choice of Law: Parties are free to choose the law of a particular jurisdiction to govern their transactions and any disputes arising out of it, as long as the chosen jurisdiction bears a reasonable relationship to the transaction. § 1-301.
3. **Waiver**: An aggrieved party may discharge any claim or right arising out of an alleged breach, in whole or in part, without consideration, by a signed writing/authenticated record. § 1-306.

D. **Duty of Good Faith and Fair Dealing**: “Every contract or duty within [the UCC] imposes an obligation of good faith in its performance or enforcement.” § 1-304.

1. Revised § 1-201(b)(20) defines “good faith” as “honesty in fact and the observance of reasonable commercial standards of fair dealing.”

2. By comparison, pre-revised § 1-201(19) generally limited good faith to “honesty in fact in the conduct or transaction concerned”; while § 2-103(1)(b) required merchants to act honestly and to observe reasonable commercial standards of fair dealing.

♦ Eleven states that have enacted Revised Article 1 (along with the eleven that not enacted it) retain the pre-revised, bifurcated good faith standard.

E. **Reservation of Rights**: “A party who with explicit reservation of rights performs or promises performance or assents to performance in a manner demanded or offered by the other party [ostensibly not in accord with the terms of or the party’s understanding of the original agreement] does not thereby prejudice the rights reserved.” § 1-308(a).

IV. **UCC Article 2**

A. **Scope**: Article 2 governs both sales of goods and contracts to sell goods, but

1. does not “impair or repeal any [federal or] state statute [or regulation promulgated thereunder] regulating sales to consumers, farmers, or other specified classes of buyers,” § 2-102, including but not limited to consumer protection laws, unfair trade practices laws, and the like; and

2. is subject to preemption by federal law or by a treaty to which the United States is a party, unless the federal law or treaty in question expressly provides otherwise.

B. **Basic Terminology**

1. **“Goods”**: Tangible, moveable objects, including “unborn young of animals,” “growing crops,” and “things attached to realty as described in” § 2-107, but excluding the money with which the buyer is paying for the goods, certificated securities, and other objects whose value is merely representative. See § 2-105(1).

2. **“Sale”**: Passing title from the seller to the buyer for a price. § 2-106(1).
3. “Contract for sale” includes both “a present sale of goods” in exchange for future payment “and a contract to sell goods at a future time” in exchange for present or future payment. § 2-106(1).

   a. “Contract”: “[T]he total legal obligation which results from the parties’ agreement as affected by this Act and any other applicable rules of law.” § 1-201(b)(12).

   b. “Agreement”: “[T]he bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance ....” § 1-201(b)(3).

   c. “Course of Performance”: A sequence of conduct between the parties to a particular transaction where (1) the agreement involves repeated occasions for performance by a party; and (2) the other party, with knowledge of the first party’s performance, accepts or acquiesces in it without objection.” § 1-303(a).

   d. “Course of Dealing”: A sequence of prior conduct between the parties “establishing a common basis of understanding for interpreting their expressions and other conduct” with regard to the present transaction. § 1-303(b).

   e. “Usage of Trade”: A “practice or method of dealing having such regularity of observance in a place, vocation, or trade so as to justify an expectation that it will be observed with respect to the transaction in question.” § 1-303(c).

B. “Mixed” Contracts

1. Basic Issue: Article 2 provides no direction on how to deal with “mixed” contracts – that is, contracts which involve both

   a. goods and services (e.g., a contract to build and maintain a custom-made computer system),

   b. goods and other personal property (e.g., a contract to sell the inventory and accounts of a going business concern), or

   c. goods and real property (e.g., a contract to sell a mobile home and the lot on which it sits).
2. **Basic Approaches**: Courts generally apply one of two tests:

a. **Majority Approach – “Predominant Purpose” Test**: What was the buyer’s predominant purpose for entering into the underlying transaction; that is, what was the buyer most interested in buying?
   
i. **If goods**, then Article 2 *applies to the whole transaction* (including the service part of it).
   
ii. **If non-goods**, then Article 2 *does not apply to any part of the transaction*.

b. **Minority Approach – “Gravamen of the Action” Test**: What part of the underlying transaction gives rise to the Plaintiff’s complaint?
   
i. **If goods**, then Article 2 *applies to the complaint*, even if the predominant purpose of the transaction was to sell or buy non-goods.
   
ii. **If non-goods**, then Article 2 *does not apply to the complaint*, even if the predominant purpose of the transaction was to sell or buy goods.

♦ **Obvious Problem**: If we use the *gravamen* test, and more than one complaint arises as a result of the transaction, we might apply Article 2 to one complaint but not the other.

C. **Special Case: “Merchants”**

1. **§ 2-104(1)**: A *“merchant”* is a person who
   
a. *deals* in goods of the kind or
   
b. otherwise by his occupation *holds himself out* as having knowledge or skill peculiar to the practices or goods involved in the transaction or
   
c. to whom such knowledge or skill may be attributed by his *employment of an agent or broker or other intermediary* who by his occupation holds himself out as having such knowledge or skill

♦ In any particular transaction, the buyer, the seller, or both may be a merchant.
2. **Consequences of Being a Merchant** *(see § 2-104 cmt. 2)*

   a. Being a merchant or not being a merchant **has nothing to do with whether Article 2 applies to a particular transaction.**

   b. However, being a merchant may subject a party to certain rules that do not apply to non-merchants, including

      i. “Merchant” rules regarding general business practices, such as answering the mail (§ 2-201(2)), giving firm offers (§ 2-205), and the like, as well as the duty of good faith and fair dealing (§ 1-304), and the like, apply to “almost every person in business.”

      ii. “Merchant” warranties (§ 2-314) apply only to merchants who “deal in goods of the kind.”

V. **UCC Article 2A:** Article 2A governs “[a]ny transaction, regardless of form, that creates a lease.” § 2A-102.

   A. **Basic Issues**

   1. **“Lease”:** “[A] transfer of the right to possession and use of goods for ... consideration”; but not a sale, sale on approval, return, or security interest. § 2A-103(1)(j).

      \[
      \begin{array}{c}
      \text{Lessor (lender)} \\
      \uparrow \\
      \downarrow \\
      \text{lease} \quad \text{goods \\ & payments} \\
      \uparrow \\
      \downarrow \\
      \text{Lessee (borrower)} \\
      \end{array}
      \]

   2. The major distinction between a sale and a lease:

      a. If you buy something, you **own** it – even though you may still owe money on the item.

      b. If you lease something, the original owner is **still** the owner; the lessee gets only the right to **use** the good for a time.

   3. **§ 1-203:** Whether a transaction is a “true lease” or a “disguised sale” is determined, in part, by

      a. whether the **lessee can terminate** her obligations under the lease;
b. whether the lease term is for the **full “economic life”** of the good(s) – that is to say, at the end of the lease, the good(s) will have little or no market value; and

c. whether the agreement gives the “lessee” an **option to purchase** the leased good(s) at the end of the lease term for **little or no additional consideration**; and

4. **Economic Realities Test:** Considers the likelihood, at the time the transaction is entered into, that the lessor will receive the goods that still have meaningful economic life at the end of the lease term. If there is a reasonable likelihood the lessor will retain some residual interest in the goods, the transaction is probably a true lease; if not, the transaction is a disguised sale intended for security.

B. **Types of Leases Identified in Article 2A**

1. **“Consumer Lease”**: a lease made by someone in the business of leasing to an individual for the individual’s personal use. § 2A-103(1)(e).

2. **“Finance Lease”**: Subject to the conditions imposed by § 2A-103(1)(g)(iii), any lease made by a lessor who

   a. does not select, manufacture, or supply the goods; and

   b. acquires from a third party, *in connection with the lease*, title or the right to possess and use.

   ![Diagram of Finance Lease]

OR

![Diagram of Alternative Finance Lease]
C. Effect of Other Laws

1. Although Article 2 purports to apply to all “transactions in goods,” it yields to the more specific rules of Article 2A when the transaction in question is a lease of goods.

2. Leases subject to Article 2A may also be subject to state certificate of title laws and consumer protection laws; and, where there is an apparent conflict between Article 2A and a state’s certificate of title and/or consumer protection laws, the latter “trump” Article 2A except that Sections 2A-105, 2A-304(3), and 2A-305(3) “trump” any other statute.

VI. The U.N. Convention on Contracts for the International Sale of Goods (CISG)

A. General Rule: Contracts for the sale of goods between a resident of the U.S. and a resident of another country are governed by the 1980 United Nations Convention on Contracts for the International Sale of Goods (“CISG”).

♦ As of August 1, 2011, the United States and 76 other countries had acceded, accepted, approved, ratified, or succeeded to the CISG and the convention was in force in all but one of those 77 countries (Benin).

B. Exceptions: The CISG does not apply to a contract for the sale of goods if

1. the foreign buyer or seller’s place of business or “habitual residence” is in a country that has not ratified the CISG, Arts. 1(1)(a) & 10(b);

2. the buyer or seller neither knew nor had reason to know that it was dealing with a party whose place of business or habitual residence was in a foreign country, Art. 1(2);

3. the goods are being purchased for personal, family, or household use, unless the seller neither knew nor had reason to know at any time prior to or at the conclusion of the contract of the goods’ intended use by the buyer, Art. 2(a);

4. the sale is otherwise excluded by Art. 2(b)-(f);

5. the buyer of specially-manufactured goods undertakes to supply the seller with “a substantial part of the materials necessary” to manufacture the goods, Art. 3(1); or

6. the preponderant part of the seller’s obligations consists of providing labor or other services, Art. 3(2).
C. Freedom of Contract

1. Parties to a contract that would otherwise be governed by the CISG may contractually agree not to be governed by it in part or in whole, Art. 6, subject to certain limitations set forth in Article 12.

2. By the same token, parties to a contract that would otherwise not be governed by the CISG may contractually agree to be governed by it in part or in whole, except to the extent that the CISG may conflict with some inalienable domestic law provision.

D. Resolving Conflicts Between the CISG and the UCC: The CISG “trumps” the UCC in cases where the CISG applies. See U.S. CONST. art. VI, cl. 2.

E. Resolving Conflicts Between Domestic and non-CISG Foreign Law: While this is a potentially sticky issue, given that a handful of the United States’ major trading partners have not ratified the CISG, in the absence of some specific foreign law, we will err on the side of oversimplifying and apply the UCC or common law, whichever is appropriate.

VII. The Uniform Electronic Transactions Act and Related Law

A. Basic Scope: UETA applies to “electronic records and electronic signatures relating to a transaction” governed, inter alia, by common law and UCC Article 2. UETA § 3(a) & (b)(2).

♦ UETA does not specifically indicate that it applies to contracts governed by the CISG. However, § 3(a) provides that, unless excluded by § 3(b), UETA applies to all transactions.

B. “Opting In”: UETA only applies to transactions “between parties each of which has agreed to conduct transactions by electronic means.” Id. § 5(b).

♦ Whether the parties agree to transact electronically “is determined from the context and surrounding circumstances, including the parties’ conduct.” Id.

♦ For example, if S faxed her offer to B, and B e-mailed his acceptance to S, the parties have agreed by conduct to transact electronically. See id. §§ 2(5) & 5 cmt. 4.

C. Procedure vs. Substance: Unlike common law, UCC Article 2, or the CISG, UETA is not intended to be a comprehensive body of law that governs electronic transactions. Rather, it is intended (not unlike Revised UCC Article 1) to cut across a number of substantive bodies of law and to supplement them in such a way as to facilitate electronic transacting. See id. § 3(d).
D. Contracts governed by the law of a state that has not enacted UETA (Illinois, New York, and Washington) – and, perhaps, contracts otherwise governed by the law of a UETA-enacting state but in which both parties have not consented to transact electronically – are subject to the federal **Electronic Signatures in Global and National Commerce Act** ("E-SIGN"), 15 U.S.C. § 7001 *et seq.*, which has much the same effect as UETA.

♦ Unlike most instances where federal and state legislation overlap, E-SIGN explicitly yields to UETA. *See* 15 U.S.C. § 7002(a)(1).