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## THE DIMINISHING DIFFERENCE BETWEEN SELLING AND LEASING TANGIBLE PERSONAL PROPERTY

RICHARD MARSHALL ABRAMS†

### I. INTRODUCTION

**T**HE LAW OF TANGIBLE PERSONAL PROPERTY has long recognized the distinction between sales and leases:

A sale transfers ownership and possession of the article in exchange for the price; a bailment for hire [lease] transfers possession in exchange for the rental and contemplates eventual return of the article to the owner. By means of a bailment parties can often reach the same business ends that can be achieved by selling and buying.<sup>1</sup>

The two categories of tangible personal property leases are the conventional or "true" lease and the finance or "security" lease.<sup>2</sup> The true lease is a bailment for hire in accordance with what is commonly meant by the term "lease."<sup>3</sup> The finance lease is basically a type of security agreement or secured installment sales contract in which a financier purchases property from the actual supplier and then rents it to the lessee.<sup>4</sup> In a true lease, the lessor is the supplier of the

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1. *Cintrone v. Hertz Truck Leasing & Rental Serv.*, 45 N.J. 434, 447, 212 A.2d 769, 776 (1965). See Farnsworth, *Implied Warranties of Quality in Non-Sales Cases*, 57 COLUM. L. REV. 653, 655 (1957); Comment, *The Extension of Article 2 of the Uniform Commercial Code to Leases of Goods*, 12 TULSA L.J. 556, 557-58 (1977).

2. See generally J. WHITE & R. SUMMERS, UNIFORM COMMERCIAL CODE § 22-3, at 759-65 (1972). The Uniform Commercial Code defines a "security interest" as "an interest in personal property or fixtures which secures payment or performance of an obligation." U.C.C. § 1-201(37). This section also provides that "[w]hether a lease is intended as security is to be determined by the facts of each case." *Id.* See also Peden, *The Treatment of Equipment Leases as Security Agreements under the Uniform Commercial Code*, 13 WM. & MARY L. REV. 110 (1971); Note, 84 YALE L.J. 1722, 1723 (1975).

3. See 1B BENDER'S UNIFORM COMMERCIAL CODE SERVICE, SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE § 29B.02[2], at 2989-90 (1975) [hereinafter cited as SECURED TRANSACTIONS]; *id.* § 29A.02-.03, at 2917-22; DeKoven, *Leases of Equipment: Puritan Leasing Company v. August, A Dangerous Decision*, 12 U.S.F. L. REV. 257, 258 (1978).

4. See 1 SECURED TRANSACTIONS, *supra* note 3, § 4A.06, at 4A-73 to 4A-112 (1977); DeKoven, *supra* note 3, at 258; Note, 56 NEB. L. REV. 354, 354 (1977).

It has been suggested that there are two kinds of leases that are security interests. J. WHITE & R. SUMMERS, *supra* note 2, § 22-3, at 762-65. The first is a secured installment sale drafted in lease terminology. *Id.* at 762. The second transaction resembles a lease exactly but the "economic realities" mandate a purchase by the lessee at the end of the term. *Id.* at

product and expects its return at the end of the lease term; in a finance lease, the lessor is not the supplier but rather the financier or secured party whose collateral is the product and who does not expect its return at the end of the lease term.<sup>5</sup> A finance lessor supplies the use of money instead of a product.<sup>6</sup> Whereas a true lessor has a reversionary right in the product, a finance lessor has a security interest in the product.<sup>7</sup>

Since the finance lease is essentially a financing arrangement in the form of a lease, it will not be considered further. The remainder of this article will deal exclusively with the true lease and its comparison with an outright sale.

The basic distinction between a lease and a sale is that the passage of title occurs in a sale but not in a lease.<sup>8</sup> It is submitted that the consequences of that distinction are rapidly diminishing. Some courts look more at the purpose and substance of the transaction than its form or the passage of title.<sup>9</sup> This type of analysis has impliedly rejected the notion that the passage or retention of title automatically

763-64. Courts have characterized both of these transactions as security interests. *See id.* One commentator has suggested that three elements must be considered in determining whether a lease is a finance lease: "(1) there must be an agreement by the lessee to pay the lessor a set amount; (2) such amount must be equivalent to the value of the leased goods; and (3) the lessee must become the owner of or have the option to become the owner of the leased goods." DeKoven, *supra* note 3, at 259 (footnote omitted).

A finance lease which is found to be a security agreement will subject the lessor to the filing and perfection requirements of article 9 of the Uniform Commercial Code, U.C.C. art. 9. *See id.* § 9-102 (1)(a). A secured party lessor will also be subject to the Uniform Commercial Code's remedial provisions in event of the lessee's default. *Id.* § 9-504.

5. *See In re Leasing Consultants, Inc.*, 351 F. Supp. 1390, 1392-93 (E.D.N.Y. 1972), *re-manded for evidentiary hearing*, 486 F.2d 367 (2d Cir. 1973); *Francioni v. Gibsonia Truck Corp.*, 472 Pa. 362, 369 n.3, 372 A.2d 736, 740 n.3 (1977); Claxton, *Lease or Security Interest: A Classic Problem of Commercial Law*, 28 MERCER L. REV. 599 (1977); DeKoven, *supra* note 3, at 259; Note, *Warranties in the Leasing of Goods*, 31 OHIO ST. L.J. 140, 147-50 (1970); Note, *supra* note 4, at 358-59; Note, *supra* note 2, at 1723. *See also* U.C.C. § 1-201(37).

6. *See Francioni v. Gibsonia Truck Corp.*, 472 Pa. 362, 369 n.3, 372 A.2d 736, 740 n.3 (1977).

7. Note, *supra* note 2, at 1723.

8. *Cintrone v. Hertz Truck Leasing & Rental Serv.*, 45 N.J. 434, 447, 212 A.2d 769, 776 (1965). The Uniform Commercial Code states that "[a] 'sale' consists in the passing of title from the seller to the buyer for a price." U.C.C. § 2-106(1). A lease, on the other hand, "merely transfers possession in exchange for the rental and contemplates the return of the chattel to the owner." Farnsworth, *supra* note 1, at 655.

9. *See, e.g.*; *KLPR TV, Inc. v. Visual Electronics Corp.*, 465 F.2d 1382, 1385 (8th Cir. 1972) (lease of television broadcasting equipment analogous to a sale); *Sawyer v. Pioneer Leasing Corp.*, 244 Ark. 943, 950-57, 428 S.W.2d 46, 50-54 (1968) (U.C.C. § 2-316(2) governing exclusion or modification of warranties is applicable to a lease where the lease provisions are analogous to a sale); *Cintrone v. Hertz Truck Leasing & Rental Serv.*, 45 N.J. 434, 445-46, 212 A.2d 769, 775-76 (1965) (implied warranties of sale at common law applicable to a lease). *See generally* BENDER'S UNIFORM COMMERCIAL CODE SERVICE, 3 SALES & BULK TRANSFERS UNDER THE UNIFORM COMMERCIAL CODE § 1.03[4], at 1-35 to 1-62 (1977) [hereinafter cited as SALES & BULK TRANSFERS].

determines the rights and obligations between the parties,<sup>10</sup> since title is not necessarily related to those rights and obligations.<sup>11</sup> The diminishing consequences of whether a transaction is a sale or a lease will be examined in the following areas of law: 1) implied warranties; 2) strict liability in tort; 3) the doctrine of unconscionability; 4) anti-trust law; and 5) tax law. Before considering these legal consequences, we will first examine some of the practical consequences of buying or leasing a product from the viewpoint of the consumer.

## II. PRACTICAL CONSEQUENCES OF A PURCHASE VERSUS A LEASE

One who wishes to acquire tangible personal property must decide whether to buy it or lease it.<sup>12</sup> There are several advantages to buying. A purchaser of a product receives an asset for his money, rather than incurring an expense by leasing, and thereby improves the appearance of his long term financial position on a balance sheet.<sup>13</sup> This permanent ownership of an asset gives the buyer an "equity" or "residual" value in the product and the opportunity to continue using it long after it has been paid for.<sup>14</sup> In addition, a purchase acts as a hedge against inflation since it is made at current prices. In contrast, when a lease expires, it costs more to replace or release the product at future prices.<sup>15</sup>

There are, however, advantages to leasing.<sup>16</sup> Since leasing does not require a large outlay of cash, working capital remains free for other uses.<sup>17</sup> Additionally, in a true lease the freed working capital

10. See Comment, *supra* note 1, at 559. One commentator has stated that "[o]ne of the most fundamental changes brought about by Article 2 was a decreased reliance on the concept of title. Pre-Code law relied on the title theory, whereby the location of title determined the rights and duties of the parties." *Id.* (footnotes omitted).

11. See U.C.C. § 2-101, Comment. The official comment to § 2-101 states that "[t]he legal consequences [of the contract for sale] are stated as following directly from the contract and action taken under it without resorting to the idea of when property or title passed or was to pass as being the determinative factor." *Id.* It would seem that those courts which apply sales principles to leases because of the similarity between the lease and a sale accept this rationale.

12. See generally *Symposium: Commercial Leasing*, 1972 U. ILL. L.F. 433 [hereinafter cited as *Commercial Leasing*]; *Symposium: Equipment Leasing*, 1962 U. ILL. L.F. 1 [hereinafter cited as *Equipment Leasing*]. For a list of factors and problems which a party should be aware of before entering into either type of transaction, see Meyers, *A Worksheet for Leasing Equipment*, 23 PRAC. LAW. 59 (July 1977) [hereinafter cited as *Leasing Worksheet*]; Meyers, *A Worksheet for Purchasing Complex and Expensive Equipment*, 20 PRAC. LAW. 53 (Oct. 1974).

13. See Boothe, *The Practical Pros and Cons of Leasing*, 1962 U. ILL. L.F. 1, 3-4; Edmonds, *An Introduction to Financial Statements for the Practicing Lawyer*, 4 BLACK L.J. 196, 198, 201-04 (1975).

14. See Adkins & Bardos, *The Leasing Transaction*, 1972 U. ILL. L.F. 16, 20; Boothe, *supra* note 13, at 3-4.

15. See Shapiro, *The ABC's of Leasing*, 1972 U. ILL. L.F. 433, 433.

16. See generally *Commercial Leasing*, *supra* note 12; *Equipment Leasing*, *supra* note 12.

17. See Dean, *The Economics of Equipment Leasing*, 1962 U. ILL. L.F. 33, 47; Shapiro, *supra* note 15, at 434. As one commentator has explained, a reason for choosing to lease is

improves the appearance of the short term financial position as indicated on a balance sheet.<sup>18</sup> Leasing is also preferable when permanent ownership is not desired, such as when a product is in a high technology field and is likely to become obsolete quickly,<sup>19</sup> is subject to frequently changing government regulations, or is likely to wear out quickly or need constant repair.<sup>20</sup>

To a company or individual experiencing a cash shortage, leasing can be a particularly useful alternative to a purchase financed by a loan.<sup>21</sup> In this situation, leasing has the additional advantages of con-

the lessee's feeling that he will be able to use the cash which is not expended for the item to generate more than sufficient profits to offset the cost of leasing. If the lessee has limited bank lines or is subject to lending restrictions imposed upon buying, he may be prevented from purchasing the equipment. In either situation, leasing has the effect of expanding the lessee's working capital.

*Id.* It has been argued, however, that although the desire to increase working capital may be a major factor in the decisionmaking process, the increased profits resulting from the freed working capital are illusory. Boothe, *supra* note 13, at 4, 10.

18. See Wyatt, *Accounting for Leases*, 1972 U. ILL. L.F. 497, 498-99. This improved financial position is due to the fact that lease payments do not appear as a liability on the balance sheet, but instead are listed as an expense. *Id.* Two basic methods are used by accountants to account for the various kinds of leases. *Id.* at 498. As one commentator has stated:

Accountants have come to classify leases for accounting purposes as either operating leases or financing leases. Operating leases are those determined to be principally in the nature of a "true" lease. The lessee is generally committing himself on a noncancellable basis for a period less than the life of the property being leased. The lessor is generally retaining significant rights in connection with the leased property so that when the lease term expires he will have control of the property either for releasing or other disposition. Under an operating lease the lessee recognizes the lease rental payments as an expense in the period in which the property is used. The lessee may additionally disclose in a financial statement footnote the commitments existing at a balance sheet date for existing leases. The lessor of an operating lease will recognize the lease rentals receivable in a period as revenue and will charge against income depreciation on the leased property, maintenance, and other related costs.

*Id.* at 498-99. The lessee in a finance or capital lease must record the present value of the noncancellable lease commitment as an asset and a similar amount as a long term liability. *Id.* at 499. The Securities and Exchange Commission (SEC) has recently adopted a rule which sets standards for the recordation of capital or nonoperating leases on financial statements. 17 C.F.R. § 210.3-16(q) (1978). See also *Accounting for Leases*, PROFESSIONAL STANDARDS: ACCOUNTING (CCH) § 4053, at 8421 (1978). The source of this section is Financial Accounting Standards Board, Statement No. 13. *Id.* The SEC incorporated this statement in promulgating 17 C.F.R. § 210.3-16(q) (1978). 42 Fed. Reg. 44,807 (1977). Financial Accounting Standards Board, Statement No. 13 has since been modified by Financial Accounting Standards Board, Statements Nos. 27 and 28.

19. See Boothe, *supra* note 13, at 13; Davis, *Tax Consequences of Leasing Transactions*, 1962 U. ILL. L.F. 56, 57; Dean, *supra* note 17, at 37; Shapiro, *supra* note 15, at 433.

20. See Dean, *supra* note 17, at 37. The lessee can shift the burden of repair to the lessor. *Id.*; Steadman, *Chattel Leasing—A Vehicle for Capital Expansion*, 14 BUS. LAW. 523, 527 (1959).

21. See Adkins & Bardos, *supra* note 14, at 18-19. A lease, unlike a purchase, does not require a down payment and therefore does not immediately drain capital. *Id.* It has been contended that in the long run leasing may be more expensive than purchasing since "the leasing company not only must borrow its money, at comparable rates, but must also add sufficient charges to cover the costs of purchasing the property, processing vendors' invoices, preparing leases and allied documentation, . . . and, presumably, returning a profit to the lessor." Boothe, *supra* note 13, at 6. This "blanket generalization" has been rejected by one commentator who argues that "[t]he acid test is the quantitative comparison of each specific lease pro-

serving credit,<sup>22</sup> of not depleting cash by requiring a down payment,<sup>23</sup> and of not increasing the long term liabilities on the balance sheet by adding a loan obligation.<sup>24</sup> Leasing is also advantageous when the lessee desires other services provided by the leasing company, such as accounting or maintenance and repair.<sup>25</sup> Since the lessee's only expense is the rental payments, bookkeeping is simplified.<sup>26</sup>

With consumer products, leasing instead of buying brings the lessee within the scope of the Consumer Leasing Act of 1976 (Act).<sup>27</sup> The Act affords protection to lessees who have entered a consumer lease, which is defined as

a contract in the form of a lease or bailment for the use of personal property by a natural person for a period of time exceeding four months, and for a total contractual obligation not exceeding \$25,000, primarily for personal, family, or household purposes, whether or not the lessee has the option to purchase or otherwise become the owner of the property at the expiration of the lease . . . .<sup>28</sup>

The Act, however, does not apply to leases for agricultural, business, or commercial purposes, or a lease to an organization.<sup>29</sup> A lessor entering a consumer lease is required by the Act to provide the lessee with a dated written statement of the following information: a description of the leased property; the amount of any advance payment, such as a security deposit; the number, amount, and due dates of the periodic payments; other payments payable by the lessee; other liabilities imposed on the lessee and whether or not he has the option to purchase the leased property; all express warranties and guarantees made by the manufacturer or lessor; insurance; and terms and conditions of termination.<sup>30</sup>

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posal with the relevant ownership alternative." Dean, *supra* note 17, at 40. This commentator indicates that the equipment user must do six things in order to decide whether to lease or to purchase: "(1) forecast the use period of the equipment in question, (2) estimate annual lease payments, (3) estimate ownership costs, (4) estimate net salvage or resale value, (5) adjust for income taxes, and (6) find the capital worth of the stream of yearly cash cost differences between owning and leasing." *Id.* at 49.

22. See Shapiro, *supra* note 15, at 434.

23. *Id.* at 433-34. See also Adkins & Bardos, *supra* note 14, at 18-19.

24. For a discussion of how leases affect the lessee's balance sheet, see note 18 *supra*.

25. See Dean, *supra* note 17, at 44-46. By leasing, financing, marketing, repairing, and record keeping functions can be transferred from the lessee to the lessor. *Id.* at 45. See note 20 *supra*.

26. See Wyatt, *supra* note 18, at 498-99.

27. 15 U.S.C. §§ 1667, 1667a-1667e (1976) (amending the Truth in Lending Act, 15 U.S.C. §§ 1601-1665a (1976)) (effective Mar. 23, 1977).

28. 15 U.S.C. § 1667(1) (1976).

29. *Id.*

30. *Id.* § 1667a.

In addition to these disclosure requirements, the Act restricts penalties that may be imposed by the lessor.<sup>31</sup> When the lessee's liability on expiration of the lease is based on the estimated residual value of the property, the Act limits this liability to "a reasonable approximation of the anticipated actual fair market value of the property on lease expiration,"<sup>32</sup> and provides for an independent professional appraisal of the property.<sup>33</sup> The Act also regulates claims made in consumer lease advertising.<sup>34</sup>

A purchase with some of the advantages of a lease can be made by the use of a conditional or installment sale.<sup>35</sup> These transactions usually require a down payment, however, and the conditional sale obligation would also have to be carried as a liability on the balance sheet.<sup>36</sup> Conversely, a lease with an option allowing the user or lessee to buy the property at the end of the lease for a nominal price is a lease with some of the advantages of a purchase.<sup>37</sup> This type of lease-purchase arrangement may be treated as a conditional sale by the Internal Revenue Service.<sup>38</sup>

31. *Id.* § 1667b(b). This section provides:

Penalties or other charges for delinquency, default, or early termination may be specified in the lease but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the delinquency, default, or early termination, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy.

*Id.*

32. *Id.* § 1667b(a).

33. *Id.* § 1667b(c).

34. *Id.* § 1667c.

35. See generally J. WHITE & R. SUMMERS, *supra* note 2, § 22-3, at 759-65. An installment sale in which the seller retains title to secure an obligation of the buyer to pay for the purchase is subject to the requirements for secured transactions of article 9 of the Uniform Commercial Code, U.C.C. art. 9. J. WHITE & R. SUMMERS, *supra* note 2, § 22-3, at 759-60. Article 9 applies "to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures." U.C.C. § 9-102(1)(a). The distinction between a conditional sale and a lease is often difficult to discern since transactions which are labelled leases frequently are in fact nothing but disguised security transactions. See J. WHITE & R. SUMMERS, *supra* note 2, § 22-3, at 759-65.

It has been suggested that the costs of leasing an item and of purchasing it with an installment sale are almost equal. Adkins & Bardos, *supra* note 14, at 17. As these authors stated:

For practical purposes, then, the amounts paid by a lessee and received by a lessor over the life of a lease of equipment (irrespective of optional renewals) will probably not differ materially from the amount which would be paid and received if such equipment were conditionally sold to the lessee. However, when the lease terminates, any residual value, whether for scrap or for use, will be in the lessor, not in the lessee.

*Id.*

36. The purchased item would be classified as an asset and therefore the corresponding sale obligation would have to be listed on the balance sheet. See generally B. FERST & S. FERST, *BASIC ACCOUNTING FOR LAWYERS* 68-73 (3d ed. 1975); Edmonds, *supra* note 13, at 198.

37. For factors relevant in determining whether to include an option to buy in a lease, see *Leasing Worksheet*, *supra* note 12, at 63.

38. See notes 141-47 and accompanying text *infra*.

All of these practical considerations become increasingly important when deciding whether to lease or purchase because of the diminishing legal differences between a lease and a sale, which will now be considered.

### III. IMPLIED WARRANTIES

The two implied warranties of quality that the Uniform Commercial Code (Code) recognizes in sales contracts are those of merchantability<sup>39</sup> and fitness for a particular purpose.<sup>40</sup> Prior to the adoption of the Code, warranties which were closely analogous to the Code's warranty of fitness for a particular purpose had been extended to bailments.<sup>41</sup> The warranties under the Code are now implied into leases as well as sales, although the warranty of fitness has been more widely accepted than the warranty of merchantability.<sup>42</sup>

#### A. Implied Warranty of Fitness

The courts now imply the warranty of fitness for a particular purpose into nonsales contracts, particularly bailments for hire.<sup>43</sup> One commentator has explained the reason for this extension as follows:

The expansion of enterprises engaged solely in bailment for hire seems to justify increasing imposition of absolute warranties, at least to the extent that they would be imposed upon a seller of similarly used goods. In addition, reliance is greater than in the typical sale, for it is generally true that the bailee for hire spends less time shopping for the article than he would in selecting like

39. U.C.C. § 2-314. This section provides in pertinent part: "Unless excluded or modified (Section 2-316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind." *Id.* § 2-314(1).

40. *Id.* § 2-315. This section provides:

Where the seller at the time of contracting has reason to know any particular purpose for which the goods are required and that the buyer is relying on the seller's skill or judgment to select or furnish suitable goods, there is unless excluded or modified under the next section an implied warranty that the goods shall be fit for such purpose.

*Id.* For a discussion of how other sections of article 2 of the Code, U.C.C. art. 2, have been applied to lease transactions, see Comment, *supra* note 1, at 556-73.

41. See, e.g., *Palmquist v. Mercer*, 43 Cal. 2d 92, 272 P.2d 26 (1954) (horses); *Hoisting Engine Sales Co. v. Hart*, 237 N.Y. 30, 142 N.E. 342 (1923) (derrick); *Dufort v. Smith*, 53 Pa. D. & C. 307 (Luzerne County C.P. 1944) (airplane); *Hilton v. Wagner*, 10 Tenn. App. 173 (1928) (automobile). See generally Farnsworth, *supra* note 1, at 655-60.

42. See Farnsworth, *supra* note 1, at 655-57; Murray, *Under the Spreading Analogy of Article 2 of the Uniform Commercial Code*, 39 FORDHAM L. REV. 447, 449-54 (1971).

43. See, e.g., *Sawyer v. Pioneer Leasing Corp.*, 244 Ark. 943, 950-57, 428 S.W.2d 46, 50-54 (1968); *Hertz Commercial Leasing Corp. v. Transportation Credit Clearing House*, 59 Misc. 2d 226, 231, 298 N.Y.S.2d 392, 398 (1969). See 3 SALES & BULK TRANSFERS, *supra* note 9, § 1.03 [4]a, at 1-37 to 1-50; Farnsworth, *supra* note 1, at 655-57; Murray, *supra* note 42, at 449-54. See also Annot., 48 A.L.R.3d 668 (1973); Annot., 68 A.L.R.2d 850 (1959).



goods to be purchased, and since the item is not one he expects to own, he will usually be less competent in judging its quality.<sup>44</sup>

Some courts have held that, as with a sale, only a lease by a merchant of the goods transferred would have the implied warranty of fitness for a particular purpose.<sup>45</sup> The policy considerations that justify the imposition of warranties in both sales and leases by merchants include

(a) public policy which requires that the party which puts goods into the stream of commerce should bear the risk of harm caused by defective goods, rather than the person injured by it; (b) the fact that one party has induced the reliance of the consumer on his skill and knowledge; (c) the fact that the former is in a better position to control the antecedents which affect the quality of the product; and (d) the fact that he is better able to distribute the loss.<sup>46</sup>

The extension of warranty protection to leases of tangible personal property has been acknowledged by the drafters of the Code in an official comment, which states that "the warranty sections of this Article are not designed in any way to disturb those lines of case law growth which have recognized that warranties need not be confined . . . to sales contracts . . . . They may arise in other appropriate circumstances such as in the case of bailments for hire . . . ." <sup>47</sup>

44. Farnsworth, *supra* note 1, at 673-74. See also *Cintrone v. Hertz Truck Leasing & Rental Serv.*, 45 N.J. 434, 446-47, 212 A.2d 769, 775-76 (1965). Discussing whether warranties should be applied to leases, the Supreme Court of Idaho has stated that "[t]he essence of both transactions is that the lessee/buyer seeks to acquire the right to use a good and the lessor/seller seeks to sell the right to use a good." *Glenn Dick Equip. Co. v. Galey Constr., Inc.*, 97 Idaho 216, 222, 541 P.2d 1184, 1190 (1975).

45. See *W.E. Johnson Equip. Co. v. United Airlines, Inc.*, 238 So. 2d 98, 100 (Fla. 1970). Although the warranty of fitness will not apply to all lease transactions, the Supreme Court of Florida reasoned that it should be recognized when appropriate. *Id.* The court stated:

Just as in sales cases, whether the warranty should be applied may depend upon whether the lessor possessed or should have possessed expertise in the characteristics of the leased chattel, whether the lessee's reliance upon the lessor's selection of a suitable chattel was commercially reasonable, and whether the lessor was a mass dealer in the chattel leased or whether the transaction was an isolated occurrence.

*Id.* See also *Glenn Dick Equip. Co. v. Galey Constr., Inc.*, 97 Idaho 216, 225, 541 P.2d 1184, 1193 (1975) (implied warranties of merchantability and fitness for a particular purpose arise because lessor was a merchant and lessee relied on merchant's expertise).

46. Commentary, *The Extension of Warranty Protection to Lease Transactions*, 10 B.C. INDUS. & COM. L. REV. 127, 140-41 (1968). Although this statement suggests that the necessity of implying a warranty of fitness for a particular purpose is most compelling where the lessor is a merchant, the lessor's status should not be controlling. *Id.* at 141-42.

Under the Code, a seller does not necessarily have to be a merchant in the goods supplied for an implied warranty of fitness for a particular purpose to apply. U.C.C. § 2-315. An official comment to this section states: "Although normally the warranty will arise only where the seller is a merchant with the appropriate 'skill or judgment,' it can arise as to non-merchants when this is justified by the particular circumstances." *Id.*, Comment 4.

47. U.C.C. § 2-313, Comment 2. The Supreme Court of Idaho listed three possible rationales for finding the implied warranty provisions of article 2 of the Code, *id.* art. 2, appli-

This trend of applying sales warranties to leases has not been confined to transactions in personal property, but has also been extended to transactions in real property as well, particularly residential realty.<sup>48</sup> Courts have found an implied warranty of fitness in contracts of sale for new houses.<sup>49</sup> As stated in one federal case involving the presence of dangerous lead based paint in a house sold by the United States Department of Housing and Urban Development:

The [United States] Supreme Court has long held that the law will imply a warranty of fitness for the purpose intended when a buyer has reason to rely on, and does rely on, the judgment of the seller who produces the product, especially, as to latent defects. . . . The application of this principle in the field of housing has resulted in the declaration of an implied warranty of habitability to exist between a builder-vendor of a new home and the purchaser thereof.<sup>50</sup>

This warranty of habitability has been implied into residential leases as well as residential sales.<sup>51</sup> The rationale for the implication of this warranty is the similarity between the lease and sale transactions,<sup>52</sup> which was also the rationale for finding a warranty of fitness in the lease of personal property.<sup>53</sup> As the United States Court of

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cable to a lease: 1) a lease was within the scope of article 2 since it was a transaction in goods; 2) a specific lease was analogous to a sale of goods since it was actually a "disguised sale" and therefore the lease was subject to article 2; and 3) the economic considerations involved in leasing and selling were so similar that certain provisions of article 2 were applicable by analogy to lease transactions. *Glenn Dick Equip. Co. v. Galey Constr., Inc.*, 97 Idaho 216, 220-21, 541 P.2d 1184, 1188-89 (1975). For a general discussion of the applicability of Code warranties to bailments for hire, see Murray, *supra* note 42, at 449-54. See also Annot., 48 A.L.R.3d 668, 674 (1973).

48. See Murray, *supra* note 42, at 454-65. See also 3 SALES & BULK TRANSFERS, *supra* note 9, § 1.03[4], at 1-44 to 1-47 (construction contracts).

49. See, e.g., *Peterson v. Hubschman Constr. Co.*, 76 Ill. 2d 31, 39-40, 389 N.E.2d 1154, 1159 (1979); *McDonald v. Mianeki*, 79 N.J. 275, \_\_\_, 398 A.2d 1283, 1292 (1979); *Elderkin v. Gaster*, 447 Pa. 118, 124-30, 288 A.2d 771, 775-77 (1972). For a discussion of the application of the doctrine of caveat emptor to the sale of houses, see McNamara, *The Implied Warranty in New-House Construction: Has the Doctrine of Caveat Emptor Been Abolished?*, 1 REAL EST. L.J. 43 (1973); Murray, *supra* note 42, at 454-59.

50. *City of Philadelphia v. Page*, 363 F. Supp. 148, 151 (E.D. Pa. 1973) (citations omitted), *motion to vacate order denied*, 373 F.Supp. 453 (E.D. Pa. 1974).

51. See, e.g., *Javins v. First Nat'l Realty Corp.*, 428 F.2d 1071, 1072-81 (D.C. Cir.), *cert. denied*, 400 U.S. 925 (1970); *Kline v. Burns*, 111 N.H. 87, 92, 276 A.2d 248, 251-52 (1971); *Marini v. Ireland*, 56 N.J. 130, 144, 265 A.2d 526, 534 (1970); *Park Hill Terrace Associates v. Glennon*, 146 N.J. Super. 271, 277, 369 A.2d 938, 942 (1977); *Morbeth Realty Corp. v. Valez*, 73 Misc. 2d 996, 999, 343 N.Y.S.2d 406, 410 (Civ. Ct. N.Y. 1973); *Fair v. Negley*, \_\_ Pa. Super. Ct. \_\_\_, 390 A.2d 240, 242-43 (1978); *Pugh v. Holmes*, 253 Pa. Super. 76, 87, 384 A.2d 1234, 1236 (1978). For a discussion of the development of implied warranties of habitability in residential leases, see Line, *Implied Warranties of Habitability and Fitness for Intended Use in Urban Residential Leases*, 26 BAYLOR L. REV. 161 (1974); Moreno, *The Warranty of Uninhabitability*, 7 SAN FERN. V. L. REV. 67 (1978); Murray, *supra* note 42, at 459-64. See also Annot., 40 A.L.R.3d 646 (1971).

52. See *Javins v. First Nat'l Realty Corp.*, 428 F.2d 1071, 1075-76 (D.C. Cir.), *cert. denied*, 400 U.S. 925 (1970).

53. See notes 44, 46 & 47 and accompanying text *supra*.

Appeals for the District of Columbia Circuit stated in the leading case of *Javins v. First National Realty Corp.*:<sup>54</sup>

The rigid doctrines of real property law have tended to inhibit the application of implied warranties to transactions involving real estate. Now, however, courts have begun to hold sellers and developers of real property responsible for the quality of their product. . . .

Despite this trend in the sale of real estate, many courts have been unwilling to imply warranties of quality, specifically a warranty of habitability, into leases of apartments. Recent decisions have offered no convincing explanation for their refusal; rather they have relied without discussion upon the old common law rule that the lessor is not obligated to repair unless he covenants to do so in the written lease contract. . . . In our judgment, the old no-repair rule cannot coexist with the obligations imposed on the landlord by a typical modern housing code, and must be abandoned in favor of an implied warranty of habitability.<sup>55</sup>

### B. Implied Warranty of Merchantability

As previously stated, the implied warranty of fitness has been more widely incorporated into leases of tangible personal property than has the implied warranty of merchantability.<sup>56</sup> Where a product was unfit for its common use, the tendency has been to consider whether it was fit for the particular use of the lessee and not whether it conformed "to a standard of 'bailability' analogous to that of merchantability."<sup>57</sup> This tendency has been changing, however, and

54. 428 F.2d 1071 (D.C. Cir.), cert. denied, 400 U.S. 925 (1970). The landlord in *Javins* sought possession of premises leased to the appellants on the grounds that the tenants had defaulted on rental payments. 428 F.2d at 1073. The tenants admitted that they had not paid the rent, but alleged as a defense that numerous violations of the District of Columbia housing regulations entitled them to a set-off. *Id.* The court held that "a warranty of habitability, measured by the standards set out in the Housing Regulations for the District of Columbia, is implied by operation of law into leases of urban dwelling units . . . and that breach of this warranty gives rise to the usual remedies for breach of contract." *Id.* at 1072-73.

55. 428 F.2d at 1076-77 (footnotes omitted). Judge Skelly Wright's opinion in *Javins*, in the words of one commentator, "denounced this blind adherence to and application of the old rules and discarded the archaic property principles as they applied to the modern landlord-tenant relationships." Moreno, *supra* note 51, at 69.

56. See text accompanying note 42 *supra*.

57. Farnsworth, *supra* note 1, at 657 (footnote omitted). See Annot., 48 A.L.R.3d 668, 673 (1973). The implied warranty of merchantability for sales is codified in U.C.C. § 2-314. *Id.* § 2-314. The Code lists six factors to be examined in determining whether a good is merchantable:

- (2) Goods to be merchantable must be at least such as
  - (a) pass without objection in the trade under the contract description; and
  - (b) in the case of fungible goods, are of fair average quality within the description; and

some courts are more willing to hold that leases contain both warranties.<sup>58</sup> In *Javins*, for example, the D.C. Circuit observed that “[c]ourts have not hesitated to find implied warranties of fitness and merchantability.”<sup>59</sup> Similarly, in a case involving the lease of a “U-Haul” trailer, a Pennsylvania lower court stated somewhat exuberantly that “the authorities are uniform in holding that the implied warranty arises in the case of a lease as freely as in the case of a sale.”<sup>60</sup>

This erosion of the distinction between an implied warranty of merchantability and one of fitness for an intended use is rational since most of the same public policy considerations apply to both warranties. A merchant who places property into the stream of commerce should bear the risk of harm caused by defects since he is better able to control its quality and distribute the loss, and to some extent has induced the public to rely on his skill and knowledge.<sup>61</sup> There is no reason why only one type of warranty should be implied into a lease.

### C. Disclaimer of Implied Warranties

The disclaimer provisions of the Code specify and limit the manner in which the implied warranties of fitness and merchantability can be excluded or modified.<sup>62</sup> To effectively exclude or modify the implied warranty of merchantability, “the language must mention mer-

- (c) are fit for the ordinary purposes for which such goods are used; and
- (d) run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved; and
- (e) are adequately contained, packaged, and labeled as the agreement may require; and
- (f) conform to the promises or affirmations of fact made on the container or label if any.

*Id.* § 2-314(2). For a discussion of the implied warranty of merchantability under the Code, see, e.g., R. NORDSTROM, *HANDBOOK OF THE LAW OF SALES* 231-38 (1970); J. WHITE & R. SUMMERS, *supra* note 2, §§ 9-6 to 9-8, at 286-96; Courts in examining lease transactions for warranties sometimes speak in terms of fitness for an intended purpose, which the Code addresses in U.C.C. § 2-314(2)(c). See, e.g., *Cintrone v. Hertz Truck Leasing & Rental Serv.*, 45 N.J. 434, 446, 212 A.2d 769, 775 (1965); *Henry v. Hostetler*, 16 Bucks 74, 75 (Pa. C.P. 1966), *reprinted in* [1967] 3 U.C.C. REP. SERV. (CALLAGHAN) 614, 615.

58. See, e.g., *Redfern Meats, Inc. v. Hertz Corp.*, 134 Ga. App. 381, 393-94, 215 S.E.2d 10, 18-19 (1975) (Code warranty provisions applicable to leases which are analogous to a sale); *Glenn Dick Equip. Co. v. Galey Constr., Inc.*, 97 Idaho 216, 225, 541 P.2d 1184, 1193 (1975) (express warranty provisions of Code extended to a lease); *Cintrone v. Hertz Truck Leasing & Rental Serv.*, 45 N.J. 434, 452, 212 A.2d 769, 778-79 (1965) (warranty of fitness for use implied into lease of a truck).

59. 428 F.2d at 1075-76.

60. *Henry v. Hostetler*, 16 Bucks 74, 75 (Pa. C.P. 1966) (citations omitted), *reprinted in* [1967] 3 U.C.C. REP. SERV. (CALLAGHAN) 614, 615.

61. See *Farnsworth*, *supra* note 1, at 655; *Commentary*, *supra* note 46, at 134; *Comment*, *supra* note 1, at 562. See text accompanying note 46 *supra*.

62. U.C.C. § 2-316.

chantability and in case of a writing must be conspicuous, and to exclude or modify any implied warranty of fitness the language must be by a writing and conspicuous."<sup>63</sup> Courts have held that this provision applies to disclaimers in leases to the same extent as to disclaimers in sales contracts.<sup>64</sup> The requirements of this provision of the Code must therefore be met to exclude or modify an implied warranty in a lease of tangible personal property.

#### IV. STRICT LIABILITY IN TORT

There is also a diminishing difference between sales and leases in the area of strict liability in tort for injuries caused by defective products.<sup>65</sup> An outgrowth of the implied warranties already discussed,<sup>66</sup> this theory of products liability is a combination of warranty and tort concepts.<sup>67</sup> Originally applicable only to sales, principles of products liability have been extended to leases in which the lessor is a merchant of goods.<sup>68</sup> As the California Supreme Court stated, in a leading case involving a fuel truck which was leased to plaintiff's employer:

[W]e can perceive no substantial difference between *sellers* of personal property and *non-sellers*, such as bailors and lessors. In each

63. *Id.* § 2-316(2).

64. *See, e.g.*, *Quality Acceptance Corp. v. Million & Albers, Inc.*, 367 F. Supp. 771, 773-74 (D. Wyo. 1973); *KLPR TV, Inc. v. Visual Electronics Corp.*, 327 F. Supp. 315, 325-26 (W.D. Ark. 1971), *rev'd on other grounds*, 465 F.2d 1382 (8th Cir. 1972). *See also* Annot., 48 A.L.R.3d 668, 679-80 (1973).

65. *See* RESTATEMENT (SECOND) OF TORTS § 402A (1965). For a general discussion of products liability, *see* W. PROSSER, *LAW OF TORTS* 641-82 (4th ed. 1971). When a lease is an isolated transaction, however, strict liability will not apply. *See, e.g.*, *Luna v. Rossville Packing Co.*, 54 Ill. App. 3d 290, 292-93, 369 N.E.2d 612, 614 (1977); *Nastasi v. Hochman*, 58 A.D.2d 564, 564, 396 N.Y.S.2d 216, 217-18 (1977).

66. *See* notes 39-64 and accompanying text *supra*. The possible defenses to a warranty action, such as a valid disclaimer under U.C.C. § 2-316 or lack of privity under U.C.C. § 2-318, often make recovery for defective products difficult. *See* W. PROSSER, *supra* note 65, at 655-56. For a discussion of the defenses available to the seller/lessor of goods under the Code, *see* J. WHITE & R. SUMMERS, *supra* note 2, §§ 11-1 to 12-12, at 326-96. In discussing the relationship of strict liability to warranty, Prosser has stated that "it gradually became apparent that 'warranty,' as a device for justification of strict liability to the consumer, carries far too much luggage in the way of undesirable complications, and is more trouble than it is worth." W. PROSSER, *supra* note 65, at 656.

67. *See* *Stang v. Hertz Corp.*, 83 N.M. 730, 731, 497 P.2d 732, 733 (1972). "Because of the shortcomings of the early theories, the courts developed a third theory of recovery which combined the strict liability of warranty with the broad reach of negligence. This theory is known as strict liability in tort and has been applied throughout the country to products liability cases." *Id.*

68. *See, e.g.*, *Price v. Shell Oil Co.*, 2 Cal. 3d 245, 253, 466 P.2d 722, 727, 85 Cal. Rptr. 178, 183 (1970); *Cintrone v. Hertz Truck Leasing & Rental Serv.*, 45 N.J. 434, 452-53, 212 A.2d 769, 778-81 (1965); *Stang v. Hertz Corp.*, 83 N.M. 730, 735, 497 P.2d 732, 737 (1972); *Nath v. National Equip. Leasing Corp.*, 473 Pa. 178, 180, 373 A.2d 1105, 1106 (1977) (*per curiam*); *Francioni v. Gibsonia Truck Corp.*, 472 Pa. 362, 369, 372 A.2d 736, 739 (1977). *See also* Annot., 52 A.L.R.3d 121 (1973).

instance, the seller or non-seller “places [an article] on the market, knowing that it is to be used without inspection for defects . . . .” . . . In the light of the policy to be subserved, it should make no difference that the party distributing the article has retained title to it. Nor can we see how the risk of harm associated with the use of the chattel can vary with the legal form under which it is held. Having in mind the market realities and the widespread use of the lease of personalty in today’s business world, we think it makes good sense to impose on the lessors of chattels the same liability for physical harm which has been imposed on the manufacturers and retailers. . . .

. . . .  
For the above reasons, we are of the opinion that the doctrine of strict liability in tort should be made applicable to bailors and lessors of personal property in the same manner as we have held it applicable to sellers of such property. . . . [W]e can find no significant difference between a manufacturer or retailer who places an article on the market by means of a sale and a bailor or lessor who accomplishes the same result by means of a lease.<sup>69</sup>

The decision to impose strict liability on the supplier of tangible personal property should not depend on whether title passes to the recipient, *i.e.*, whether the transaction is a lease or a sale.<sup>70</sup> Imposing liability on the basis of title alone would disregard the policy basis for strict liability that a person in the business of supplying products must assume a special responsibility toward the consuming public.<sup>71</sup> The Pennsylvania Supreme Court recently stated: “What is crucial to the rule of strict liability is not the means of marketing but rather the fact of marketing, whether by sale, lease or bailment, for use and consumption by the public.”<sup>72</sup>

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69. *Price v. Shell Oil Co.*, 2 Cal. 3d 245, 251-53, 466 P.2d 722, 726-27, 85 Cal. Rptr. 178, 182-83 (1970) (citation omitted) (emphasis in original), quoting *Greenman v. Yuba Power Prods., Inc.*, 59 Cal. 2d 57, 62, 377 P.2d 897, 900, 27 Cal. Rptr. 697, 700 (1963). In *Price*, plaintiff’s employer leased a gasoline tank truck with a ladder from the defendant in 1958. 2 Cal. 3d at 248, 466 P.2d at 723, 85 Cal. Rptr. at 179. The defendant lessor replaced the ladder at the employer’s request and both parties inspected the installation. *Id.* at 248, 466 P.2d at 723-24, 85 Cal. Rptr. at 179-80. The plaintiff, who was injured when the ladder split into segments, brought an action against the lessor alleging negligence and breach of warranty. *Id.* at 248-49, 466 P.2d at 724, 85 Cal. Rptr. at 180. Nonsuited these allegations, the trial court on its own motion then submitted the case to the jury on a theory of strict liability in tort. *Id.* at 249, 466 P.2d at 724, 85 Cal. Rptr. at 180.

70. *See* 2 Cal. 3d at 253, 466 P.2d at 727, 85 Cal. Rptr. at 183.

71. *See Greenman v. Yuba Power Prods., Inc.*, 59 Cal. 2d 57, 63, 377 P.2d 897, 901, 27 Cal. Rptr. 697, 701 (1963). In *Greenman*, Justice Traynor stated that “[t]he purpose of such liability is to insure that the costs of injuries resulting from defective products are borne by the manufacturers that put such products on the market rather than by injured persons who are powerless to protect themselves.” *Id.*

72. *Francioni v. Gibsonia Truck Corp.*, 472 Pa. 362, 367, 372 A.2d 736, 738 (1977).

For the same reasons that implied warranties may arise from both sales and leases,<sup>73</sup> strict liability may also arise from sales and leases since the consumer or user needs protection against product failure whether he buys or leases the item.

## V. THE DOCTRINE OF UNCONSCIONABILITY

The doctrine of unconscionability under the Code<sup>74</sup> is much broader than at common law, where a contract was unconscionable if it was "such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other."<sup>75</sup> In contrast, under the Code:

The basic test [of unconscionability] is whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract. . . . The principle is one of the prevention of oppression and unfair surprise . . . and not of disturbance of allocation of risks because of superior bargaining power.<sup>76</sup>

Although article 2 of the Code<sup>77</sup> was enacted to cover sales,<sup>78</sup> the Code provisions on unconscionability have been applied to nonsales transactions including leases.<sup>79</sup> This is consistent with the

73. See note 46 and accompanying text *supra*.

74. U.C.C. § 2-302. This Code section on unconscionable contracts or clauses provides:

(1) If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

(2) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination.

*Id.* See also *id.* § 2-316(1) (words or conduct negating express warranty are inoperative to the extent that such construction is unreasonable); *id.* § 2-718(1) (provisions fixing unreasonably large liquidated damages are void as penalties); *id.* § 2-719(3) (consequential damages may be limited or excluded unless unconscionable; limitation of consequential damages for personal injury is prima facie unconscionable but limitation to commercial loss is not). For related concepts in article 1 of the Code, *id.* art. 1, see *id.* § 1-102(3) (obligations of good faith, diligence, and care imposed by the Code may not be disclaimed by agreement); *id.* § 1-203 (obligation of good faith in performance or enforcement imposed on every contract or duty in the Code).

75. *Earl of Chesterfield v. Janssen*, 2 Vesey Sr. 125, 155, 28 Eng. Rep. 82, 100 (Ch. 1750). See also *Hume v. United States*, 132 U.S. 406, 411 (1889); *Mandel v. Leibman*, 303 N.Y. 88, 94, 100 N.E.2d 149, 152 (1951). For a discussion of the common law doctrine of unconscionability, see J. CALAMARI & J. PERILLO, *THE LAW OF CONTRACTS* 318-22 (2d ed. 1977).

76. U.C.C. § 2-302, Comment 1 (citation omitted).

77. *Id.* art. 2.

78. See Comment, *supra* note 1, at 559.

79. See, e.g., *Walter E. Heller & Co. v. Convalescent Home of the First Church of Deliverance*, 49 Ill. App. 3d 213, 220, 365 N.E.2d 1285, 1290 (1977) (in equipment lease analogous

general provisions of the Code which, by their own terms, encourage the modernization and expansion of commercial law.<sup>80</sup> Moreover, this broadened application is consistent with certain specific provisions of article 2 which indicate that many of its principles apply to nonsales transactions as well as sales.<sup>81</sup>

A recent New York decision, *Industralease Automated & Scientific Equipment Corp. v. R.M.E. Enterprises, Inc.*,<sup>82</sup> applied these principles of article 2 to a lease of industrial equipment.<sup>83</sup> In *Industralease*, the owners of a picnic grove entered into a lease-purchase arrangement for two incinerators which failed to work.<sup>84</sup> The lease, which disclaimed all warranties, required the rent to be paid whether the incinerators worked or not.<sup>85</sup> Although the disclaimer satisfied the requirements necessary to exclude warranties under section 2-316 of the Code,<sup>86</sup> the court held that the lease was nevertheless subject to invalidation for unconscionability.<sup>87</sup> The court further held that the disclaimer was in fact unconscionable because: 1) the owners were not familiar with the operating characteristics of the incinerators; 2) the disclaimer of warranties was in a second lease, which was substituted for a prior lease with warranties shortly before the incinerators were to be installed and was represented to the lessee as being necessary to assure timely delivery of the incinerators; and 3) the incinerators never worked.<sup>88</sup> Since this was a commercial lease of business equipment and not a lease of consumer goods, a

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to a sale, U.C.C. § 2-302 is controlling in determining if a clause in the lease is unconscionable); *Industralease Automated & Scientific Equip. Corp. v. R.M.E. Enterprises, Inc.*, 58 A.D.2d 482, 487-90, 396 N.Y.S.2d 427, 430-32 (1977) (disclaimer of warranty in an industrial lease held unconscionable); *United States Leasing Corp. v. Franklin Plaza Apartments, Inc.*, 65 Misc. 2d 1082, 1086, 319 N.Y.S.2d 531 (Civ. Ct. N.Y. 1971) (a lease which in substance was an installment sale held unconscionable). See also J. CALAMARI & J. PERILLO, *supra* note 75, at 322; 3 SALES & BULK TRANSFERS, *supra* note 9, at 1-52; Murray, *supra* note 42, at 452; Comment, *supra* note 1, at 563.

80. See U.C.C. § 1-102; *id.*, Comment 1. See also Commentary, *supra* note 46, at 139-40; Comment, *supra* note 1, at 567-70.

81. See U.C.C. § 2-102. This section provides that "[u]nless the context otherwise requires, this Article applies to transactions in goods." *Id.* Unlike U.C.C. § 2-314 and U.C.C. § 2-315, which are worded in terms of sales, see notes 39-61 and accompanying text *supra*, the Code provision on unconscionability makes no reference to sales, buyers, or sellers. See U.C.C. § 2-302. For the text of § 2-302, see note 74 *supra*. Since there are no express limitations on the scope of the unconscionability provision, it is submitted that § 2-302 could be applied to those lease transactions which are within the meaning of "transactions in goods." See R. NORDSTROM, *supra* note 57, at 41-44; 3 SALES & BULK TRANSFERS, *supra* note 9, at 1-35 to 1-62.

82. 58 A.D.2d 482, 396 N.Y.S.2d 427 (1977).

83. *Id.* at 486-87, 396 N.Y.S.2d at 429-30.

84. *Id.* at 483, 396 N.Y.S.2d at 428.

85. *Id.*

86. U.C.C. § 2-316. For the text of this section, see note 74 *supra*.

87. 58 A.D.2d at 487, 396 N.Y.S.2d at 430.

88. *Id.* at 489-90, 396 N.Y.S.2d at 432. The *Industralease* court concluded that giving effect to the disclaimer would be "a result so 'one-sided' . . . that the disclaimer in good conscience should not be enforced." *Id.* at 490, 396 N.Y.S.2d at 432 (footnote omitted).



possible bias in favor of consumers was not present.<sup>89</sup> The transaction also did not involve personal injury, which eliminates a possible prejudice in favor of injured parties.<sup>90</sup> Accordingly, *Industrallease* demonstrates a court's willingness to expand the reach of the Code's doctrine of unconscionability even to purely commercial situations where tangible personal property is leased as well as sold.

## VI. ANTITRUST LAW

In a recent case, *Continental T.V., Inc. v. GTE Sylvania Inc.*,<sup>91</sup> the Supreme Court of the United States overruled its decision in *United States v. Arnold, Schwinn & Co.*,<sup>92</sup> which had attached great antitrust consequences to the difference between sales and bailments of tangible personal property.<sup>93</sup> The *Schwinn* Court held that if a manufacturer parted with title, dominion, and risk of loss with respect to products sold to its distributors and retailers, then it was illegal per se for the manufacturer to seek to restrict or control either the territorial areas where the distributors and retailers could sell the products or the customers to whom they could sell.<sup>94</sup> If the man-

89. See *id.* at 489, 396 N.Y.S.2d at 431. See also *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449-50 (D.C. Cir. 1965); J. WHITE & R. SUMMERS, *supra* note 2, § 4-3, at 118-19.

90. See 58 A.D.2d at 489, 396 N.Y.S.2d at 431.

91. 433 U.S. 36 (1977).

92. 388 U.S. 365 (1967). The Government brought a civil antitrust suit against Arnold, Schwinn & Company (Schwinn) alleging a conspiracy to fix prices, to allocate exclusive territories to wholesalers, and to restrict merchandise to franchised dealers in violation of § 1 of the Sherman Act, 15 U.S.C. § 1 (1976). 388 U.S. at 367. Schwinn had three principal methods of selling its bicycles: 1) sales to distributors; 2) sales to retailers by consignment or agency arrangement with distributors; and 3) sales to retailers by the Schwinn Plan where the distributor took the order, Schwinn shipped directly to the retailer and then invoiced the dealer and paid the distributor a commission for taking the order. *Id.* at 370. Schwinn assigned specific territories to its distributors who "were instructed to sell only to franchised Schwinn accounts and only in their respective territories which were specifically described and allocated on an exclusive basis." *Id.* at 371. Schwinn's franchised retailers were prohibited from selling to anyone other than consumers. *Id.* at 372. The district court held that Schwinn's territorial limitation agreements with the distributors were per se violations of § 1 of the Sherman Act although its decision was limited to transactions where the distributor purchased the bicycles from Schwinn. *Id.* at 376. The court held that Schwinn was free to make territorial restrictions when the transaction involved consignment, agency, or the Schwinn Plan. *Id.* The Government appealed, arguing, *inter alia* that "the decree should not be confined to sale transactions between Schwinn and wholesalers but should reach territorial restrictions upon distributors whether they are incident to sale and resale transactions or to consignment, agency or Schwinn-Plan relationship between Schwinn and the distributors." *Id.* at 377 (emphasis in original).

93. 388 U.S. at 379-80.

94. *Id.* at 379. The Supreme Court stated:

Under the Sherman Act, it is unreasonable without more for a manufacturer to seek to restrict and confine areas or persons with which an article may be traded after the manufacturer has parted with dominion over it. . . . Such restraints are so obviously destructive of competition that their mere existence is enough. If the manufacturer parts with

ufacturer retained title, dominion, and risk of loss, however, then such conduct was not *per se* unreasonable, but was to be judged by the rule of reason to determine whether or not it was illegal.<sup>95</sup> The *Schwinn* doctrine was subsequently summarized by the *Continental T.V.* Court as follows: "The pivotal factor was the passage of title: All restrictions were held to be *per se* illegal where title had passed, and all were evaluated and sustained under the rule of reason where it had not."<sup>96</sup>

The Supreme Court's *Continental T.V.* decision swept aside this artificial distinction, concluding "that the distinction drawn in *Schwinn* between sale and nonsale transactions is not sufficient to justify the application of a *per se* rule in one situation and a rule of reason in the other."<sup>97</sup> The Court then held that both types of transactions should be judged under the rule of reason.<sup>98</sup>

Although neither *Schwinn* nor *Continental T.V.* dealt specifically with leases, the broad language used by the Supreme Court and the rationale underlying its decisions suggest that the rule of reason test

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dominion over his product or transfers risk of loss to another, he may not reserve control over its destiny or the conditions of its resale.

*Id.* (citations and footnote omitted).

95. *Id.* at 380. As the *Schwinn* Court explained:

Where the manufacturer retains title, dominion, and risk with respect to the product and the position and function of the dealer in question are, in fact, indistinguishable from those of an agent or salesman of the manufacturer, it is only if the impact of the confinement is "unreasonably" restrictive of competition that a violation of § 1 results from such confinement, unencumbered by culpable price fixing.

*Id.* (citation omitted).

96. 433 U.S. at 52. In an attempt to improve its market share, GTE Sylvania Inc. (Sylvania) eliminated its wholesale distributors and sold directly to a limited number of franchisees who were required to sell Sylvania products only from the franchised location. *Id.* at 38. As a result of a dispute with Continental T.V., Inc., (Continental), one of its retail franchisees, Sylvania cancelled the franchise and its finance company brought suit to recover money owed and merchandise held by Continental. *Id.* at 40. Continental claimed that Sylvania's franchise agreements prohibiting the sale of Sylvania products other than from specified locations violated § 1 of the Sherman Act, 15 U.S.C. § 1 (1976). 433 U.S. at 40. The trial judge instructed the jury according to the *per se* standard enunciated in *Schwinn*. *Id.* at 40-41. The jury found that Sylvania had violated antitrust laws and awarded damages to Continental. *Id.* at 41. The United States Court of Appeals for the Ninth Circuit reversed, concluding that *Schwinn* was distinguishable and that the franchise agreement should have been judged under the rule of reason. *Id.*

The Supreme Court found that "[i]n intent and competitive impact, the retail customer restriction in *Schwinn* is indistinguishable from the location restriction in the present case." *Id.* at 46. The Court, however, agreed to reconsider the *per se* rule stated in *Schwinn*. *Id.* at 47.

97. 433 U.S. at 57. The Court stated that "[t]he market impact of vertical restrictions is complex because of their potential for a simultaneous reduction of intrabrand competition and stimulation of interbrand competition" and "that this distinction [in *Schwinn*] between sale and nonsale transactions resulted from the Court's effort to accommodate the perceived intrabrand harm and interbrand benefit of vertical restrictions." *Id.* at 51-52 (footnotes omitted). The Court acknowledged that there was "substantial scholarly and judicial authority" supporting the economic utility of vertical restrictions. *Id.* at 57-58. Since the possible benefits to interbrand competition could not be evaluated when the *Schwinn* *per se* rule was applied to vertical restrictions, that decision had to be overruled and the rule of reason restored. *Id.*

98. *Id.* at 57. The *Continental T.V.* Court reasoned: "When anticompetitive effects are

for violations of section 1 of the Sherman Act<sup>99</sup> would apply equally to leases and to sales.<sup>100</sup> Antitrust law thus further illustrates the diminishing consequences of whether a transaction is a sale or a lease.

## VII. TAX LAW

The difference in the overall tax consequences of whether a transaction is a sale or a lease is also diminishing. It is important to note that this discussion extends only to sale and lease transactions that are intended to acquire property from someone else who already owns the property and not sale and leaseback situations.<sup>101</sup> Although a detailed discussion of tax law is beyond the scope of this article, a general survey of the tax differences between sales and leases is pre-

shown to result from particular vertical restrictions they can be adequately policed under the rule of reason, the standard traditionally applied for the majority of anticompetitive practices challenged under § 1 of the Act." *Id.* at 59.

99. 15 U.S.C. § 1 (1976).

100. See notes 94-98 and accompanying text *supra*.

101. See *Frank Lyon Co. v. United States*, 435 U.S. 561 (1978). In *Frank Lyon*, Worthen Bank & Trust Company (Worthen) wanted to construct a building for its use but was prevented by state and federal regulations from obtaining conventional financing. *Id.* at 563-64. Worthen entered into a sale and leaseback agreement with Frank Lyon Company (Lyon) by which Lyon took title to the building, obtained a construction loan and permanent mortgage financing, and leased the building back to the bank for long term use. *Id.* at 565-66. Pursuant to this agreement, Worthen was obligated to pay rent equal to Lyon's principal and interest payments and Worthen had an option to repurchase the building at various times. *Id.* at 566-67.

After the building was completed and Worthen took possession, Lyon filed an income tax return which accrued the rent as income and deducted depreciation, interest, and related payments. *Id.* at 568. The Commissioner of Internal Revenue disallowed the deductions claiming that the transaction was a sham and assessed a deficiency which Lyon paid. *Id.* at 568-69. Lyon brought suit to recover the amount paid. *Id.* at 569. Although the district court allowed recovery, the judgment was reversed by the United States Court of Appeals for the Eighth Circuit. *Id.* at 569-70.

The United States Supreme Court reversed the decision of the Eighth Circuit and concluded that Lyon was entitled to the deductions. *Id.* at 583-84. The Court explained:

In short, we hold that where, as here, there is a genuine multiple-party transaction with economic substance which is compelled or encouraged by business or regulatory realities, is imbued with tax-independent considerations, and is not shaped solely by tax-avoidance features that have meaningless labels attached, the Government should honor the allocation of rights and duties effectuated by the parties. Expressed another way, so long as the lessor retains significant and genuine attributes of the traditional lessor status, the form of the transaction adopted by the parties governs for tax purposes. What those attributes are in any particular case will necessarily depend upon its facts. It suffices to say that, as here, a sale-and-leaseback, in and of itself, does not necessarily operate to deny a taxpayer's claim for deductions.

*Id.* at 583-84 (footnote omitted).

Although this decision upholds the asserted distinctions between a sale and a lease, it also demonstrates the Supreme Court's commitment to a case-by-case evaluation to determine whether the substance of a transaction is evident in the form of the agreement. As the *Frank Lyon* Court noted, "the characterization of a transaction for financial accounting purposes, on the one hand, and for tax purposes, on the other, need not necessarily be the same." *Id.* at 577 (citations omitted). See also Shapiro, *supra* note 15, at 433, 438-40, 438 n.5.

sented from the viewpoint of the user wishing to acquire the property and from the viewpoint of the supplier of the property.<sup>102</sup>

### A. *Acquiring the Property*

One who purchases tangible personal property for use in a trade or business or for the production of income makes a capital expenditure, and the depreciation on that property is tax deductible.<sup>103</sup> The purchaser is also entitled to any applicable investment credit.<sup>104</sup> If he borrows to finance the purchase, the interest on the loan is also deductible.<sup>105</sup> If the purchase is financed by an installment sale contract, then the portion of each installment payment which represents imputed interest is deductible.<sup>106</sup> If the property is leased rather than bought, the rental payments are deductible,<sup>107</sup> but depreciation is not.<sup>108</sup>

In deciding the method by which to acquire property, one must compare the depreciation and interest deductions available to a

102. See generally Gallagher, *Tax Consequences of a Leveraged Lease Transaction*, 52 TAXES 356 (1974); Landis, *Tax Aspects of Leasing*, 79 COM. L.J. 8 (1974); Lefevre, *The Tax Law of Lease Transactions Revisited*, 53 TAXES 765 (1975); Morris, *Taxation of Leases: Profits and Pitfalls*, 30 Sw. L.J. 435 (1976); Schmidt & Larsen, *Leveraged lease arrangements: Tax factors that contribute to their attractiveness*, 41 J. TAX. 210 (1974). For a discussion of equipment leasing as a tax shelter and its treatment under the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520, see Wiesner, *Tax Shelters—A Survey of the Impact of the Tax Reform Act of 1976*, 33 TAX L. REV. 5, 69-78 (1977). See also TAX MNGM'T (BNA) No. 12-5th (1978).

103. I.R.C. § 167(a). The general rule on depreciation is as follows: "There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—(1) of property used in the trade or business, or (2) of property held for the production of income." *Id.*

104. *Id.* §§ 38, 46-50.

105. *Id.* § 163(a).

106. *Id.* §§ 163(b), 483. See also *Commissioner v. Wilshire Holding Corp.*, 288 F.2d 799 (9th Cir. 1960) (taxpayer is entitled to apportion interest and principal payments for federal income tax purposes).

107. I.R.C. § 162(a)(3). This section states in relevant part that a taxpayer is entitled to a deduction for "rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity." *Id.*

108. *Id.* § 167. Only those capital improvements made by the lessee on the lessor's property are deductible by him. *Id.* § 178. See Treas. Reg. § 1.178-1 to -3 (1960). Treas. Reg. § 1.167(a)-4, T.D. 6520, 1961-1 C.B. 52, 62, provides in part:

Capital expenditures made by a lessee for the erection of buildings or the construction of other permanent improvements on leased property are recoverable through allowances for depreciation or amortization. If the useful life of such improvements in the hands of the taxpayer is equal to or shorter than the remaining period of the lease, the allowances shall take the form of depreciation under section 167 . . . . If, on the other hand, the estimated useful life of such property in the hands of taxpayer, determined without regard to the terms of the lease, would be longer than the remaining period of such lease, the allowances shall take the form of annual deductions from gross income in an amount equal to the unrecovered cost of such capital expenditures divided by the number of years remaining of the term of the lease. Such deductions shall be in lieu of allowances for depreciation.

*Id.* See also Davis, *supra* note 19, at 59.

purchaser with the rental deductions available to the lessee.<sup>109</sup> This analysis depends upon the relative lengths of the depreciable life of the property and the term of the lease,<sup>110</sup> and the method of depreciation used.<sup>111</sup> If the useful economic life of the asset is longer than the lease, then the lease provides a shorter write off period for tax purposes.<sup>112</sup> Although the timing of the tax payments may vary, there is often little difference in the total tax payable under a sale or a lease, since the total purchase price of the asset, including financing, usually approximates the total rental due on a lease.<sup>113</sup> The total depreciation and interest deductions, therefore, approximate the total rental deductions.<sup>114</sup>

Similarly, there is a diminishing difference between the effect of the investment credit in a purchase as compared with its effect in a lease.<sup>115</sup> As indicated, a purchaser can use the investment credit if applicable,<sup>116</sup> but a lessee can also use the credit under certain circumstances.<sup>117</sup> A lessor, other than certain persons,<sup>118</sup> of most tangible personal property<sup>119</sup> produced or acquired after December 31, 1961,<sup>120</sup> can elect to treat the lease as an acquisition by the lessee, and therefore the lessee may be entitled to claim the investment credit.<sup>121</sup> A sublessor can similarly make this election to pass through the investment credit to its sublessee.<sup>122</sup> In order for the lessee to claim the credit, the property must meet the above qualifications in the hands of the lessee as well as of the lessor.<sup>123</sup> For the

109. See Lefevre, *supra* note 102, at 766.

110. *Id.* See Davis, *supra* note 19, at 56-57.

111. See I.R.C. § 167(b).

112. *Id.* §§ 162(a)(3), 167. See Dean, *supra* note 17, at 39.

113. See Lefevre, *supra* note 102, at 772-73. See also Boothe, *supra* note 13, at 3; Dean, *supra* note 17, at 39.

114. This might not be true, however, for users subject to the minimum tax in I.R.C. §§ 55-58.

115. See I.R.C. § 38. This section provides a tax credit for investment in certain depreciable property. *Id.* Section 46 of the Internal Revenue Code, *id.* § 46, governs the amount of the credit which can be claimed under § 38. *Id.* § 46(a). Section 48 of the Internal Revenue Code, *id.* § 48, supplies the definitions and rules for § 38 property. *Id.*

116. *Id.* §§ 38, 46-50.

117. *Id.* § 48(d). See generally TAX MNGM'T (BNA) No. 12-5th, at A-11 to A-22 (1978).

118. I.R.C. § 48(d)(1). Those persons who are not eligible for the investment tax credit are described in § 46(e)(1) of the Internal Revenue Code, *id.* § 46(e)(1). They include: 1) those mutual savings banks, cooperative banks, and domestic building and loan associations to which I.R.C. § 593 applies; 2) regulated investment companies or real estate investment trusts subject to taxation under subchapter M, *id.* §§ 851-860; and 3) cooperative organizations described in I.R.C. § 1381(a). *Id.* § 46(e)(1).

119. *Id.* § 48(a).

120. *Id.* § 48(b).

121. *Id.* § 48(d). See Treas. Reg. § 1.48-4(e), T.D. 7203, 1972-2 C.B. 12, 28.

122. Treas. Reg. § 1.48-4(e), T.D. 7203, 1972-2 C.B. 12, 28.

123. I.R.C. § 48(d)(3); Treas. Reg. § 1.48-4(a), T.D. 7203, 1972-2 C.B. 12, 26-27. The regulations provide that the following conditions must be satisfied before the lessor can elect to treat

lessee to qualify for the credit, he must be the original user of the property, *i.e.* the first person to use the property for its intended function.<sup>124</sup> This requirement prevents the lessee from claiming credit for property which he sold to the lessor and then leased back.<sup>125</sup>

If the lessee does not meet these requirements, or cannot otherwise take full advantage of the investment credit, he can allow the lessor to use the credit in exchange for lower rental charges.<sup>126</sup>

### B. Supplying the Property

The seller of tangible personal property will recognize gain or loss on its sale, which will be classified as either capital or ordinary, depending on the character of the asset in the hands of the seller.<sup>127</sup> Ordinary income is defined by the Internal Revenue Code to include "any gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231(b)." <sup>128</sup> A seller in the business of supplying property to buyers would not be selling either capital assets<sup>129</sup> or section 1231(b)<sup>130</sup> property since those items do not include "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."<sup>131</sup> A seller in the business of supplying property to potential buyers or

the lessee as the purchaser of the property for purposes of the I.R.C. § 38 credit: 1) the property must be § 38 property in the lessor's hands; 2) the property must be new § 38 property in the lessee's hands and the original use of the property must start with the lessor; 3) the property would have been new § 38 property to the lessee if he had actually purchased the property; 4) a statement of election to treat the lessee as purchaser must be filed; and 5) the lessor cannot be a prohibited person under I.R.C. § 46(d)(1). Treas. Reg. § 1.48-4(a)(1), T.D. 7203, 1972-2 C.B. 12, 26-27.

124. Treas. Reg. § 1.48-4(a)(1)(ii), T.D. 7203, 1972-2 C.B. 12, 26; Treas. Reg. § 1.48-4(b) (1964).

125. The lessor is also not entitled to credit for this property since leased back property is excluded from the definition of "used property" in I.R.C. § 48(c)(1). *Id.* This section provides: "Property shall not be treated as 'used Section 38 property' if, after its acquisition by the taxpayer, it is used by a person who used such property before such acquisition. . . ." *Id.*

126. See generally Canellos, *The Investment Credit: Problem Areas and Planning Possibilities*, 30 TAX LAW. 85 (1976); Schmidt & Larsen, *supra* note 102.

127. Ordinary gains and losses are defined in I.R.C. §§ 64, 65. *Id.* Capital assets are defined in I.R.C. § 1221. *Id.*

In certain situations, the gain will be ordinary even if the asset is capital. See *id.* § 1245. One such situation is when depreciation is recaptured under section 1245 of the Internal Revenue Code, *id.* § 1245. See generally Schapiro, *Recapture of Depreciation and Section 1245 of the Internal Revenue Code*, 72 YALE L.J. 1483 (1963). Another example is when a sale of depreciable property takes place between spouses, between an individual and a corporation controlled directly or indirectly by the individual, or between two corporations controlled directly or indirectly by the same individual. I.R.C. § 1239. For the counterpart of this section in the partnership area, see *id.* § 707(b)(2).

128. I.R.C. § 64.

129. See § 1221.

130. *Id.* § 1231(b).

131. *Id.* § 1231(b)(1)(B).

lessees would therefore realize ordinary income.<sup>132</sup> Moreover, any gain on the transaction may be eligible for installment reporting.<sup>133</sup>

A lessor of the property realizes rental income which will be taxed as ordinary income.<sup>134</sup> As the owner of the property, the lessor will be entitled to deductions for depreciation<sup>135</sup> and any applicable investment credit,<sup>136</sup> unless he elects to pass through the credit to the lessee.<sup>137</sup>

For one who is in the trade or business of supplying a product, the taxable income from either a sale or a lease will thus be ordinary income.<sup>138</sup> If the sale is on an installment basis, then the timing of the income payments will also be the same for a sale and a lease. As previously stated, the investment credit treatment as well may be the same under the pass through election.<sup>139</sup> The only significant difference in the tax consequences to a supplier of a product in the ordinary course of business is that a lessor can take a deduction for depreciation whereas a seller cannot.<sup>140</sup>

### C. Leases Treated as Sales

The tax differences between sales and leases are therefore becoming less important in many cases. Even in those situations in which these differences would be significant, the importance of the distinction has been diminished by the fact that, under certain circumstances, leases may be treated as conditional sales for tax purposes.<sup>141</sup> These circumstances include, but are not limited to, the following: whether the user of the property can acquire it at the end of the lease for either nominal or no consideration;<sup>142</sup> whether the user acquires an equity interest in the property during the lease

132. *Id.* §§ 64, 1001(b).

133. *See id.* § 453.

134. *See id.* § 61(a)(5).

135. *Id.* § 167.

136. *See id.* §§ 38, 46-50.

137. *See* notes 118-25 and accompanying text *supra*.

138. *See* I.R.C. § 64.

139. *See* notes 118-25 and accompanying text *supra*.

140. *See* Davis, *supra* note 19, at 59-60. *See* notes 103-08 and accompanying text *supra*.

141. *See generally* Osterreich v. Commissioner, 226 F.2d 798, 802-03 (9th Cir. 1955); LTV Corp. v. Commissioner, 63 T.C. 39, 49-51 (1974); Northwest Acceptance Corp. v. Commissioner, 58 T.C. 836, 844-50 (1972), *aff'd per curiam*, 500 F.2d 1222 (9th Cir. 1974); Rev. Proc. 76-30, 1976-2 C.B. 647; Rev. Proc. 75-28, 1975-1 C.B. 752; Rev. Proc. 75-21, 1975-1 C.B. 715; Gallagher, *supra* note 102; Landis, *supra* note 102, at 10; Lefevre, *supra* note 102.

142. *See* Lockhart Leasing Co. v. United States, 446 F.2d 269, 272 (10th Cir. 1971); Osterreich v. Commissioner, 226 F.2d 798, 802-03 (9th Cir. 1955); LTV Corp. v. Commissioner, 63 T.C. 39, 50 (1974); Northwest Acceptance Corp. v. Commissioner, 58 T.C. 836, 847-48 (1972), *aff'd per curiam*, 500 F.2d 1222 (9th Cir. 1974); Rev. Proc. 75-21, § 4(3), 1975-1 C.B. 715, 716.

term;<sup>143</sup> whether the lessor does not bear the full economic risk of gain or loss during the lease by requiring the user to buy the property at a given price or having the user bear the risk of casualty loss;<sup>144</sup> whether the lessor has a substantial interest in the property;<sup>145</sup> a comparison between the term of the lease and the useful economic life of the property;<sup>146</sup> and the nature of the property and its relationship to the facilities of the user.<sup>147</sup>

### VIII. CONCLUSION

Although there are still differences between a sale and a lease, these differences are rapidly diminishing, particularly in the areas of implied warranties, strict liability in tort, the doctrine of unconscionability, antitrust law, and tax law. This has resulted because courts are becoming more concerned with the purpose and substance of the transaction rather than with its form.<sup>148</sup> By analyzing these transactions according to business realities rather than legal formalities, the law is becoming more rational.

143. See *Lockhart Leasing Co. v. United States*, 446 F.2d 269, 271 (10th Cir. 1971); *LTV Corp. v. Commissioner*, 63 T.C. 39, 51 (1974); Rev. Proc. 75-21, § 4(4), 1975-1 C.B. 715, 716.

144. See *Mt. Mansfield Television, Inc. v. United States*, 239 F. Supp. 539, 544 (D. Vt. 1964), *aff'd per curiam*, 342 F.2d 944 (2d Cir.), *cert. denied*, 382 U.S. 818 (1965); *LTV Corp. v. Commissioner*, 63 T.C. 39, 49-50 (1974); *Northwest Acceptance Corp. v. Commissioner*, 58 T.C. 836, 849-50 (1972), *aff'd per curiam*, 500 F.2d 1222 (9th Cir. 1974); Rev. Proc. 75-28, § 4(.02), 1975-1 C.B. 752, 752-53; Rev. Proc. 75-21, § 4, 1975-1 C.B. 715, 716.

145. See *Lockhart Leasing Co. v. United States*, 446 F.2d 269, 271 (10th Cir. 1971); *Bolger v. Commissioner*, 59 T.C. 760, 768-69 (1973); *Northwest Acceptance Corp. v. Commissioner*, 58 T.C. 836, 849-50 (1972), *aff'd per curiam*, 500 F.2d 1222 (9th Cir. 1974); Rev. Proc. 75-21, § 4(1), 1975-1 C.B. 715, 715-16; Lefevre, *supra* note 102, at 773-76.

146. See Rev. Rul. 55-541, 1955-2 C.B. 19; Lefevre, *supra* note 102, at 770-71.

147. See *Estate of Starr v. Commissioner*, 274 F.2d 294, 295-96 (9th Cir. 1959); *Mt. Mansfield Television, Inc. v. United States*, 239 F. Supp. 539, 544 (D. Vt. 1964), *aff'd per curiam*, 342 F.2d 944 (2d Cir.), *cert. denied*, 382 U.S. 818 (1965); *LTV Corp. v. United States*, 63 T.C. 39, 51 (1974).

148. See *Mt. Mansfield Television, Inc. v. United States*, 239 F. Supp. 539, 543 (D. Vt. 1964), *aff'd per curiam*, 342 F.2d 944 (2d Cir.), *cert. denied*, 382 U.S. 818 (1965); *LTV Corp. v. United States*, 63 T.C. 39, 51 (1974); *Northwest Acceptance Corp. v. Commissioner*, 58 T.C. 836, 845 (1972), *aff'd per curiam*, 500 F.2d 1222 (9th Cir. 1974).