

1-1-1974

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## Recommended Citation

Allen Bruce Bottini, Comment, *Automobile Leasing: Is the Moscone Act Really Protecting the Consumer*, 14 SANTA CLARA LAWYER 612 (1974).

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# AUTOMOBILE LEASING: IS THE MOSCONE ACT REALLY PROTECTING THE CONSUMER?

## INTRODUCTION

Automobile leasing is rapidly becoming one of the most common methods utilized by consumers to satisfy their transportation needs. Of the 12,324,000 motor vehicles registered in California in 1971,<sup>1</sup> more than five percent were acquired as a result of automobile leasing agreements.<sup>2</sup>

At the present time these lease transactions are regulated solely by the Moscone Automobile Leasing Act, enacted in 1969.<sup>3</sup> The purpose of this act is to protect consumers from the pressure of artful and unscrupulous automobile lessors who have long taken advantage of them.<sup>4</sup> The Act requires full disclosure of

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1. U.S. BUREAU OF THE CENSUS, STATISTICAL ABSTRACT OF THE UNITED STATES: 1972, at 546 (93d ed. 1972). More recently in the Annual Report to Congress for the year 1973 by the Board of Governors of the Federal Reserve System, it was stated:

Automobile manufacturers currently estimate that by 1980 some 40% of their production will be leased rather than sold. In the last ten years, lease and fleet registrations on new cars have increased 127% while new car sales have increased only 42%.

CCH CONS. CRED. GUIDE 15 (Jan. 16, 1974).

2. Interview with A.M. Garfield, attorney for San Francisco Auto Leasing Association, in San Francisco, California, November 21, 1972.

3. CAL. CIV. CODE §§ 2985.7-.93 (West Supp. 1974).

4. Since leasing eligibility is based on one's financial stability, automobile lessees traditionally have been persons in the middle to upper income brackets. Nonetheless, to the lessor, each individual lessee's financial capability is still a matter of concern, because in the lease transaction there is no substantial down payment to protect the lessor against the automobile's depreciation. Thus, if the lessee defaults early in the lease term, the lessor will be unable to recover any amount other than the depreciated value of the automobile which is realizable upon its sale. See Comment, *Automobile Leasing: A Subject for Legislative Consideration*, 13 U.C.L.A. L. REV. 138 [hereinafter cited as *Automobile Leasing*].

Frequently the lessee gains possession of a new car by remitting one month's payment and making a small security. For example, a car costing the lessor \$3,000 is given to a lessee after one month's advanced payment of \$80 and a deposit of \$100 are made. If the resale value of the car drops an estimated \$800 when the car is driven off the premises, the lessor incurs a loss if the lessee defaults and becomes judgment proof two weeks later. In this situation the lessor would lose \$620, as the car would only bring \$2,200 on resale and the lessor has only received \$180 from the lease. Therefore, to reduce such risk, lessors will enter into leases only with those who have superior credit ratings.

*Id.* at 138 n.1.

In an effort to expand the available market among a wide economic spectrum of consumers, automobile lessors have looked to new methods:

the consumer's liability and the nature and extent of his payments.<sup>5</sup>

Prior to enactment of the Moscone Act it was argued that leases were subject to the more comprehensive provisions of the Rees-Levering Act<sup>6</sup> which governs any conditional sale contract arising out of the sale of a motor vehicle.<sup>7</sup> Under the lease contract the lessee was responsible for paying a sum substantially equivalent to the value of the leased property. Thus, it was felt that such an agreement was in substance a sale of the motor vehicle, not a simple lease for a term.<sup>8</sup> Nonetheless, the passage of the Moscone Act made it clear that it was not the intent of the legislature to include automobile leasing within the same comprehensive scheme of procedural safeguards found in the Rees-Levering Act.<sup>9</sup> The result has been that despite the disclosure

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(a) By leasing lower cost automobiles, the percentage and amount of initial depreciation will be less than the depreciation of a higher-priced automobile. Furthermore, the smaller the potential loss the greater are the lessor's chances of recovering that loss through wage garnishments and attachments.

(b) By requiring larger security deposits, the lessor is better able to protect against loss due to default.

(c) By requiring a co-signer or "guarantor" the lessor provides himself with an alternative source of revenue in the event the primary lessee defaults.

(d) Until recently, a few lessors insisted on a security interest or lien on property other than the leased automobile. *See generally* Thomas v. Wright, 21 Cal. App. 3d 921, 98 Cal. Rptr. 874 (1971). Recent legislation prohibits this practice. CAL. CIV. CODE § 2985.81 (West Supp. 1974).

5. Letter from Senator George Moscone to Governor Ronald Reagan, April 8, 1969, on file in the offices of Senator George Moscone, Sacramento, California, and the *Santa Clara Lawyer*. *See also* CAL. CIV. CODE § 2985.8 (West Supp. 1974).

6. CAL. CIV. CODE §§ 2981-84.4 (West Supp. 1974).

7. E. GIACOMINI, CALIFORNIA RETAIL INSTALLMENT SALES § 2.13, at 44 (California Continuing Education of the Bar 1969).

8. *See* Thomas v. Wright, 21 Cal. App. 3d 921, 98 Cal. Rptr. 874 (1971); E. GIACOMINI, CALIFORNIA RETAIL INSTALLMENT SALES § 2.13, at 44 (California Continuing Education of the Bar 1969).

9. This intent is manifested by Civil Code section 2985.92 which expressly excludes retail installment sales of automobiles from the Moscone Act's coverage. In September, 1973, in an effort to prevent any possible suggestion that certain lease transactions may be subject to the provisions of the Rees-Levering Act, the California legislature narrowed the definition of a "conditional sale contract" in Civil Code section 2981(a)(2). That section now dictates that in order for an automobile leasing contract to fall within the coverage of the Rees-Levering Act, it is necessary that the lessee agree to pay a sum substantially equivalent to or greater than the value of the automobile at the time the leasing contract is executed. Further, it must be agreed that the lessee will become, or has the option of becoming, the owner of the automobile upon full compliance with the terms of the contract for no additional consideration, or for nominal consideration. To emphasize the distinction, in 1973, the legislature added Civil Code section 2981.5 which states:

A contract for the bailment or leasing of a motor vehicle . . . which establishes the maximum for which a bailee or lessee could be held liable at the end of the lease or bailment period, or upon an earlier termi-

requirements of the Moscone Act, the consumer continues to be exploited. Although the Moscone Act moves in the right direction, its provisions do not effectively protect the consumer from the lessor's subtle and oftentimes misleading sales techniques.

It is the purpose of this comment to examine the mechanics of the automobile lease transaction in order to expose continuing consumer problems, some of which include unexpected lease-end balloon payments, inflated lease-end "reconditioning" costs and misleading advertisements, and then to recommend necessary remedial legislation to prevent such problems.

### *The Mechanics of the Automobile Lease Transaction*

To fully appreciate the obligations the lessee assumes upon entering an automobile lease agreement it is necessary to have an understanding of the two basic types of lease transactions. These are commonly referred to as closed end and open end lease agreements.<sup>10</sup>

The closed end lease<sup>11</sup> is one in which the lessee is obligated to keep the automobile for the full fixed term of the lease and the lessor absorbs any gain or loss from his disposal of the vehicle at the end of the lease term.<sup>12</sup> Since the lessor assumes the risk of depreciation, the lessee need not be concerned with the portion of each monthly payment which is applied toward recovery of the motor vehicle's depreciation in value. His sole obligation is to make a designated number of payments for the period fixed by the lease agreement and maintain the vehicle

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nation, by reference to the value of the vehicle at such time, is *not* a contract by which the bailee or lessee will become or for no other or for a nominal consideration has the option of becoming the owner of the vehicle, for the purposes of paragraph (2) of subdivision (a) of Section 2981 or any other provision of this chapter. (emphasis added).

These sections clearly demonstrate that, absent an option to purchase at the end of the lease period, automobile lease agreements are not considered to be within the coverage of the Rees-Levering Act.

10. *Automobile Leasing*, *supra* note 4, at 138; DEPARTMENT OF MOTOR VEHICLES REPORT OF INVESTIGATION C 155768 (2-20) (April 10, 1969), on file in the office of the *Santa Clara Lawyer* [hereinafter cited as DMV REPORT].

11. A closed end lease is referred to as a "walkaway" lease by some lessors for euphonic reasons. One survey indicates that people tend to distrust the term "closed" and prefer "walkaway." DMV REPORT, *supra* note 10, at 7.

12. *Automobile Leasing*, *supra* note 4, at 139; Interview with Mr. Rand Miller, Leasing Representative, First National Bank Leasing Center, in San Jose, California, March 18, 1974. It must be noted that there exists a lack of consistency in the authorities on whether a lessee has any lease-end liability in a closed end lease agreement. A Department of Motor Vehicles investigation found that at least one agency appraised the automobile at the termination of the lease. If the appraised value was lower than the then existing Kelley Blue Book value, the lessee was required to make up the difference. DMV REPORT, *supra* note 10, at 5.

in a reasonable manner. This type of lease is very much akin to the short-term rental of chattels.

Since, in a closed end lease, the lessor will suffer any unexpected loss in value upon his resale of the automobile at the end of the lease term, he is careful to project accurately the automobile's estimated resale value in order to fully recapture the amount of capital he originally expended to obtain the automobile for leasing purposes. To lighten the lessor's burden of recapturing the automobile's depreciation, the lessee may be assessed a charge for unusually excessive mileage. This assessment is rationalized on the basis that the automobile's mileage is a critical resale factor over which the lessor has no control.<sup>13</sup>

The open end lease, like the closed end lease, is drawn with a specific period in mind, usually from twenty-four to sixty months. However, under the open end lease agreement the lessee may terminate at any time prior to the stipulated termination date of the lease.<sup>14</sup> If the lessee keeps the automobile for the full lease term, the lease resembles a closed end lease if the estimated termination value of the automobile equals its actual resale value at the conclusion of the lease period. However, if the lessee returns the automobile prior to the termination date of the lease, he will be liable for any unpaid balance remaining on the lease.<sup>15</sup>

13. The lessee may also be subject to a deficiency charge if the resale value of the automobile is unusually low due to the lessee's excessive use thereof. DMV REPORT, *supra* note 10, at 7 and 11.

14. The lessee's ability to terminate is often qualified in many lease agreements by a requirement that the lessee keep the automobile for a minimum period of six to twelve months. See, e.g., the following motor vehicle lease agreements on file in the office of the *Santa Clara Lawyer*: Cenval Leasing, Oakland, California; Fazackerly Leasing Co., So. San Francisco, California; Redwood Leasing Co., Redwood City, California.

15. This liability may be illustrated by examining the figures of an actual case in which the lessee returned the automobile to the lessor after 16 months of a 36 month open end lease. In the lease agreement the vehicle's lease-end termination value was estimated to be \$3,650. Of the total monthly payment of \$142.02, \$87.61 was contributed monthly to recapturing the automobile's depreciation. The remainder of each monthly payment consisted of a monthly lessor's fee of \$47.65 and a use tax of \$6.76.

Automobile: 1970 Porsche 914-6	
Original Agreed Upon Value	\$6807.00
(capitalized cost)	
Total of Monthly Amounts credited to lessee	
(16 × \$87.61)	— 1401.76
Payoff Amount on Lease	5405.24
Kelley Blue Book Value of Automobile	
high	\$5200
low	4200
Amount Realized on Lessor's Resale	— 4500.00
Immediate Lessee Liability	\$ 905.24

Lease of automobile by author, April 17, 1970, from Cenval Leasing Co., Oakland, California, on file with the *Santa Clara Lawyer*.

The lessee's liability may be computed by deducting from the original "agreed upon value" of the automobile, the amount which has been credited to the lessee's obligation (representing the lessor's recapture of depreciation) and the resale value of the returned vehicle.

The "agreed upon value" or "capitalized cost" of the automobile in an open end lease is analogous to the sales price in an automobile sale and usually represents the capital expended by the lessor in acquiring the automobile from the dealer<sup>16</sup> plus a percentage mark up.<sup>17</sup> The capitalized cost of the automobile is repaid to the lessor and credited to the lessee's obligation by applying a portion of each lease payment to a fund usually designated the "monthly depreciation allocation" or "depreciation reserve fund."

An estimate of the depreciated or resale value of the automobile at the termination date of the lease is one of the factors which determines the amount of the monthly payment. This monthly payment is computed by deducting the "estimated" resale value of the automobile from the capitalized cost, and dividing the resulting figure by the number of months the lease is to run. To this monthly depreciation allocation is added the

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16. Traditionally, the lessor and dealer have been separate and distinct parties. However, it has become common for dealers to establish their own leasing corporations. These corporations usually operate on the same premises as those of normal dealerships. In such cases, the dealer's transfer of the automobile to the leasing corporation often amounts to nothing more than a paper transaction.

17. This mark up affords the lessor an additional source of income above the lessor's monthly fee for his services. The mark up is justified as a service charge for the lessor's ability to acquire the automobile at a cost below the manufacturer's retail list price. Interview with leasing representative, Atlantic Leasing Co. in San Jose, California, Nov. 14, 1972.

An example of a typical method of computing the "capitalized cost" is illustrated by the following calculations used by Atlantic-Pacific Leasing Company. This estimate was given to the author by an Atlantic-Pacific leasing representative, Nov. 14, 1972.

Dealer Invoice Price	
1973 Ford Pinto Sedan	\$1790.00
Dealer Profit	75.00
AM Radio	50.29
Total Cost to Lessor	<u>\$1915.29</u>
ADD Lessor Mark Up	
(approximately 10%)*	203.71
Capitalized Cost to Lessee	<u><u>\$2119.00</u></u>

\*Figure in this case higher.

Leasing companies are usually unable to obtain a foreign automobile at the same reduced rates available on domestic automobiles. Therefore, the capitalized cost of a foreign car will often be greater than the dealer's retail list price. Good examples of high capitalization are found in the leasing of Volkswagens and Porsches. This is due primarily to the high demand for such cars, aggravated by their relatively short supply. One case reported to the Department of Motor Vehicles involved a \$6,755 capitalization of a Porsche 911T valued at \$6,241.70. DMV REPORT, *supra* note 10, at 3 and 10.

lessor's rental fee, a use tax, and a charge for maintenance and insurance premiums if these are included in the particular lease agreement.

When the lease period expires, the lessee either returns the automobile to the lessor for sale or he may be allowed to sell the car himself.<sup>18</sup> The final obligation of the lessee is determined by adding the amount which has been accumulated in the depreciation reserve fund to the amount realized from the lease-end sale of the automobile and deducting this figure from the capitalized cost. If the sum of these funds exceeds the capitalized cost, the lessee will receive a refund subject to the terms of the particular lease agreement. Alternatively, if the capitalized cost is greater than the sum of these funds, the lessee is liable for the difference.<sup>19</sup> The accuracy of the "projected resale" or "termination" value of the automobile is critical, since this value will determine whether the lessee will be liable for an amount above the aggregate of his monthly payments. When the *actual* resale value is less than the figure which was projected at the time of the lease's execution—as the result, for example, of damage caused by the lessee's unreasonable use of the automobile—the lessee must reimburse the lessor for the resulting deficiency. Since the amount of the monthly payment in an open end lease is freely negotiable, an unscrupulous lessor, under the guise of offering a competitively attractive price, may unduly lower his monthly payments, contributing insufficient funds to the depreciation reserve and creating a deficiency at the end of the lease term. This may be accomplished by projecting an unreasonably high resale or termination value. If the lease-end sale price is less than this overestimated termination value, the responsibility for the deficiency rests with the lessee. Unfortunately, a lessee who is unfamiliar with the mechanics and terminology employed in the lease transaction often is not aware of the liability which may await him at the termination of the lease period.<sup>20</sup>

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18. See DMV REPORT, *supra* note 10, at 7. A suggested third alternative would be to allow the lessee to purchase the automobile himself. However this option is purposely excluded from the lease agreement due to the lessor's fear that the lease contract will be considered a "conditional sale contract," thereby calling into play the stringent requirements of the Rees-Levering Act. If such an option were included in the agreement, the lessee arguably would have "the option of becoming the owner of the vehicle upon full compliance with the terms of the contract" within the meaning of Civil Code § 2981(a)(2) (Rees-Levering Act).

19. It is this liability that prompted the enactment of the Moscone Act. Many consumers assumed that the mechanics of the automobile lease transaction were analogous to the leasing of most chattels. Thus, they usually believed that their lease obligation was limited to the designated number of monthly payments absent any unusual damage caused by them.

20. Even if the consumer is familiar with the obligations present in the open

## PROVISIONS OF THE MOSCONE ACT

While the Moscone Act contains significantly fewer consumer safeguards and remedies for automobile lease transactions than the Rees-Levering Act provides for retail sales agreements, the Moscone Act, nonetheless, was enacted with an eye toward assuring that the lessee is apprised of his potential liability.<sup>21</sup> Specifically, the Moscone Act covers open end lease transactions<sup>22</sup> under which a motor vehicle is "bought for use primarily for personal or family purposes."<sup>23</sup> A "leasing contract" is said to be a contract whose performance exceeds four months duration and by its terms causes the lessee to bear the risk of the automobile's depreciation.<sup>24</sup> However, the lessee's liability is limited. A recent legislative amendment prevents the lessor from imposing a lien upon any property other than the leased vehicle to insure payment of any lessee liability.<sup>25</sup>

*Disclosure*

The basic disclosure requirements of the Moscone Act are embodied in section 2985.8 of the California Civil Code. A lease agreement is to be contained in a single document which must be

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end lease agreement, the lessor's oral representations that a particular automobile will depreciate less or at a slower rate than other makes of automobiles may influence the consumer significantly. Furthermore, the lessor may reassure the lessee that, in all probability, there will be no lease-end liability since he can expertly project an accurate resale value. Either of these claims may fool even the most knowledgeable consumer into the belief that there will be virtually no obligation beyond the monthly payments.

21. See note 5 *supra*. For a comparison of the safeguards provided in the Rees-Levering Act and those in the Moscone Act, see text accompanying notes 38-71 *infra*.

22. Unlike the closed end lease which typically places the risk of the automobile's depreciation upon the lessor absent unreasonable use by the lessee, the open end lease places this risk with the lessee. In the latter case, the lessee is obligated to pay for any depreciation beyond the estimated termination value at the end of the lease term. See notes 18-20 and accompanying text *supra*. This liability is described in the Moscone Act, Civil Code section 2985.7(b), which defines a "leasing contract" to be "any contract for the bailment or leasing . . . of a motor vehicle by which it is agreed that the . . . lessee bear the risk of the motor vehicle's depreciation." (emphasis added). See Supplementary Comment on S.B. 1399, Reg. Sess. (April 8, 1969) on file in the offices of Senator George Moscone, Sacramento, California, and the *Santa Clara Lawyer*. See also Warren and Larmore, *Truth in Lending: Problems of Coverage*, 24 STAN. L. REV. 793, 804 n. 39 (1972) [hereinafter cited as Warren & Larmore].

23. CAL. CIV. CODE § 2985.7(a) (West Supp. 1974). The term "bought" seems to be used in a rather questionable context for it appears to perpetuate the confusion as to whether a leasing agreement is, in fact, a conditional sale contract.

24. CAL. CIV. CODE § 2987.2(b) (West Supp. 1974). Presumably, the requirement that the duration of the lease exceed four months is to exclude short-term rentals from the Moscone Act's coverage.

25. CAL. CIV. CODE § 2985.81 (West Supp. 1974).



free from blanks at the time of execution.<sup>26</sup> In addition, the lessee must be given a copy of the lease agreement at the time the leasing contract is signed.<sup>27</sup> Section 2985.8 further requires that every leasing contract disclose in writing: (a) the value or capitalized cost of the automobile;<sup>28</sup> (b) the total amount of periodic payments to be credited to the lessee;<sup>29</sup> (c) the sum of the portions of each monthly payment representing the lessor's rental fee which will not be so credited;<sup>30</sup> (d) the maximum amount for which the lessee could be liable at the conclusion of the lease term;<sup>31</sup> (e) the price of any insurance obtained through the lessor and the terms of its coverage;<sup>32</sup> and, (f) a notice in eight-point type which reads: "Notice to the lessee: (1) Do not sign this agreement before you read it or if it contains any blank spaces to be filled in. (2) You are entitled to a completely filled-in copy of this agreement."<sup>33</sup>

### *Penalties for Non-Disclosure*

The lessor's violation of any of the disclosure provisions set forth in section 2985.8 will render the lease agreement unenforceable, unless it is the result of an accidental or bona fide error of computation. Under this circumstance, the lessee may recover any payments made in accordance with the lease agreement. But, a violation will not destroy the validity of the agreement when it is sought to be enforced by a bona fide purchaser, assignee or pledgee for value<sup>34</sup> or when the violation has been cor-

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26. CAL. CIV. CODE § 2985.8 (West Supp. 1974).

27. CAL. CIV. CODE § 2985.8 (West Supp. 1974) provides in pertinent part:

Every leasing contract for the lease or bailment of an automobile . . . shall contain in a single document all of the agreements of the lessor and lessee. . . . [a]n exact copy thereof shall be furnished the lessee by the lessor at the time the lessor and the lessee have signed the contract.

28. *Id.*

29. *Id.* A portion of each lease payment is credited to the lessee, thereby progressively reducing his liability for the capitalized cost of the automobile. This amount is accumulated in the "depreciation reserve" and represents the lessor's recapture of the automobile's depreciation. See notes 16-18 and accompanying text *supra*. At the end of the lease, the sum of these credits is deducted from the value or capitalized cost of the automobile. The resulting figure is the amount the automobile must realize upon resale. Should this resale yield less than this figure a deficiency is charged against the lessee.

30. *Id.* This figure is independent of the lessor's recapture of the automobile's depreciation, and represents the lessor's fee for leasing the automobile from which he is able to recoup his overhead and obtain additional profit.

31. *Id.* This figure is designated as the "projected depreciation" or "termination value" and typically equals the projected wholesale value of the automobile at the end of the lease term.

32. *Id.*

33. *Id.*

34. CAL. CIV. CODE § 2985.9 (West Supp. 1974).

rected within the time permitted pursuant to Civil Code section 2985.91.<sup>35</sup> That section states that a failure to comply with the provisions of Civil Code section 2985.8 may be corrected by the holder of the leasing contract. If the failure to comply is a willful violation appearing on the face of the contract it must be corrected within thirty days after execution or within twenty days after the sale, assignment, or pledge of the contract, whichever is later.<sup>36</sup> This twenty-day period commences with the initial sale, assignment or pledge of the leasing contract. A correction increasing the amount owing on the balance or the amount of any installment will not be effective unless the lessee consents in writing to the correction. In the event an amount is improperly collected by the lessor, it must either be credited or refunded to the lessee. If the lessor fails to comply with the Act he must notify the lessee of his failure, a correction must be made within ten days after the lessee receives the notice and a corrected copy of the contract must then be mailed to the lessee. Section 2985.91 of the Civil Code concludes by stating that a properly corrected violation cannot serve as the basis for any recovery by the lessee and will not affect the holder's right in enforcing the contract.<sup>37</sup>

#### A COMPARISON: THE MOSCONE ACT AND THE REES-LEVERING ACT

While the Moscone Act requires only that a lessor make certain specific disclosures at the time of a lease's execution, the Rees-Levering Act, in addition to prescribing the form and content of the conditional sale contract, regulates: (1) the method by which a seller may procure financing for a buyer;<sup>38</sup> (2) the rates of finance charges which may be assessed on the amount financed;<sup>39</sup> (3) the procedure to be followed upon resale of the automobile after default<sup>40</sup> and, (4) the acceleration of payments permitted to the seller upon the buyer's default.<sup>41</sup>

Since a purchaser under a conditional sale contract and a lessee under a leasing contract are both ultimately liable for the agreed-upon value of the respective goods involved<sup>42</sup> and are often subjected to similar coercive treatment by businessmen, it is

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35. *Id.* § 2985.91 (West Supp. 1974).

36. Since the section deals with the procedure to be followed in correcting a willful violation of Civil Code § 2985.8, by implication a lessor is allowed to correct a non-willful violation of that section at any time.

37. CAL. CIV. CODE § 2985.91 (West Supp. 1974).

38. *Id.* § 2982.5.

39. *Id.* § 2982(c).

40. *Id.* § 2983.2.

41. *Id.* § 2983.3.

42. Compare CAL. CIV. CODE § 2981(a) (West Supp. 1974), with CAL. CIV. CODE § 2985.7(b) (West Supp. 1974).

curious that policy considerations leading to the enactment of statutes stringently regulating retail sales transactions have not compelled the promulgation of laws providing similar protection for the leasing consumer. The California state legislature, after first unsuccessfully attempting to include automobile leasing within the coverage of the Rees-Levering Act, did not carry over to the Moscone Act many of the Rees-Levering Act's provisions pertinent to leasing.<sup>43</sup> It is unclear why the legislature assumed that lease transactions were not subject to the same abuses which existed in the area of automobile sales. Regardless of the reasons, it left the lessee with little protection against the practices of unethical lessors.<sup>44</sup> An analysis of the provisions of the Rees-Levering Act which could have been adapted to leasing transactions illustrates the narrow scope and limited effectiveness of the Moscone Act.<sup>45</sup>

a) The Rees-Levering Act requires that the contract contain the following statement:

If you default in the performance of your obligations under this agreement, the vehicle may be repossessed and you may be subject to suit and liability for the unpaid indebtedness evidenced by this agreement.<sup>46</sup>

The Moscone Act fails to require a similar warning to the lessee of his probable liability upon default in payment or other breach of his lease obligations. The only notice provision which the Moscone Act requires in the lease contract is a statement cautioning the lessee to read the agreement and to refrain from signing if it contains any blank spaces.<sup>47</sup> Thus, unless the lessee is familiar with leasing terminology and the legal implications of the figures which the Moscone Act requires to be disclosed, he has no real practical notice of his potential liability.

b) The Rees-Levering Act not only requires disclosure of the finance charge which is applied to the unpaid balance, but

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43. See Cal. S.B. 1399, Reg. Sess. (April 8, 1969), introduced by Senator George Moscone, the first draft of which attempted to amend the Rees-Levering Act's definition of a "conditional sale contract" so as to include the leasing of automobiles.

44. See notes 72-168 and accompanying text *infra*.

45. To this date, there have not been any reported appellate decisions involving provisions of the Moscone Act. This may indicate that the Act lacks sufficient "bite" since essentially the lessor owes no further obligation to the lessee beyond the disclosure of the six items required to be listed in the lease agreement. This stands in marked contrast to the large number of suits litigated pursuant to the provisions of the Rees-Levering Act. See, e.g., *Thomas v. Wright*, 21 Cal. App. 3d 921, 98 Cal. Rptr. 874 (1971); *Golden West Credit Corp. v. Maury*, 270 Cal. App. 2d 913, 75 Cal. Rptr. 757 (1969); *Katsaros v. O.E. Saugstad Co.*, 197 Cal. App. 2d 745, 17 Cal. Rptr. 453 (1961).

46. CAL. CIV. CODE § 2982(a)10 (West Supp. 1974).

47. *Id.* § 2985.8(f).

also limits this finance charge.<sup>48</sup> Although there is no finance charge per se in a lease agreement (since technically the lease is not considered a sale) the lessee is still paying a sum for the lessor's services independent of the amount exacted for payment of the lessor's recapture of depreciation. While the Moscone Act requires that the total amount of the lessor's fee be set forth in the lease agreement,<sup>49</sup> there is neither a percentage limitation on this amount nor a requirement that this figure be represented as a percentage amount to provide potential lessees a basis for comparing the service rates charged by different lessors.<sup>50</sup>

c) The Rees-Levering Act imposes limitations on both the amount and number of charges which may be assessed to the

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48. *Id.* § 2982(c) provides:

The amount of the finance charge in any conditional sale contract for the sale of a motor vehicle, with or without accessories, shall not exceed 1 percent of the unpaid balance multiplied by the number of months (computed on the basis of a full month for any fractional month period in excess of 15 days) elapsing between the date of the contract and the due date of the last installment, or twenty-five dollars (\$25), whichever is greater. The contract may provide for a delinquency charge or charges on any installment in default for a period of not less than 10 days in an amount not to exceed in the aggregate 5 percent of the installment, which amount may be collected only once on any installment regardless of the period during which it remains in default. The contract may provide for reasonable collection costs and fees in the event of delinquency.

49. *Id.* § 2985.8.

50. Typically, in computing the amount of the monthly lease fee (service charge), a lessor will multiply the capitalized cost of the automobile by a specific percentage figure providing a monthly "fee" to be added to the regular installment payments. See DMV REPORT, *supra* note 10, at 10. An example of this computation appears in the DMV's report. Employing the figures in note 15 *supra* the monthly lease fee would be computed as follows:  $\$6807 \times 0.7\% = \$47.65$ . This figure is not separately set forth in the leasing contract; thus, the lessee is unable to compare the "cost" of leasing among various lessors.

Traditionally, it has been assumed that open end leasing was not a "credit sale" and was therefore immune to the credit disclosure requirements of the Truth in Lending Act, 15 U.S.C. §§ 1601-65 (1970). However, this assumption has been criticized as not totally accurate. See Warren & Larmore, *supra* note 22. In discussing the applicability of this Act to the open end lease transaction, William D. Warren, a former consultant to the Board of Governors of the Federal Reserve System on Truth in Lending, and Thomas R. Larmore, formerly a member of the Truth in Lending Staff of the Board of Governors of the Federal Reserve System, stated:

Though the language of the Act does not fit the case, it is clear that the open end lease amounts to a credit sale. At first glance it may appear that the lessee has contracted to pay substantially less than the value of the property for the two year lease and that he could opt to become the owner only upon payment of a sum substantially in excess of anything that could be called nominal. A closer look at the transaction, however, reveals that the lessee has taken on the liabilities of a buyer rather than those of a lessee. . . . In both the credit sale and the open end lease the dealer is guaranteed compensation for the use of capital and for the original cash price of the automobile and in both cases the customer takes the risks of the condition of the car and the state of the second-hand market. These are buyer's risks, and the open end lease is, in effect, a sale.

*Id.* at 806-07.

buyer on installment payments delinquent for more than ten days.<sup>51</sup> The Moscone Act places no similar restriction upon the lessor, allowing the lessor to exercise total discretion in determining when a lease payment is delinquent and the amount of the penalty to be assessed as a result.

d) Under the Rees-Levering Act, when an automobile is repossessed, the holder of the contract must notify the defaulting purchaser either personally or by certified mail of his intent to sell the repossessed automobile within ten days.<sup>52</sup> This notice must inform the purchaser of his right to redeem the automobile and set forth the total amount necessary to do this.<sup>53</sup> In addition, the notice must contain an itemization of delinquency costs and repossession fees together with any credit for unearned finance charges or cancelled insurance.<sup>54</sup> Furthermore, it must contain the following,

Notice: You are subject to suit and liability if the amount obtained upon sale of the vehicle is insufficient to pay the contract balance and any other amounts due.<sup>55</sup>

In a lease transaction, if the lessee defaults in his lease obligations he must either obtain the lessor's permission to sell the automobile or return the automobile to the lessor. Usually, the lessee will be required to return the automobile to the lessor. The lessor—as in the case when a seller repossesses an automobile under a conditional sale contract—will then sell the automobile and the proceeds of this sale will be credited toward the balance owed on the lease contract. Despite this similarity between retail sales and leasing repossession techniques, the Moscone Act does not require the lessor to notify the lessee of his intent to sell the automobile. Instead, the lessee is usually notified of the lessor's sale after the latter has disposed of the automobile, precluding the former from attempting either to redeem the automobile or to secure the highest possible sale bid.

e) While the Rees-Levering Act authorizes the award of reasonable attorney's fees to the prevailing party in litigation arising out of an automobile sale transaction,<sup>56</sup> no such language appears in the Moscone Act. There is little incentive for lessees, especially those with limited means, to seek redress for a viola-

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51. CAL. CIV. CODE § 2982(c) (West Supp. 1974).

52. *Id.* § 2983.2.

53. *Id.* This section is consistent with the procedure set forth in the California Commercial Code which conditions a debtor's right of redemption of collateral upon his tendering fulfillment of all obligations, including all acceleration payments and expenses incurred by the secured party in retaking and preparing the collateral for disposition. CAL. COMM. CODE § 9506 (West 1964).

54. CAL. CIV. CODE § 2983.2 (West Supp. 1974).

55. *Id.*

56. *Id.* § 2983.4.

tion of the disclosure provisions of the Moscone Act because the recovery sought by the lessee is often substantially less than the legal costs involved in pursuing such an action.

f) The Rees-Levering Act provides that the buyer may assert against the seller's assignees all equities and defenses which exist against the seller at the time of the assignment.<sup>57</sup> In addition, it prohibits the seller from including in the contract a provision stipulating that the buyer will not assert a claim or defense against an assignee of the seller.<sup>58</sup>

Since the Moscone Act does not contain similar restrictions, it is common practice for leasing companies to assign the lease contract to a lending institution at a discounted rate. Under the Moscone Act, the lessor is free to include in the contract an assignment provision in an attempt to cut off the lessee's rights against the assignee. As a result most lease agreements include a clause which stipulates that the right of an assignee shall be free from all defenses, set-offs and counterclaims of every kind which the lessee may be entitled to assert against the lessor.<sup>59</sup> Under the Rees-Levering Act, this type of clause is clearly proscribed. Despite the lack of any specific statutory interdiction under the Moscone Act, several California courts have held that it is questionable whether the lessee can be bound by such a provision.<sup>60</sup>

g) The Rees-Levering Act, in addition to providing the buyer with the right to rescission for a seller's violation of the disclosure or finance charge provisions,<sup>61</sup> stipulates that *willful* violations of its provisions shall be deemed a misdemeanor.<sup>62</sup> Presumably, the threat of possible misdemeanor prosecution encourages potentially unscrupulous dealers to comply with the requirements of the Act. In contrast, under the Moscone Act the only remedies

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57. *Id.* § 2983.5.

58. *Id.* § 2983.7(a).

59. *See, e.g.*, the following motor vehicle lease agreements on file in the office of the *Santa Clara Lawyer*: Cenval Leasing, Oakland, California; Fazackerly Leasing Co., So. San Francisco, California; Redwood Leasing Co., Redwood City, California.

60. *See Commercial Credit Corp. v. Orange County Mach. Works*, 34 Cal. 2d 766, 214 P.2d 819 (1950); *American Nat'l Bank v. A.G. Somerville*, 91 Cal. 364, 216 P. 376 (1923). *See also* SIMPSON, *CONTRACTS* § 133 (2d ed. 1965). In discussing the defenses to which an assignee of a contract is subject, Professor Simpson states:

An assignment is a transfer of a right, and if the right is limited in the hands of the assignor it is to the same extent limited in the hands of the assignee. Accordingly, the assignee takes subject to all defenses which are inherent in the contract that created the rights assigned; and the fact that he took for value and without notice of the defect does not affect the result.

*Id.* § 133, at 279.

61. CAL. CIV. CODE §§ 2982.7, 2983 (West Supp. 1974).

62. *Id.* § 2983.6.

available to a lessee are civil remedies for breach of contract.<sup>63</sup>

h) The Rees-Levering Act *prohibits* the seller from including within a conditional sale contract any provision by which:

- 1) The buyer agrees not to assert against the seller or his assignee any claims or defenses arising out of the sale.<sup>64</sup>
- 2) The buyer gives the seller or holder a power of attorney to confess judgment, assign wages, or act as his agent in the collection of payments under the contract or in the repossession of the automobile.<sup>65</sup>
- 3) The buyer waives any cause of action arising from the commission of illegal acts in the collection of payments or the repossession of the automobile.<sup>66</sup>
- 4) The buyer relieves the seller from liability for any legal remedy which he may possess under the terms of the contract or a separate instrument.<sup>67</sup>
- 5) The buyer gives the seller or holder of the contract the right to commence any action on the contract in any county which the seller or holder selects without proper venue.<sup>68</sup>

The Moscone Act does not impose any limitation upon what provisions may be included in a lease agreement, leaving the lessor free to incorporate restrictions in the contract which would fail under the proscriptions of the Rees-Levering Act.

i) The Rees-Levering Act further requires that any action on the contract arising under the provisions of the Act must be tried,

in the county in which the contract was in fact signed by the buyer, in the county in which the buyer resided at the time the contract was entered into, *in the county in which the buyer resides at the commencement of the action* or in the county in which the motor vehicle is permanently garaged.<sup>69</sup>

Furthermore, the plaintiff, in conjunction with the filing of the complaint, must file an affidavit with the court stating facts that support venue in that county.<sup>70</sup>

Since the Moscone Act contains no similar provision, an action involving a lease contract must be brought pursuant to section 395(b) of the Code of Civil Procedure which provides that a cause of action in contract must be brought,

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63. *Id.* § 2985.9.

64. *Id.* § 2983.7(a). For a discussion of assignee liability under the Moscone Act see text accompanying notes 59-60 *supra*.

65. *Id.* § 2983.7(b) & (d).

66. *Id.* § 2983.7(c).

67. *Id.* § 2983.7(e).

68. *Id.* § 2983.7(f).

69. *Id.* § 2984.4 (emphasis added).

70. *Id.*

in the county in which the defendant in fact signed the contract, the county in which the defendant resided at the time the contract was entered into, or the county in which the defendant resides at the commencement of the action . . . .<sup>71</sup>

The language of the two sections is parallel, and indeed, if the *seller* or the *lessor* commences suit, the defendant buyer or lessee is equally protected under either provision. However, because the Code of Civil Procedure speaks in terms of the "defendant" rather than "buyer" or "lessee," whenever the lessee is the *plaintiff*, he will not necessarily be able to file suit in the county in which he resides as he would under the Rees-Levering Act. Thus, a buyer, unlike a lessee, is able to bring suit in any county to which he may move subsequent to executing the contract.

Many of the Rees-Levering Act's requirements which could reasonably have been made applicable to an automobile lease transaction go beyond the moment of execution and provide the consumer with various procedural safeguards throughout the duration of the contractual relationship. Despite the similar liability of the lessee and buyer in procuring an automobile under contract, the legislature has neglected to provide the lessee the protection afforded his purchasing counterpart under the Rees-Levering Act.

#### DEFICIENCIES IN THE MOSCONE ACT: ABUSES WHICH THE ACT DOES NOT PROHIBIT

The most enticing element of leasing likely to attract consumers is the low capital outlay required as a condition to acquisition of a new automobile. To the sophisticated consumer, leasing an automobile offers him an opportunity to retain his capital for other investment purposes and, in addition, if the vehicle is utilized in his trade or business, enables him to deduct the lease payments in computing his tax liability.<sup>72</sup>

Problems exist, however, with the less informed consumer. Automobile leasing for personal use is a relatively new development in the consumer market. As a result, unscrupulous individuals are able to employ various deceptive tactics to take advantage of consumers who are unacquainted with automobile lease transactions and their hidden liabilities. Because of the inadequate protection afforded consumers by the present law, it is necessary to examine the continuing problems experienced by consumers despite the passage of the Moscone Act.

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71. CAL. CIV. PRO. CODE § 395(b) (West 1974).

72. INT. REV. CODE OF 1954, § 162.



*Misleading and Bait Advertising*

Typically, advertisements to lease automobiles entice consumers by offering a low monthly payment on an automobile which the consumer could not otherwise afford.<sup>73</sup> Being generally familiar with the leasing of apartments or houses, the consumer is under the impression that, absent unusual damage to the lease vehicle, his liability is limited to the payment of monthly rental fees for the duration of the lease term.

The unsuspecting consumer is often led to believe that for "no down payment" or "\$100 on any new car lease" he is able to use a new automobile merely by making "low lease payments." The fact that the consumer will be liable for a stipulated termination value<sup>74</sup> is either undisclosed or intentionally deemphasized. Not surprisingly, an unsophisticated consumer will "shop around" for the lowest *monthly* lease payment, thinking that the lower the rental payments the better the deal.<sup>75</sup>

This is clearly not the case. As a consequence of offering *low* monthly payments the termination value is inflated above the price which can reasonably be expected from the sale of the automobile at the end of the lease term. The lessee will find himself with an unanticipated debt since under the terms of the lease agreement he is obligated to pay any deficit resulting from realizing proceeds which fall short of the projected termination value.

Often an advertisement, by setting forth only the amount of a monthly payment, will appear to solicit a sale rather than a lease, inducing a naive consumer to believe that he will be able to purchase a relatively expensive automobile at no greater expenditure than the low monthly payments advertised. To further distort the lessee's true liability, the lessor may tell the consumer that although the payments advertised actually pertain to a lease agreement, the payments simply defer the down payment to the end

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73. Typically, a lease advertisement will contain the amount of the monthly payment in large bold print and the term of the lease, failing to similarly emphasize the other aspects of a lessee's obligations. This practice clearly falls short of the *Recommended Standards of Practice for Advertising, Selling, Rental, or Leasing of Automobiles* prepared by the National Automobile Dealer's Association in conjunction with the Association of Better Business Bureaus published in May, 1969. Section 38 thereof states that:

If a rate is advertised, and the lessee may be required to meet any additional financial obligation or expense either during or at the end of the lease period, the specific obligations of the lessee shall be set forth in the advertising.

74. See text accompanying notes 16-20 *supra*.

75. DMV REPORT, *supra* note 10, at 11; Interview with Mr. Rand Miller, Leasing Representative, First National Bank Leasing Center, in San Jose, California, March 18, 1974.

of the lease term should he eventually decide to purchase the automobile, at which time they will be credited toward the "original selling price."<sup>76</sup>

The Board of Governors of the Federal Reserve System (hereinafter the Board) has determined that leasing does not fall within the definition of a "credit sale"<sup>77</sup> set forth in Regulation Z,<sup>78</sup> thereby exempting lessors from the credit disclosure requirements of the federal Truth in Lending Act.<sup>79</sup> As a result, leasing advertisers need not disclose the lessor's monthly leasing fee<sup>80</sup>—the equivalent to the finance charge assessed in retail sale contracts. Instead, only the total monthly lease payment is provided, preventing even the most sophisticated consumer from determining or comparing the different costs of leasing from various companies. The Board's refusal to apply the Act's credit disclosure requirements to leasing transactions is attributable to its belief that a lease is not a purchase or sale and therefore does not involve an extension of credit. The validity of this view is open to serious examination.<sup>81</sup> Initially, upon executing the agreement, the lessee, like the purchaser in an automobile sales contract, agrees not only to guarantee the lessor total reimbursement for the agreed upon value of the automobile, but also assumes the risk of depreciation. It is of no real consequence that the lessee must

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76. See note 88 *infra* for a comparison of the expenditures involved in leasing as opposed to purchasing an automobile.

77. 12 C.F.R. 226.2(n) (1973) states that:

"Credit sale" means any sale with respect to which consumer credit is extended or arranged by the seller. The term includes any contract in the form of a bailment or lease if the bailee or lessee contracts to pay as compensation for use a sum substantially equivalent to or in excess of the aggregate value of the property and services involved and it is agreed that the bailee or lessee will become, or for no other or for a nominal consideration has the option to become, the owner of the property upon full compliance with his obligations under the contract.

Section 2981(a)(2) of the Civil Code (Rees-Levering Act) has virtually duplicated this language for purposes of defining a "conditional sale contract".

78. 4 CCH CONS. CRED. GUIDE ¶ 30,117 (Federal Reserve Board Letter no. 50 (July 28, 1969)). See also Warren & Larmore, *supra* note 22, at 803. Regulation Z is the official name of the codification of the rules and regulations promulgated by the Federal Reserve Board to aid in the interpretation and enforcement of the Truth in Lending Act. See note 79 *infra*.

79. 15 U.S.C. §§ 1601-65 (1970). Section 105 of the Truth in Lending Act (15 U.S.C. § 1604) authorizes the Board of Governors of the Federal Reserve System to promulgate regulations to carry out the purposes of that act. These regulations, designated as "Regulation Z" are designed:

[T]o assure that every customer who has need for consumer credit is given meaningful information with respect to the cost of that credit . . . so that the customer may readily compare the various credit terms available to him from different sources and avoid the uninformed use of credit.

12 C.F.R. 226.1(a)(2) (1973).

80. See text accompanying note 50 *supra* and notes 116-28 *infra*.

81. See Warren & Larmore, *supra* note 22.

return the vehicle rather than pay the balance remaining on a conditional sale contract, for the lessee's failure to return the vehicle will result in liability similar to that imposed upon a defaulting purchaser. In either instance, upon breach of the agreement the vehicle will be repossessed and the proceeds from the vendor's sale will be deducted from the contract balance in order to determine the amount, if any, of the deficit.<sup>82</sup> Moreover, it is unrealistic to assume that leasing does not involve the extension of credit.<sup>83</sup> The Board has defined "credit" as "the right granted by a creditor to a customer to defer payment of debt, incur debt and defer its payment, or purchase property or services and defer payment therefor."<sup>84</sup> It cannot be disputed that the lessee has, in fact, incurred a debt for the agreed upon value of the leased automobile. Furthermore, whether leasing is characterized as a purchase of property or services, the lessee's ability to defer payment of the debt over the duration of the base period is a right granted by the creditor-lessor. This "right" is often stressed in advertising the desirability of automobile leasing.

The present lack of statutory legislation in the area of automobile lease advertisements enables lessors to exploit consumer naivete by exclusively emphasizing attractive low monthly payments without disclosing the extent of a lessee's actual liability. There is an urgent need for legislation directed toward apprising the consumer of the true nature of the lease transaction and its attendant obligations.<sup>85</sup> He should be presented with meaningful information with respect to the cost of leasing so that he may readily compare the various lease terms available. At the least, the lessor should be required to disclose in his advertisements as well as in the lease agreement both the amount of the monthly lease fee, expressed either as a dollar amount or a percentage of the capitalized cost, and the maximum amount for which the lessee may be liable at the end of the lease term.<sup>86</sup> The former is extremely important, for an exorbitant monthly lease fee may

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82. See notes 15-20 and accompanying text *supra*.

83. See Warren & Larmore, *supra* note 22, at 803 n.36.

84. 12 C.F.R. 226.2(1) (1973).

85. This need has already been recognized by the Board of Governors of the Federal Reserve System. At this writing efforts are being made to include leasing within the coverage of Regulation Z. Telephone interview with William D. Warren, Professor of Law, Stanford University, February 14, 1974, former consultant to the Board of Governors of the Federal Reserve System on Truth in Lending. Furthermore, the Attorney General's Office of the State of California is also considering proposing legislation at the state level which would require lease advertisements to include in their descriptions the amount for which a lessee may be liable at the end of the lease term. Telephone interview with Herschel T. Elkins, Deputy Attorney General, Consumer Protection Division, Office of the Attorney General of the State of California, January 10, 1974.

86. See appended Proposed Legislation § 3 *infra*.

be disguised in a low monthly payment. In addition, it is essential that lease advertisements set forth the "capitalized cost" of the automobile to provide the consumer with a basis for comparing the "capitalized cost" with the automobile's actual purchase price.<sup>87</sup> Without such legislative protection consumers will continue to fall prey to deceptively attractive leasing arrangements.

### *Misleading Representations of Salesmen*

The potential for exploiting consumer unfamiliarity with leasing becomes more apparent when one considers that the subtle techniques of a skillful salesman can be more persuasive than a newspaper advertisement. Consumers who are unacquainted with automobile leasing are especially vulnerable to sales representations which glamorize the attributes of lease arrangements.

Frequently, a combination dealer/lessor will suggest leasing as an alternative to purchasing an automobile when it becomes apparent that the customer is unable or unwilling to spend the high monthly payments necessary to buy the automobile of his desire.<sup>88</sup> The dealer's preference for leasing rather than selling the

#### 87. *Id.*

88. A survey of seven leasing agencies, including several combination dealer/lessors, conducted by the author in January, 1973, indicated that the majority of these agencies recommended leasing rather than buying to their customers. To convince their customers of the benefits of leasing, most agencies stressed the low lease payments and the prestige of driving a more expensive car. Some simply stated that, in the long run, leasing was more economical and convenient.

Figures acquired from Stevens Creek Toyota (Personal Auto Leasing), a combination dealer/lessor, indicate that this assertion is highly questionable. The following figures compare the actual cost of leasing to the cost of purchasing a 1973 Toyota whose projected termination value was estimated to be \$1,000.

	Lease	Sale
Retail list price	\$2500	\$2500
Lessor markup	100	
"Capitalized Cost"	2600	
Security Deposit	65.62	125 (use tax)
License	55	55
	<u>2720.62</u>	<u>2780</u>
Down payment	186.24	400
Amount to be financed	2534.38	2380
Amount to be recaptured through monthly payments	1534.38	2380
Payments	\$65.62 × 35 mo's (\$2296.70)	\$75 × 36 mo's (\$2700)
Add down payment	<u>186.24</u>	<u>400</u>
Total cost out of pocket	\$2482.94	\$3100
Value of automobile at end of 36 months	\$1000 (Title w/lessor)	1000
		<u>2100</u>
Sale of auto by lessor may create liability if sale price is less than \$1000		

automobile may be prompted by several considerations. If the consumer's credit is approved, the dealer will be able to lease an automobile he might otherwise have been unable to sell due to high monthly payments.<sup>89</sup> Furthermore, since leasing requires no down payment the dealer may be able to dispose of a higher priced automobile by suggesting that the lessee supplement the monthly amount he was originally willing to pay under a purchase agreement with the capital saved by avoiding the down payment. An additional consideration which may affect the dealer's preference for leasing is the relative lack of comprehensive statutory regulation of automobile leasing.<sup>90</sup> While the sale of an automobile is subject to Truth in Lending credit disclosures,<sup>91</sup> Department of Motor Vehicles licensing and regulation,<sup>92</sup> and the comprehensive procedural and disclosure requirements of the Rees-Levering Act,<sup>93</sup> leasing is exclusively governed by the comparatively lax requirements of the Moscone Act.

The fact that a lessee will be liable for the "termination value" of the automobile may be deemphasized or ignored until

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Total cost of automobile	\$2482.94	\$2100
	+ liability	
	created at lease-end sale	
(Security deposit refunded if no liability is created).		

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Most leasing agencies pointed out, in passing, the tax advantages of leasing, but only a few stipulated that this could be done only if the automobile was employed in a business capacity. Other features suggested by these lessors included the safety features provided by a new automobile, the inevitability of making car payments under a purchase contract for the rest of the purchaser's life, the unlikelihood that a person would wish to drive an automobile for more than three years, and the probability that there would be a rebate received upon returning the automobile at the end of the lease term. Those surveyed included: Atlantic-Pacific Leasing Company, San Jose, California; Courtesy Chevrolet, San Jose, California; Douglas Lease Company, San Jose, California; Norm Anderson Volkswagen, San Jose, California; Personal Auto Leasing Company, Santa Clara, California; Southwest Leasing Corporation, San Jose, California; Varner-Ward Leasing Company, Santa Clara, California [hereinafter cited as Author's Survey].

89. An additional incentive is provided by manufacturers of American automobiles who typically offer factory rebates to leasing companies and dealers on each unit sold or leased. At this time such rebates are as large as \$500 on larger American automobiles due to the recent "energy crisis". Interview with Mr. Rand Miller, Leasing Representative, First National Bank Leasing Center, in San Jose, California, March 18, 1974.

90. See text accompanying notes 38-71 *supra*.

91. 15 U.S.C. §§ 1601-65 (1970).

92. CAL. VEH. CODE §§ 11700-900 (West 1971). Until recently it has been assumed that the Department of Motor Vehicles had no regulatory jurisdiction over leasing agencies. However, a recent DMV interagency opinion concludes that the department does in fact have such jurisdiction. See DMV Opinion 73-2-6 (Feb. 27, 1973). At this writing budgetary allocations for the fiscal year 1975 have been granted by the legislature for four new investigators. Telephone interview with Mr. Frank Broadhurst, Director of Division of Compliance of the Department of Motor Vehicles, in Sacramento, California, December 18, 1973.

93. CAL. CIV. CODE §§ 2981-2984.4 (West Supp. 1974).

the lessee has passed a credit check and is "sold" on the idea of acquiring a new automobile for a low monthly payment.<sup>94</sup> Even if the consumer is aware of the significance of the "termination value" he may be told that a lease-end deficiency is virtually impossible since the lessor's expertise in the automobile industry enables him to estimate accurately the resale or "termination value."<sup>95</sup>

Automobile leasing presents a difficult problem to those concerned with adequately protecting the interests of the consumer because the manner in which leasing transactions are presented and entered into is frequently manipulated by the lessor to camouflage the consumer's actual liability. While the Moscone Act attempts to educate consumers by requiring lessors to set forth certain figures in the actual lease agreement, this protection is illusory. A consumer rarely sees the lease agreement until a few moments before execution. Prior to that time the consumer's only real knowledge of the leasing arrangement comes from the oral representations made by the lessor. Moreover, even when he receives a filled-in copy of the lease agreement it is unlikely that he will be any more enlightened than he was when he stepped into the dealer/lessor's showroom.

The problems resulting from consumer unawareness in automobile leasing cannot be solved by simply requiring more stringent disclosure requirements of those seeking to engage in the

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94. Author's Survey, *supra* note 88. Most of those questioned did not mention the significance of the termination value. Instead it was most often emphasized that the only real responsibilities imposed upon the lessee were to make the monthly payments and return the automobile in reasonable condition at the end of the lease term. Those who did mention the termination value generally discounted its importance by stressing that they had the prescience to depreciate realistically the automobile over the duration of the lease term.

95. *Id.* One such representation commonly made by the lessor which deserves particular mention usually occurs after the lessee has decided to lease the automobile. This involves the lessor's statements that the automobile may be less marketable at the end of the lease if certain options are not included. Some lessors may tell the lessee that the automobile simply cannot be acquired without certain options, or that the lessee must "special order" the automobile if the lessee insists on a lesser-equipped model. When the lessee is notified that the automobile he wishes to lease has arrived, he may find certain options included in the automobile which he neither ordered nor desired. If the lessee has anticipated delivery of the automobile for a long period of time, it is not unreasonable to assume that he will reluctantly acquiesce to the addition of these accessories in order to take delivery of the automobile. The experience of this author involved the leasing of a foreign car in relatively short supply. An agreement was reached with the lessor to lease the automobile and it was ordered from the distributor. When the author returned to take delivery and sign the agreement he discovered that a \$200 radio was in the process of being installed in the vehicle thus raising the monthly lease payment an additional \$6 per month. The addition of this option was not reflected in the lessor's sale proceeds, nor for that matter, would the lessor have been unable to sell the automobile without it.

business of leasing automobiles. This is clearly evidenced by the abuses which continue to exist despite the Moscone Act's disclosure provisions. Rather than seeking to impose the total burden of understanding upon the consumer, remedial legislation should concentrate on regulating the lessor who purports to offer "expert" services to a relatively unsophisticated consuming public. This may be accomplished by enacting legislation which would limit not only the amount a lessor may charge for his services,<sup>96</sup> but also the amount of any deficiency he may seek to recover from a lessee at the end of the lease term.<sup>97</sup>

### *Copy of Lease Agreement*

Although the Moscone Act requires that a lessee be furnished with a filled-in copy of the lease agreement,<sup>98</sup> this requirement by itself will not inform the consumer of the obligations underlying an open end lease transaction. The Moscone Act imposes no obligation on the lessor to supply the consumer with a copy of the lease agreement *until it has been executed* by both parties.<sup>99</sup> Although the lessee must be provided with a memorial of his agreement, it may be "too little too late" in view of the fact that the lessee is frequently given no opportunity to read the lease agreement thoroughly in advance of the time for his signing. Furthermore, even if the consumer is provided with a copy of the lease form prior to execution, it is unlikely that he will completely understand its provisions.

Typically, the lease contract is filled in by the salesman and presented to the lessee only when the latter has decided to acquire

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96. See appended Proposed Legislation § 10.

97. *Id.* § 8. Although such legislation might appear to work an undue hardship on lessors, the policy behind these restrictions is comparable to that which underlies the theory of strict liability in tort. For more than a decade, the California courts have recognized the concept of strict liability. Under this doctrine, liability is imposed upon the seller regardless of negligence or fault.

The purpose of such liability is to insure that the cost of injuries resulting from defective products are borne by the manufacturers that put such products on the market rather than by the injured persons who are powerless to protect themselves.

*Greenman v. Yuba Power Products, Inc.*, 59 Cal. 2d 57, 63, 377 P.2d 897, 901, 27 Cal. Rptr. 697, 701 (1962). It is equally possible for the legislature to apply this sort of reasoning to legislation affecting automobile leasing. The lessee should not be forced to totally bear the risk of insuring the accuracy of the lessor's representations any more than the buyer is forced to guarantee the safety and suitability of the product he uses. For a discussion of possible ways in which the legislature might wish to limit lessee lease-end liability see text accompanying notes 143-47 *infra*.

98. CAL. CIV. CODE § 2985.8 (West Supp. 1974).

99. *Id.* There is no language in this section which requires the lessor to furnish a prospective lessee with a copy of a lease agreement.

a particular automobile and both parties have agreed to the terms of the contract.<sup>100</sup> To the ordinary lessee, the terms on which he and the salesman have agreed may consist solely of the amount and number of required monthly payments. Yet, the Moscone Act assumes the lessee is not only cognizant of the amount and number of monthly payments, but also fully understands the myriad other terms of the written contract and the full extent of his obligations. This assumption is unwarranted in the face of the lack of legal sophistication of most leasing consumers. Furthermore, it is unlikely that an uninformed lessee will attempt to carefully wade through the lease agreement's several pages of finely-printed legal "jargon." At best, he will cursorily read the agreement, relying primarily on the salesman's assurances that the terms and obligations in the agreement are identical to those previously discussed. If the lessee balks or hesitates, the salesman may employ various tactics to overcome his reluctance to sign.<sup>101</sup> Moreover, if the lessee does decide to sign the agreement, the salesman may, at the moment of execution, pencil in a "forgotten" figure which the lessee may dismiss as being an insignificant formality.<sup>102</sup>

Remedial legislation should provide the prospective lessee with an unharassed opportunity to read the agreement and to confer with others who are more knowledgeable than he and less biased than the typical salesman or lessor. Since lessors almost universally insist upon a credit check of the prospective lessee prior to execution of the lease agreement, during this time the lessee should be afforded the opportunity to take a copy of the filled-in agreement home with him. An honest leasing agency has nothing to lose by complying with such a requirement since the consumer, upon a careful reading of the agreement, will discover that what he has been told by the lessor is true. The enactment of a provision similar to that provided in California Civil Code section 1689.5,<sup>103</sup> which regulates home solicitation contracts, allowing the buyer a right to cancel the contract up to three days after signing the agreement, could be of great value in protecting the rights of lessees against unscrupulous lessors and high-pressure salesmen.<sup>104</sup> The period while the lessee's credit is

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100. Author's Survey, *supra* note 88. This survey demonstrated that lessors are reluctant to provide a prospective lessee with a filled-in copy of the lease agreement unless the lessee manifestly intends to lease an automobile at that time.

101. See text accompanying notes 88-95 *supra*.

102. This was the experience of the author in leasing an automobile on April 17, 1970, from Cenval Leasing Co., Oakland, California.

103. CAL. CIV. CODE § 1689.5 (West Supp. 1974).

104. See appended Proposed Legislation § 4 *infra*.



being checked (prior to the time the lessor actually procures the automobile) could be designated as a mandatory "cooling-off period" during which the lessee may scrutinize and thereafter reject or ratify the lease agreement.

### *Capitalized Cost*

In every lease, the lessee is responsible to the lessor for the capitalized cost of the automobile. This cost is akin to the purchase price in an automobile sale transaction.<sup>105</sup> In most lease arrangements, vehicles are purchased from dealers by the lease company at about ten percent above the dealer's invoice price.<sup>106</sup> In the case of most automobiles, the lessor will then mark the price up an additional ten percent or more over the amount he has paid the dealer. The resulting figure constitutes the capitalized cost.<sup>107</sup>

Leasing companies typically represent to the consumer that they can acquire an automobile for his use at a lower price than the price which would be charged if he purchased it.<sup>108</sup> Some lessees have complained that the capitalized cost of the automobile in a lease agreement was actually *greater than* the sale price charged by the dealer.<sup>109</sup> One such case, investigated by the Department of Motor Vehicles (DMV), involved the capitalization of a leased automobile at more than \$500 above the manufacturer's retail list price.<sup>110</sup> The lessee later discovered a bank which would have leased him the same automobile for only \$36 above the "sticker price," to cover handling charges.

The investigator in this case found over-capitalization to be a regular practice in the leasing trade.<sup>111</sup> One reason for the difference in capitalization costs charged between banks and leasing companies is that while the latter are unregulated as to the amount of mark up they may charge, banks under identical lease arrangements are forbidden by law to make a profit on the purchase price of leased automobiles and are closely regulated by federal auditors.<sup>112</sup> Banks obtain their profit from applicable in-

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105. *Automobile Leasing*, *supra* note 4, at 139; DMV REPORT, *supra* note 10, at 5; Warren & Larmore, *supra* note 22, at 806-07.

106. See text accompanying notes 16 and 17 *supra*. See also DMV REPORT, *supra* note 10, at 3.

107. DMV REPORT, *supra* note 10, at 9.

108. *Id.* at 5. Results of the author's survey of seven leasing agencies affirmed this representation. The agencies surveyed are those listed in note 88 *supra*.

109. Interview with Mr. Frank Broadhurst, Director of Division of Compliance of the Department of Motor Vehicles, in Sacramento, California, November, 1972. See also DMV REPORT, *supra* note 10, at 3.

110. DMV REPORT, *supra* note 10, at 3.

111. *Id.* at 9. See also *Automobile Leasing*, *supra* note 4, at 138.

112. DMV REPORT, *supra* note 10, at 5.

terest and finance charges plus a rebate from the manufacturer.<sup>113</sup> This rebate, usually amounting to approximately \$50, is also made available to leasing companies when they lease an American car.<sup>114</sup>

As is readily apparent from the DMV's investigation, one of the major problems confronting the consumer who attempts to negotiate with a leasing company is that he simply does not know the manufacturer's suggested retail selling price. If the consumer is seriously contemplating either renting or leasing a particular automobile he should be furnished with sufficient information for him to make an informed choice with regard to the costs involved and the possible financing alternatives available to him. That is, he should be informed that despite the lessor's representations, the amount for which he will be responsible in a lease transaction may often be greater than the amount necessary to *purchase* the same automobile. If lessors are to be permitted to make the claim that the cost of leasing is less expensive than purchasing, it does not seem unduly burdensome to require the lessor to substantiate such an allegation. To require that the manufacturer's suggested retail price be displayed on the agreement along with the capitalized cost of the automobile for leasing purposes allows the prospective lessee to evaluate more critically the alternatives of purchasing or leasing a particular automobile.<sup>115</sup>

### *The Lease Fee—How Much Is the Lessee Paying?*

In every open end lease agreement there is a charge for the services rendered by the leasing agency.<sup>116</sup> This portion of each monthly lease payment is usually designated as the rental or monthly "lease fee."<sup>117</sup> In some instances, however, the monthly rental fee is not clearly designated.<sup>118</sup> Instead, it may appear as a figure multiplied by the number of months the lease is to con-

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113. *Id.* at 3.

114. *Id.* at 11. See also note 89 *supra*.

115. See appended Proposed Legislation § 4 *infra*. See also § 3 of the Proposed Legislation which would require similar disclosures in automobile lease advertisements.

116. In an effort to discover the component parts of this fee and how it is determined, an inquiry was made of an attorney representing a large metropolitan leasing association. In response to the author's question concerning how this fee is computed he stated that such information was "private." Upon further inquiry he revealed that the fee is for "salesmen's commissions, overhead, and things like that." Interview with A.M. Garfield, attorney for San Francisco Auto Leasing Association, in San Francisco, California, November 21, 1972.

117. See text accompanying notes 17 and 18 *supra*.

118. See, e.g., motor vehicle lease agreement, Redwood Leasing Co., Redwood City, California, on file in the office of the *Santa Clara Lawyer*.

tinue, yielding the "total amount of periodic payments not credited" to the lessee's obligation of recapturing the automobile's depreciation.<sup>119</sup> Although this calculation will satisfy the Moscone Act's disclosure requirements it can hardly be contended that it is a sufficiently meaningful disclosure of the lessor's fee.

Under most lease arrangements, the lessee has no real basis for comparing the fee rates charged by different leasing companies. Traditionally, such a fee has not been considered a finance charge<sup>120</sup> since a finance charge has typically been associated with the sale of an automobile. There is, however, as earlier indicated, a growing view that automobile leasing does, in fact, amount to a sale<sup>121</sup> where deferred payment constitutes an extension of credit subject to the credit disclosure requirements of the federal Truth in Lending Act.<sup>122</sup>

With regard to leasing, it is particularly important that a prospective lessee be able to intelligently evaluate the various lease fees proposed to him, since the amount of such fees will directly affect his ultimate liability. In other words, while it may appear that two leasing companies offering the same automobile for an identical monthly payment are extending the same terms, the extent of liability underlying each offer may be different as a result of variations in the size of the monthly lease fee. If one lessor charges a smaller monthly leasing fee, a greater amount of the payment will be credited each month to the lessee's depreciation reserve fund.<sup>123</sup> On the other hand, a low monthly lease payment may include an exorbitant monthly lease fee, resulting in the contribution of a minimal portion of each monthly lease payment to the lessee's depreciation reserve fund. At the end of the lease, the lessee will be liable for a high termination value which will not be satisfied by the resale proceeds of the automobile.

The prospective lessee should be provided with some objective guidelines which will enable him to informatively select that lease company with the most reasonable rate. Presently, the Moscone Act requires only that a leasing contract disclose the amount representing the aggregate of the lessor's monthly lease fees.<sup>124</sup>

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119. See, e.g., motor vehicle lease agreement, Fazackerly Leasing Co., So. San Francisco, California, on file in the office of the *Santa Clara Lawyer*.

120. 4 CCH CONS. CRED. GUIDE ¶ 30,117 (Federal Reserve Board Letter no. 50, July 28, 1969).

121. BOARD OF GOVERNORS, FED. RESERVE SYSTEM, ANNUAL REPORT TO CONGRESS 1973, CCH CONS. CRED. GUIDE 15 (Jan. 16, 1974); Warren & Larmore, *supra* note 22, at 806.

122. 15 U.S.C. §§ 1601-65 (1970).

123. See text accompanying notes 18-20 *supra*.

124. CAL. CIV. CODE § 2985.8(c) (West Supp. 1974).

There is no requirement that the lessor's fee assessment be set forth either as a monthly amount or as a percentage figure of the capitalized cost. Furthermore, unlike the Rees-Levering Act,<sup>125</sup> there is no limitation on the leasing fee which may be imposed for extending the lessee's obligation for the unpaid balance of the capitalized cost over the duration of the lease term.

Legislation should be enacted which would limit leasing fees to a reasonable rate.<sup>126</sup> Without such legislation, unscrupulous lessors may continue to snare unsophisticated consumers into paying low monthly payments which contain exorbitant lease fees. In addition, legislation similar to that found in the Truth in Lending Act should require the lessor to set forth the monthly lease fee both on the face of the lease agreement and in any leasing advertisements he may cause to be distributed.<sup>127</sup> This fee could be stated as a dollar amount or as a percentage of the capitalized cost of the automobile. Leasing agencies already employ this method in determining the amount of lease charges to be imposed on automobiles of varying values.<sup>128</sup> It does not seem unduly burdensome to require them to disclose this figure to the lessee. The consumer should not be saddled with the onerous burden of computing the various credit or leasing charges exacted by different leasing companies, nor should such a task operate to obscure the comparative advantages or disadvantages between purchasing and leasing agreements.<sup>129</sup>

### *The Break-Even Point—Is There Such a Thing?*

A common representation made by many leasing agencies is that there exists a "break-even point" in the lease period.<sup>130</sup>

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125. *Id.* § 2982(c).

126. *See* appended Proposed Legislation § 10 *infra*.

127. *Id.* §§ 3, 4.

128. The last available source of information disclosing the amount of such charges was provided in 1969. A Department of Motor Vehicles interview with a lease company official revealed that the average monthly service charge prevailing within the industry was then ranging from between 0.55% and 0.7% of the original capitalized cost plus about sixty cents per month. DMV REPORT, *supra* note 10, at 10. However, a 1972 interview with the lease manager of Personal Automobile Leasing, San Jose, California, revealed that some lessors compute their fee on a much higher percentage than the aforementioned figures.

129. The Board of Governors of the Federal Reserve System has recognized this need and has recommended to Congress that a leasing program be implemented so that the consumer may intelligently "shop" the expanding leasing market. *See* BOARD OF GOVERNORS, FED. RESERVE SYSTEM, ANNUAL REPORT TO CONGRESS 1973, CCH CONS. CRED. GUIDE 16 (Jan. 16, 1974).

130. *See, e.g.,* Southwest Leasing Corporation promotional brochure, San Jose, California, on file in the office of the *Santa Clara Lawyer*, which contains the following statement:

*After the halfway point in your lease, we start looking for the optimum moment to dispose of your car. When we see a strong market, we can,*

This term, as used in open end leasing, means that after a certain number of months into the lease the lessee may return the automobile to the lessor or resell it himself, if this is allowed by the terms of the lease, without incurring any further liability. Supposedly, the amount in the depreciation reserve fund when coupled with the proceeds realized from the resale of the automobile will equal or exceed the pay-off amount still due on the lease.

One local dealer labeled this practice a "fraud," stating that a break-even point simply does not exist, and that it is used merely to avoid making the lessee feel that he is "locked" into the lease for the full lease period.<sup>131</sup> As discussed earlier, the amount of each rental payment that is applied to the depreciation reserve fund is constant throughout the term of the lease.<sup>132</sup> However, by comparison, an automobile does not depreciate at a constant rate. While its value declines greatly in the early months, the rate of depreciation tends to level off beyond the initial period of use.<sup>133</sup> Thus, the amount accumulating in the depreciation reserve fund is significantly less than the actual depreciation during the early months and greater than the actual depreciation in the later months of the lease term.

If the termination value of the automobile has been accurately estimated, the lease-end balance of the lessee's depreciation reserve fund will equal the actual depreciation of the automobile during the duration of the lease period. Under this condition, the lessee is assured that he will not suffer any lease-end deficiency if he keeps the automobile for the agreed length of the lease term since the remainder of his obligation will equal the proceeds realized from the resale of the automobile. Therefore, the assertion that the amount owing on a lease can balance the amount credited to the lessee *prior* to the termination of the original lease period is patently erroneous. On the other hand, if there does exist such a break-even point and a guarantee to that effect is made, the lessor cannot complain against legislation requiring him to warrant such a representation in the lease agreement.<sup>134</sup>

### *Deficiency Payments—Who Pays for the Mistakes?*

Lease companies, in their efforts to attract consumer patronage, place singular emphasis on the low monthly amount re-

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if you so desire, rotate you to a new car and *dispose of your old car without penalties* (emphasis added).

131. Interview with lease manager of Personal Auto Leasing, in San Jose, California, October, 1972.

132. See text accompanying notes 17 and 18 *supra*.

133. *Automobile Leasing*, *supra* note 4, at 145.

134. See appended Proposed Legislation § 4 *infra*.

quired as a condition to acquiring the use of a new automobile. No mention is made of the termination value of the automobile or its significance in determining whether an additional "balloon payment" will be due at the end of the lease term. Even if a particular consumer is familiar with the importance of an accurately estimated termination value, the lessor's claim touting his purported ability to depreciate realistically the lease-end value of the automobile may often quell consumer concern. Thus, a prospective lessee may often be led to believe that his only real lease obligation is the payment of the stipulated monthly lease payments.

In open end lease agreements the amount of the monthly lease payment is extremely flexible. Hypothetically, an automobile could be leased for one dollar per month, but the minimal size of such a payment would preclude the lessor from recapturing the automobile's depreciation during the lease term.<sup>135</sup> As a result, the "projected termination value" of the automobile will be substantially greater than the proceeds realized from its resale at the end of the lease period. The difference between these figures would be assessed as a deficiency against the lessee. Such a deficiency arises because the proceeds from the resale when coupled with the amount accumulated in the depreciation reserve fund cannot equal the capitalized cost of the automobile.<sup>136</sup>

It is clear that in order to avoid a lease-end deficiency the termination value must be accurately estimated. If the estimated lease-end value is high then the amount contributed to the depreciation reserve fund will be low. Thus, if that evaluation proves to be in excess of the actual resale price received at the end of the lease, the reserve fund will not cover the depreciation suffered by the automobile involved. The lessee will then be held liable for the resulting deficiency.

The method by which lease companies project the termination value of a leased vehicle consists of assigning to the automobile the present Kelley Blue Book value of an identical model equal in age to that which the lease vehicle will be at the end of the lease term.<sup>137</sup> For example, assuming the lease term is three years, in projecting the termination value of a 1974 Chevrolet Impala the lessor will look to the present value of a 1971 Chevrolet Impala which is similar to the vehicle sought to be leased. A problem arises when automobiles of a relatively new vintage, such

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135. DMV REPORT, *supra* note 10, at 9.

136. The lessee is ultimately liable for the capitalized cost of the automobile. See notes 15-17 and 105-07 and accompanying text *supra*.

137. DMV REPORT, *supra* note 10, at 6. Interview with lease manager, Varner-Ward Leasing Co., in San Jose, California, November, 1972.

as a 1974 Mazda, are valued. In such cases the lessor will look to the present value of several 1971 automobiles similar to the one being leased.

Despite lessors' representations to the effect that they have a "secret analysis"<sup>138</sup> to accurately estimate termination values, or are able to select "high-resale, low maintenance"<sup>139</sup> automobiles, it is clear that their methods of forecasting the termination value of a lease automobile are not infallible. The reliability of forecasting future values based on past depreciation trends of one make of car is highly speculative.<sup>140</sup>

Reputable leasing firms require that the lessee's monthly contribution to the depreciation reserve fund be slightly higher than is necessary to depreciate the automobile to its lease-end whole-sale value. This practice, in effect, provides the lessee with a cushion against any possible lease-end deficiency, since the actual termination value of the automobile is frequently lower at the end of the lease period than the fair market value projected at the time of the lease's execution. However, because of the highly flexible and negotiable nature of open end lease payments, some lessors are able to attract business by advertising and negotiating unrealistically low monthly payments, the monthly reserve portion of which cannot possibly recapture the automobile's depreciation over the stipulated lease term.

Although leasing companies commonly represent themselves as being "experts" in the automobile industry, it is the lessee who ultimately becomes the guarantor of the accuracy of such a representation.<sup>141</sup> From the standpoint of the lessee, it is immaterial

138. See, e.g., advertisement of Oxford Leasing Co., San Jose, California in yellow pages of Pacific Telephone Directory, 1973.

139. See, e.g., Southwest Leasing Corp., San Jose, California, promotional brochure on file in the office of the *Santa Clara Lawyer*.

140. The speculative nature of this forecasting is demonstrated by the deficiencies which are now being assessed against lessees of large "luxury" automobiles as a result of the unexpected decrease in the demand for these automobiles caused by the recent energy crisis. Telephone interview with Mr. Frank Broadhurst, Director of Division of Compliance of the Department of Motor Vehicles, December 18, 1973. Interview with Mr. Rand Miller, Leasing Representative, First National Bank Leasing Center, in San Jose, California, March 18, 1974.

141. This claim of expertise becomes more doubtful when lessors attempt to project the fair market value of an automobile five years from the date of the lease's execution. The growing practice of leasing used automobiles further increases the likelihood of an inaccurate estimate of the termination value of a lease automobile.

At Douglas Leasing, San Jose, California, the following estimate of the termination value of a leased automobile was made: A 1973 Firebird, capitalized at \$4500, was offered at a monthly lease rate of \$86.42 on a 36 month open end lease. The monthly contribution to the depreciation reserve fund was \$56.22 and the termination value was set at \$2477.

Capitalized Cost	\$4500.00
Deprec. Res. Fund	— 2023.92 (36 months × \$56.22)
Termination Value	\$2476.08

whether the lessor's incorrect estimate of the termination value was the result of a mistake or of an intentional miscalculation, since he will be liable for the deficiency in either case.

The automobile lessee's lease-end liability stands in juxtaposition to the limited obligations involved in the leasing of other types of property. In the case of chattels other than automobiles it is typically the lessor, and not the lessee, who assumes any increase or decrease in the leased property's value.<sup>142</sup> Given the fact that a lessee of most chattels is not entitled to any unforeseen appreciation in value of the lease property over the duration of the lease term, logically neither should he be forced to bear the risk of the leased property's depreciation. In the rental or leasing of most chattels, it is usually implicit that the lessor will recapture his investment in the lease property plus a reasonable rate of return solely from the periodic payments made by the lessee.

Legislation should be enacted to protect the consumer from having to pay "built in" lease-end deficiencies. Since lessors represent themselves as experts in the automobile industry and, compared with lessees, are in a better position to evaluate future market trends, the primary burden should rest with them to make reasonably accurate estimates of an automobile's lease-end resale value. By imposing a ceiling on the amount which the lessor could recover from the lessee at the end of the lease term, the lessor would be forced to estimate more accurately the termination value of the automobile. However, the legislature must make

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When questioned about the accuracy of the termination value, the salesman indicated that it was actually the projected *wholesale* value of the automobile and that, in all probability, the automobile could be sold for as much as \$300 above this figure at the end of the lease term. The accuracy of this estimate seems questionable in light of the fact that the *retail* asking price of a similarly equipped 1970 Firebird was, at that time, approximately \$2400. In truth, the lessee under this lease would be liable for the projected *retail value* of the automobile at the end of the lease term. However, once the lessee returns the car to the lessor, lessors and dealers commonly dispose of the automobile in a *wholesale* market. See generally Shuchman, *Profit on Default: An Archival Study of Automobile Repossession and Resale*, 22 STAN. L. REV. 20 (1969); Note, *California's Automobile Deficiency Judgment Problem*, 4 U.C.D. L. REV. 91 (1971). As a result, the projected termination value (\$2477) would be, in all likelihood, greater than the proceeds which would be realized from a lease-end wholesale disposal of the automobile.

142. This assumption of the risk in the lease property's value is minimized by what some lessors designate as a "full payout" lease. In this type of lease the lessor recaptures his total investment plus a reasonable rate of return from the lessee's lease payments. However, in order to avoid any question that the lease is, in fact, a sale, the lessee will typically be required to pay an additional amount at the termination of the lease if he desires to purchase the leased property. Telephone interview with Mr. John Moskol, First National Bank Leasing Center, April 4, 1974. See also Comment, *Selected Problems In California Chattel Leasing*, 13 U.C.L.A. L. REV. 125, 128 (1965).



a policy decision concerning the amount the lessor should be permitted to recover at the end of the lease term. To prevent lessor abuse of consumers, the legislature may choose to hold the lessor strictly liable and deny any lease-end recovery since it is the lessor who is the expert and better able to insure against any unforeseen losses.<sup>143</sup> Alternatively, it may choose to allow the lessor some margin of error in making his estimates due to market fluctuations not reasonably foreseeable at the inception of the lease agreement.<sup>144</sup>

If a limitation were imposed upon the amount lessors could recover at the end of the lease term, exception would have to be provided for those lessees who nevertheless wish to make monthly payments lower than are necessary to recapture the automobile's depreciation over the lease term.<sup>145</sup> Such a reduction in the monthly payments will result in a substantial lease-end payment. In effect, the lessee, by opting for a larger lease-end payment, will be waiving the lease-end liability limitation and therefore consenting to an inflated termination value. In such a case, a reasonably accurate estimate of the probable lease-end deficiency together with a notice in ten-point bold type explaining the significance of this figure should be designated clearly in the lease agreement.<sup>146</sup> Furthermore, the signature of the lessee should appear immediately after the waiver provision. This signature would be in addition to the lessee's subscription normally found beneath the main provisions of the lease contract and would serve to apprise the lessee of the significance of his waiver.<sup>147</sup>

### *Security Deposits*

In some cases a lessor will insist that the lessee pay a security deposit to cover any deficiency which may arise at the termination of the lease period. This charge, when properly used, partially protects both the lessor's investment in the leased automobile and diminishes his reliance on the integrity of the lessee. Use of the security deposit has been abused in the leasing of both real and personal property including automobile leasing. Security de-

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143. See note 97 *supra*.

144. See, e.g., UNIFORM CONSUMER CREDIT CODE § 2.406 (Revised Final Draft, 1969), which would restrict the lease-end liability of a lessee to an amount no greater than the sum of two monthly payments. See also appended Proposed Legislation § 8 *infra*.

145. See appended Proposed Legislation § 4 *infra*.

146. *Id.*

147. Unfortunately, the existence of a statutory provision providing for a waiver of any lease-end limitation on lessee liability may be exploited by unscrupulous lessors, especially in the case of unsophisticated lessees who are likely to be easily convinced by such lessors' explanations that the waiver is a mere legal formality which will not increase a lessee's obligations.

posits function as a "cushion" for the lessor who offers unrealistically low monthly lease payments which will not adequately cover the lease automobile's depreciation over the lease term. One lessor stated that he seldom returns a security because "there's always something that is wrong" with the leased automobile when it is returned to him.<sup>148</sup>

The lessee's obligation to reimburse the lessor for the amount the resale proceeds fall short of the projected termination value virtually guarantees the lessor recovery of his investment in the automobile. Therefore, extracting a pre-termination security deposit, usually clothed in the guise of the last monthly payment, is unnecessary and probably unconscionable.

Some leases further require the lessee to pay a one-time, non-refundable lessor's fee.<sup>149</sup> Other than enhancing the lessor's profit margin, it is difficult to imagine what purpose this "lessor's fee" serves, especially when one considers that the lessor, in all likelihood, has assigned a capitalized cost to the lease automobile above the amount he has paid for it and, in addition, will receive a monthly lease fee throughout the duration of the stipulated lease term.

#### *The Manner of Resale: Is It Commercially Reasonable?*

A lessee is generally required to return the leased automobile to the lessor either when the lease term expires or at any time prior thereto when the lessee decides to terminate his lease obligation. The lessor will then resell the leased vehicle and apply the proceeds realized to the amount contributed to the depreciation reserve fund. If the sum of these funds is less than the capitalized cost, the lessee is obligated under the contract to reimburse the lessor immediately for the deficiency.

In reselling the leased vehicle, the lessor will normally solicit bids. Frequently, the lessee is also given the right to seek bids on the vehicle. Some agreements, but not all, provide that the lessor must notify the lessee of the bids received and obtain the latter's authorization to sell the leased vehicle to the highest bidder.<sup>150</sup> If the lessee fails to object within a specified period, the lessor may sell the automobile for the highest price offered him. It is not uncommon for the bids to be unusually low since normally the lessor will only solicit wholesale bids from automobile dealers.<sup>151</sup>

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148. Interview with lease manager of Personal Auto Leasing, in San Jose, California, October, 1972.

149. See motor vehicle lease agreement, Fazackerly Leasing Co., So. San Francisco, California, on file in the office of the *Santa Clara Lawyer*.

150. *Id.*

151. *Id.* See also note 141 *supra*.

A problem arises when the highest bid is for an amount less than the projected termination value. Many lessees, unaware of the scope of their lease-end liability, will naturally fail to appreciate the implications of a low resale bid.<sup>152</sup> Furthermore, even if a lessee is aware of the importance of obtaining a high resale bid,<sup>153</sup> he is usually in no position to seek higher bids himself. Normally, he will not even have the automobile in his possession. In these circumstances, the lessee almost inevitably finds himself forced to accept the bid procured by the lessor, which results in a liability chargeable to the lessee.

When the automobile is sold by the lessor, the proceeds are often subject to a deduction by the lessor for the "costs" incurred by him in connection with the sale of the automobile.<sup>154</sup> The proceeds may be reduced further by a "sales fee" deduction usually computed as a percentage amount either of the proceeds realized or of the original capitalized cost of the vehicle.<sup>155</sup> It is difficult to understand the justification for either of these fees since by the payment of the lease fee and other ancillary charges the lessee has presumably compensated the lessor for his services,<sup>156</sup> including his services expended in reselling the automobile.

The Moscone Act, in contrast to the Rees-Levering Act, makes no provision for the procedure by which the returned lease vehicle must be resold. The only statutory regulation potentially applicable to this situation is California Commercial Code section 9504, which sets forth the procedure a secured party must follow when repossessing an automobile from a defaulting purchaser or lessee.<sup>157</sup> In disposing of the property, the secured party must carry

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152. See text accompanying notes 15-20, 73-75, 136-140 *supra*.

153. *Id.*

154. See motor vehicle lease agreement, Frazackerly Leasing Co., So. San Francisco, California, on file in the office of the *Santa Clara Lawyer*.

155. *Id.* The deduction in this particular lease is equal to 2% of the sale proceeds. Under the Cenval Lease Co. agreement (see notes 14-15 *supra*), a similar fee is imposed when the lessee prematurely terminates the agreement.

156. See text accompanying notes 15-18 and 116-129 *supra*.

157. CAL. COMM. CODE § 9504 (West 1964). The application of this section to automobile leasing is premised upon California Commercial Code section 9102, which sets forth the policy and scope of the statutory division governing secured transactions. The pertinent provisions of that section read:

This division applies so far as concerns any personal property and fixtures within the jurisdiction of this State (a) to any transaction (regardless of its form) which is intended to create a security interest in personal property including goods, documents, instruments, general intangibles, chattel paper, accounts or contract rights. . . . This division applies to security interests created by contract including pledge, assignment, chattel mortgage, chattel trust . . . other lien or title retention contract and lease or consignment intended as security (emphasis added).

The lessor's retention of title in the leased automobile in order to secure payment of the capitalized cost would seem to fall within the broad language of this section. This notion is further reinforced by the growing view that leasing is, in

out his activities in a "commercially reasonable manner" lest he be liable for any loss caused by unreasonable commercial conduct.<sup>158</sup> This standard is satisfied "[i]f the secured party either sells the collateral in the usual manner in any recognized market . . . or if he sells at the price current in such market at the time of his sale . . . ."<sup>159</sup> However, this section, when applied to the resale of automobiles, loses much of its effectiveness since the secured party's "recognized market" typically consists of other automobile dealers who generally pay far below what would usually be considered a fair and reasonable price.<sup>160</sup>

Remedial legislation is needed to define the meaning of disposing of the leased automobile at the end of the lease term in a "commercially reasonable manner." At the minimum, such conduct should be defined as that which is sufficient to cause the automobile to realize upon resale proceeds equal to, or greater than, the prevailing wholesale price within the industry at the end of the lease term.<sup>161</sup> Further, absent a waiver by the lessee, the lessor should be required at the inception of the lease term to estimate a realistic projected wholesale value at the end of that term.<sup>162</sup> Under these proposals, lease-end deficiencies will be minimized since the lessor will be required to project the actual end-of-term wholesale value of the automobile at the time of exe-

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effect, a secured sale of the leased automobile since the lessee, as the purchaser, must reimburse the vendor for the agreed value of the vehicle and assume the risk of depreciation. See also *Thomas v. Wright*, 21 Cal. App. 3d 921, 98 Cal. Rptr. 874 (1971); BOARD OF GOVERNORS, FED. RESERVE SYSTEM, ANNUAL REPORT TO CONGRESS 1973, CCH CONS. CRED. GUIDE 15 (Jan. 16, 1974); Warren & Larmore, *supra* note 22. For a discussion of Article Nine's (U.C.C.) applicability to leases and the distinction drawn between "real leases" and contracts intended for security, see Headrick, *The New Article Nine of the Uniform Commercial Code: An Introduction and Critique*, 34 MONT. L. REV. 28, 30 (1973); Leary, *Leasing and Other Techniques of Financing Equipment Under the U.C.C.*, 42 TEMP. L.Q. 217 (1969); Comment, *Selected Problems in California Chattel Leasing: Equipment Leasing Under the U.C.C.*, 13 U.C.L.A. L. REV. 125 (1965).

158. CAL. COMM. CODE § 9507 (West 1964). See also *California Auto. Corp. v. C. W. Jones*, 415 F.2d 554 (6th Cir. 1969); *Elster's Sales v. El Bodrero Hotel, Inc.*, 250 Cal. App. 2d 258, 58 Cal. Rptr. 429 (1967).

159. CAL. COMM. CODE § 9507(2) (West 1964) states in part:

The fact that a better price could have been obtained by a sale at a different time or in a different method from that selected by the secured party is not of itself sufficient to establish that the sale was not made in a commercially reasonable manner. If the secured party either sells the collateral in the usual manner in any recognized market therefor or if he sells at the price current in such market at the time of the sale or if he has otherwise sold in conformity with reasonable commercial practices among dealers in the type of property sold he has sold in a commercially reasonable manner.

160. See note 142 *supra*.

161. See appended Proposed Legislation § 9 *infra*.

162. *Id.* § 7.

cution and to procure that amount upon the resale of the automobile at the lease's termination.

Due to unforeseen market fluctuations, the projected wholesale value will not always equal the actual lease-end wholesale value. In such instances, if the lessor can show through Kelley Blue Book valuation that his original estimate of the lease-end wholesale value was established in good-faith and that he, in fact, realized the going wholesale value of the automobile at the end of the lease term, he should be allowed some lease-end recovery since the deficiency is attributable to factors beyond his control.<sup>163</sup> However, such recovery should be limited to a specific amount since, as an expert, he is better able to predict and insure against losses caused by market fluctuations than is the lessee.<sup>164</sup>

### *Inflated Reconditioning Costs*

Closely related to the manner in which the lessor conducts the resale of the leased automobile is the method the lessor follows in determining the cost of reconditioning the automobile for resale. Although the lease term may extend over a period of five years, the lessee is usually obliged to return the leased automobile in the *same* condition as when received, less "reasonable" wear and tear. Upon the vehicle's return, the lessor will in all likelihood dispose of the automobile through a wholesale market.<sup>165</sup>

Often when the lessee returns the lease vehicle he will be assessed various repair charges by the lessor for restoring the automobile to the "same" condition it was in when originally leased.<sup>166</sup> Since the need for these repairs is usually determined after the lessee has returned the automobile to the lessor, the amount of such charges is within the discretion of the lessor. Often a lessor appraises as damages that which is merely the result of reasonable wear and tear, thereby providing himself an additional source of income. Because the lessee is no longer in possession of the automobile, he is unable to verify the accuracy of such "damage" assessments. Furthermore, it is highly unlikely that the amount invested in repairing the automobile will be reflected in the amount realized upon its subsequent wholesale disposal.

Unless the damage is so extreme as to render the automobile unmarketable, the practice of restoring the vehicle to the "same"

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163. *Id.* § 8.

164. *Id.*

165. See note 141 *supra*.

166. Interview with lease manager of Personal Auto Leasing, in San Jose, California, October, 1972.

condition it was in when received is of questionable validity, since the extent of any unreasonable damage will be clearly reflected in the wholesale proceeds the automobile will realize upon its resale. In any event, the lessor is assured compensation for this loss since the lessee is still bound by the terms of the lease contract to compensate the lessor for the difference between the amount realized upon resale and that amount still owing on the contract. The motivation for such repair is thus suspect. Under appropriate legislation the lessor could be forced to allow the market to determine the extent of such lessee misuse, leaving him with his contractual right to recover the remainder of the capitalized cost.<sup>167</sup> However, if such reconditioning costs are to be allowed, in no event should the lessor be permitted to assess costs greater than the difference between the lease-end wholesale value of the lease automobile and the market value of a damaged automobile of the same make as the automobile subject to the terms of the particular lease agreement.<sup>169</sup>

#### CONCLUSION

The growth of automobile leasing for personal use in the last decade has been phenomenal and such growth promises to continue at an even more rapid rate. This popularity is primarily attributable to the low capital expenditure required as a condition to the acquisition of a new automobile. Despite this attractive characteristic, there are many attendant obligations of which the typical consumer is unaware. As a result unscrupulous lessors are able to capitalize upon consume naïveté.

Recognizing this lack of sophistication on the part of consumers, the California legislature in 1969 enacted legislation commonly referred to as the Moscone Act, which was designed to inform the consumer of his potential obligations under a motor vehicle lease agreement. This legislation, however, is far less comprehensive than its counterpart, the Rees-Levering Act, which regulates the purchase of an automobile pursuant to a conditional sale contract. Many abuses common to both the leasing and purchasing of automobiles continue to exist only in leasing arrangements. Furthermore, due to consumer unfamiliarity with the mechanics of the lease transaction, there are additional problems unique to automobile leasing which continue to exist despite the presence of the Moscone Act. Some of these include misleading advertisements and representations by lessors, exorbitant leasing fees, "built-in" lease-end deficiency payments and inflated lease-end reconditioning costs.

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167. See appended Proposed Legislation § 9 *infra*.

Enactment of remedial legislation similar to that which is appended to this comment would alleviate many of the problems discussed herein. Such legislation balances present inequities without unduly hampering commercially ethical activity. Without such legislation, consumers will continue to bargain from their present position which, in the final analysis, is really not a bargaining position at all.

*Bruce Allen Bottini*

## APPENDIX

### PROPOSED LEGISLATION REGULATING THE LEASING OF MOTOR VEHICLES

#### § 1 Definitions

As used in this Act, unless the context otherwise requires:

- (a) "Motor vehicle" means any vehicle required to be registered under the Vehicle Code which is leased primarily for personal or family purposes.
- (b) "Leasing contract" or "lease" means any contract for the bailment or leasing of a motor vehicle for a term of four or more months under which it is agreed that the lessee will bear the risk of the motor vehicle's depreciation.
- (c) "Lessor" shall include any firm, agency, partnership, corporation or person who engages in the leasing of motor vehicles for a term of four or more months.
- (d) "Lessee" includes any person other than a lessor who enters into a leasing contract.
- (e) "Value" or "capitalized cost" shall mean the total value assigned at the time of execution of a lease agreement to the motor vehicle to be leased and for which the lessee will be liable. If the proceeds from the lease-end resale of the motor vehicle together with the lease-end balance in the monthly reserve are less than the capitalized cost or value of the motor vehicle, the amount of the deficiency will be immediately assessed against the lessee.
- (f) "Monthly reserve" is that portion of the lessee's monthly payment which, when accumulated over the term of the lease, will be credited to the lessee's depreciation account.
- (g) "Monthly lease fee" is that portion of each monthly lease payment not credited to the lessee which represents the lessor's fee charged to the lessee for allowing the use of the motor vehicle and the extension of repayment of the motor vehicle's capitalized cost over the duration of the lease term.
- (h) "Termination value" or "depreciated value" is the projected lease-end value of the motor vehicle determined by the lessor at the time of the lease's inception. Such value shall be the projected wholesale value of the motor vehicle at the end of the stipulated lease term unless the lease contract contains an express agreement to the contrary.
- (i) "Costs of reconditioning" shall consist of those costs reasonably necessary to restore a motor vehicle, damaged by the lessee's unreasonable misuse, to a condition that enables the motor vehicle to be resold at the end of the lease term.
- (j) "Break-even point" is that point in time in an open-end lease



when the lessee may return the motor vehicle to the lessor, prior to the originally agreed upon expiration date of the lease term, without incurring any liability or deficiency.

(k) "Advertisement" means any commercial message in any newspaper, magazine, leaflet, flyer, or catalog, on radio, television, or public address system, in direct mail literature or other printed material, or any interior or exterior sign or display, in any window display, in any point-of-transaction literature or price tag which is delivered or made available to a lessee or prospective lessee in any manner whatsoever.

(l) "License" shall be that permit, issued by the Department of Motor Vehicles, which permits a lessor to engage in the leasing of motor vehicles within this State.

### § 2 Lessors Subject to Department of Motor Vehicle Regulation

Any firm, agency, partnership, corporation, or person who engages in the leasing of motor vehicles shall register with the Department of Motor Vehicles. The Department shall have the power to issue a license authorizing such a party to engage in the business of motor vehicle leasing. The Department shall have the power to refuse to issue, revoke, or suspend such a license for the violation of either the provisions of this chapter or the applicable provisions of the Vehicle Code (CAL. VEH. CODE §§ 11700-900).

### § 3 Required Disclosures in the Advertising of Motor Vehicle Leasing

Any advertisement of a motor vehicle lease setting forth a schedule of monthly payments shall be clearly designated a lease and shall also include the value of the automobile, the manufacturer's suggested selling price, the length of the lease term, the termination value, the monthly reserve and the monthly lease fee, the latter of which is to be set forth both as a dollar amount and as an annual percentage amount of the capitalized cost.

Any violation of this section shall give rise to a cause(s) of action under sections 17500 of the Business and Professions Code and 3369 of the Civil Code which may be instituted by the Attorney General, district attorney, or any private party acting in the public interest.

### § 4 Contracts for Lease or Bailment: Form and Content

Every leasing contract for the lease of a motor vehicle shall be in writing and printed in eight-point type and shall contain in a single document all of the agreements of the lessor and lessee with respect to the rights and obligations of each party. The lessee shall be informed by the lessor in said document of the former's right to a filled-in copy of the leasing contract prior to the execution of the agreement. If the lessee waives this option, the lessor may obtain the signature of the lessee provided that such contract contains no blank spaces to be filled in after the contract has been so signed and executed. The contract shall be signed by the lessor or his authorized representative, and an exact copy thereof shall be furnished the lessee by the lessor.

The lessee shall have the right to cancel a leasing contract until midnight of the third calendar day (excluding Sunday and holidays) after the day on which he receives a signed copy of the leasing contract. Notice of cancellation must be given by the lessee in writing but need not take a particular form, and however expressed, is effective if it indicates the intention of the lessee not to be bound by the leasing contract. If the lessee does not notify the lessor by delivery of the notice in person or by mail postmarked within the prescribed period of his desire to exercise such an option to cancel, he will be bound by the terms of the leasing contract and the lessor may proceed to carry out his obligations under the agreement. No motor vehicle shall be delivered until the lessor delivers to the lessee a fully executed copy of the leasing contract and the three day period for cancellation has elapsed without notice of an election to cancel by the lessee.

Every leasing contract shall contain the following separate items although not necessarily in the sequence or order set forth below:

- (a) The date the leasing contract is executed.
- (b) The value or capitalized cost of the motor vehicle.
- (c) The manufacturer's suggested retail selling price.
- (d) The total amount and the monthly amount to be credited to the lessee in computing his lease-end obligation for the termination value. The amount to be credited will be the result of multiplying the monthly reserve by the number of months the lease is to continue.
- (e) The amount, if any, included for insurance if such insurance is provided by the lessor, and the coverage of such insurance with the cost for each form of coverage stated separately.
- (f) The break-even point in the lease term if the lessor represents that such a point exists.
- (g) Any security deposit to be paid by the lessee and a clear explanation of its purpose.
- (h) The termination value, which shall equal the projected wholesale value of the motor vehicle, absent an express agreement to the contrary. This value shall equal the difference between the total amount which will be credited to the lessee at the end of the lease period and the present value or capitalized cost of the motor vehicle.
- (i) A notice in at least ten-point type reading as follows: "NOTICE TO THE LESSEE: (1) DO NOT SIGN THIS AGREEMENT BEFORE YOU READ IT OR IF IT CONTAINS ANY BLANK SPACES. (2) YOU ARE ENTITLED TO A COMPLETELY FILLED-IN COPY OF THIS AGREEMENT AND HAVE THREE DAYS (EXCLUDING SUNDAYS AND HOLIDAYS) FROM THE DATE OF RECEIPT OF A SIGNED COPY OF THIS DOCUMENT TO BE RELEASED FROM THE OBLIGATIONS OF THIS LEASING CONTRACT PROVIDED THAT WITHIN THAT THREE DAY PERIOD YOU NOTIFY THE LESSOR IN WRITING, DELIVERED IN PERSON OR BY MAIL AND POSTMARKED NOT LATER THAN MIDNIGHT OF THE THIRD DAY, OF YOUR DE-

CISION NOT TO BE BOUND BY THIS AGREEMENT. (3) IF YOU DEFAULT IN THE PERFORMANCE OF YOUR OBLIGATIONS UNDER THIS LEASE THE VEHICLE MAY BE REPOSSESSED AND YOU MAY BE SUBJECT TO SUIT AND LIABILITY FOR THE UNPAID INDEBTEDNESS STILL OWING ON THE CONTRACT. (4) BEYOND THE MONTHLY LEASE PAYMENTS YOU MAY BE LIABLE FOR A FINAL PAYMENT EQUAL TO THE AMOUNT, IF ANY, BY WHICH THE PROJECTED RESALE VALUE USED IN THIS LEASE EXCEEDS THE PROCEEDS ACTUALLY REALIZED FROM THE SALE OF THE VEHICLE YOU HAVE LEASED."

(j) The amount of the lessor's monthly lease fee expressed as both a monthly dollar amount and as a percentage of the capitalized cost of the motor vehicle.

(k) If the lessee consents to be liable for a projected value of the motor vehicle which is greater than the motor vehicle's projected wholesale value, a notice additional to that required by subdivision (i) of this section, in at least ten-point type at the end of the lease, setting forth both the termination value as defined in Section 1, subdivision (h), the projected wholesale value, and the difference between these amounts. Such notice shall be followed by the lessee's signature. The signature shall be in addition to any other subscription normally required to execute a lease agreement under this Act. The notice shall read: "I AM FULLY AWARE THAT THE REDUCTION IN THE AMOUNT OF MY MONTHLY LEASE PAYMENTS IS DUE TO THE FACT THAT I HAVE CONSENTED TO BEING LIABLE AT THE END OF THE LEASE PERIOD FOR A PAYMENT EQUAL TO THE DIFFERENCE BETWEEN THE AGREED UPON LEASE-END RESALE VALUE OF THE MOTOR VEHICLE SET FORTH IN THIS AGREEMENT (set forth value here) AND THE PROJECTED WHOLESALE VALUE (set forth projected wholesale value here). NOTWITHSTANDING ANY AGREEMENT TO THE CONTRARY, I REALIZE THAT, ABSENT UNREASONABLE DAMAGE CAUSED BY MY MISUSE, THE LESSOR, IN ALL LIKELIHOOD, WILL RECEIVE THE WHOLESALE VALUE OF THE MOTOR VEHICLE WHEN HE RESELLS THE MOTOR VEHICLE AT THE END OF THE LEASE. I AM FULLY AWARE THAT THIS ADDITIONAL LEASE-END PAYMENT FOR WHICH I WILL BE LIABLE AFTER THE LESSOR HAS RESOLD THE MOTOR VEHICLE MAY BE AS GREAT AS (set forth difference between projected wholesale value and agreed upon projected value here).

(Signature of Lessee)

#### § 5 Violation of Contract—Unenforceability

If the lessor, except as the result of an accidental or bona fide error of computation, violates any provision of Section 4, the leasing contract shall not be enforceable, except by a bona fide purchaser,

assignee or pledgee for value or until after the violation is corrected as provided in Section 6; and, if the violation is not corrected, the lessee may recover from the lessor double the total amount paid by the lessee to the lessor or to his assignee or pledgee, pursuant to the terms of the contract. This section shall not be construed to allow enforcement of a leasing contract violating Section 4 of this Act by an assignee who regularly engages in the practice of purchasing leasing contract rights.

#### § 6 Correction of Violation—Time Allotted

Any failure to comply with section 4 may be corrected by the lessor or holder of the leasing contract, except that a willful violation may not be corrected unless it is a violation appearing on the face of the contract and is corrected within thirty days after the execution of the contract or within twenty days after its sale, assignment or pledge, whichever is later, provided that the twenty-day period shall commence with the initial sale, assignment or pledge of the contract, and provided that any other violation appearing on the face of the contract may be corrected only within such time period. A correction which will increase the amount of the contract balance or the amount of any monthly lease payment as such amounts appear on the leasing contract shall not be effective unless the lessee concurs in writing to the correction. If the lessee is notified in writing by the lessor of such a failure to comply with any provision of this chapter, the correction shall be made within ten days after such notice. Where any provision of a leasing contract fails to comply with Section 4, the correction shall be made by mail or delivery of a corrected copy of the contract to the lessee. Any amount improperly collected by the lessor or holder of the leasing contract from the lessee shall be credited against the indebtedness evidenced by the contract or returned to the lessee. A violation corrected as provided in this section shall not be the basis of any recovery by the lessee or affect the enforceability of the contract by the holder unless it is determined that such a violation may have materially misled the lessee as to the true extent of his obligations. Notwithstanding any corrected violations, if the lessee can prove that the uncorrected copy of the lease agreement materially misrepresented the true extent of his obligations, the lessee shall have the right to cancel the leasing contract until midnight of the third calendar day (excluding Sundays and holidays) after the day on which the lessee receives a corrected copy of the leasing contract.

#### § 7 Depreciated Value—Presumption

The depreciated or termination value of the motor vehicle shall be equal to, and not greater than, the projected wholesale value of the motor vehicle at the end of the lease period, provided that the lessee may consent to liability at the end of the lease term for an amount greater than the projected wholesale value only in the manner prescribed in Section 4, Subdivision (k) of this Act.

### § 8 Limitation on Lessee's Lease-End Deficiency Liability

The amount the lessor may recover from the lessee beyond the stipulated number of monthly lease payments shall be limited as follows: in the event that the proceeds realized from the lease-end resale of the lease vehicle are less than the projected value, the extent of the lessee's lease-end liability shall be no greater than the sum of two monthly lease payments. This section shall not apply to a lessee who has consented to the liability permitted under Section 4, Subdivision (k), of this Act or in the event that unreasonable damage has been caused by the lessee's misuse, which substantially reduces the amount realized from the resale of the motor vehicle at the termination of the lease term. This section shall not apply to a lessee who returns a motor vehicle to the lessor prior to the stipulated termination date of the lease term. In such case, the lessee shall be liable for the difference between the capitalized cost of the motor vehicle and the sum of the proceeds from the resale of the motor vehicle and the amount then existing in the monthly reserve.

### § 9 Disposal of Motor Vehicle—Presumption

In disposing of the motor vehicle the lessor shall act in a commercially reasonable manner. At the end of the lease term, the sale of the leased motor vehicle will be presumed capable of realizing proceeds equal to, or greater than, the wholesale price then prevailing in the industry. This presumption may be rebutted only upon certain proof that unreasonable damage to the motor vehicle, caused by the lessee's misuse thereof, has rendered the vehicle unsalable or has substantially impaired the ability of the lessor to realize upon resale the wholesale price then prevailing in the industry. In this event, the lessor shall have the option of reselling the motor vehicle or acquiring three repair bids from independent sources and presenting them to the lessee. The lessee either may demand that the vehicle be sold "as is", thus incurring liability for the difference between the projected wholesale value and the amount actually received, (notwithstanding the limitation of the lessee's liability set forth in Section 8 of this Act) or he may consent to an assessment equal to the lowest bid for such repairs necessary to restore the vehicle to a condition which will enable the lease vehicle to be resold for an amount substantially equivalent to that presumed by this section. Nothing in this section shall be construed to prevent the lessee from obtaining and using his own bids in lieu of those tendered by the lessor for repair of a motor vehicle rendered unsalable by the lessee's misuse. This section does not authorize the repair of defects which are attributable to normal wear and tear resulting from the use of a motor vehicle for a period similar in duration to that of the stipulated lease period. In no event shall such reconditioning costs exceed the difference in value between a damaged motor vehicle similar to the one subject to the terms of a lease contract and the average wholesale value of a like automobile of average marketable condition.

### § 10 Limitation on Lessor's Fees

The amount of the lessor's monthly lease fee shall not exceed one per cent of the capitalized cost of the vehicle per month. The contract may provide for a delinquency charge on any monthly lease installment in default for a period not less than ten days in an amount not to exceed five percent of the installment, which amount may be collected only once on any installment regardless of the period during which it remains in default. The contract may provide for reasonable collection costs and fees in the event of delinquency; however, charges in the form of a penalty are prohibited.

### § 11 Notice of Intent to Sell Repossessed Motor Vehicle: Rights and Liabilities of Persons Liable on Contract

Notwithstanding any provision in any leasing contract for the lease of a motor vehicle which either has been repossessed by the lessor or returned by the lessee prior to the termination of the stipulated lease period, at least ten days' written notice of intent to sell such a motor vehicle must be given by the lessor or his assignee to all persons liable on the leasing contract. The notice shall be personally served or shall be sent by certified mail, return receipt requested, directed to the address of the persons shown on the contract, unless such persons have notified the lessor or holder of the leasing contract in writing of a different address. The notice shall state that there is a right to redeem the motor vehicle and the total amount required as of the date of the notice to redeem; may inform such persons of their privilege of reinstatement of the contract, if the holder extends such privilege; shall give notice of the holder's intent to resell the motor vehicle at the expiration of ten days from the date of giving or mailing the notice, or if given by mail and either the place of deposit in the mail or the place of address is outside of this state, the period of notice shall be twenty days instead of ten days; shall disclose the place at which the motor vehicle will be returned to the lessee upon redemption or reinstatement; and shall designate the name and address of the person to whom payment shall be made. The notice shall also notify the persons shown on the contract of their right to personally secure bids for the sale of the automobile. Such persons shall be liable for any deficiency after sale of the repossessed or returned motor vehicle only if the notice prescribed by this section is given within sixty days of repossession or return and includes the following:

1. A notice, in at least ten-point bold type if the notice is printed, reading as follows: "NOTICE: YOU ARE SUBJECT TO SUIT AND LIABILITY IF THE AMOUNT OBTAINED UPON THE SALE OF THE VEHICLE IS INSUFFICIENT TO PAY THE CONTRACT BALANCE AND ANY OTHER AMOUNTS DUE."

2. An itemization of the contract balance and of any delinquency, collection, or repossession costs and fees. In addition, the notice shall either set forth a computation of the amount of any credit for unearned leasing charges or cancelled insurance as of the date of the

notice or shall state that such a credit may be available against the amount due.

## § 12 Prohibited Provisions in Motor Vehicle Leasing Contracts

No leasing contract shall contain any provision by which:

(a) the lessee agrees not to assert against the lessor a claim or defense arising out of the lease or agrees not to assert against an assignee such a claim or defense;

(b) a power of attorney is given to confess judgment in this state, or an assignment of wages is given, provided that nothing herein contained shall prohibit the giving of an assignment of wages contained in a separate instrument pursuant to Section 300 of the Labor Code;

(c) the lessee waives any right of action against the lessor or holder of the contract or other person acting on his behalf for any illegal act committed in the collection of payments under the contract or in the repossession of the motor vehicle;

(d) the lessee executes a power of attorney appointing the lessor or the holder of the contract or other person acting on his behalf as the lessee's agent in the collection of payments under the contract or in the repossession of the motor vehicle;

(e) the lessee relieves the lessor from liability for any legal remedies which the lessee may have against the lessor under the contract or any separate instrument executed in connection therewith;

(f) the lessor or holder of the contract is given the right to commence action on the contract under the provisions of this chapter in a county other than the county in which the contract was in fact signed by the lessee, the county in which the lessee resides at the commencement of the action, the county in which the lessee resided at the time the contract was entered into, or in the county in which the motor vehicle leased pursuant to such contract is permanently garaged.

## § 13 Attorney's Fees and Costs

Reasonable attorney's fees and costs shall be awarded to the prevailing party in any action on a leasing contract subject to the provisions of this Act, regardless of whether the action is instituted by the lessor, holder or lessee. Where the defendant alleges that he tendered to the plaintiff the full amount to which he was entitled, and thereupon deposits in court, for the plaintiff, the amount so tendered, and the allegation is found to be true, then the defendant is deemed to be a prevailing party within the meaning of this section.

## § 14 Assignee Subject to Equities and Defenses of Buyer

An assignee of the lessor's rights is subject to all equities and defenses of the lessee against the lessor existing in favor of the lessee at the time of the assignment.

## § 15 Violation a Misdemeanor

Any person who shall willfully violate any provision of this chapter shall be guilty of a misdemeanor.

§ 16 Action on Contract—Where Tried: Plaintiff's Affidavit

An action on a contract under the provisions of this Act shall be tried in the county in which the contract was in fact signed by the lessee, in the county in which the lessee resided at the time the contract was entered into, in the county in which the lessee resides at the commencement of the action or in the county in which the motor vehicle leased pursuant to such contract is permanently garaged.

Commencement of an action by the lessor or holder in a county other than the foregoing shall be deemed a violation of this Act. The lessor or holder will be subject to liability for double the amount which he recovered against the lessee in an action commenced in such county. The lessee shall have the right to pursue his cause of action against the lessor or holder for violation of this section in any of the counties set forth in this section.

In any action subject to the provisions of this section, concurrently with the filing of the complaint, the plaintiff shall file an affidavit stating facts showing that the action has been commenced in a county or judicial district which is a proper place for the trial of the action described in this section. Such facts may be stated in a verified complaint and shall not be stated on information or belief. When such affidavit is filed with the complaint, a copy thereof shall be served with a summons. If a plaintiff fails to file the affidavit or state facts in a verified complaint required by this section, no further proceedings shall be had, but the court shall, upon its own motion or upon motion of any party, dismiss any such action without prejudice; however, the court may, on such terms as may be just, permit the affidavit to be filed subsequent to the filing of the complaint and a copy of such affidavit shall be served on the defendant. The time to answer or otherwise plead shall date from such service. A plaintiff shall be liable for reasonable attorney's fees proximately caused by any levy made pursuant to a writ of attachment issued upon an affidavit which does not comply with this section.