#50 9/16/68

First Supplement to Memorandum 68-74

Subject: Study 50 - Leases

In this supplement we review the comments received after distribution of the tentative recommendation on leases. The time allowed for comments did not permit some persons to send us written comments. We attach as exhibits the comments we received. We also note in this supplement comments received by telephone.

We sent a copy of the tentative recommendation to each of the approximately 350 persons who are included on our list of persons interested in this topic and followed up that distribution with a letter to each such person requesting his comments and specifically requesting comments on the problem of discounting rent.

The tentative recommendation on leases was distributed with Memorandum 67-74.

General reaction

There were a number of generally favorable comments on the tentative recommendation. However, the California Real Estate Association urges the Commission to hold its recommendation:

> for further consideration and review. We reluctantly conclude that it would be necessary for us to oppose passage of legislation introduced to implement the proposal contained in the tentative recommendation . . . our objection . . . in general terms . . . result from the omission of significant new material to the law generally in such areas as liquidated damages, separate treatment for residential leases where warranted, specificity in definitions and others; and our objection to the particulars of the recommendation on mitigation, forfeiture of advance payments and some other points.

In view of these objections, it is doubtful that we can submit a recommendation on this subject to the 1969 Legislature. A decision as to whether a recommendation can be submitted in 1969 should, however, be made after the Commission has considered all the comments.

Mr. Albert J. Forn, Los Angeles attorney, criticized the recommendation (Exhibit IV) as follows:

> Unlike the Commission's recommendations in other fields of law, this particular treatise strikes me as being decidedly biased, debilitatingly narrow in its treatment of the subject, and entirely blind to the rights and equities of the majority of tenants.

Mr. Forn further notes (Exhibit IV): "It occurs to me that perhaps the Commission undertakes an impossible task if it attempts to express one statement of law that applies to all lessors and all lessees." He concludes: "Generally, it is my impression that your Recommendation fails to give any protection to the small tenant of the large landlord because it suffers from an over-anxiety to protect the small landlord from the large tenant." In a second letter, Mr. Forn further states: "As the Tentative Recommendation Re Leases appears to overlook, many office leases are virtual contracts of adhesion, loaded with exculpatory language which in sum excuses the lessor from all his obligations."

Generally speaking, the other letters make specific suggestions for revision of the tentative recommendation rather than general objections such as that made by Mr. Forn. See, however, Exhibit I, which contains a number of general objections, most of which are based on a failure to understand the tentative recommendation or are otherwise without merit.

The following is a section by section analysis of the comments on the tentative recommendation.

Section 1951 (page 14)

The CREA (Exhibit XI) suggests that examples of "charges equivalent to rent" be set forth in the statutory definition of "rent." As is, the Comment to Section 1951 makes reference to two such charges--payment of taxes and payment of insurance premiums--and no additional examples are suggested by CREA. The question seems really to be whether these examples should be incorporated into the statute or left in the Comment. The present method of dealing with the problem seems satisfactory. An attempt to list various examples--even with an "including but not limited to" clause--seems doomed to failure and might restrict the otherwise broad language "charges equivalent to rent."

CREA also recommends that the parties be given explicit permission to define rental equivalents in their lease. This is essentially a problem of whether a liquidated damages clause is effective and is discussed later in connection with that problem.

CREA suggests that a definition of "reasonable expenses of releting" as that term is used in Section 1951.2 be included in Section 1951. This apparently reflects a desire to incorporate into the statute what presently is set forth in Comment form. The Comment to Section 1951.2 (page 17) already indicates that damages (and expenses of releting) may include expenses of refurbishment and repair, and attorney's fees where so provided. Further illustrations, such as advertising and commissions, could be included there, but it appears unnecessary to specify this detail in the statute.

Section 1951.2 (page 15)

It seems abundantly clear that Section 1951.2 permits the lessor to institute an action for damages immediately upon abandonment by the lessee or termination by the lessor; the addition of Sections 337.5 and 339.5 to the Code of Civil Procedure dictate this conclusion. Nevertheless, the complaint is lodged by CREA (see Exhibit XI, page 2) that Section 1951.2 is not perfectly explicit in this regard. The CREA objection could be met by providing:

> Section 1951.2. (a) . . . , if a lessee of real property breaches the lease and abandons the property before the end of the term or if his right to possession is terminated by the lessor because of a breach of the lease, the lease terminates and the lessor has an immediate cause of action for damages and may recover from the lessee: . . .

Section 1951.2(a)(2). The CREA comments as follows (Exhibit XI, page 2):

> In Subsection (a) 2, the measure of damages is stated as "the worth at the time of judgment" of the unpaid rent. This is changed from the existing Section 3308 (and the change is effected in the revision of Section 3308 as proposed by the Commission as well) from "the worth at the time of termination." The reason for this change is not explained and it would seem obviously less advantageous to the lessor and may create additional hardship if the tenants breach is caused by insolvency.

The change was made because it is at the time of judgment that the lessor will actually receive his award and it would be unfair to him to discount his damages starting at any earlier point. Up to the time of judgment the lessor should receive the full difference between the unpaid rent and the rent that the lessee proves could have reasonably been obtained from another plus interest on this difference. This is explained in the Comment to the section at the bottom of page 16 of the Recommendation. Whether the tenant's breach is caused by insolvency

or not seems completely irrelevant.

The CREA goes on to state (Exhibit XI, page 2):

> It is our belief that the worth of the present rent should be calculated at termination, a date which is fixed and known when the action is commenced, rather than at the time of judgment. If there is any fluctuation in the rental market the litigation could be prolonged to influence the extent of damages.

This comment really seems to be directed towards the fixing of the discount rate, the next problem to be considered.

One commentator (oral communication) believes that it is still unclear that the computation made under this paragraph is accomplished by (1) determining the amount payable under the lease, (2) subtracting from that the amount capable of being avoided through mitigation, and then (3) discounting the remainder to reflect the fact that it is being prepaid. Perhaps too great a familiarity with the intention of this section has caused a failure to recognize ambiguities, but the staff feels that the statute and Comment (pages 16 and 17) are satisfactory, as is, in this regard.

Conflict exists concerning the desirability of including a fixed discount rate to be used to determine the worth at the time of judgment of the amount of unpaid rent recoverable. The comments received cover the full range of possible alternatives. Two suggest an invariable fixed rate (see Exhibits III and VII), with the possibility that this rate be determined by reference to the United States Federal Reserve Board Discount rate (Exhibit III); one suggests a fixed rate subject to modification by the parties within a statutorily permissible range (Exhibit VIII); another approves the present provision allowing the rate to be determined independently as a question of fact in each case that

arises (Exhibit IX); finally, the CREA apparently accepts the present provision, but would specifically provide that the parties may agree in advance to the rate of discount. (One commentator (Exhibit IX) suggests that the comment to this subpart clearly indicate that the burden of proving the extent of the discount is on the lessee. If the existing provision is retained, the staff recommends that this latter suggestion be adopted by adding a sentence at the end of the paragraph on line 3, page 17, as follows: "The burden of proving the extent of such discount rests with the lessee.") The staff does not feel that there is an overwhelming consensus of opinion favoring any one position, but the Commission may wish to reconsider this problem in light of the various suggestions made by commentators.

Finally, the CREA comments (Exhibit XI, page 3):

> The principal change in this same subsection is the permitted credit against unpaid rent for the mitigation to the extent that the lessee proves damage could have been reasonably avoided. Insofar as this involves re-leasing the premises we believe that it should be clearly stated that such re-leasing should only be required to a tenant of equal repute and for similar or equal purposes and further providing that the lessor is not required to expend money for such re-letting. Any required expenditure of money would in many instances only increase the lessor's loss.
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> Previously, Section 3308 was silent as to the matter of the burden of proof and as noted in the Commission's comments you have adopted a rule previously only applied in actions for breach of employment. In our view, it is doubtful whether this unrelated concept adds any measurable advantage to the section for we are unaware that this provision has proven its value in employment contract situations. Even under existing law the lessee has been permitted to offer such proof as he had to the effect that the lessor could have re-leased the property more advantageously. The added verbage may be just an illusion and may promote litigation or prolong such litigation.

As to the first point, the statute presently provides for mitigation by offsetting against the lessor's damages "the amount of

rental loss that the lessee proves . . . could be reasonably avoided. . . ."

The staff suggests that the following additional material be inserted in the Comment to Section 1951.2 following the first full paragraph on page 17:

> The general principles that govern mitigation of damages apply in determining what constitutes a "rental loss that the lessee proves . . . could be reasonably avoided." These principles were recently summarized in Green v. Smith, 261 A.C.A. 423, 427-428 (1968):
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> > The plaintiff cannot be compensated for damages which he could have avoided by reasonable effort or expenditures. . . . The frequent statement of the principle in the terms of a "duty" imposed on the injured party has been criticized on the theory that a breach of the "duty" does not give rise to a correlative right of action. . . . It is perhaps more accurate to say that the wrongdoer is not required to compensate the injured party for damages which are avoidable by reasonable effort on the latter's part. . . . As Judge Friendly observed in Ellerman Lines, Ltd. v. The President Harding, supra, at p. 290, the current phraseology of the principle may lead to sounder results than its statement in terms of a "duty."
> >
> > The doctrine does not require the injured party to take measures which are unreasonable or impractical or which would involve expenditures disproportionate to the loss sought to be avoided or which may be beyond his financial means. . . . The reasonableness of the efforts of the injured party must be judged in the light of the situation confronting him at the time the loss was threatened and not by the judgment of hindsight. . . . The fact that reasonable measures other than the one taken would have avoided damage is not, in and of itself, proof of the fact that the one taken, though unsuccessful, was unreasonable. . . . "If a choice of two reasonable courses presents itself, the person whose wrong forced the choice cannot complain that one rather than the other is chosen." (McCormick, Damages, p. 134.) The standard by which the reasonableness of the injured party's efforts is to be measured is not as high as the standard required in other areas of law. . . . It is sufficient if he acts reasonably and with due diligence, in good faith. [Citations omitted.]

The staff believes that the general test of reasonableness in the statute is not only the only satisfactory test, but is far better than the alternative suggested by CREA. This is especially true if the Comment is supplemented as suggested by the staff. In most situations the present test would require reletting only "to a tenant of equal repute and for similar or equal purposes;" however, it is not difficult to imagine circumstances where it would be reasonable to require reletting for either a different purpose or to a tenant of lesser, but still excellent, repute. A statutory provision prescribing rules to the contrary could be a source of great injustice. In view of the fact that in the event of litigation, the lessee has not only the burden of proof but the unenviable position of standing in court as the defaulting party, the present test seems to adequately protect the lessor but still provides some desirable measure of flexibility. The same arguments apply to the suggestion that the lessor never be required to expend money for reletting. Generally, this will be the case; obviously where such expenditures would merely increase his loss they will not be required. Again, however, certain expenditures in a given situation may reasonably be required and a rule permitting arbitrary and unreasonable refusal to make such expenditures seems unwise.

As to the second point, the statute by including the phrase "the lessee proves" specifically places the burden of proof of showing an offset on the lessee--one, because as a matter of policy he is obviously the party who should carry such burden, and two, in order to eliminate any doubt concerning who has this burden, thereby removing one potential source of dispute. The inclusion is not of major significance and probably anticipates the rule that would be adopted in its absence, but the criticism of the CREA appears completely unjustified.

Section 1951.2(a)(3). The criticism has been made (oral communication) that this section of the statute and the Comment thereto lack specific guidance as to what items of detriment are compensable after the lessee's breach. While the statute is concededly and deliberately general in its language, the Comment to this paragraph seems to contain a perfectly adequate discussion of what is encompassed by the statute.

In view of the sometimes difficult proof problems both here and under paragraph (2), when a subsequent tenant has not in fact been secured but the defaulting lessee attempts to show that the damages should be mitigated, one commentator (Exhibit X) seems to suggest that the statute provide that a certain percentage of the unpaid future rents be fixed as the measure of damages for all claims to future damages and rent. The staff feels that the proof problems are not insurmountable and that the alternative suggested is a problem of liquidated damages.

We do believe, however, that the Comment should be revised on page 17 of the tentative recommendation to read in part:

> For example, it will usually be necessary for the lessor to take possession for a time to prepare the property for reletting and to secure a new tenant. The lessor is entitled to recover for the expenses incurred for this purpose that he would not have had if the lessee had performed his obligations under the lease. In addition, the lessor is entitled to recover his expenses in retaking possession of the property, making repairs that the lessee was obligated to make, refurbishing and preparing the property for reletting, and in reletting the property. Thus, the cost of moving partitions or of installing partitions or other modifications designed to meet the needs of the new tenant would be recoverable by the lessor from the defaulting lessee. However, expenditures by the lessor in remodeling the premises would not be recoverable to the extent that they constitute a capital improvement in the property. In some cases, a portion of expenditures in remodeling will be

recoverable as refurbishing (such as moving partitions and repainting) but the remainder (such as improvements designed to modernize the property) would constitute a capital improvement the need for which was not caused by the tenant's breach and will not be recoverable by the lessor.

The CREA comments on the question of attorney's fees as follows:

> Under subsection (a)(3), the provisions of Civil Code section 3300 allowing additional damages "proximately caused" is added. In considering this together with section 1951.6 as proposed, it would appear that attorney's fees even though incurred because of a lessee's breach and which would thus be "proximately caused" might not be recoverable unless they were specifically mentioned in the lease. Civil Code 1517 as added by AB 563, 1968, refers only to those cases where a contract specifically calls for the payment of attorney's fees. We suggest that it should be made clear either in this subsection or elsewhere in the Commission's proposal that attorney's fees proximately caused by the lessee's breach are collectible.

The intent of the recommendation is that attorney's fees should not be recoverable unless specifically mentioned in the lease. This is the rule applicable to contracts generally and seems appropriate here. If this policy is not changed, the staff recommends that this intention be clarified by modifying the comment to this section, on line 3, page 18, as follows: "However, attorney's fees may only be recovered if ~~the lease so provides~~ they are recoverable under Section 1951.6. "

Liquidated damages:

CREA comments:

> CREA was very disappointed that the Commission did not take the initiative to overcome the unfortunate and often ridiculous results of court interpretations of liquidated damage clauses as a result of the decision in Freedman v. Rector, 37 C 2d 16. This case and those following it have made the drafting of a meaningful liquidated damage clause in California contracts most difficult. See Continuing Education of the Bar, California Real Estate Sales Transactions, page 443.
>
> We propose a clear-cut right in the statute to liquidate damages by a meaningful agreement between the parties, permitting forfeiture of a reasonable percentage of the rent as one possible approach. This may include appropriate changes in Civil Code 1670 and 1671. Such change is long overdue. We noted with interest the staff draft of May 1, 1968, with proposals for such a clause. That draft utilized language based on Section 2718 of the Commercial Code which, however, has been criticized severely for uncertainty by Professor Alphonso Squillante in a series of articles in Commercial Law Journal, 1968.
>
> Therefore, we feel that the staff proposal of May 1 needs revision but we strongly feel that some provision for liquidated damages should be incorporated if the Commission's proposal in this subject area is to be meaningful. We are prepared to work with the Commission in any further consideration of this topic.

This apparently is a matter of major importance to CREA.

Exhibit XII (John H. Wallace) comments:

> The Commission's comment on page 20 that the parties may provide for liquidated damages is questionable, and appears to ignore the opinion in Electrical Products Corp. v. Williams, 117 CA2 Supp. 813. Specific statutory language may be necessary to overcome Civil Code sections 1670 and 1671. The Commercial Code, in its section 2718, permits such provisions in the case of sales, thereby recognizing the desirability of such provisions under modern business conditions.

Exhibit X (Orville C. Pratt, IV) comments on the recommendation that lessor have a right to suit for his losses immediately upon termination of the lease as follows:

> The only problem which is quite important in commercial leases is that it would be hard to prove in the beginning if it were a long term lease whether one could obtain another tenant with a favorable tax clause or not. This is an element of damage together perhaps with whether one could obtain a tenant who

would be willing to pay insurance which could be most difficult to prove. It occurs to me that the fairest way to both parties might be for our Civil Code to state a certain percentage of the unpaid future rents would be in full damages for all these claims. I think this is fair to both parties and see no other practical way to meet it.

Mr. Pratt appears to be suggesting that the Civil Code contain, in effect, a liquidated damages provision because of the difficulty in proving the various losses that go into the damages recoverable by the lessor. The staff believes, however, that such a suggestion is undesirable; it would be a better solution to his problem to permit the parties to draft a liquidated damages provision in light of all the circumstances of the particular lease.

The May draft referred to by CREA provided:

1951.5. Liquidated damages

1951.5. (a) Damages for breach of a lease of real property by either the lessor or lessee may be liquidated in the lease but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A provision in the lease fixing unreasonably large liquidated damages is void as a penalty.

(b) If the lease is printed, a provision for liquidated damages is valid only if a recital of the fact that such a provision is contained in the lease appears in at least eight-point boldface type immediately prior to the place where the lessee executes the agreement or, if the lease contains a provision described in Section 1945.5, immediately prior to the recital referred to in that section.

Comment. Subdivision (a) of Section 1951.5 establishes the criterion for determining the validity of a liquidated damage provision in a lease. The subdivision is the same in substance as subdivision (1) of Section 2718 of the California Commercial Code and is in more liberal terms than Civil Code Sections 1670 and 1671 which apply to contracts in general and under which all clauses fixing damages are void except when "from the nature of the case, it would be impracticable or extremely difficult to fix the actual damage." Under prior California law, a liquidated damage provision in a lease was void. E.g., Jack v. Sinsheimer, 125 Cal. 563, 58 Pac. 130 (1899); McCarthy v. Tally, 46 Cal.2d 577, 297 P.2d 981 (1956). The provision that liquidated damages

must be reasonable is consistent with California law. E.g., Freedman v. Rector, Wardens & Vestrymen of St. Matthais Parish, 37 Cal.2d 16, 230 P.2d 629 (1951).

Subdivision (b) is designed to protect the unwary. The subdivision is based on the similar requirement found in Civil Code Section 1945.5 (automatic renewal or extension provision).

This obviously is a matter the Commission has considered before. The recommendation presently treats the subject of liquidated damages in a comment only, at page 20. In essence, it is indicated there that a liquidated damage provision in a lease should be valid if it meets the requirement of Civil Code Sections 1670 and 1671 relating to such provisions in contracts generally. The CREA and other commentators believe that this is a matter that should be dealt with in the statute.

Section 1951.2(b). Mr. Jack T. Swafford, Exhibit II, suggests a revision of subdivision (b), to read:

> Efforts by the lessor to mitigate the damages caused by the lessee's breach of the lease do not waive the lessor's right to recover damages under this section. Unless the parties otherwise agree, if the lessor relets the property after the lease terminates under this section, he is not accountable to the lessee for any rent received or to be received from the reletting; but ~~such rent~~ the worth of such rent at the time of judgment, less the ~~reasonable~~ actual expenses of reletting, shall be offset against any amount ~~sought to be recovered~~ recoverable under this section.

We believe that his deletions and additions of "or to be received" and "the worth of such rent at the time of judgment" and "recoverable" are desirable changes. We do not recommend that "actual" be substituted for "reasonable" although it can be argued that the lessor should recover an expense actually incurred even if he did not necessarily act "reasonably."

Section 1951.4 (page 21)

Some minor variations of the language of this section have been suggested. (See Exhibit II, page 2.) These may be examined but for the most part, the staff believes that the varistions perhaps unintentionally, would work possible substantive changes and are therefore undesireable. One change that does seem desireable, however, would be the addition of the phrase--"if the lessor does not terminate the lessee's right to possession and"--after the third word, in line 5 of subdivision (a). As the commentator points out, this is one of two conditions which must exist before the lessor has the right granted by subdivision (a) and should therefore be included in that subdivision. Also the deletion of "by the lessor" from paragraph (1) of subdivision (c) seems desirable.

It has also been suggested that the last phrase--"or for such subletting or assignment"--in subpart (2) of subdivision (a) be deleted. (See Exhibit III, pages 2-3.) The suggestion apparantly reflects a misunderstanding of the intent of the statute. The intention is to prohibit the lease from providing unreasonable standards for either the acceptability of the tenant or for subletting or assigning generally. Perhaps this would be clearer if Section 1951.4(a) were in part redrafted as follows:

> (1) Either to sublet the property or to assign his interest in the lease, or both, and the lease does not set any unreasonable standard for, nor impose any unreasonable condition on, such subletting or assignment.
>
> (2) Either to sublet or to assign his interest in the lease, or both, to any person reasonably acceptable as a tenant to the lessor and the lease does not set any unreasonable standard for the determination of whether a person is reasonably acceptable as a tenant.

Finally, neither the statute nor the comments give the court guidance as to the restrictions that may reasonably be imposed on the acceptability of a new tenant. (See CREA, Exhibit XI, Comment D.2. page 4.)

The reasonableness of any restriction is so largely dependent on the facts of the given situation that predetermined statutory guidelines are likely to be either unduly confining or too broad to be meaningful and helpful.

The Commission might, however, consider the addition to the Comment of a statement generally along the following lines:

> No definitions can be fixed as to the reasonableness of any restriction on the acceptability of a new tenant. There are many factors that may be considered in a given situation: e.g., the credit rating of the new tenant; the use he plans to make of the property and its similarity to the previous use; the nature or character of the new tenant--cafeteria or hot dog stand versus swank restaurant; bargain basement versus prestige clothier--the use may be similar but the effect on other tenants may be quite different; the requirements of the new tenant for services furnished by the lessor; the impact of the new tenant on common facilities--parking lots, walkways, etcetra. The determination whether a particular restriction is reasonable must be made in the light of all the relevant existing circumstances.

Concerning the application of this section to residential leases the CREA observes:

> . . . that Section 1951.4 is not readily adaptable to residential leasing because of the undesirable rights to subletting. When Section 1951.8, which practically disallows forfeiture of advance payments, is taken into consideration, the net result is that the residential lessor is left with Section 1951.2 as his sole remedy of money damages which is not a very satisfactory solution in our view.
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> This particular section presumably has been added to accomodate financing interests involved in "net lease financing" and public lease-back arrangements. While this special accomodation has been granted by the Commission for lessors in these circumstances lessors who normally are of such size and capacity to adequately protect their own interests through representation and careful lease drafting--no comparable protection through special individualized treatment is granted for the residential lessor who often does not have the resources or the expertise to give him similar protection. As is observed later, we believe that special innovative, imaginative treatment should also be provided for this special category.

No concrete alternatives are suggested by the CREA and it is difficult to imagine what better alternative could exist. Residential leases are

almost invariably prepared by the lessor; if he does not choose to provide himself with the alternative remedy afforded by Section 1951.4 that is his choice, but the section permits him to set any reasonable standard for subletting or assignment and this seems to be all that he should be entitled to do. Obviously one of the major policy decisions effectuated by this recommendation is that property should not be left vacant and damages must be mitigated. Perhaps underlying the concern with residential leases is a feeling that the lessor should be permitted to make a much more subjective choice of lessees. To some extent, this concern should be alleviated by the relatively short term of such leases. Moreover, many, many perfectly objective standards can be utilized that permit an exercise of subjective choice--e.g., no pets, no children,--although unusual in residential leases, a certain credit rating can be demanded of the new tenant. In short, as noted above, the lessor can incorporate any standard he chooses subject only to a test of reasonableness.

Section 1951.8 (page 26)

One commentator is bothered by the use of "advance payment" both as the term to be defined and as a part of the definition. (see Exhibit II, page 3) The staff feels that in this case the use is not objectionable and is preferable to the alternative suggested--"initial payment." The definition proposed by the commentator also restricts the section to "moneys paid at the time of execution of the lease."

The CREA here makes a number of additional comments (Exhibit XI, page 5):

1. This section would vest powers in a court by interpretation to ascertain what is an appropriate consideration in a lease contract even though that contract has been carefully drafted with adequate knowledge of all parties as to the impact and the consequences.

2. Currently in many situations this question of advance payments is dealt with in varying fashions because of the tax consequences which themselves can be a significant consideration in the amount of those advance payments. Section 1951.8 threatens to disrupt the possibilities of favorable tax considerations which can now often be garnered.

3. This section would seem to be an additional step in the direction of outside interference with contractual control and damages and represents a direct invitation to nuisance law suits. The parties can no longer agree to any forfeiture but must leave the "balancing of the equities" to the court.

4. The proposed section may also effect the determination of the trustee in bankruptcy's right to an advanced payment upon lessees breach caused by insolvency.

5. The staff draft of May 1, 1968, was an attempt to provide for an elective retention of deposit or advance payment as damages. We prefer that approach but believe that that draft would require further refinement if the Commission were willing to reinstate that concept.

6. Action in this field in either approach would seem to precipitate a requirement to protect the lessee against the loss of advance payment due to sale or foreclosure. See N.Y. Penal Law 1302a. [now N.Y. General Obligations Law § 7-105 (1967)--this section requires a vendor of leased property to either deliver advance payments to the vendee or retain such payments and in either case notify the lessee of the disposition, or simply return the advance payment to the lessee.]

In response, obviously the section contemplates some judicial supervision to prevent forfeitures; however, just as clearly within this overriding limitation, the parties are given complete freedom to make their own decisions. The significance of the section is that it attempts to eliminate the possibility of judicial decisions based merely on labels. In this regard, it may very possibly do no more than anticipate or even state existing law. The former draft, providing for retention of advance payments, conditioned retention on the sum being not unconscionable. In substance, this seems to simply be a different way of saying there must not be a forfeiture.

Whether provisions similar to those in New York regarding the disposition of advance payments are necessary or whether this matter can be left to the parties to negotiate might be considered. The staff feels that such provisions are unnecessary; we are aware of no problem under existing law, and we do not feel that Section 1951.8 alters the situation enough to create any new difficulties.

In short, the thrust of the CREA comments appears to reflect a desire that the lessor be permitted to demand an advance payment that can be retained regardless of future developments. This position has been rejected by the Commission, and the staff feels that no change in this section is required. Possibly, however, the section could be omitted entirely.

CCP Sections 337.5 and 339.5. It has been noted that these Statute of Limitations sections fail to cover the cause of action granted the lessee to recover so much of an advance payment as he proves would result in a forfeiture. The staff recommends the omission be rectified by the addition of a reference to Section 1951.8 in each section. The Comment to Section 337.5 should also include a reference to Section 1951.8, as follows:

> Under Civil Code Section 1951.8, a lessee may recover so much of an advance payment as he proves would result in a forfeiture if retained by the lessor.

Section 3308 (page 34)

This section has been extensively reviewed by an attorney representing a major lessor engaged in leasing industrial and commercial equipment. See Exhibit XII. He makes many of the same points regarding prejudgment interest, fixing of discount rates, sanctioning of liquidated damages provisions that were made earlier in connection with these problems under real property leases. Other concerns are unique to this section and its application to equipment leasing. It is hoped that many of these problems can be alleviated, if not completely ended, by substantially redrafting the Comment to this section. His comments and the staff's reactions and recommendations follow.

1. General.

> The tentative recommendation causes one general concern by creating doubt as to what principles of law - real property or contract - govern equipment leases.
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> The sections which are proposed to be added to the Civil Code (sections 1951 to 1952.6), express the intent to reform historical rules governing leases of real property by applying principles of the law of contracts. The exclusion of personal property leases from the sections provides a basis for litigants to argue that the legislature intended that the benefits conferred on lessors of real property by the proposed sections were not to be extended to lessors of personal property - instead leases of personal property are to be governed by the prior law of landlord and tenant, except as modified by section 3308. . . .
>
> The amendment of Section 3308 in accordance with the recommendation would not appear to overcome such an argument for the following reasons: a) in stating the lessor's remedies, proposed section 3308 omits some matters which are included in the sections which the Commission proposes be added, (the matters stated in subparagraphs 3(b) and 3(c) of proposed section 1951.2 and the matters contained in proposed section 1951.4), thereby implying the imposition or retention of restrictions in the case of personal property leases; b) the tentative recommendation itself lends support to the view that personal property leases are governed by the law of landlord and tenant except to the extent it is modified by section 3308 in that the comment to section 3308 (p.35) equates personal property and real property leases by referring to the comment to proposed section 1951.2 "for further

discussion"; and c) it is well known that section 3308 was enacted for the limited purpose of permitting a lessor, by specifically providing in the lease for the relief described in section 3308, to overcome the judge-made rule that a lessor cannot sue for entire breach of a lease until the end of the lease term.

It is reportedly the view of the Commission that personal property leases are (and should be) governed by the law of contracts. The comments to the proposed legislation do not, however, contain any expression of this view and subparagraph (a)(3) of section 3308 does not necessarily express it, as this is simply a repetition of what is provided in section 1951.2, in a statute which is subject to a very narrow construction.

If the Commission is proceeding on the assumption that contract rules apply generally to personal property leases and that it is not intended by the enactment of section 1951 to 1952.6 to deny to a lessor of personal property any remedy or benefit conferred on a lessor of real property by the proposed sections or to prohibit any otherwise lawful agreement between a lessor and of personal property, it would appear, at the very least, that the comments should reflect this assumption and, ideally, section 3308 itself should so state.

The staff does believe that personal property leases are and should be governed by the law of contracts and that the danger of a strained statutory interpretation, as suggested above, being placed on this recommendation is remote. Nevertheless, to eliminate the possibility, the first paragraph of the Comment to this section could be revised as follows:

> Section 3308 has been revised to exclude reference to leases of real property because, insofar as the section related to real property, it has been superseded by Sections 1951-1952.6. This section now refers solely to leases of personal property, which are governed generally by the law of contracts. It is not intended by the elimination of real property leases here or by the enactment of Sections 1951-1952.6 to deny to a lessor or a lessee of personal property any remedy or benefit available to him under Section 3308 or under the rules applying to contracts generally.

Should Section 3308 include a statement to the effect that the rights and remedies under a lease of personal property are the same as under any other contract?

2. Mitigation of damages . His comments go on to say:

> The Commission has considered the effect of "net financing" in determining what remedies should be available to a lessor of real property. This consideration is equally applicable to leases of personal property. The typical equipment lease provides for rentals that are designed to return the cost of the equipment, plus a reasonable profit, to the lessor over the primary term of the lease (without consideration of the residual value of the equipment, renewals or options to purchase). The lease is assigned customarily to a lending insitution as security for a loan with which the equipment lessor pays for the equipment. The lessor and lender each assume that in the event of a breach by the lessee, the remedies provided for by the lease and Civil Code section 3300 will be applicable. It is believed to be understood generally that the remedies available as a matter of law (consistent with section 3300) in the event of a breach of the entire lease agreement and repossession of the equipment permit the recovery against the lessee of the following: the amount of unpaid rental installments falling due to the time of judgment with interest thereon at the legal rate or such higher lawful rate as may be specified in the lease from the time each falls due; the amount of the rentals which would have been received after judgment, discounted to value at the time of judgment at such rate as to yield a compensatory sum; if the equipment has been sold, the amounts expended prior to sale to repossess, store, insure, and pay taxes on it, the expenses of sale, and the value the equipment would have had at the end of the lease term (lessor's reversionary interest); if the equipment has been relet, the amounts expended prior to reletting to repossess, store, insure and pay taxes on it and the expenses of reletting. Against these amounts the lessee is entitled to credit for the actual proceeds of sale or reletting, or such larger amounts as the lessee can prove should have been obtained by the lessor if the lessor acted in a commercially reasonable way. Credit is to be applied as of the time of actual receipt (or when it should have been received if the lessor did not act in a commercially reasonable way), first to interest then to principal.

The staff feels that neither Section 3308 nor the remainder of the recommendation will, in any way, affect the remedies listed above. Indeed, the preceding passage is close to a paraphrase of the discussion in the Comment to Section 1951.2, relating to the effect of that section. We suggest, however, that the Comment to Section 3308 be expanded to include a listing of the remedies referred to in the material quoted above.

Consistent with the investment or financial nature of an equipment lease, a recent California case, Challenge-Cook Bros., Inc., v. A.G. Lantz, 64 Cal Rptr 239, 256 ACA 597, held that a lessor who was ready, able and willing to perform could recover rentals due as they accrued, even though the lessor has repossessed the equipment. In another recent case, Associates Discount Corp. v. Tobb Co., 241 CA2 541, 50 Cal Rptr 738, it was held that where the lessee was allowed to remain in possession, the lessor could accelerate the rent and recover judgment for the full amount thereof. Neither case imposed any condition that the lease allow assignment or subletting. The remedies were provided for in the leases themselves.

The financial nature of the equipment lease makes remedies such as those enforced in the Lantz and Tobb cases highly desirable and fair when the lessee is solvent but recalcitrant. On the other hand, if the lessee is insolvent, the economic reality that the money it gets from sale or reletting may be all that it will ever collect will force the lessor to try to mitigate. It would appear appropriate, therefore, that the comment to section 3308 contain a statement excluding any implication from the provisions on mitigation and from proposed section 1951.4 that the parties are not free to provide by contract for remedies such as those that were contained in the leases in Lantz and Tobb, or that the section itself so provide.

The Lantz case is predicated in part on the finding that the lessor for a period of time repossessed the property as "security" and did not "terminate" the lease. Thus, he was entitled to recover rent accrued prior to termination. The Tobb case is analogous to the situation covered by Section 1951.4, i.e., the tenant remains in possession and rent can continue to be collected by the lessor. Obviously, the thrust of the entire recommendation, including the conforming revision of Section 3308, is to promote mitigation of damages. Nevertheless, the parties are left largely free to provide by contract for remedies such as those in Lantz and Tobb, and the staff does not believe that anything more on this point is needed either in the statute or the Comment.

3. Interest. His comments continue:

That portion of section 3308 making the measure of damage in part subject to deduction for avoidable rental loss creates a

serious question as to the allowability of interest before judgment. The Commission comments (on page 16), that interest must be added to the amount by which the rental payment exceeds the amount of avoidable rental loss, but there is no wording to overcome the specific provisions of section 3287 limiting interest to "damages certain or capable of being made certain by calculation" or the holding in Peterson v. Larquier, 84 CalApp 174. (See also Rose v. Hecht, 94 CA2 662.)

The statement in Coleman Engineering Co. v. North American Aviation, Inc., 65 Cal 2d 396, that ". . . reductions in damages due to plaintiff's efforts to mitigate damages should not preclude an award for prejudgment interest. . . .", is not to be construed as applying to a situation where the very measure of damages is the amount by which the rents receivable under the lease exceeds the amount of rental loss, ". . . that could have been or could be reasonably avoided; . . . ." In the Coleman Engineering case, the unliquidated credits or offsets consisted of reduction of damages "due to settlement of claims and salvage of materials." It would appear that to overcome the specific provisions of Civil Code section 3287, section 3308 should, at a minimum, describe the amounts proved by the lessee as rental loss that could have been avoided as unliquidated credits or offsets, but preferably should provide specifically for prejudgment interest on the difference between the rental loss and the amount thereof that was or could have been avoided. If such interest is not allowed, the lessor is deprived of the benefit of his bargain and may even incur a loss.

This is a point that was raised earlier in connection with Section 1951.2. As noted above, the staff believes that the Comment to Section 1951.2 insures that interest on prejudgment rental loss will be awarded and no change is required. It might, however, be helpful to expand the second paragraph in the Comment to this section and discuss interest, discounting, and sale of property as these matters relate to use of personal property.

4. Discount. His comments continue:

The intent expressed in subsection (a) of section 3308 (and the same subsection in section 1951.2) is apparently that the worth at time of judgment of any rental payments that would have fallen due after the date of the judgment be determined by applying a discount rate for the purpose of obtaining a "present value" as of the time of judgment of the future rentals. Selecting an appropriate discount rate is not a simple matter, of course, but if the matter is

left unresolved, the courts may end up with very different conclusions on very similar facts. As a solution, section 3308 could contain a provision permitting the lease to establish a discount rate.

Any decision made in regard to discount rates under Section 1951.2 should, of course, be reflected here. It might be noted that the recommendation, as is, at least is no different and therefore no worse than existing law. Whether it can be improved upon is debatable. The danger of permitting the parties to establish a discount rate is that, where there is a great disparity in bargaining power in favor of the lessor, one may wind up with no discount at all which would clearly thwart the entire purpose.

5. Liquidated damages.

The Commission's comment at page 20 that the parties may provide for liquidated damages is questionable, and appears to ignore the opinion in Electrical Products Corp. v. Williams 117 CA2 Supp 813. Specific statutory language may be necessary to overcome Civil Code sections 1670 and 1671. The Commercial Code, in its section 2718, permits such provisions in the case of sales, thereby recognizing the desirability of such provisions under modern business conditions.

Again the plea is made that more be done concerning liquidated damages. The Williams case cited was not ignored; it is simply a holding that the lessor must plead and prove that damages resulting from a failure to pay the rent were "from the nature of the case" impracticable or extremely difficult to fix. In Williams, there was a complete failure of proof on this point and the facts recited suggested that damages would in fact be rather easy to calculate; in any event, judgment in favor of the lessor was reversed to permit him to prove either the validity of the liquidated damages clause or the extent of his damages. As noted above, the real concern of those critical of the present treatment of liquidated damages is that the basic Civil

Code Sections 1670 and 1671 are unsatisfactory or at least have been poorly applied. Possibly, Section 3308 could adopt by reference the Commercial Code section as the test for the validity of a liquidated damages provision.

6. Mandatory nature of Section 3308 as amended. The comments continue:

> The amended section would appear to require an express exclusion of its application to a lease of personal property. This may create an implication that its provisions express a legislative or public policy so that remedies provided by a lease are not enforceable unless they are consistent with that policy. It would appear that the section would still achieve its primary purpose of establishing a cause of action, before the end of the lease term, for an entire or material breach of the lease by providing that, in addition to any remedies provided by the lease or conferred by law, a lessor "may" recover from the lessee according to the damages rules set forth in the amended section.

The above comment is a valid one. If the establishment of a cause of action is all that is intended, a Comment clarifying this point should be included. If, on the other hand, a broader legislative policy is intended, that should be indicated in the Comment. As is, the section is ambiguous in its implications, and a definite policy decision should be made in this regard.

The intention of this recommendation was to improve the law of real property as it applied to leases. Certainly, it would be easiest, and the staff believes it would be accurate, to disavow in the Comment any intention of changing the law generally relating to leases of personal property.

7. Right to sell. The comments continue:

> Experience has shown in the case of personal property leases, that in most instances it is impractical to relet the equipment after default by the lessee and repossession. Since the greatest mitigation in such cases is achieved by sale of the equipment, the comment might well state that nothing in section 3308 is to be construed as prohibiting sale rather than reletting if the evidence establishes that sale was the most effective way to mitigate.

The suggestion above is an excellent one. Obviously, sale in the real property situation would be unusual; with regard to personal property, it is quite common. The suggestion can be adopted by simply incorporating the underlined statement above at the end of the second paragraph of the Comment.

8. Use of word "termination."

> The use of the word "termination" in section 3308 is questionable. As used in this section it appears to have a meaning inconsistent with its definition in the Commercial Code [see section 2106 (3)] and in some cases (see Corbin, Contracts section 1229, 1952 edition), where it has been interpreted to mean a complete relinquishment of rights by the non-breaching party. The term is made ambiguous also by the fact that section 1951.2 contains an express reservation of indemnification rights under the lease "for liability arising prior to termination of the lease", while section 3308 does not contain any such reservation.

The use of the word "termination" simply follows the usage in the original section enacted in 1937. It is true that it is inconsistent with the Commercial Code which provides that "'termination' occurs when either party pursuant to a power created by agreement or law puts an end to the contract otherwise than for its breach." We are advised that it has been argued that the concept of "surrender" is applicable to personal property leases and this is based in part on the word "termination."

Respectfully submitted,

Jack Horton
Junior Counsel

1st Supp. Memo 68-74 EXHIBIT I

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OF COUNSEL
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NEW YORK, NEW YORK

August 19, 1968

California Law Revision Commission
School of Law
Stanford University
Stanford, California 94305

Re: Proposed recommendation relating to leases

Gentlemen:

I have received your Revised Tenative Recommendations Relating to Leases dated July 31, 1968, and in accordance with your inquiry make the following comments.

First let me say that a detailed study of the proposed recommendations would need to be made by any attorney examining same, but even a cursory examination creates the following questions which I believe must be considered by you before recommending passage to the legislature.

1. In Point One re "Right of Lessor to Recover Damages Upon Lessee's Abandonment of Leased Property" you are recommending to the legislature that lessor be entitled to sue immediately for all damages present and future caused by the abandonment of the property or the termination of the lease. It seems to me as an attorney heavily involved in real property matters that if the lessor under our Rules of Procedure must include all of his claims in one litigation and cannot bifurcate causes of action or commence an action upon determination of losses in the future, to impose upon the lessor the burden of presenting all of his damages for the future is almost an impossibility. Speculation is not permitted under our law for a determination of damages and there would be no way that a lessor could with any degree of responsibility be able to, in fact, determine what his future

losses might be as the result of lessee's activities.

I would suggest that the right to commence an action for future losses be awarded to the lessor even though he might be able to bring his action in the present as opposed to the future for such future losses under the above circumstance.

That same point also runs through your second point namely "The Right of Lessor to Recover Damages Upon Breach by Lessee Justifying Termination of Lease."

Under the duty of lessor to mitigate damages it is my personal belief that the entire obligation on the part of the lessor to attempt to mitigate damages should be eliminated. Why is a lessor in any different position than any other person with whom a contractual arrangement has been entered into whereby he is forced to go out and attempt to lease on behalf of the lessee or otherwise that premise which he has already found a tenant who now has defaulted under the terms. It seems to me that the lessee is given the advantage over the lessor. Practically speaking the lessor will attempt to obtain a tenant for his premise because the duty to repair same and keep in order such premises is a valuable asset to the lessor, and rather than have a vacant unit or building he will attempt to mitigate in that sense. I would suggest that the lessor be granted the option to mitigate and then apply the loss of the bargain rule accordingly. This might tend to discourage lessees from abandoning or leaving premises when they realize that if the lessor does not wish to do so, he need not make any effort to mitigate and that the lessee will remain 100% responsible. As to the balance of your suggestions in this heading I concur that the lessor will be allowed to recover all costs directly or indirectly related to the lessee's breach. The lessor need not notify the lessee before reletting the property on mitigation grounds.

Under your lease provision relieving the lessor of the burden of mitigating damages I concur.

Under the heading Forfeiture of Advanced Payments it is my personal view that if the lessee has in fact breached his lease, there is no intelligent reason to repay him anything. If we are to honor contractual arrangements between individuals, it appears in good conscience to me regardless of the language used in the leasehold agreement that where the buyer has repudiated his contract through breach or otherwise all sums of money deposited with the lessor, be it cleaning deposits, advanced rentals, or security deposits, should remain and become the absolute property of the lessor subject only to a court of competent jurisdiction determining otherwise for whatever valid reason that court might have. I believe the lessor should have the right to exact forfeitures be it by the artful use of language in the lease or by the conduct of the lessee himself.

As to the balance of the various recommendation I am basically in accord with the suggestions that you make, except in the area of the effect on unlawful detainer where you suggest that the lessor be entitled to recover immediately for future losses. The burden imposed upon the lessor with your recommended changes would require the lessor to bring two separate actions, one for recovery of the real property and two for the damages sustained. I think that the damages and recovery can easily be combined into one action and in turn we will be expediting the lessor's rights and saving the time of court and counsel.

I hope that my suggestions are of some value to you and that you will consider them in making your report to the appropriate legislative committee.

Very truly yours,

ROBERT M. ARAN

RMA:me

1st Supp. Memo 68-74

EXHIBIT II

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OTIS H. CASTLE
SPECIAL COUNSEL

August 26, 1968

John H. DeMoully
Executive Secretary
California Law Review Commission
School of Law
Stanford University
Stanford, California 94305

Re: Tentative Recommendation Relating to Leases.

Dear Commissioner DeMoully:

I have received and reviewed the Commission's tentative recommendations relating to leases and have the following comments:

I would suggest the following revision of §1951.2(b):

> "Efforts by the lessor to mitigate the damages caused by the lessee's breach of the lease do not waive the lessor's right to recover damages under this section. Unless the parties otherwise agree, if the lessor relets the property after the lease terminates under this section, he is not accountable to the lessee for any rent received [or to be received] from the reletting; but ~~such rent~~ [the worth of such rent at the time of judgment,] less the ~~reasonable~~ [actual] expenses of reletting, shall be offset against any amount ~~sought to be recovered~~ [recoverable] under this section."

Comment: I think my reasons for suggesting the proposed changes are evident from the changes made.

I suggest the following revision of §1951.4:

"(a) A lease of real property continues in effect after the lessee has breached the lease and abandoned the property and the lessor may enforce all his rights and remedies under the lease, including the right to recover the rent as it becomes due under the lease, [if the lessor does not terminate the lessee's right to possession and] if the lease ~~so provides and~~ permits the lessee to do any of the following:

* * *

(2) Either to sublet the property or to assign his interest in the lease, or both, to any person reasonably acceptable as a tenant to the lessor and the lease does not set any unreasonable ~~standards~~ [standard] for ~~the determination of~~ [determining] whether a person is reasonably acceptable as a tenant ~~or for such subletting or assignment~~.

* * *

(b) Nothing in subdivision (a) affects any right the lessor may have to terminate the lessee's right to possession. ~~A lease described in subdivision (a) terminates when the lessor terminates the lessee's right to possession.~~

(c) For the purposes of subdivision ~~(b)~~ (a), the following do not constitute a termination of the lessee's right to possession:

(1) Acts of maintenance or preservation or efforts to relet the property ~~by the lessee~~.

* * *"

Comment:

1. It seems to me that the subject of the second sentence in subdivision (b) is more properly a part of subdivision (a), in that it is really one of the two conditions which must exist before the lessor has the right granted by subdivision (a).

2. With respect to (a)(2) it seems to me it is better to speak without reference to any standard for determining the matter. Further, the concluding phrase "or for such subletting or assignment" is superfluous in that the single question under the provision as written relates to a determination of the acceptability of the tenant. If it is desired to reach provisions which impose other guide lines for determining whether the lessee can sublet or assign his lease, then the sentence needs to be restructured at the beginning.

3. I think the reasoning behind the other changes is self-evident.

With respect to §1951.8, I suggest that subdivision (a) be revised as follows:

> (a) As used in this section, "~~advance~~ [initial] payment" means moneys paid [at the time of execution of the lease] to the lessor of real property . . ."

Comment:

I am always bothered when a statute defines a term by using the term itself. Hence, I think that by using a broader term which covers all four clauses, there will be less confusion.

I also think that the second sentence of subsection (b) of §1951.8 is really a separate concept and should be made a separate subsection (c).

Very truly yours,

Jack T. Swafford

Jack T. Swafford
of BURRIS & LAGERLOF

JTS/jba

1st Supp. Memo 68-74 EXHIBIT III

461 South Boylston Street
Los Angeles, California 90017
September 5, 1968

California Law Revision Commission
School of Law
Stanford University
Stanford, California 94305

Attention: Mr. John H. DeMoully
Executive Secretary

Re: Tentative Recommendation of California Law Revision Commission relating to Leases

Gentlemen:

In response to your letter of August 28, 1968, I would suggest that the method of determining the discount rate for prepaid rentals under proposed Section 1951.2 (a) (2) be included in the wording of that section. Recommended revised wording of that section is as follows:

> "1951.2 (a) (2) The amount by which the unpaid rent for the balance of the term after termination, discounted at the United States Federal Reserve Board Discount Rate at the time of the judgment for the Federal District within which the leased property is situate plus one percent (1%), exceeds the amount of rental loss that the lessee proves could have or could be reasonably avoided; and"

The Federal Reserve Board Discount Rate should serve as a relative stable reference for the purpose of discounting prepaid rentals and, in addition, would provide the same standard for all lease termination situations. I understand that the prevailing bank loan rates are set at one percent (1%) higher than the Federal Reserve Board Discount Rate, hence the provision for adding one percent to the rate. California is now located within Federal Reserve Board District Number 12.

Very truly yours,

J. S. Place
Attorney

JSP:lh

1st Supp. Memo 68-74 EXHIBIT IV

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September 5, 1968

California Law Revision Commission
School of Law
Stanford University
Stanford, California 94305

Gentlemen:

Thank you for sending me a copy of the Commission's Tentative Recommendation Re Leases. Unlike the Commission's recommendations in other fields of law, this particular treatise strikes me as being decidedly biased, debilitatingly narrow in its treatment of the subject, and entirely blind to the rights and equities of the majority of tenants.

It occurs to me that perhaps the Commission undertakes an impossible task if it attempts to express one statement of law that applies to all lessors and all lessees. Merely because the word lessor describes an individual's status under a particular written instrument does not mean that in truth he can be classified as belonging in the same legal genus as another individual who also fits under the title of lessor.

The lessor of a 15-story office building containing one million square feet of rentable space is in an entirely different position with relation to a tenant who is renting only 400 square feet within his building than the lessor who owns fifty thousand square feet of land which he is leasing to a billion-dollar corporation as his only tenant. Conversely, the lessee of a 400-foot office space is, and at law should be treated as, an entirely different type of individual than the huge corporation which demands and gets all or nothing from its lessor. The differences among these individuals are not merely in size, but at the very least differences of species. In my mind they are even of different genus.

Perhaps, therefore, the Commission should take a fresh look at this problem, recognizing that it may be unrealistic, and even improper to speak of the rights of a "landlord" or of a "tenant" as if those two concepts were all that existed in real life. I would suggest that the

defect begins first with the limitations of our language. We really need some new and additional words to distinguish among the creatures that people this field of law which is presently named lessor-lessee or landlord-tenant. I personally have not given the matter sufficient thought to suggest any new words, because actually this letter is a somewhat spontaneous reaction to the Recommendation, and I haven't had the time to focus in on the subject too sharply. However, I feel that it is inescapable that the use of the same word, such as lessor or landlord, to designate a relationship, such as the owner of the fee, makes it unnecessarily difficult to recognize that the owner of 50,000 square feet of land dealing with one corporate tenant should not be regarded as the same type of legal power as the owner of the one million square foot office building dealing with the lessee of 400 square feet of office space.

I would suggest that the individuals that are now lumped together under the tab of lessors might be classified at law in a way approximating their classification in life; and likewise lessees should be classified at law in a way that attempts to reflect their actual status in the economic world.

Generally, it is my impression that your Recommendation fails to give any protection to the small tenant of the large landlord because it suffers from an over-anxiety to protect the small landlord from the large tenant.

Very truly yours,

ALBERT J. FORM

AJF:zm

P.S. Please note my change of address on your records.

1st Supp. Memo 68-74

EXHIBIT V

ALBERT J. FORN
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September 5, 1968

California Law Revision Commission
School of Law
Stanford University
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Gentlemen:

I have just received your August 28, 1968 circular re problems that have arisen under Civil Code Section 3308.

As the Tentative Recommendation Re Leases appears to overlook, many office leases are virtual contracts of adhesion, loaded with exculpatory language which in sum excuses the lessor from all his obligations.

In this type of situation a Section 3308 problem arises when the lessor of the office building cuts down on the elevator service, janitorial services and sanitation services in the process of "bleeding" the building. The lessee of one of the offices accordingly abandons his leasehold although he may still be liable for three or four years on the lease. ("It's either me or the cockroaches.") Because of the landlord's own conduct the rental value of the premises has nose-dived to practically zero, making Section 3308 entirely useless from the lessee's point of view. A similar situation exists in landlord-created slums.

I would propose that the State legislature classify lessors according to their economic power relative to their lessees; and as to lessors who fit the above illustration transfer all of the burden of proof to them. I would also propose that wherever the lease gives the lessor a right to attorneys fees, the statute should bestow the same right to attorneys fees on the lessee. In other words, the prevailing party will always be entitled to an award of attorneys fees if either party contracts for such right. I would also propose that, at least to certain classifications of lessors, the real property concept of leases be abolished; that the rule of severable covenants be abolished; and that pure contract

and equity rules be applied to leases.

Very truly yours,

ALBERT J. FORM

AJF:zm

1st Supp. Memo 68-74 EXHIBIT VI

CALIFORNIA REAL ESTATE ASSOCIATION
and California Real Estate Magazine

Telephone
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EXECUTIVE OFFICES
520 SOUTH GRAND AVE.
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11th and L Bldg., Suite 503
Sacramento, California
September 5, 1968

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
School of Law, Stanford University
Stanford, California 94305

Dear Mr. DeMoully:

Thank you for your letter of August 27 advising of the extension of time to September 12 for submission of comments of the California Real Estate Association on your proposal with respect to Abandonment of Leases.

It is possible that I can get this material in your hands by the 12th. I understand that if I am unable to that you will nonetheless circulate these comments and that they will receive consideration even though your report has been sent to the printer.

It appear at this time from reactions I have received from committee members who have studied the issue that we will have some rather significant objections to portions of your recommendation. I do not wish to transmit these to you in their present form without obtaining a consensus of the appropriate persons within CREA and I am attempting to precipitate such a consensus at the earliest possible time.

Unfortunately we have conflicted recently with vacation season (including my own following the session) and in ensuing days with requirements for attendance at a meeting of the California Constitution Commission on September 5 and 6 and the Senate Finance Committee considering Proposition 9 on September 10, 11 and 12.

In any event I will get these comments in your hands at the earliest possible time and I appreciate your patience and consideration which has been extended.

Sincerely,

Dugald Gillies
Legislative Representative

DG/jw
cc: W. R. Hamsher
H. J. Pontius

1st Supp. Memo 68-74 EXHIBIT VII
DONALD MCCLURE

September 5, 1968

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
School of Law
Stanford University
Stanford, California

Re: Tentative Recommendation of California Law Revision Commission Relating to Leases

Dear Mr. DeMoully:

Responding to your inquiry of August 28, 1968 regarding the above matter, I make the following comment:

You ask if I am aware of any problems that have arisen under Section 3308 in determining the "discount rate" for prepaid rent and, further, you ask "do you believe this matter should be dealt with in the statute, and if so, what provision I might suggest can be included in the statute?"

First, I am not aware of any problems that have arisen under CC Section 3308, because I have not been in a position to discover any.

Second, "discount rate" for prepaid rent to me, means the value of money paid in advance of the time due. Such a discount rate, should, in my opinion, be incorporated in the statute to avoid controversy and might be included under Section 1951.2 (b) after the word, "reletting" appearing on the second line from the bottom of page 15.

Sincerely,

Donald McClure

DMcC:rb

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1st Supp. Memo 68-74 EXHIBIT VIII

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CABLE ADDRESS
ROHL

September 7, 1968

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
School of Law, Stanford University
Stanford, California 94305

Re: Tentative Recommendations Relating to Leases

Dear Sir:

In response to your letter of August 28, 1968, I would like to make the following comment with respect to existing Civil Code Section 3308:

I suggest that the discount rate be handled as follows: The parties should be specifically authorized to fix the discount rate for this purpose in the lease itself. Minimum and maximum rates, however, should be set, and a rate should be automatically provided in the event the lease does not specify a figure. Perhaps the legal rate of interest could be incorporated by reference as the automatic rate in absence of a specific provision in the lease.

Very truly yours,

ALVIN G. BUCHIGNANI

AGB:eb

1st Supp. Memo 68-74 EXHIBIT IX

TISHMAN REALTY & CONSTRUCTION CO., INC.
SINCE 1898

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PHONE 385-9361

September 9, 1968

John H. De Moully, Esq.
Executive Secretary
California Law Revision Commission
School of Law
Stanford University
Stanford, California 94305

Re: Tentative Recommendations Related to Leases

Dear John:

I have reviewed the July 31, 1968 revision in the above matter and wish to recommend the two following major changes therein:

(a) Sec. 1951.2, Comment, Page 17: Granting for the sake of argument that the worth at the time of judgment of future rents "must be discounted to reflect the fact that it is being prepaid", I am sure that it would be unfair to both lessor and lessee to insert, in either the Comment or the Section, any fixed-figure as the rate of discount. Rather, the extent of discount of this prepaid item should be treated as a question of fact provable by affirmative evidence which,- as with all matters in diminution of lessor's prima facie case,- is the burden of the lessee. Since the judgment for future rent is analogous to a promissory note not yet due, the most objective measure of the proper discount rate is the commercial discount rate at the situs of the land from which the rent issues forth. I therefore recommend that the following language be added as a sentence after the third line on page 17 of the Tentative Recommendation:

> "The burden of proving the extent of such discount,- as with all matters in reduction of the lessor's claimed damages,- rests with the lessee, but the situation should normally be analogous to the discounting at a commercial bank of a promissory note not yet due."

(b) Secs. 337.5 and 339.5 of the Code of Civil Proceedure: Apparently the Commission inadvertently failed to consider the Statute of Limitations problem created by proposed Civil Code Section 1951.8. Inasmuch as Sec. 1951.8 grants the lessee a brand new cause of action to recover so much of an advance payment as he proves would result in a forfeiture if retained by the lessor, and since such a claim is not limited to merely an offset in an action brought by the lessor for damages due to lessee's breach, it is appropriate that some Statute of Limitations be provided with reference thereto. Obviously, the best Statute of Limitations is that established in the Tentative Recommendations for Civil Code Section 1951.2.

Your attention is invited to the enclosed "scratch-sheet" upon which I have indicated not only the extent and point-of-insert for these matters, but also additional technical recommendations and/or typographical corrections with respect to certain additional pages of the Tentative Recommendation.

Looking forward to seeing you on the evening of Thursday, September 26th, I am,

Cordially,

RONALD P. DENITZ
Assistant General Counsel

RPD:ere
encl.

1st Supp. Memo 68-74 EXHIBIT I

PRATT, BERMAN & CAMERA
ATTORNEYS AT LAW

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September 9, 1968

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
School of Law, Stanford University
Stanford, California 94305

Dear Mr. DeMoully:

Thanks so very much for furnishing me with tentative recommendation relating to leases.

Because of the shortness of time from your deadline of September 10 and receipt of this by me, I am replying in part and request you let me have three or four more days to comment on the proposed recommended legislation to be added to the Civil Code.

I am in accord with the Commission's conclusion that when the tenant breaches the lease and abandons the property, the lessor should have immediate right to sue for damages. Since a lease is a contract, the theory of anticipatory breach should be available to the landlord. There is only one California decision suggesting this right, which is Gold Mining Company v. Swinerton, 23 C. 2d 19 (1943). At page 31 the measure of damages would be the difference between what landlord may be able to rent the premises for and the price agreed to be paid under the lease. Or the lease itself might stipulate a fixed amount as liquidated damages to be paid in such event.

Likewise I concur in the Commission's recommendation lessor might in the alternative treat a breach by the tenant as a partial breach and sue for damages, or sue to cancel the lease. The duty of the lessor to mitigate damages under the existing law is unsatisfactory. I feel again that the principles of contract law should be applied and the burden of proof should be on the landlord to prove that he has made reasonable efforts. Lessor should be entitled to recover unpaid future rents less such amount as tenant proves could or could have been obtained by reletting the property to a similar type tenant acceptable to the lessor. Likewise the landlord should be entitled to recover for detriment caused by breach by tenant such as expenses

in retaking possession of the property, making repairs lessee had promised to make under the lease, advertising and real estate commissions to secure a new tenant. The only problem which is quite important in commercial leases is that it would be hard to prove in the beginning if it were a long term lease whether one could obtain another tenant with a favorable tax clause or not. This is an element of damage together perhaps with whether one could obtain a tenant who would be willing to pay insurance which could be most difficult to prove. It occurs to me the fairest way to both parties might be for our Civil Code to state a certain percentage of the unpaid future rents would be in full damages for all these claims. I think this is fair to both parties and see no other practical way to meet it.

With regard to forfeiture of advance payments, I feel that an advance payment of rent, or a payment termed consideration for execution of the lease should be applied to the damages fixed by the court. This would avoid the problem of forfeiture and immediately compensate the landlord for the loss of his bargain when the tenant defaults.

I likewise concur in amendment to 3308 of the Civil Code to limit its application to personal property and also not to make recommended legislation retroactive.

Thanking you for your anticipated indulgence in letting me have three or four more days beyond September 10 to comment on recommended legislation.

Yours very truly,

Orville C. Pratt, IV

OCP:sw

1st Supp. Memo 68-74 EXHIBIT XI

CALIFORNIA REAL ESTATE ASSOCIATION
and California Real Estate Magazine

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EXECUTIVE OFFICES
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Sacramento, California
September 11, 1968

Mr. John H. DeMoully
Executive Secretary
California Law Revision Commission
School of Law
Stanford University
Stanford, California 94305

Dear Mr. DeMoully:

The California Real Estate Association urges the California Law Revision Commission to hold its recommendations relating to Abandonment of Leases for further consideration and review. We reluctantly conclude that it would be necessary for us to oppose passage of legislation introduced to implement the proposal contained in the tentative recommendation of the Commission dated July 31, 1968.

An attempt is made in this communication to spell out to some degree our objections to the tentative recommendation but in general terms they result from the omission of significant new material to the law generally in such areas as liquidated damages, separate treatment for residential leases where warranted, specificity in definitions and others; and our objection to the particulars of the recommendations on mitigation, forfeiture of advance payments and some other points.

In more specific terms the following terms are made:

A. Section 1951---Definitions:

In defining "rent" to include charges equivalent to rent, we believe that language should be added, such as, "including but not limited to..." and then setting forth examples of equivalents. This would eliminate some vagueness and the need for court interpretation,

the effects of which are often not fully understood by smaller lessors or lessees. This definition could also incorporate permission to substitute a definition for rental equivalents in the lease itself.

We would also recommend the inclusion of a definition of "reasonable expenses of re-letting" as that term is proposed in Section 1951.2(b) to insure that such expenses include real estate broker's fees, attorney's fees, advertising, etc. We would be happy to attempt a definition of such if the Commission desires. (Note however our later stated reservations regarding mandated costs of re-letting).

B. Section 1951.2---Damages:

While the stated intention of the Commission is that the lessor shall have the immediate right to instigate an action and need not wait until the expiration of the original lease term, that is not specifically set forth. We believe that such a statement in the statute would be preferable. See Phillips Hellman v. Peerless Stages, 210 C 253; 291 P 178.

In Subsection (a) 2, the measure of damages is stated as "the worth at the time of judgment" of the unpaid rent. This is changed from the existing Section 3308 (and the change is effected in the revision of Section 3308 as proposed by the Commission as well) from "the worth at the time of termination". The reason for this change is not explained and it would seem obviously less advantageous to the lessor and may create additional hardship if the tenants breach is caused by insolvency.

It is our belief that the worth of the present rent should be calculated at termination, a date which is fixed and known when the action is commenced, rather than at the time of judgment. If there is any fluctuation in the rental market the litigation could be prolonged to influence the extent of damages.

In the comments on this same Subsection appearing on page 16 of your draft of July 31, it is indicated that at the time damages are ascertained the amount by which rental payments exceed the amount of avoidable rental loss must be discounted to reflect the fact that it is being prepaid. This is a procedure common in lease clauses. See Friedman, Preparation of Leases, page 48, note 15. Problems however can arise concerning the amount of discount. It is suggested that for clarification the section specifically provide that the parties may agree in advance to the rate of discount. The present silence of the section may be permission to so define the discount rate but this would depend upon court interpretation.

The principal change in this same subsection is the permitted

credit against unpaid rent for the mitigation to the extent that the lessee proves damage could have been reasonably avoided. Insofar as this involves re-leasing the premises we believe that it should be clearly stated that such re-leasing should only be required to a tenant of equal repute and for similar or equal purposes and further providing that the lessor is not required to expend money for such re-letting. Any required expenditure of money would in many instances only increase the lessor's loss.

Previously, Section 3308 was silent as to the matter of the burden of proof and as noted in the Commission's comments you have adopted a rule previously only applied in actions for breach of employment. In our view, it is doubtful whether this unrelated concept adds any measurable advantage to the section for we are unaware that this provision has proven its value in employment contract situations. Even under existing law the lessee has been permitted to offer such proof as he had to the effect that the lessor could have re-leased the property more advantageously. The added verbage may be just an illusion and may promote litigation or prolong such litigation.

We have made additional comments on mitigation under Section 1951.4.

Under subsection (a) (3), the provisions of Civil Code section 3300 allowing additional damages "proximately caused" is added. In considering this together with section 1951.6 as proposed, it would appear that attorney's fees even though incurred because of a lessee's breach and which would thus be "proximately caused" might not be recoverable unless they were specifically mentioned in the lease. Civil Code 1717 as added by AB 563, 1968, refers only to those cases where a contract specifically calls for the payment of attorney's fees. We suggest that it should be made clear either in this subsection or elsewhere in the Commission's proposal that attorney's fees proximately caused by the lessee's breach are collectible.

C. Liquidated Damages:

The comments accompanying the Commission's proposals (page 20, draft of July 31) state that "a prior decision holding liquidated damages provisions in leases to be void are no longer authoritative..." You cite the case of Seid Pake Sing v. Barker, 197 C 321; 240 P. 765 (1925). Much later cases, as for example McCarthy v. Tally, 46 C 2d 555 (1957) make liquidated clauses in leases void. We believe that this should definitely be clarified in the statute itself.

CREA was very disappointed that the Commission did not take the initiative to overcome the unfortunate and often ridiculous results of court interpretations of liquidated damage clauses as

does not have the resources or the expertise to give him similar protection. As is observed later, we believe that special innovative, imaginative treatment should also be provided for this special category.

E. Section 1951.8---Advance Payments:

1. This section would vest powers in a court by interpretation to ascertain what is an appropriate consideration in a lease contract even though that contract has been carefully drafted with adequate knowledge of all parties as to the impact and the consequences.

2. Currently in many situations this question of advance payments is dealt with in varying fashions because of the tax consequences which themselves can be a significant consideration in the amount of those advance payments. Section 1951.8 threatens to disrupt the possibilities of favorable tax consideration which can now often be garnered.

3. This section would seem to be an additional step in the direction of outside interference with contractual control and damages and represents a direct invitation to nuisance law suits. The parties can no longer agree to any forfeiture but must leave the "balancing of the equities" to the court.

4. The proposed section may also effect the determination of the trustee in bankruptcy's right to an advanced payment upon lessees breach caused by insolvency.

5. The staff draft of May 1, 1968, was an attempt to provide for an elective retention of deposit or advance payment as damages. We prefer that approach but believe that that draft would require further refinement if the Commission were willing to reinstate that concept.

6. Action in this field in either approach would seem to precipitate a requirement to protect the lessee against the loss of advance payment due to sale or foreclosure. See N. Y. Penal Law 1302a.

F. Separate Treatment for Differing Leases:

We have alluded previously in this communication to the need in our view to evolve separate provisions relating to damages under leases for each of several distinct types of leases. It seems to us that the Commission's tentative recommendation of July 31 is weighted to accommodate the large commercial lessor who is really a financier and who has many resources available to

n for his protection in the execution of leases.

While exceptions have been made for "net lease financing", and ase purchase agreements of public entities (to some degree), we el that further attention should be given to developing distinct es of leases for residential properties, commercial properties, perhaps leases of personal properiy.

Much of our objection is based on the failure to make such inctions as well as the specific omissions and objections ed herein.

don the length of this communication. We would be pleased to lt additional views should the Commission desire them.

Sincerely,

Dugald Gillies
Legislative Representative

bl
H. Jackson Pontius
W. R. Hamsher
George Coffin III
Kenneth R. Ladd
Erik Jorgensen
Lloyd Hanford
Henry Beaumont
Colonel Donald McClure

1st Suppl. Memo 68-74 EXHIBIT XII

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September 11, 1968

California Law Revision Commission
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Stanford, California 94305

Re: Tentative Recommendation Relating to Leases

Dear Sirs:

The undersigned has been requested by United States Leasing Corporation, a California corporation engaged in leasing industrial, transportation and office equipment and other personal property, to write you concerning its views, as a lessor, of the Commission's tentative recommendations, revised July 30, 1968, relating to leases. Those views are set forth in the memorandum enclosed herewith.

As the Commission may know, large scale industrial leasing originated in California in the post war years. It is estimated that more than a billion dollars of leases for industrial equipment alone are entered into each year in the United States, and the business is still growing. California has, of course, its share of the leases and, in addition, many leases of equipment in other states provide that they are governed by the law of California. United States Leasing Corporation feels, therefore, that any general legislation on leases should avoid creating new legal questions and resolve as many as possible of those that exist at present.

Respectfully,

John H. Wallace

JOHN H. WALLACE

JHW:mj
Enclosure

MEMORANDUM: Tentative Recommendation Relating to Leases - California Law Revision Commission

1. General

The tentative recommendation causes one general concern by creating doubt as to what principles of law - real property or contract - govern equipment leases.

The sections which are proposed to be added to the Civil Code (sections 1951 to 1952.6), express the intent to reform historical rules governing leases of real property by applying principles of the law of contracts. The exclusion of personal property leases from the sections provides a basis for litigants to argue that the legislature intended that the benefits conferred on lessors of real property by the proposed sections were not to be extended to lessors of personal property - instead leases of personal property are to be governed by the prior law of landlord and tenant, except as modified by section 3308. Those making this argument will find some support in the case of Automobile, et al. v. Salladay, 55 CalApp 219 (see particularly page 222) and in the practice of indexing some personal property lease cases under "Landlord and Tenant" in the General Digest (Key System).

The amendment of Section 3308 in accordance with the recommendation would not appear to overcome such an argument for the following reasons: a) in stating the lessor's remedies, proposed section 3308 omits some matters which are included in the sections which the Commission proposes be added, (the matters

stated in subparagraphs 3(b) and 3(c) of proposed section 1951.2 and the matters contained in proposed section 1951.4), thereby implying the imposition or rentention of restrictions in the case of personal property leases; b) the tentative recommendation itself lends support to the view that personal property leases are governed by the law of landlord and tenant except to the extent it is modified by section 3308 in that the comment to section 3308 (p. 35) equates personal property and real property leases by referring to the comment to proposed section 1951.2 "for further discussion"; and c) it is well known that section 3308 was enacted for the limited purpose of permitting a lessor, by specifically providing in the lease for the relief described in section 3308, to overcome the judge-made rule that a lessor cannot sue for entire breach of a lease until the end of the lease term.

It is reportedly the view of the Commission that personal property leases are (and should be) governed by the law of contracts. The comments to the proposed legislation do not, however, contain any expression of this view and subparagraph (a) (3) of section 3308 does not necessarily express it, as this is simply a repetition of what is provided in section 1951.2, in a statute which is subject to a very narrow construction.

If the Commission is proceeding on the assumption that contract rules apply generally to personal property leases and that it is not intended by the enactment of section 1951 to 1952.6 to deny to a lessor of personal property any remedy or benefit conferred on a lessor of real property by the proposed sections or to prohibit any otherwise lawful agreement between a

lessor and lessee of personal property, it would appear, at the very least , that the comments should reflect this assumption and, ideally, section 3308 itself should so state.

2. Proposed Amendment of Section 3308

a. Mitigation of damages

The Commission has considered the effect of "net financing" in determining what remedies should be available to a lessor of real property. This consideration is equally applicable to leases of personal property. The typical equipment lease provides for rentals that are designed to return the cost of the equipment, plus a reasonable profit, to the lessor over the primary term of the lease (without consideration of the residual value of the equipment, renewals or options to purchase). The lease is assigned customarily to a lending institution as security for a loan with which the equipment lessor pays for the equipment. The lessor and lender each assume that in the event of a breach by the lessee, the remedies provided for by the lease and Civil Code section 3300 will be applicable. It is believed to be understood generally that the remedies available as a matter of law (consistent with section 3300) in the event of a breach of the entire lease agreement and repossession of the equipment permit the recovery against the lessee of the following: the amount of unpaid rental installments falling due to the time of judgment with interest thereon at the legal rate or such higher lawful rate as may be specified in the lease from the time each falls due; the amount of the rentals which would have been received

after judgment, discounted to value at the time of judgment at such rate as to yield a compensatory sum; if the equipment has been sold, the amounts expended prior to sale to repossess, store, insure, and pay taxes on it, the expenses of sale, and the value the equipment would have had at the end of the lease term, (lesser's reversionary interest); if the equipment has been relet, the amounts expended prior to reletting to repossess, store, insure and pay taxes on it and the expenses of reletting. Against these amounts the lessee is entitled to credit for the actual proceeds of sale or reletting, or such larger amounts as the lessee can prove should have been obtained by the lessor if the lessor acted in a commercially reasonable way. Credit is to be applied as of the time of actual receipt (or when it should have been received if the lessor did not act in a commercially reasonable way), first to interest then to principal.

Consistent with the investment or financial nature of an equipment lease, a recent California case, Challange-Cook Bros., Inc. v. A.G. Lantz, 64 Cal Rptr 239, 256 ACA 597, held that a lessor who was ready, able and willing to perform could recover rentals due as they accrued, even though the lessor has repossessed the equipment. In another recent case, Associates Discount Corp. v. Tobb Co., 241 CA2 541, 50 Cal Rptr 738, it was held that where the lessee was allowed to remain in possession, the lessor could accelerate the rent and recover judgment for the full amount thereof. Neither case imposed any condition that the lease allow assignment or subletting. The remedies were provided for in the leases themselves.

The financial nature of the equipment lease makes remedies such as those enforced in the Lantz and Tobb cases

highly desirable and fair when the lessee is solvent but recalcitrant. On the other hand, if the lessee is insolvent, the economic reality that the money it gets from sale or relet-ting may be all that it will ever collect, will force the lessor to try to mitigate. It would appear appropriate, therefore, that the comment to section 3308 contain a statement excluding any implication from the provisions on mitigation and from proposed section 1951.4 that the parties are not free to provide by contract for remedies such as those that were contained in the leases in Lantz and Tobb, or that the section itself so provide.

b. Interest

That portion of section 3308 making the measure of damage in part subject to deduction for avoidable rental loss creates a serious question as to the allowability of interest before judgment. The Commission comments (on page 16), that interest must be added to the amount by which the rental payment exceeds the amount of avoidable rental loss, but there is no wording to overcome the specific provisions of section 3287 limiting interest to "damages certain or capable of being made certain by calculation" or the holding in Peterson v. Larquier, 84 CalApp 174. (See also Rose v. Recht, 94 CA2 662.)

The statement in Coleman Engineering Co. v. North American Aviation, Inc., 65 Cal 2d 396, that"...reductions in damages due to plaintiff's efforts to mitigate damages should not preclude an award for prejudgment interest....", is not to be construed as applying to a situation where the very measure of damages is the amount by which the rents receivable under

the lease exceeds the amount of rental loss, "...that could have been or could be reasonably avoided;...." In the Coleman Engineering case, the unliquidated credits or offsets consisted of reduction of damages "due to settlement of claims and salvage of materials." It would appear that to overcome the specific provisions of Civil Code section 3287, section 3308 should, at a minimum, describe the amounts proved by the lessee as rental loss that could have been avoided as unliquidated credits or offsets, but preferably should provide specifically for prejudgment interest on the difference between the rental loss and the amount thereof that was or could have been avoided. If such interest is not allowed, the lessor is deprived of the benefit of his bargain and may even incur a loss.

c. Discount rate

The intent expressed in subsection (a) of section 3308 (and the same subsection in section 1951.2) is apparently that the worth at time of judgment of any rental payments that would have fallen due after the date of the judgment be determined by applying a discount rate for the purpose of obtaining a "present value" as of the time of judgment of the future rentals. Selecting an appropriate discount rate is not a simple matter, of course, but if the matter is left unresolved, the courts may end up with very different conclusions on very similar facts. As a solution, section 3308 could contain a provision permitting the lease to establish a discount rate.

The Commission's comment at page 20 that the parties may provide for liquidated damages is questionable, and appears

to ignore the opinion in Electrical Products Corp. v. Williams 117 CA2 Supp 813. Specific statutory language may be necessary to overcome Civil Code sections 1670 and 1671. The Commercial Code, in its section 2718, permits such provisions in the case of sales, thereby recognizing the desirability of such provisions under modern business conditions.

d. Mandatory nature of section 3308 as amended.

The amended section would appear to require an express exclusion of its application to a lease of personal property. This may create an implication that its provisions express a legislative or public policy so that remedies provided by a lease are not enforceable unless they are consistent with that policy. It would appear that the section would still achieve its primary purpose of establishing a cause of action, before the end of the lease term, for an entire or material breach of the lease by providing that, in addition to any remedies provided by the lease or conferred by law, a lessor "may" recover from the lessee according to the damages rules set forth in the amended section.

e. Right to sell

Experience has shown in the case of personal property leases, that in most instances it is impractical to relet the equipment after default by the lessee and repossession. Since the greatest mitigation in such cases is achieved by sale of the equipment, the comment might well state that nothing in section 3308 is to be construed as prohibiting sale rather than reletting if the evidence establishes that sale was the most effective way to mitigate.

f. Use of word "termination"

The use of the word "termination" in section 3308 is questionable. As used in this section it appears to have a meaning inconsistent with its definition in the Commercial Code [see section 2106 (3)] and in some cases (see Corbin, Contracts section 1229, 1952 edition), where it has been interpreted to mean a complete relinquishment of rights by the non-breaching party. The term is made ambiguous also by the fact that section 1951.2 contains an express reservation of indemnification rights under the lease "for liability arising prior to termination of the lease", while section 3308 does not contain any such reservation.

In summary, in the interest of not creating more legal issues and of assuming that personal property leases are governed by the law of contracts and the rule that damages should be compensatory, it is submitted that any proposed legislation on leases should do the following:

a. Make it clear that leases of personal property are subject to the law of contracts, including specifically section 3300 of the Civil Code;

b. Make it clear that the benefits of any statutory changes in the law or landlord and tenant based on contractual principles may be applied to personal property leases but that such statutory changes do not imply any limitation on the use of provisions in leases of personal property which would otherwise be lawful;

c. Authorize specifically the allowance of prejudgment interest;

d. Authorize the setting of a discount rate by agreement for determining present value;

e. Make the provisions of section 3308 optional rather than mandatory when the lease fails to "otherwise provide";

f. Recognize the right of the lessor to sell repossessed equipment when sale will result in the greatest mitigation; and

g. Define the word "termination" or consider using some other word or clause so as to have uniformity of meaning of contractual terms and not create ambiguities.