

11 USC §365  
ORS 71.2010(37)(a)

In re Colin

Case No. 391-32884-H13

10-30-91

The court held that two agreements between the debtors and a creditor were true leases under ORS 71.2010(37)(a) and must be assumed or rejected under §365. Since the debtors' plan failed to treat the agreements as leases, the creditor's objection on that basis was sustained.

P91-32(10)

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UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF OREGON

In Re )  
 ) Case No. 391-32884-H13  
MICHAEL V. COLIN )  
SANDRA K. COLIN ) OPINION  
 )  
Debtors. )

This matter comes before the court upon an objection to confirmation of the debtors' proposed chapter 13 plan. The objections were filed on behalf of Affordable Rent To Own, Inc. dba Rentown USA ("Rentown"). The debtors are represented by Magar E. Magar of Portland, Oregon and Rentown is represented by Kolleen Sebby, of Vancouver, Washington.

The creditor objects to the proposed plan on the ground that it treats two agreements it entered into with one of the debtors as one contract of sale rather than two leases. One of the agreements was entered into on August 1, 1989 (the "first agreement") and the other on June 8, 1990 (the "second agreement"). Both agreements

1 allow the debtor to terminate the contract at any time without  
2 further obligation to pay. Both agreements also provide that upon  
3 completion of the payments under the agreements, the debtor becomes  
4 the owner of the goods in question without further obligation.  
5 Upon early termination of the agreements by failure to pay or  
6 otherwise, the debtor must return the goods. It appears undisputed  
7 that the debtor is in default under both agreements. Copies of  
8 both agreements are attached as exhibits "A" and "B". The creditor  
9 argues that the agreements are true leases and must be assumed or  
10 rejected under 11 U.S.C. §365.

11 The debtors respond that the agreements are actually contracts  
12 of sale under Oregon law and can be treated as such in the plan.  
13 Alternatively, the debtors argue that, even if the agreements are  
14 true leases, the contracts are unconscionable under Oregon law and  
15 should not be enforced. The unconscionability argument stems  
16 solely from the allegation that the price charged for the use or  
17 purchase of the goods is too high. The debtors request a further  
18 hearing to offer evidence as to the appropriate price for the goods  
19 in question.

20 1. Contract of sale versus lease.

21 a. The Second Agreement.

22 At the time the second agreement was entered into, ORS  
23 71.2010(37)(a) provided the following:

24  
25 Whether a transaction creates a lease or  
26 security interest is determined by the facts

1 of each case; however, a transaction creates a  
2 security interest if the consideration the  
3 lessee is to pay the lessor for the right to  
4 possession and use of the goods is an  
5 obligation for the term of the lease not  
6 subject to termination by the lessee ... .  
7

8 Since the second agreement does not create an obligation for  
9 the term of the lease and is subject to termination by the lessee,  
10 ORS 71.2010(37)(a) does not require that the court treat the  
11 agreement as a contract of sale and security interest. Thus, the  
12 court must determine whether the facts of this case are sufficient  
13 to cause the court to treat the agreement as a contract of sale.

14 The principle feature of a contract of sale is that the buyer  
15 becomes obligated to pay the purchase price of the goods in  
16 exchange for the right to receive title to the goods. Thus, where  
17 an alleged lease agreement provides that the lessee may terminate  
18 his obligations under the agreement at any time for any reason with  
19 no further obligation to pay, the agreement cannot be a contract of  
20 sale.

21 When faced with a similar contract, the Bankruptcy Court for  
22 the Northern District of Oklahoma made the following observation:

23 Under the terms of the Agreement, the lessee  
24 is not required to make the payments but can,  
25 at any time, unilaterally terminate the  
26 Agreement and return the property. This is  
27 the essence of a lease.  
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29 In re Blevins, 119 B.R. 814, 817 (Bankr. N.D. Okla. 1990). This  
30 court agrees. Thus, the court concludes that the second agreement  
31 is a true lease.

1           b. The First Agreement.

2           The first agreement was entered into in August, 1989 and is  
3 governed by the law in existence at the time it was entered into.

4 At that time, Oregon law provided as follows:  
5

6           Whether a lease is intended as security is to  
7 be determined by the facts of each case,  
8 however, . . . an agreement that upon  
9 compliance with the terms of the lease the  
10 lessee shall become or has the option to  
11 become the owner of the property for no  
12 additional consideration or for a nominal  
13 consideration does make the lease one intended  
14 for security.  
15

16           ORS 71.2010(37).  
17

18           If the literal language of this statute is applied to the  
19 first agreement, the agreement must be treated as a contract of  
20 sale. On the other hand, as just discussed, it would be absurd to  
21 hold that an agreement that does not require the lessee to pay the  
22 purchase price of a good is a contract of sale. Indeed, the  
23 provisions of the termination clauses in the contracts at issue  
24 embody "the essence of a lease." Blevins, at 817.

25           The language of the statute reveals that the purpose of ORS  
26 71.2010(37) is to effectuate the contracting parties' intent  
27 regardless of the title they give to their agreement. In a  
28 contract of sale, the parties intend that the purchaser will pay  
29 the purchase price of the goods over time and will ultimately  
30 acquire title to the goods.

31           If a "lessee" must pay the entire lease obligation and then

1 has the option to buy the goods for a price that is substantially  
2 below market value, it is difficult for the "lessor" to  
3 convincingly argue that a sale wasn't intended all along. The key  
4 facts are:

- 5 1. That the lessee MUST pay the entire contract price; and
- 6 2. That the option price is significantly less than the value  
7 of the property so that the lessee cannot, as a practical  
8 matter, refuse to exercise the option.

9 In this case, the first element is missing. Since the lessee  
10 can terminate the agreement at any time, it does not appear that  
11 the parties intended a sale rather than a lease. Thus, there is no  
12 reason to treat the agreement as a contract of sale except for the  
13 literal language of the statute.

14 A court may not normally refuse to apply the literal language  
15 of a statute. U. S. v. Ron Pair Enterprises, Inc. 489 U.S. 235  
16 (1989). A court may do so, however, if rote application of the  
17 statute will lead to an absurd result. U. S. v. American Trucking  
18 Assns., Inc., 310 U.S. 534 (1940). This court believes that a  
19 literal application of the statute in question would lead to an  
20 absurd result. Such an interpretation would call an agreement a  
21 contract of sale even though it lacked one of the essential  
22 elements of a contract of sale, namely an obligation to pay the  
23 purchase price agreed upon. Thus, the court rules that the first  
24 agreement is also a true lease.

1 2. Unconscionability.

2 The debtors argue that both contracts are unconscionable  
3 because the total price to be paid for the goods leased under the  
4 agreements greatly exceeds the value of the goods. In effect, the  
5 debtors argue that a lease may be declared unconscionable solely on  
6 the ground that the rental charged by the lessor is too high.

7 The debtors argue that they should be permitted to present  
8 evidence concerning the details of the lessor's financial affairs  
9 so that the court can determine what a "reasonable profit" would be  
10 for the lease of goods such as these.

11 The debtors have not cited any Oregon authorities to the  
12 effect that price alone can render a contract unconscionable. The  
13 debtors have cited several cases from other jurisdictions that  
14 consider price in assessing whether a contract is unconscionable.  
15 In every case reviewed by the court on this issue, however, there  
16 have been other facts present that indicate overreaching or  
17 inequitable conduct on the part of the seller or lessor in addition  
18 to the consideration charged under the agreement. No such  
19 additional facts have been alleged by the debtors in this case.

20 Moreover, this court believes that price alone may not render  
21 a contract unconscionable. It is not appropriate for a court to  
22 substitute its judgment for that of buyers and sellers in a free  
23 market. Such action by the courts would ultimately result in a  
24 controlled economy that limited an honest seller's profit or an

1 informed buyer's ability to obtain a bargain and would completely  
2 undermine the economic principles upon which the economy of this  
3 country operates.

4 The common law instructs that a court will not examine the  
5 adequacy of consideration. While the Uniform Commercial Code was  
6 intended to change certain aspects of the common law and to grant  
7 consumers special rights, there is no indication that the UCC was  
8 intended to supplant this fundamental and necessary aspect of the  
9 law. This is especially true where there is no allegation of  
10 wrongdoing or inequitable conduct on the part of the lessor.

11 Finally, the court recognizes the axiom that a contract will  
12 be considered unconscionable where it shocks the court's  
13 conscience. Such a finding should require exceptionally egregious  
14 facts. In this case, the agreements clearly point out that the  
15 lessee has no obligation to retain the goods and that he may  
16 terminate the agreement at any time. The agreements even explain  
17 to the lessee that he may acquire the goods at a lower total cost  
18 if he simply purchases them outright. Also, the second contract  
19 provides that the first month's rent is free. Thus, under that  
20 contract, the lessee could have retained the goods for one month  
21 and then returned them without having paid or become obligated to  
22 pay the lessor anything.

23 It also appears that the debtor went to the lessor after the  
24 first contract had been in force for nearly a year and executed a



1 second, nearly identical agreement for the rental of additional  
2 property. If the first agreement's terms were so unfair as to be  
3 unconscionable, it is unlikely the debtor would return nearly a  
4 year later for more economic abuse.

5 When considering the agreements as a whole, the court  
6 concludes, as a matter of law, that the agreements are not  
7 unconscionable in any respect. Accordingly, Rentown's objection to  
8 confirmation will be sustained. The court will enter an order  
9 requiring the debtors to promptly assume or reject the leases under  
10 \$365 and denying confirmation of the proposed plan. Having so  
11 ruled, the court perceives no need for an evidentiary hearing at  
12 this time.

13 DATED this \_\_\_\_\_ day of October, 1991.

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16 Henry L. Hess, Jr.  
17 Bankruptcy Judge  
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25 cc: Magar E. Magar  
26 Kolleen Sebby  
27 Robert W. Myers, Trustee