

WHAT'S NEW IN THE LAW

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Ability to Collect Rentals Under Article 2A Finance Leases or Leases with “Hell or High Water” and/or Waiver of Defenses Provisions

Wells Fargo Bank Minnesota, National Association v. CD Video, Inc., 802 N.Y.S.2d 423 (App.Div. 2005) *

This decision affirms a lower court's grant of summary judgment in favor of an assignee of an equipment lease containing a waiver of defenses, stating that a good-faith, for-value assignee was not required to prove the original lessor's performance as a condition of enforcing the lessee's obligations.

Wells Fargo Bank, N.A. v. BrooksAmerica Mortgage Corporation, 419 F.3d 107 (2nd Cir. 2005)

In a case in which the lessee entered into a sale-leaseback of computer equipment but was never paid by the lessor, the U.S. District Court for the Southern District of New York granted a motion for summary judgment by the lessor's assignee for past due payments and a declaration that the lessee remains obligated for remaining payments due under the lease (2004 WL 2072358). The district court decision strongly supported the enforcement of waiver of defense and “hell or high water” provisions – whether or not the lease qualifies as a true lease governed by Article 2A. The Second Circuit affirms; however, its reasoning highlights the sophistication of the lessee without indicating the significance of that characterization.

Lyon Financial Services, Inc. v. Woodlake Imaging, LLC, 2005 WL 331695 (U.S. Dist. Ct. E.D. Pa. Feb. 9, 2005)

In deciding a motion by an assignee of a lessor to dismiss certain counterclaims and defenses of the lessee, while the court finds that it cannot determine the outcome without an evidentiary record, it does have occasion to comment upon Article 2A's finance lease “hell or high water” provisions and Article 9's waiver of defense provisions. The court strongly endorses a number of examples of enforcement of “hell or high water” provisions including one that notes how important such provisions are for the leasing industry. However, the court also seems more hesitant to enforce such provisions than the District Court in the *BrooksAmerica* case discussed above if the purported lease turns out instead to create a security interest. The court also makes note of the criteria given in Article 9 for an assignee to enforce a waiver of defense provision. It is important to remember that while often having the same effect, these two different types of provisions emanate from different parts of the UCC and may need to be distinguished.

Sony Financial Services, LLC v. Multi Video Group, Ltd., 2005 WL 91310 (U.S. Dist. Ct. S.D.N.Y. Jan. 18, 2005), report and recommendation adopted by 2005 WL 309753 (U.S. Dist. Ct. S.D.N.Y. Feb. 9, 2005)

A lessor's summary judgment motion is granted notwithstanding the lessee's claims that equipment and services to be provided by an affiliate of the lessor were not as promised. The court cited language in the lease clearly distinguishing between the lessor and the equipment vendor, and cited cases enforcing Article 2A finance leases in which the lessor was an affiliate of the equipment vendor.

Eureka Broadband Corporation v. Wentworth Leasing Corporation, 400 F.3d 62 (1st Cir. 2005)

After entering into an Article 2A finance lease, the lessee discovered that the lessor had never paid either of the two equipment vendors when the vendors began demanding money from the lessee. After returning the equipment to the vendors (along with the payment of some money), the lessee sued the lessor for rental payments made to the lessor. The lessor counterclaimed that the "hell or high water" provision in the lease and the finance lease provisions of Article 2A entitled it to continued payments under the lease. This decision affirms the lower court's awarding of damages to the lessee and holds that fraud on the part of a lessor constitutes an exception to 2A-407, entitling a lessee to cancel the lease.

Fillmore v. Leasecomm Corporation, 2004 WL 3091642 (Mass. Super. Nov. 15, 2004)

In determining that a purported lease was not unconscionable, the court characterizes the agreement as a standard Article 2A finance lease arrangement (notwithstanding that the subject matter of the agreement was a license for accessing an internet payment gateway enabling merchants to process credit card transactions rather than a transfer of a right to possess goods). The court notes that the lessor was acting as a financing source only and was not responsible for failures on the part of the service provider.

Copelco Capital, Inc. v. Johnson, 2004 WL 1559652 (Cal. App. 2 Dist. July 13, 2004) (not officially published)

Summary judgment in favor of an assignee of a lease of a copier is upheld based upon the "hell or high water" and waiver of defenses provisions found in the lease, notwithstanding the failure of the original lessor to service the copier as required by the lease. The court commented that the assignee had not sought to collect payment of amounts due on the maintenance agreement, though it was not made clear whether or how the lease distinguished between payments for maintenance and those strictly for the use of the equipment.

Rhythm & Hues, Inc. v. The Terminal Marketing Company, Inc., 2004 WL 941908 (U.S. Dist. Ct. S.D.N.Y. May 4, 2004)

Without any evidence of bad faith on the part of the assignee, Wells Fargo Bank Minnesota, a summary judgment motion by such assignee on the enforceability of a waiver of defenses clause in a lease is granted. At the same time, the court denies a summary judgment motion by the lessee with respect to a different lease based in part on

an argument that the lessee's obligations had not commenced because the lease indicated no commencement date (the lessee having not challenged the commencement of other leases also indicating no commencement date).

Jaz, Inc. v. Foley and First Hawaiian Leasing, Inc., 85 P.3d 1099 (Hawai'i Intrmed.Ct. App. 2004)

Notwithstanding its having signed an acceptance certificate in connection with a "hell or high water" master lease, a lessee that never received the equipment is found not to have become obligated to make all rental payments and not to bear the risk of loss either under the terms of the lease or under Article 2A finance lease provisions. Analyzing this transaction under leasing law (despite referring to the lessee as having purchased or acquired the equipment under its lease with the lessor), the court emphasizes that a lessee must have a reasonable time to inspect the equipment before being said to have accepted it. The court points out that the lessor could have had the lessee agree to be responsible for reimbursing the lessor in the event that the lessor was required to pay the vendor before shipment and the equipment was not delivered. The decision raises issues for lessors who rely on acceptance certificates without somehow verifying delivery and the passage of a reasonable time to inspect.

Harte-Hanks Direct Marketing/Baltimore, Inc. v. Varilease Technology Finance Group, Inc., 299 F.Supp.2d 505 (D. Md. 2004)

In the course of discussing a lessee's obligation under a lease of printing equipment that also provided for servicing of the equipment by the lessor, the court holds that the enforceability of a "hell or high water" obligation to make lease payments is not affected by the lessor's failure to provide the services. The decision does, however, permit the lessee to attempt to prove fraud in the inducement to enter into the lease, in which case the lease would be voidable at the option of the lessee.

Wells Fargo Bank Minnesota, N.A. v. Nassau Broadcasting Partners, L.P., 2003 WL 22339299, 52 UCC Rep.Serv.2d 249 (S.D.N.Y. Oct. 10, 2003)

Lessee held to have unconditional obligation to make lease payments under "hell or high water" provision in lease notwithstanding lessor's failure to make all payments owing to lessee under sale/leaseback arrangement – based upon finding that lessee had agreed that its rent payment obligations commenced after disbursement of "any" (as opposed to "all") funds by lessor. In the context of discussing the validity of assignments of the lease by the original lessor, dicta in the decision erroneously refer to a "hell and high water" provision as "simply one variant of a waiver of defense and is subject to U.C.C. Sec. 9-403."

Unistar Leasing v. Lipkin, 2004 WL 2650825 (N.Y.App.Div. Nov. 19, 2004)
Unistar Leasing v. Betco, Inc., 2004 WL 2650771 (N.Y.App.Div. Nov. 19, 2004)
Preferred Capital, Inc. v. Sturgil, 2004 WL 1882865 (OhioApp. 9 Dist. Aug. 25, 2004)
Information Leasing Corporation v. King, 800 N.E.2d 73, 155 Ohio App.3d 201 (Ohio App. 2003)
Information Leasing Corporation v. Borda, 2003 WL 22103377 (OhioApp. 1 Dist. Sept. 12, 2003)
Information Leasing Corporation v. Chambers, 789 N.E.2d 1155, 152 Ohio App.3d 715 (OhioApp. 2003)
Information Leasing Corporation v. GDR Investments, Inc., 787 N.E.2d 652, 152 Ohio App.3d 260 (OhioApp. 2003)

Series of cases upholding the “hell or high water” obligations of lessees (and their guarantors) signing Article 2A finance leases. The lessees had ATM machines installed on their business premises by Credit Card Center, a vendor of ATM services who offered lease financing to lessees approved by the lessor. After the vendor filed bankruptcy, it ceased servicing the ATM machines and the lessees ceased making payments under the leases. These decisions held that the lessees remained liable under apparently well-drafted leases – good unconditional payment language, thorough Article 2A finance lease provisions, disclaimers of warranties regarding the equipment, statements that the lessor was not responsible for the vendor’s acts -- notwithstanding lessee claims that the vendor’s false promises were to be attributed to the lessor. However, certain of these decisions also held that both common law and Article 2A require a lessor to minimize damages – something the lessor had failed to do in some instances when it did not pick up the machines after being notified that they were available.

True Lease versus Security Interest: In General

Cook Sales, Inc. v. Shores (*In re Shores*), 332 B.R. 31 (U.S.Dist.Ct. M.D.Fl. 2005) *

Notwithstanding the fact that the lessee had the right to terminate the lease at any time, the Bankruptcy Court in this district held that a lease was not a true lease because the lessee had the option of purchasing the goods (a portable building) for no additional consideration after paying rent for thirty-six months, at which time the goods were expected to have a remaining useful economic life extending well into the future. The District Court reverses on the ground that a lessee’s right to terminate at any time (i.e., where the lessee has no obligation to make rental payments for any period of time past the latest rental period) strongly indicates that the lease is a true lease, along with the equipment’s lengthy useful life and various requirements in the lease regarding protection of the lessor’s interest in the equipment.

United Airlines, Inc. v. HSBC Bank USA, N.A., 416 F.3d 609 (7th Cir. 2005), rehearing and rehearing en banc denied (Aug. 23, 2005), petition for cert. filed (Nov. 18, 2005) *

The Seventh Circuit holds that a particular airport facilities lease entered into by the airline debtor is a secured loan, and not a true lease, for purposes of federal bankruptcy law. Although the subject matter of the lease was not personal property, the court’s discussion of the extent to which state law concerning the distinction between true

leases and security interests controls federal bankruptcy law relating to that same subject is instructive – and potentially threatening to the treatment of TRAC leases in bankruptcy. According to the court, “A state law that identified a ‘lease’ in a formal rather than a functional manner would conflict with the Code, because it would disrupt the federal system of separating financial from economic distress...”

In re Bailey, 2005 WL 1120308 (Bankr.W.D.Ark. May 10, 2005)

In determining whether a purported lease of two trucks was a true lease, the court holds that the lessee had no other reasonable alternative than to exercise his purchase option, which the court characterizes as “nominal.” Rather than finding nominality simply as a result of the option price being substantially below the expected residual value, the court appears to consider lost opportunity cost when considering whether the facts fit the statute’s statement that “additional consideration is nominal if it is less than the lessee’s reasonably predictable cost of performing under the lease agreement if the option is not exercised.” The court also cites the *Buehne* case discussed below for the proposition that certain factors – even those that are listed in the statute as not in themselves implicating a security interest – are “signposts indicative of a sale.”

In the matter of Sanford, 2005 WL 629022 (Bankr.M.D.La. Jan. 31, 2005)

The lessee had entered into an equipment rental agreement providing for no specific term, month-to-month rental payments, and a purchase option that would apply a portion of the rental payments made toward the purchase price. Because the lease was terminable at any time by the lessee, the court holds that the lease did not create a security interest, denies the lessee’s claim that it had purchased the equipment and holds that the lessor had terminated the lease before the lessee filed for bankruptcy and thus had the right to recover the equipment.

In re Buehne Farms, Inc., 321 B.R. 239 (Bankr.S.D.Ill. 2005)

In deciding that a lease of cows was actually a disguised security agreement, the court focuses on the “economic realities” of the transaction (in this case, the fact that no reasonable lessee would fail to exercise the purchase option), but also includes some confusing analysis such as identifying nominality of a purchase option price with the economic realities test and, in dicta, citing other factors as pointing to the creation of a security interest such as the lessee bearing the risk of loss and costs of insurance, upkeep and taxes, which factors are listed in the statute as not in themselves implicating a security interest. Although this lease contained a residual guaranty by the lessee similar to TRAC provisions in motor vehicle leases, the decision does not discuss the economic effect of such a provision.

Perez v. Rent-A-Center, Inc., 375 N.J.Super. 63, 866 A.2d 1000 (App.Div. 2005)

Although this decision does not discuss the distinction between leases and security interests directly, it provides an interesting perspective on the treatment of “rent-to-own” contracts. It concludes that neither the New Jersey Retail Installment Sales Act nor its criminal usury statute is applicable to the contracts at issue, primarily because the customers were not bound to make all the payments which would entitle them to become the owners of the goods. An Appendix to the decision lists applicable statutes in other

states, most of which (unlike New Jersey) have statutes explicitly regulating rent-to-own contracts as a distinct transactional form.

In re Grubbs Construction Company, 319 B.R. 698 (Bankr.M.D.Florida 2005)

In the course of finding a number of purported leases (which, if true leases, would have constituted executory contracts subject to termination prior to bankruptcy) to be secured transactions, this court manages to invoke many different concepts employed in other cases and in commentary for distinguishing between true leases and secured transactions. With respect to four of the five leases, the court appears to rely heavily on its determination that, given the particular terms of those lease schedules, the lessee had little economic choice other than to purchase the equipment under an early buyout option. With respect to the fifth lease, referred to as a TRAC lease, the court finds that the economic substance was no different than a typical installment loan with a balloon payment at the end. Evidently this TRAC lease did not involve motor vehicles (the type of equipment was not identified), which likely would have necessitated consideration of a state TRAC statute, inasmuch as the court's discussion of perfection of the lessor's security interests involved only the filing of UCC financing statements, and not notation of liens on certificates of title.

CIT Technology Financing Services, Inc. v. Tricycle Enterprises, Inc., 787 N.Y.S.2d 133 (App.Div. 2004)

A lease with a five-year term and a purchase option of "10% of Total Cash Price" is held to be a true lease. The court first determined that "total cash price" should be read to mean the total of all payments to be made over the five-year term of the lease (rather than the price of the equipment at the beginning of the lease). Ten percent of that aggregate amount equaled thirty percent of the anticipated remaining market value of the equipment at the end of the lease term. Because the lease stated that it was governed by Massachusetts law, the court determined that the lease was a true lease based upon a "rule of thumb" employed by Massachusetts courts that a purchase option price greater than twenty-five percent of market value at the end of the lease term should not be considered "nominal" and thus not creating a security interest under Section 1-201(37).

Fifth Third Bank v. Roberts, 2004 WL 2785955 (Ohio App. 3 Dist. December 6, 2004)

In finding a purported lease to be a true lease, this court focuses both upon the intent of the parties as evidenced by the wording and provisions of the lease document (notwithstanding the Official Comment to the UCC definition of "security interest" in which the focus of the definition was stated to have shifted from intent to economics) as well as the economic fact that the purchase option amount was not nominal.

Ray Lebron d/b/a Lebron Electronics v. Citicorp Vendor Finance, Inc. f/k/a Copelco Capital, Inc., 2004 WL 1615837 (Tex.Ct.App. July 20, 2004)

Judgment in favor of a lessor is affirmed in which the lessee had unsuccessfully argued that equipment leases were transactions creating security interests and were usurious. The court applies what is sometimes referred to as a "bright line" version of UCC Section 1-201(37) by stating that in order for a lease to create a security interest, the transaction must not be subject to termination by the lessee and at least one of four

additional factors must be satisfied. After finding none of such four factors to apply in this case, the court holds that the transactions are leases. This analysis contrasts with decisions of other courts that have looked at other facts (sometimes referred to as “economic realities”) in holding that a security interest has been created even when the “bright line” test for true lease status has been passed.

In re Fleming Companies, Inc., 308 B.R. 693 (Bankr.D.Del. 2004)

Responding to a motion by a lessor for assumption or rejection of a lease, the court holds that the purported lease creates a security interest under 1-201(37), primarily because the equipment will have little or no value at the end of the lease term and also because the economic realities were such that the lessor would have no incentive to take the equipment back at the end of the lease term.

Legends Gym v. ABCO Leasing, 383 F.Supp.2d 911 (W.D.Texas 2004)

The lessee attempted to argue that it was not liable for failing to make payments under a lease because the lease was actually a usurious loan – void and unenforceable. The court holds that the transaction was a lease, rather than a secured loan, because the lessee was not obligated to buy the equipment, the rental payments were not applied to the purchase price, and the purchase option price was fair market value, which the court says, “by definition, is not nominal.” The decision does not touch on other issues (which may not have been raised by the parties), such as the economic life of the equipment, that might bear on true lease status.

Sankey v. ABCO Leasing, Inc. (In re Sankey), 307 B.R. 674 (D. Alaska 2004)

An interesting discussion of the factors to be employed in determining whether a purported lease is true or not. After quoting from *White & Summers* regarding the need in some cases to look beyond the “per se” or “bright line” tests for creation of a security interest in order to determine whether a transaction provides the lessor with a meaningful reversionary interest – and is therefore a true lease – the court expresses what it believes should be the basic test: “If the lease terms provide that at the end of the lease the lessor will receive either return of the leased goods or the reasonably predicted fair market value the goods will have at the time the option is to be performed, the lessor has retained a meaningful reversionary interest.”

Duke Energy Royal, LLC v. Pillowtex Corporation (In re Pillowtex, Inc.), 349 F.3d 711 (3rd Cir. 2003)

Application of 1-201(37) to a services agreement providing for the use of equipment by Pillowtex with rather unusual end-of-term provisions giving the lessor a number of options with regard to that equipment. In deciding that the agreement was not a true lease, but instead created a security interest, the court emphasizes a factor enunciated in an prior bankruptcy case as evidence of non-true lease status – the present value of the scheduled lease payments being greater than the cost of the leased property (i.e., a full-pay-out lease). Since the cited case, this factor has been explicitly enumerated in the latest version of 1-201(37) as a factor that does not in and of itself create a security interest – a point that goes unnoticed in this decision. The same result could have been

justified instead by relying on the economic reality that the lessor would never have undertaken the expense of removing the equipment.

In re QDS Components, Inc., 292 B.R. 313 (Bankr.S.D.Ohio 2002)

While holding against a party claiming that leases were disguised security agreements, this decision includes a lengthy discussion of past and present versions of 1-201(37) and of cases and commentary interpreting them. Consistent with certain cases and commentary, the court comments that present 1-201(37) falls short in defining when a lessor retains a “meaningful reversionary interest.”

Chance Industries, Inc. v. TCF Leasing, Inc. (In re Chance Industries, Inc.), 2002 WL 32653678 (Bankr.D.Kan. March 29, 2002)

Four lease agreements are held to secured transactions under Section 1-201(37). After finding an early termination right (at month twelve in a thirty-six month term) to be economically harsh – rendering the agreement effectively not subject to termination by the lessee for thirty six months and thus satisfying one aspect of the circumstances deemed to create a security interest – the court examined the purchase options at the thirty-sixth month and found that they could be exercised for “nominal additional consideration,” which completed the description of one of the security-interest-creating circumstances in the UCC’s definition of “security interest.” The decision relies on a variety of factors in determining what is “nominal,” including a comparison of the purchase option prices with both the original purchase price of the equipment and the total lease payments during the initial term. In addition – and perhaps most important of all – the court recites that portion of 1-201(37) stating, “Additional consideration is nominal if it is less than the lessee’s reasonably predicible cost of performing under the lease agreement if the option is not exercised.” Each of the four leases at issue required the lessee to renew the lease for twelve more months for an aggregate rental of more than the option price if the lessee did not exercise the option.

True Lease versus Security Interest: TRAC Leases and TRAC Statutes

Zions Credit Corporation v. Rebel Rents, Inc. and Perry Valley Rentals, Inc. (In re Rebel Rents, Inc.), 291 B.R. 520 (Bankr.C.D.California 2003)

Lease transaction containing a TRAC provision and also a repurchase agreement from the truck dealer, each providing for an anticipated residual value to be paid to the lessor, held to constitute a true lease under 1-201(37).

Morris v. Dealers Leasing, Inc. (In re Beckham), 275 B.R. 598 (D.Kansas 2002); aff’d *In re Beckham*, 52 Fed. Appx. 119, 2002 WL 31732497 (10th Cir. Dec. 6, 2002)

TRAC lease held not to constitute a security agreement inasmuch as (i) the lessee was not obligated or compelled to purchase the vehicles (e.g., under a “no lessee in its right mind test” where the lessee has no rational economic alternative but to purchase the goods); (ii) a TRAC clause provides an incentive to maintain vehicles in good condition; and (iii) a Kansas TRAC amendment to Article 2A (K.S.A. Sec. 84-2a-110) providing

that TRAC clauses do not themselves create security interests itself was meant to clarify existing law.

Morris v. U.S. Bancorp Leasing and Financial (In re Charles), 278 B.R. 216 (Bankr.D. Kansas 2002)

Fairly thorough parsing of factors expressed in 1-201(37) in holding that a TRAC lease does not create a security interest [disagreeing with *In re Zerkle*, 132 B.R. 316 (Bankr.S.D.W.Va. 1991), which held that TRAC leases create an option to purchase for no additional consideration], then further holding that Kansas' TRAC statute hobbles any argument that TRAC leases are secured transactions.

In re Damron, 275 B.R. 266 (Bankr.E.D.Tenn. 2002)

TRAC lease held not to constitute a security interest under 1-201(37). The TRAC rider stated that the estimated residual value was a reasonable current estimate of fair market value and the court found that value to be a reasonable figure designed to encourage maintenance of the vehicles. No mention was made of Tennessee's 47-2A-110, a TRAC amendment similar to that in Kansas mentioned in the two cases discussed immediately above.

Measures of Lessors' Damages

U.S. Bancorp Oliver-Allen Technology Leasing v. Hall, Dickler, Kent, Goldstein & Wood, LLP, 2005 WL 1875459 (U.S. Dist. Ct. S.D.N.Y. August 8, 2005)

A discussion of the appropriateness of summary judgment relating to various claims for damages. While the amount of liquidated damages under the lease was not in dispute, the lessee argued that trial was necessary with regard to attorneys' fees, the proceeds of sale of returned equipment and the value of missing equipment. Under the facts of this case, the court holds that only the dispute concerning the value of missing equipment created a genuine issue of material fact for trial.

New York Career Guidance Services, Inc. v. Wells Fargo Financial Leasing, Inc., 2005 WL 1252315 (N.J. Super. May 2, 2005) (unpublished opinion)

Notwithstanding that the plaintiff was, according to the court's description, "a serially delinquent lessee of office equipment," the court grants the plaintiff's motion to certify a class and denies the defendant's motion to dismiss in this case relating to leases that permit the lessor to charge a late fee of ten percent of the late payment or up to \$50, at the lessor's discretion. In this case, the lessor had attempted to collect a \$50 late fee with respect to a monthly lease payment of not much more than that amount, with respect to which the court commented, "I have grave doubts that a late charge in a commercial environment of more than 90% of the late payment is reasonable." Although employing the word "commercial," the court comments that the plaintiff's New Jersey Consumer Fraud Act claim remains viable (in addition to common law and unjust enrichment theories of liability).

Oaks v. Bank One Corporation, 2005 WL 293677, 2005 Fed.App. 0096N (U.S.Ct.App.6th Cir. Feb. 8, 2005) (not recommended for full text publication)

The court holds that Tennessee law does not require a lessor to notify the lessee before disposing of the leased goods after a lessee default, even in the context of a lease that required such a sale to be done in a commercially reasonable manner. The court rejected lessee arguments invoking cases and statutes involving notice provisions found in Articles 2 and 9, as opposed to Article 2A.

Raymond Leasing Corporation v. Callico Distributors, Inc., 2005 WL 39772 (Mass.App. January 11, 2005)

The remedies provision of the lease in this case provided that the proceeds of any sale of the equipment after a lessee default would be deemed the rental value of the equipment for the remaining term of the lease, with the effect that all such proceeds would be credited against the lessee's obligations for such remaining term. This appellate court denies the lessor's appeal of the trial court decision, which applied the language of such remedies provision literally so as to include any residual interest the lessor may have had in the credit to the lessee.

AAR International, Inc. v. Vacances Heliades S.A., 349 F.Supp.2d 1114 (N.D.Ill. 2004)

In declaring a liquidated damages clause in an aircraft lease to be unenforceable (in the context of deciding certain motions before a trial to determine the lessor's damages), the court indicates that a lessor will not be permitted simultaneously to recover both actual and liquidated damages. Since in this case the lessor had repossessed the aircraft after the lessee defaulted early during the lease term, the court also notes that the liquidated damage provision did not credit the lessee with the difference between the estimated residual value expected at the end of the initial term of the lease and the greater value of the aircraft when it was repossessed in the early portion of that term.

Goodin v. TBF Financial, LLC, 2004 WL 813352 (Ky.App. April 16, 2004) (unpublished)

Section 2A-528, providing a formula for calculating damages after a lessee default in certain situations – including a provision for present-valuing the difference between the future rentals required by the lease and the market rent for the remainder of the term – is held not to be applicable inasmuch as the lease itself provided an alternative formula: an acceleration clause requiring the lessee to pay the sum of the remaining rentals. The court calculates the lessor's damages using this accelerated amount, crediting the lessee with the amount that the lessor received for the sale of the equipment.

Information Leasing Corporation v. Pall, Inc., 806 N.E.2d 178, 156 Ohio App.3d 378 (Ct. App. 2004)

In a case that appears mistakenly to apply leasing law to a transaction creating a security interest (the documentation included an obligation on the part of the lessee to buy the equipment at the end of the lease), the court discusses Article 2A's measure of damages following a lessee default in a case where the lessor retakes and sells the goods – employing the difference between the present value of the future rent due under the lease and the present value of the market rent over the same term.

Winthrop Resources Corporation v. Eaton Hydraulics, Inc., 361 F.3d 465 (8th Cir. 2004)

Upholds the propriety of a liquidated damages clause based upon pre-determined casualty values, even where this may result in a payment of four or five times the fair market value of the equipment, inasmuch as the end-of-term value of the computer equipment was speculative at the time the lease was entered into by sophisticated companies who had negotiated the lease – i.e., the casualty loss value was a reasonable forecast of just compensation for a harm that was very difficult of accurate estimation.

The CIT Group/Equipment Financing, Inc. v. Super DVD, Inc., 8 Cal.Rptr.3d 927 (Cal.App. 2004)

Lease provisions for calculating damages found to be sufficiently clear and definite to justify issuance of a writ of attachment under a California law requiring that the amount of the claim be a “fixed or readily ascertainable amount.” The court also dismissed a contention that the declaration submitted in support of the right to attach order did not provide information regarding whether the equipment was sold in a commercially reasonable manner as required by Article 9, by stating that “Assuming division 9 is even applicable, the record reflects that appellants’ contention is without merit.”

In re Snelson, 305 B.R. 255 (Bankr.N.D.Texas 2003)

In a case involving a breach of a lease after it had been assumed by the debtor in bankruptcy, the court discusses the debtor’s claim that the liquidated damages clause in the lease constituted a penalty in violation of New Jersey’s Article 2A-504. The clause, which provided for discounting to present value the remaining rentals and the anticipated residual value of the equipment at the end of the lease term with a credit for disposition proceeds, was found to be reasonable and distinguishable from the clause determined to be a penalty in In re Montgomery Ward Holding Corp., 326 F.3d 383 (3rd Cir. 2003).

Wells Fargo Bank Northwest, N.A. v. Taca International Airlines, S.A. and JHM Cargo Express, S.A., 50 UCC Rep. Serv. 2d 811, 2003 WL 21180415 (S.D.N.Y. 2003)

Summary judgment granted to aircraft lessor seeking to enforce a liquidated damages formula including the present value of the amounts by which the stated rentals for the remainder of the lease term exceed the fair market rental value determined, as provided in the lease, by an appraiser chosen by the lessor.

ePlus Group, Inc. v. Panoramic Communications LLC, 2003 WL 1572000 (U.S. Dist. Ct. S.D.N.Y. March 27, 2003)

A lessor’s motion for summary judgment based on a liquidated damages provision is denied on the basis that factual issues were in dispute which would indicate whether or not the provision would place the lessor in a better position than if the lease had been fully performed – a factor cited by the court as important for determining whether a liquidated damages provision is reasonable.

Linc Equipment Services, Inc. v. Signal Medical Services, Inc., 319 F.3d 288 (7th Cir. 2003)

Analysis by Judge Easterbrook of a lessor's claim for damages due to the equipment having been damaged during return and having to be taken out of service for ten months, in which the court cites Hadley v. Baxendale, 9 Ex. 341, 156 Eng. Rep. 145 (1854), and notes that while Article 2A does not explicitly provide for recovery of a lessor's consequential damages (specifying only incidental damages), neither does it preclude recovery of such damages. (The recently approved amendments to Article 2A add provisions for a lessor's recovery of consequential damages in 2A-530.)

Renewals, Automatic Renewals, Return of Equipment

Dayton Development Company v. Gilman Financial Services, Inc., 419 F.3d 852 (8th Cir. 2005)

After the lessor on a lease with the equipment user sold its interests in the equipment to another party and leased the equipment back from such other party, that other party brought suit against the sublessor after the sublessor (i) permitted the user to renew the user lease without providing written notice and (ii) thereafter negotiated a purchase price with the user under a fair market value purchase option. The court affirms the district court's decision that the plaintiff had no right to compel the sublessor to participate in an alternative valuation method for determining fair market value (to be employed if the parties to the user lease could not agree) and that the sublessor had not violated its agreement with the plaintiff not to modify the user lease without the plaintiff's consent by permitting the user to renew without having given written notice. With respect to the latter claim, the court holds that the sublessor had waived a requirement in the user lease, as opposed to modifying the lease. It seems apparent that the plaintiff's agreement with the sublessor was not as precise as it could have been in specifying exactly what the sublessor could and could not do in dealing with the user under the user lease.

Commonwealth Capital Corp. v. Getronics, Inc., 2005 WL 1817170 (U.S.Ct.App. 3d Cir. August 3, 2005)(not precedential)

Affirmation of a district court decision holding that a lease did not obligate the lessee to notify the lessor of repairs made to the equipment (unlike required notification for improvements) and that the lessor had failed to present enough evidence that the equipment was not returned in the condition required by the lease (as opposed to being returned with damages constituting only ordinary wear and tear or with missing parts that were insubstantial). The case illustrates the importance of precise wording in a lease regarding return conditions and the importance of presenting clear evidence of violation of those return conditions.

Information Leasing Corporation v. McGladrey & Pullen, L.L.P., 2005 WL 1706113 (U.S.Dist.Ct. D.Minn. July 21, 2005)

Another case illustrating the importance of very careful drafting of lease provisions regarding return and renewal. The court denies a lessor's summary judgment

motion due to ambiguity of a lease provision clearly requiring prior notice of intent to exercise an option to purchase the equipment or renew the lease schedule, but not clearly requiring prior notice of intent to return the equipment. With respect to the lessor's claim that equipment returned by the lessee had not be returned in a timely manner, the court also finds that the lease did not explicitly require return by the expiration date of the schedule, and looks instead to usage of trade (based on 2A-202) to consider extrinsic evidence presented by the lessee that return within thirty days after expiration was all that was required.

Bradstreet Personnel Group, Inc. v. Wells Fargo Financial Leasing, Inc., 2005 WL 1252333 (N.J.Super. May 2, 2005) (unpublished opinion)

The same judge who decided the *New York Career Guidance Services* case discussed in the "Measures of Lessors' Damages" section above finds that the New Jersey Consumer Fraud Act applies as well to corporate and commercial entities, but rules against the plaintiffs with respect to its claim that an automatic renewal provision in a lease form violated such Act. While admitting that they had not read the lease agreement to begin with, the plaintiffs argued that the renewal provision was so ambiguous that reading it would not have made a difference. Finding that the plaintiffs would have had the opportunity to inquire about the renewal requirements if they had read the provision, the court granted summary judgment in favor of the lessor with regard to the plaintiffs' claims of deceptive and unfair practices.

Dynamics Comm. Funding Corp. v. Robert W. Baird & Co., Inc., 2004 WL 1310155 (Va.Cir.Ct. May 5, 2004)

A strong affirmation of a lessor's right to enforce an automatic renewal provision requiring the lessee to give notice of termination ninety days before the end of the initial or any extended term. The facts of this case, however, indicate that only software was being financed and that the document gave the lessee a \$1 purchase option at the end of the initial term (setting forth an understanding by both parties that such a purchase option operated only to release the lessor's interest in the software license). In addition to marking the end of a lessor's rights to the subject matter of a lease (whether equipment or software), the time for exercising a \$1 purchase option might be thought also to signal the end of the lessor's right to collect rents.

Protection Industries Corp. v. DDB Needham Worldwide, Inc., 763 N.Y.S.2d 546 (App.Div. 2003)

Despite the lessee having made payments after the scheduled termination of an eight year lease, an eight-year automatic renewal clause in the lease is held to be not effective due to non-compliance with New York's General Obligations Law Sec. 5-901. This law – making unenforceable automatic renewal provisions for greater than a thirty day renewal period in personal property leases unless the lessor provides its lessee with fifteen to thirty days advance written notice of the date required in the lease for the lessee to give the lessor notice of the lessee's intention to terminate the lease – has previously been held to apply to New York lessees even when the lease is stated to be governed by the law of another state: Andin International, Inc. v. Matrix Funding Corporation, 756 N.Y.S.2d 724 (Sup.Ct. 2003). A more recent case, Ludl Electronics Products, Ltd. v.

Wells Fargo Financial Leasing, Inc., 2004 WL 737049 (N.Y.App.Div. March 8, 2004), holds that this law cannot be used by lessees to recover lease payments made after the end of the initial term if the lessees have continued their beneficial use of the equipment.

Winthrop Resources Corporation v. Advanced Telecomm of Pittsburgh, 2002 WL 31777799 (D.Minn. Dec. 10, 2002)

Another in a series of victories for this lessor with respect to an evergreen renewal clause, following the earlier decisions mentioned below – in this case one year renewals unless one hundred twenty days prior notice of termination is given.

Winthrop Resources Corporation v. Spearhead System Consultants (US), Ltd., 2002 WL 1127713 (D.Minn. May 29, 2002)

Lessor's summary judgment motion granted with respect to a lease provision mandating automatic one year renewals unless written notice of termination was provided one hundred twenty days before the scheduled end of the lease term – despite the court's stated reservations about such evergreen provisions (opining that it would be a better practice to ensure that both parties are notified in advance of such dates for notice of termination). It seems somewhat ironic, given the court's inclinations, that the possible application of the New York statute referenced in Andin above was not raised inasmuch as the lessee was a New York corporation with its primary place of business also in New York.

Winthrop Resources Corporation v. North American Lighting, Inc., 2002 WL 334410 (D. Minn. Feb. 12, 2002)

Lessor's summary judgment motion granted with respect to lease provision requiring automatic renewal for one hundred twenty day periods unless either party gave the other party written notice one hundred twenty days prior to scheduled termination.

[Another variation in State law on this subject: since June 1, 2000, Illinois statutes have required that any provision for automatic renewal in a contract must appear in a **clear and conspicuous manner** for the provision to be enforceable. 815 ILCS 601/1 et. seq.]

Vicarious Liability of Lessors (mostly Motor Vehicle Lessors)

Chieffo v. Clifford, 2005 WL 2981771 (Conn.Super. Oct. 20, 2005) (unpublished opinion) *

After Connecticut had amended its vicarious liability statute to except leases of private passenger motor vehicles if the total lease term is one year or more and the leased vehicle is insured for bodily injury liability in certain minimum amounts, the plaintiff argued that the statute was unconstitutional on various state and federal grounds in order to recover from the vehicle's lessor for injuries. This court finds against each of the plaintiff's grounds for unconstitutionality and grants the lessor summary judgment.

Moncrease v. Chase Manhattan Auto Finance Corp., 2005 WL 2650788 (Conn.Super. Sept. 27, 2005) *

Under the Connecticut vicarious liability statute in effect at the time of the accident, a lessor of a motor vehicle was stated to be liable for damage to person or property to the same extent as the operator of the vehicle. In this case, the court grants summary judgment in favor of the lessor, avoiding liability, since the driver of the car under lease (the lessee's unlicensed daughter) was not an authorized driver under the terms of the lease agreement, which prohibited use of the vehicle by unlicensed drivers.

Sigovich v. Norma J. Haynes Trucking Co., 2005 WL 1971883 (Conn.Super. July 28, 2005)(unpublished opinion)

Lessor of a trailer moved for summary judgment in an action brought by a plaintiff injured in an accident allegedly caused by the negligence of the driver of the tractor (which driver was said by the trailer's lessor to have no relationship with such lessor) to which the trailer was attached. The lessor contested theories of liability based upon both a statutory presumption of agency in a motor vehicle context and statutory strict liability for motor vehicle lessors. Holding that there exists a split of authority as to both (1) whether summary judgment is appropriate in the context of the agency issue and (2) whether a trailer is a motor vehicle for purposes of the vicarious liability statute, the court denies the lessor's motion.

Coleman v. Windham Aviation Inc., 2005 WL 1793907 (R.I.Super. July 18, 2005)(unpublished opinion)

In deciding a summary judgment motion by a plaintiff requesting a declaration that the owner and lessor of an aircraft is vicariously liable under state law (both Connecticut and Rhode Island are similar in this respect) for injuries caused by the negligent operation of an authorized operator, the court rejects the lessor's argument that federal law preempts such state laws. Notwithstanding apparently clear language in the federal statute supporting the lessor's preemption argument, the court examines the recodification that resulted in the present federal statute and concludes that such recodification impermissibly extended the scope of the exemption beyond the intent of the predecessor statute.

Fredette v. Keybank, USA, 2005 WL 1670808 (Conn.Super. June 14, 2005) (unpublished opinion)

After characterizing Connecticut's statute imposing vicarious liability on motor vehicle lessors for injuries caused by the negligence of its lessees as a "statutory suretyship," the court upholds the lessor's right to seek contractual (under the lease agreement) and common-law indemnity from the lessee and the lessee's permitted driver.

Chilberg v. Chilberg, 788 N.Y.S.2d 533 (App.Div. 2004)

In denying Ford Motor Credit Company's contention that Section 388 of New York's Vehicle and Traffic Law providing for the vicarious liability of owners of motor vehicles for damages caused by the negligence of the operators of such vehicles is unconstitutional as applied to long-term vehicle lessors, the court notes that the legislative purpose was to ensure that injured persons would have recourse to a

financially responsible party and that imposing such liability on long-term lessors is not an unreasonable means of accomplishing that purpose.

Lanni v. O'Donnell, 2004 WL 2550452 (Mass.Super. Oct. 12, 2004)

Interpreting a Massachusetts law (General Laws c. 231, Sect. 85A) providing that registration of a motor vehicle in the name of the defendant in an action for damages arising out of an accident involving such motor vehicle is *prima facie* evidence that the driver was acting as an agent of the owner (requiring an affirmative defense by the owner that it was not responsible for the actions of the driver), the court denies a motion for summary judgment brought by the lessor/owner (Honda Lease Trust, a/k/a American Honda Finance Corp.) of the automobile. The court characterized standard lease provisions requiring greater than mandatory liability insurance, indemnity for claims arising from use of the automobile, and covenants regarding the vehicle's use, location and alteration as "measures of control" that create genuine issues of material fact about an agency relationship between the lessee and its lessor.

Litvak v. Fabi, 8 A.D.3d 631, 780 N.Y.S.2d 155 (App.Div. 2004)

Reversal of lower court ruling in favor of Keybank, which ruling was premised on a finding that the bank only held a security interest in a vehicle involved in an accident and thus could not be liable as an owner under New York's vicarious liability statute. Though the basis for the lower court's finding is not made clear, the appellate court finds that because the agreement between the bank and the customer was a lease and the bank held title to the vehicle, the bank was an owner within the meaning of the vicarious liability statute.

Adreozzi v. Brownell, 2004 WL 1542228 (R.I. Super. July 8, 2004) (unpublished opinion)

Automobile lessor is held to be subject to one of two Rhode Island statutes (G.L.1956 Sec. 31-33-6 and 31-34-4) providing for vicarious liability for injuries caused by the negligence of its lessee. The decision cites Oliveira v. Lombardi, 794 A.2d 453 (R.I. Sup. Ct. April 3, 2002), in which the Rhode Island Supreme Court found that the purpose of that state's statute was to find "well-funded pockets" and "additional sureties" for the satisfaction of negligence claims, and commented that if this would have a negative impact on the motor-vehicle financing business in the state, the forum for seeking change was the state legislature. After the lease discussed in this case had been entered into, Rhode Island's legislature did indeed amend those two statutes to provide for either no owner liability or liability limits under various circumstances; however, those amendments contained a sunset provision making them effective only until July 1, 2004, originally, which sunset date has been twice extended until July 1, 2006. The decision also cites a recent article surveying the laws of thirteen states providing for unlimited or potential vicarious liability of motor vehicle lessors: Kenneth J. Rojc and Kathleen E. Stendahl, *Vicarious Liability of Motor Vehicle Lessors*, 59 Bus.Law. 1161 (2004).

Gardner v. Hinman, 2004 WL 616140 (Conn. Super. March 17, 2004)

Commenting that Connecticut's General Statute Sec. 14-154a imposing liability on lessors of motor vehicles for damages caused by the operators to whom the motor vehicles are leased creates a liability even greater than vicarious liability at common law, this court holds that a discharge of the operator's liability in bankruptcy does not bar a claim against the lessor under this statute. The court distinguishes the legal consequences of such a bankruptcy discharge from those of a release of an operator (and his insurer in return for a payment to the injured party) which was held also to release the lessor in Cunha v. Colon, 792 A.2d 832 (Conn. Sup. Ct. April 2, 2002).

Sierra v. A Betterway Rent-A-Car, Inc. d/b/a Budget Rent-A-Car of Atlanta, 863 So.2d 358 (Fl.Ct.App. 2003, rehearing denied Jan. 16, 2004)

Georgia car rental company that knew a car would be driven to Florida and did nothing to prohibit such is held to be subject to personal jurisdiction in Florida and the plaintiff's vicarious liability claim is to be governed by Florida, rather than Georgia, law. [Morales v. The Coca-Cola Company, 813 So.2d 162 (Fla. Dist. Ct. App. 2002) holds that under Florida's common law dangerous instrumentality doctrine as applied to motor vehicles (unique to Florida, according to the court), the owner of a motor vehicle is liable to third parties for injuries caused by the negligent use of the motor vehicle by someone to whom the owner entrusted the vehicle. While "mere naked title" may not entail vicarious liability, the beneficial ownership ordinarily evidenced by legal title does.]

[Vicarious liability for motor vehicle lessors has been the subject of much controversy in recent years. Threats of withdrawal from the motor vehicle leasing business by various finance companies caused Connecticut to amend its version of such a vicarious liability statute (General Statute Sec. 14-154a) not to apply to certain motor vehicle leases of one year or longer and caused Rhode Island to amend its statutes as noted above. Many motor vehicle leasing companies ceased doing business in New York, which maintained unlimited vicarious liability for lessors. On August 10, 2005, a federal highway, transit and reauthorization bill (H.R. 3, Public Law 109-59) was enacted, a portion of which is intended to preempt state law concerning vicarious liability of motor vehicle lessors. It remains to be seen (a) whether such preemption will be challenged by groups with contrary interests such as the New York State Trial Lawyers Association and (b) what the effect will be of its provision stating that it does not preempt state law imposing liability on lessors for failing to meet financial responsibility or liability insurance requirements.]

Product Liability of Lessors

Wengenroth v. Formula Equipment Leasing, Inc., 784 N.Y.S.2d 123 (App.Div. 2004)

In a product liability action for injuries incurred by an operator of a tractor hitched to a water wagon, summary judgment motions of the manufacturers of the tractor and wagon and of the leasing company who leased the two pieces of equipment to the employer of the operator are denied. The court held that the lessor may be held liable regardless of the fact that it did not manufacture either part of the vehicle inasmuch as it

selected the tractor without a door and installed a non-oscillating hitch – each being an issue that raised potential liability (to be decided at trial) for the manufacturers as well.

Svege v. Mercedes-Benz Credit Corp., 329 F.Supp.2d 272 (D.Conn. 2004)

Assignee of a truck lease is held to be a “product seller” under Connecticut’s Product Liability Act and thus potentially liable for damages resulting from a motor vehicle accident involving the truck. While the court comments that being an assignee of a lease or providing financing for the product manufacturer does not necessarily entail potential liability under this Act, Mercedes-Benz Credit Corp.’s financing program with Freightliner is held to constitute sufficient involvement in the stream of commerce sending Freightliner trucks into the state so as to render MBCC a “product seller” under the Act. The court also comments in a footnote that MBCC did not argue, and the court did not therefore address, whether the Connecticut Supreme Court would reject strict product liability for entities performing the role of “finance lessor,” as has been the case in certain other states.

Ordinary Course Buyers from Lessees

Mercedes-Benz Credit Corporation v. Johnson, 1 Cal.Rptr.3d 396 (Ct.App. 2003)

In a dispute between an individual who had purchased a car from a used car dealer, which dealer had previously leased the car for his personal use, and the lessor of the car to the dealer, the court holds that the lessor had the superior right to the car. The decision rests on the court’s interpretation of “entrusted” as employed in California’s version of 2A-305, which states that an ordinary course buyer from a lessee, who is in the business of dealing in the kind of goods entrusted by the lessor to the lessee, takes free of the existing lease contract. Article 2A-103(3) refers to Article 2-403(3) for a definition of “entrusting.” To the concepts of delivery and acquiescence in retention of possession found in the standard version of Article 2, California added the phrase “for the purpose of sale, obtaining offers to purchase, locating a buyer, or the like.” The lessor here had no such purpose. The court goes on to opine that even the ordinary dictionary definition of “entrust” indicates that a lessor under a lease prohibiting assignment could not be said to have entrusted the car to someone who would be expected to default on the lease by selling the car and running off with the proceeds.

Leasing One Corporation v. Caterpillar Financial Services Corp., 776 N.E.2d 408, 48 UCC Rep. Serv.2d 1505 (Ind.Ct.App. 2002)

Decision in which the facts are unfortunately not made clear and the statements of law appear to be mistaken. A lessee (which may or may not be a dealer in the type of equipment being leased) under a lease agreement (which may or may not be a true lease) sold the equipment being leased to a third party (who is alternatively stated to be the user of the equipment or its source of financing). While this case is not very clear concerning the facts and the law, different variations on the factual background can be used to illustrate the rights of third parties who buy from someone who either has granted a security interest to, or has leased the equipment from, a financing source.

Vendor Issues

Leasecomm Corporation v. Starbuck, 2005 WL 1009740 (Mass.Super. March 14, 2005)

In an action by a leasing company against an equipment vendor for violation of a vendor agreement between such parties, the court awards damages to the lessor after finding that an employee of the vendor had either forged or fraudulently obtained signatures of lessees on leases of equipment paid for by the lessor.

Wiltel Communications, LLC v. Sunrise International Leasing Corporation, 2005 WL 354030 (Minn.App. Feb. 15, 2005) (unpublished opinion)

Summary judgment granted by a lower court against a lessor in favor of a manufacturer is reversed. The manufacturer shipped equipment to a lessee after (i) the lessor and lessee had signed lease documents, (ii) the lessor had collected a down payment from the lessee (consisting of the first and last months' rent), and (iii) the lessor had placed two purchase orders with the manufacturer. The lessor argued that the manufacturer had never accepted the purchase orders by providing proper invoices indicating delivery of the equipment and that the lease transaction had never closed. The lessee filed for bankruptcy in the meantime, and the lessor did not pay the manufacturer for the equipment. Notwithstanding the lower court's ruling that the lessor owed the manufacturer for the equipment, this court holds that there are material issues of fact regarding the existence of a contract between the manufacturer and the lessor.

Engel Machinery, Inc. v. Wells Fargo Equipment Finance, Inc., 2004 WL 2973824 (U.S. Dist.Ct. N.D.Ill. Nov. 30, 2004)

In connection with a proposed lease, the prospective lessor/finance company entered into certain agreements with the equipment vendor including, among other provisions, that the finance company would not fund the vendor until the lease had commenced. The equipment was delivered before, but was only fully installed and accepted after, the finance company's commitment to fund, as expressed in its agreements with the vendor, had expired. The finance company never signed the lease with the lessee (a condition for the commencement of the lease) and shortly thereafter the lessee filed bankruptcy with the vendor not having been paid. This decision grants the finance company's motion for summary judgment based in part on the court's reading of the Illinois Credit Agreements Act to mean that the finance company would have had to sign the lease before it would be considered bound under that Act to pay the vendor.

Fortinet, Incorporated v. OFC Capital, 2004 WL 2496184 (U.S. Dist.Ct. N.D.Cal. Nov. 5, 2004)

Summary judgment is denied an equipment vendor suing a leasing company for failure to pay for equipment delivered to a lessee, which shortly thereafter entered bankruptcy. Although the vendor argued that a contract for payment was established by a series of e-mails between the vendor and the lessor, the court noted some additional correspondence that conditioned the lessor's payment on such steps as installation and inspection of the equipment and the lessee's execution of a delivery and acceptance form.

Wells Fargo Financial Leasing, Inc. v. LMT Fette, Inc., 382 F.3d 852 (8th Cir. 2004)

Notwithstanding claims by the equipment vendor made to the lessee that he was acting as an agent for the lessor on a lease of the equipment and promises by such vendor to take over the lease, the court refused to release the lessee from liability to the lessor in the absence of any showing of fraud or misconduct by the lessor, citing clear language in the lease that the vendor was not the agent of the lessor and could make no representation on behalf of the lessor.

Transfer of a Manufacturer's Warranty to a Lessee

A. Lopresti & Sons, Inc. v. General Car & Truck Leasing System, Inc., 79 Fed.Appx. 764, 2003 WL 22442932 (U.S.Ct.App. 6th Cir. Oct. 27, 2003)

After finding no evidence that a truck lessor had not fulfilled its obligations to service the trucks and that the lessor had made no warranty that the trucks delivered would be free from mechanical defects, the court goes on to consider the lessee's claim against the manufacturer of the engines. This claim is denied on the basis that the manufacturer's warranty ran to the owner (i.e., the lessor) and that there was no evidence that the lessor had transferred the warranty to the lessee. The court evidently did not have to consider whether the warranty was assignable.

Purchase Option Provisions

Frost National Bank v. L&F Distributors, Ltd., 165 S.W.3d 310 (Texas May 27, 2005)

After an intermediate appellate court had ruled that language in a lease giving the lessee the right to buy the equipment for a stated amount "on or before the Expiration" of the lease meant that the lessee could purchase the equipment for that amount at any time before the end of the scheduled sixty month term, the Texas Supreme Court holds that the poorly worded provision could only have been meant to permit the exercise of that option at the end of the term and that the lessee's and appellate court's interpretation was "unreasonable, inequitable and oppressive."

First American Commercial Bancorp, Inc. v. Interior Architects, Inc., 2004 WL 2011398 (U.S. Dist.Ct. N.D.Ill. Aug. 31, 2004)

Citing a lease's integration clause and Article 2A-202, Final Written Expression: Parol or Extrinsic Evidence, the court holds that an unsigned facsimile side letter placing a cap on the fair market value purchase option found in an addendum to the master lease could not be enforced by the lessee. Prior to the initiation of litigation, there had been a number of instances in which the lessor and lessee had negotiated purchase prices that exceeded the purported cap. The court also held that the term "fair market value" – not defined in the lease – was not ambiguous as a matter of law, at least with respect to the purported cap at issue. The court cites definitions of "fair market value" in *Black's Law Dictionary* and in some Illinois case law, while acknowledging that there may be a number of nuances in determining fair market value – none of which were present in this case.

Central Funding, Inc. v. CompuServe Interactive Services, Inc., 2003 WL 22177226 (Ohio App. 10 Dist. Sept. 23, 2003), appeal not accepted for review, 802 N.E.2d 155 (OhioSup.Ct. 2004)

A case illustrating the benefits of very careful wording – in this case, in connection with a lessee’s exercise of a fair market value purchase option. Following lessee’s timely notice of its intent to exercise that purchase option, the lessor attempted to set the purchase price based upon a formula for early buy-out during the lease term. After the lessee rejected this suggestion and the lessor rejected a lessee suggestion for fair market value appraisals, the lessor demanded return of the equipment and the lessee refused. The definition of fair market value in the lease stated that “Fair Market Value is mutually determined by Lessor and Lessee as the amount obtainable in a transaction between an informed and willing user...”, but the lease provided no required mechanism to determine that value. Holding that the language was ambiguous and that in the absence of sufficient parol evidence, the language should be construed against the drafter, the court rejects the lessor’s argument that exercise of the option by the lessee depended upon mutual agreement as to the purchase price – finding instead that the lessee’s exercise had created an obligation on the part of the lessor to sell at fair market value and that such exercise by the lessee also extinguished any obligations under the lease after the scheduled end of term.

Accepting an Offer from a Lessee in Default to Return the Equipment

IOS Capital, Inc. v. Jacobi, 105 S.W.3d 909 (Mo.Ct.App. 2003)

After picking up its equipment following the defaulted lessee’s request to pick it up and cancel the lease, the lessor sued to recover the balance owing under the lease. Although the trial court held that the parties had reached an accord and satisfaction releasing the lessee from further obligations, the appellate court reverses inasmuch as the lessor was merely exercising its rights to the equipment under the lease and there was not any evidence that the lessor was accepting the lessee’s offer to pick it up in return for canceling the lease. The lower court’s decision is difficult to understand in view of the lessee’s testimony that no one from the lessor had ever told her that the lease would be canceled and the fact that the receipt provided by the lessor when it picked up the equipment specifically stated that the lessee’s obligations were not being released.

Lease Treatment for “Software Leases”

In re CNB International, Inc., 307 B.R. 363 (Bankr.W.D.N.Y. 2004)

A lease schedule including only software (related hardware was listed on a separate schedule) is held not to be a lease for purposes of obtaining the advantages of Section 365(d)(10) of the Bankruptcy Code. Having made no arrangement with the licensor of the software to obtain possessory and conditional use rights to the software – with an understanding that the possessory right would be transferred to the lessee – the lessor never had a possessory interest in the software that it could transfer to the lessee as

required by Article 2A's definition of "lease" (2A-103(1)(j) in the uniform version): "No lessor may lease that which it does not own or in which it does not enjoy at least some interest or right of possession." It would be interesting to know how this court would have ruled if the hardware and related software had been included on the same schedule. While such a document would be considered "chattel paper" for purposes of Revised Article 9, courts could conceivably adopt this decision's view for bankruptcy and other purposes and attempt to separate the two components.

Indemnity Clauses

Eagle High Reach Equipment, Inc. v. Precision Drywall, Inc., 2004 WL 938428 (Cal. App. 2 Dist. May 3, 2004) (unpublished opinion)

Summary judgment in favor of a lessor based upon a lease provision requiring the lessee to indemnify the lessor against third-party claims for injuries caused by use of leased equipment is upheld where the indemnity clause was not unconscionable and there was no evidence of active negligence on the part of the lessor.

Forum Selection Clauses and Other Jurisdictional Issues

SRH, Inc. v. IFC Credit Corporation, 619 S.E.2d 744 (Ga.App. 2005)

After the trial court had dismissed a lessee's action for rescission of a lease against the lessor's assignee, which dismissal was based upon the type of forum selection clause discussed in the cases below (the lessee had brought the action in a court within its state rather than in the state of the lessor's assignee, as provided in the lease), this appellate court reverses the dismissal and holds that a complaint alleging fraud on the part of both the original lessor and its assignee should not be dismissed unless there are no possible sets of facts that would entitle the lessee to relief.

Popular Leasing USA, Inc. v. Terra Excavating, Inc., 2005 WL 1523950 (U.S.Dist.Ct. E.D.Mo. June 28, 2005)

This decision is a strong endorsement of the enforceability of the kind of "floating" forum selection clause discussed in the cases below. In its decision the court also (i) holds that a fraud will only render the clause invalid if the inclusion of that clause in the contract was itself the product of fraud or coercion, and (ii) places a relatively heavy burden on the defendant (not overcome in this case) before it would consider granting a motion to transfer venue.

Preferred Capital, Inc. v. Aetna Maintenance, Inc., 2005 WL 1398549 (U.S.Dist.Ct. N.D. Ohio June 14, 2005)

In granting this Florida-based defendant's motion to dismiss for lack of personal jurisdiction, the court holds that the kind of forum selection clause at issue in other cases summarized below (in which the lessee agrees to the jurisdiction of courts located in whatever state the lessor or its assignee maintains its principal offices) is not enforceable when the lessor knew its assignee's location before the lease was executed, but did not so

inform the lessee. The court states that if the lessee had been informed, the clause would have been enforceable.

IFC Credit Corporation v. Burton Industries, Inc., 2005 WL 1243404 (U.S. Dist. Ct. N.D. Ill. May 12, 2005)

The same court as in the *Eastcom* case discussed below (a different judge, however) holds that the same type of forum selection clause at issue in *Eastcom* and a number of the other cases summarized in this section is enforceable. In this case, the defendant is located in Michigan and is characterized by the court as a sophisticated business enterprise capable of bargaining for a different clause.

Studebaker-Worthington Leasing Corp. v. Michael Rachlin & Co., LLC, 357 F. Supp. 2d 529 (E.D.N.Y. 2004)

After being sued in a New York state court by an assignee of a lease containing a forum selection clause permitting the assignee to choose a court near its location, the lessee (based in New Jersey) removed the case to a New York federal court and argued that the case should be heard by the bankruptcy court (in New Jersey) presiding over the bankruptcy of the original lessor, because the lessee intended to assert a counterclaim against the assignee related to a claim of fraud against the lessor. The federal court in New York holds that such does not constitute sufficient grounds to confer subject-matter jurisdiction and remands the case to the New York state court. [It is not clear why this case is said to be decided on February 22, 2004, while referencing dates related to the original lessor's bankruptcy in June and July of 2004.]

IFC Credit Corporation v. Eastcom, Inc., 2005 WL 43159 (U.S. Dist. Ct. N.D. Ill. Jan. 7, 2005)

The court grants the lessee-defendant's motion to transfer the case from the jurisdiction in which the principal offices of the assignee of the lessor (the plaintiff) are located to the jurisdiction in which the lessee and the leased equipment are located, notwithstanding a forum selection clause in the lease agreeing to venue in whatever jurisdiction the lessor's assignee happens to be located. The court questions whether Illinois law would enforce such a provision that fails to specify a particular jurisdiction, but bases its decision on an evaluation of the convenience and fairness of transfer given the facts of this case (including the fact that the defendant is located in California).

Commerce Commercial Leasing, LLC v. Jay's Fabric Center, 2004 WL 2457737 (U.S. Dist. Ct. E.D. Pa. Nov. 2, 2004)

In denying a lessee's motion to dismiss a breach of contract action brought by the lessor's assignee for lack of personal jurisdiction, the court cites well-established authority for generally enforcing forum selection clauses – even those that refer only to whatever forum that the lessor or its assignee (unknown at the time the lease is signed) chooses.

Ex parte Leasecomm Corporation (In re Sisk v. Kelleher), 879 So.2d 1156 (Ala.Sup.Ct. 2003)

Although a lessee sued his lessor with regard to malfunctioning equipment and alleged fraud in the inducement as a general matter, the Alabama Supreme Court enforced the forum selection clause contained in the lease (choosing Massachusetts as the exclusive forum) in favor of the lessor, since the lessee had not established that he was fraudulently induced to permit that particular clause to be included in the lease (and the clause was not otherwise unfair or unreasonable).

Statute of Limitations under Article 2A

ESP Financial Services, LLP v. Vielot, 794 N.Y.S.2d 337 (App.Div. 2005)

The court holds that a lease provision waiving, to the extent permitted by law, “any and all rights and remedies conferred upon a lessee by Article 2A” did not include Massachusetts’ Article 2A’s four-year statute of limitations. Since the plaintiff brought this suit more than four years after it had declared the lessee to be in default – but within the six-year period for actions on a contract that would otherwise apply – and the waiver was held not to apply, the lessee’s motion to dismiss was granted.

Waivers of Trial by Jury

Popular Leasing USA, Inc. v. Terra Excavating, Inc., 2005 WL 2468069 (U.S.Dist.Ct. E.D.Mo. Oct. 6, 2005) *

This decision holds that the lessee/defendant did not knowingly and voluntarily waive its right to a jury trial inasmuch as the waiver clause was placed inconspicuously at the end of a paragraph titled “Applicable Law”, which paragraph was printed in the same small font as most of the rest of the lease. The court comments that, although the Eighth Circuit has apparently not yet decided which party bears the burden of proving that such a waiver is knowing and voluntary, the court is persuaded that the party seeking to enforce the waiver should bear the burden. The court notes its disagreement with other judges in the same district that have reached a contrary conclusion regarding a jury trial waiver documented on the same form of lease (which is the same form of lease at issue in a number of the forum selection clause cases discussed above).

FGDI, Inc. v. Bombarier Capital Rail Inc., 383 F.Supp.2d 1350 (M.D.Fla. 2005)

A master lease was amended by the parties so as to change the governing law and venue from Minnesota to Florida. While the original paragraph in the master lease (entitled “Governing Law”) also contained an irrevocable waiver by both parties of the right to a trial by jury, the paragraph in the amendment (entitled “Governing Law and Venue”) did not. The court grants the plaintiff’s demand for a jury trial after finding that (i) there is a strong preference in the federal courts for permitting jury trials, (ii) the jury waiver provision in the amended lease was ambiguous (in that it was not clear whether the paragraph in the amendment was intended to replace all or merely a part of the

original paragraph), and (iii) ambiguities in contracts should generally be construed against their drafters.

Wells Fargo Bank, National Association v. Stargate Films, Inc., 795 N.Y.S.2d 18 (App.Div. 2005)

A brief opinion holding that an equipment lease's waiver of a right to trial by jury does not apply to a sufficiently pleaded defense by the lessee that amounts to a claim of fraudulent inducement challenging the validity of the lease. The court goes on to say that the lease assignee/plaintiff's claim to be a holder in due course, entitling it to enforce the "hell or high water" clause in the lease regardless of the lessee's fraud defense, was premature and therefore not properly raised on this appeal.

Assignments of Leases

Day v. Case Credit Corporation, 427 F.3d 1148 (8th Cir. 2005)*

An equipment dealer for Case International Harvester first orally negotiated terms for financings (mostly leases) of farm equipment and then fraudulently prepared written agreements (representing sales) with higher payment terms, employing forged signatures of its farmer-customers, before assigning such agreements to Case Credit. When Case became aware of the fraud, it attempted to have the farmers sign verifications of the written agreements – which the farmers initially refused to do because of the inflated payment amounts, but then agreed after assurances from Case that the verification forms would only be used to confirm their possession of the equipment. Case later allegedly attempted to use these verifications to collect the full higher amounts. Holding that Case could enforce neither the forged written agreements – since they were void – nor the oral agreements – on the basis that no one ever contemplated that oral agreements would be assigned – the Eighth Circuit reversed the District Court's grant of summary judgment in favor of Case under a contract theory of liability. While the Circuit Court agreed with the District Court that there was no evidence that Case had acted as an agent of the fraudulent dealer, it agreed with the farmers that evidence of Case's "unclean hands" conduct might bar it from recovering on a theory of unjust enrichment, and remanded to the District Court for further proceedings.

Savings Bank of Manchester v. Ralio Financial Services, Inc., 881 A.2d 1035 (Conn.App. 2005)

After the lessee defaulted on its lease entered into with the lessor/defendant, the assignee of the lease sued the lessor for alleged misrepresentations in the assignment documents regarding, among other things, the location of the equipment at the time of the assignment. Reversing the judgment of the trial court in favor of the assignee, the appellate court holds that since the assignee's loan officer had testified that he knew the equipment had not been delivered to the place designated in the lease at the time of the assignment, the assignee could not have reasonably relied on that misrepresentation and therefore could not prevail in its action for negligent misrepresentation.

General Electric Capital Corporation v. ePlus, Inc., 2005 WL 700954 (U.S. Dist. Ct. S.D.N.Y. March 24, 2005)

As an assignee of certain leases, the plaintiff attempted to recover post-petition rentals from the lessee's successor under Bankruptcy Code Section 365(d)(10) after such successor had filed bankruptcy. After the bankruptcy and district court (on appeal) both held that the lease was not a true lease (i.e., it was instead a lease that created a security interest), the plaintiff brought a summary judgment motion against the lessor's successor based on an alleged breach of its warranty in the non-recourse loan and security agreements that it had good title to the equipment. The court holds that the phrase "except for the interest of the Lessee under the Lease" qualifying the good title warranty created enough of an ambiguity to deny summary judgment. The court also noted evidence offered by the defendant of examples of warranty clauses that much more clearly guarantee true lease characterization. This case indicates why lessors, who are unsure about the characterization of leases they wish to finance, should consider warranting either good title or a first priority security interest.

Kipperman v. NetBank, FSB (In re Commercial Money Center, Inc.), 2005 WL 1365055 (Bankr.S.D.Cal. Jan. 27, 2005)

Following an assignment of payment streams under equipment leases to a bank, the assignor filed for bankruptcy and its trustee sought to recover the rights to such payment streams from the bank by arguing both that the assignment was a loan, rather than a true sale, and that the assignment had not been perfected as required by the UCC. Although the bank countered that the assignment constituted a true sale of payment intangibles – and thus was automatically perfected under the UCC – the court held that (i) the payment streams constituted "chattel paper" (as opposed to payment intangibles) as to which perfection could occur only by filing or by taking possession of the leases (neither of which the bank had done), and (ii) the substance of the transaction was in fact a loan secured by the payment streams, in which case perfection could not be automatic (only a sale of payment intangibles is automatically perfected under Article 9, not a security interest in payment intangibles). With regard to the first point, the court comments that adopting the bank's position would lead to confusion in the equipment leasing and financing world insofar as lease streams could be purchased without the purchaser providing any notice to the rest of the world.

Lessors' Rights in Bankruptcy Proceedings

In re The IT Group, Inc., 331 B.R. 597 (Bankr.D.Del. 2005) *

The court finds in favor of defendants from whom allegedly preferential payments were sought to be recovered based upon the "Kiwi Defense." This defense is predicated on a Third Circuit decision involving Kiwi Airlines, which held that assumption of an unexpired lease or executory contract under Section 365 of the Bankruptcy Code bars the later recovery under Section 547 of pre-petition payments made during the preference period under such lease or contract.

CIT Communications Finance Corporation v. Midway Airlines Corporation (*In re Midway Airlines Corporation*), 406 F.3d 229 (4th Cir. 2005)

This Circuit Court agrees with the majority interpretation of Bankruptcy Code Section 365(d)(10) as it relates to a case where no post-petition payments had been made on a lease prior to its rejection. The court holds that the lessor's claim for all payments owing under the lease following the sixty-day period after the bankruptcy filing should be entitled to administrative expense treatment, rejecting the trustee's and bankruptcy court's position that the lessor was entitled only to a reduced allowance because the equipment was of little use to the lessee. The court also rules, however, that immediate payment of the amount claimed by the lessor was not required.

In re Smith, 315 B.R. 77 (Bankr.W.D.Ark. 2004)

Decision illustrating that if a lease has been assumed by a debtor in bankruptcy and is later rejected, the damages resulting from such breach are generally entitled to administrative priority.

*Bartholomew v. General Electric Capital Corporation (*In re Tricord Systems, Inc.*)*, 2004 WL 2066817 (U.S. Dist.Ct. D.Minn. August 27, 2004)

In a case in which the lessor drew on a letter of credit while its lessee was in bankruptcy, the court affirms that letters of credit are not assets of the bankruptcy estate and that drawing on them is not a violation of the automatic stay. However, the district court remanded to the bankruptcy court the issue of whether the lessor drew on the letter of credit for an amount greater than the amount to which it was entitled under the lease agreement. After remand and another appeal to the District Court, the lessor was held liable for drawing too much. 2005 WL 910531 (D.Minn. April 15, 2005)

In re BankVest Capital Corp., 360 F.3d 291 (1st Cir. 2004), cert. denied, 124 S.Ct. 2874 (2004)

The First Circuit holds that Section 365(b)(2)(D) does not require that non-monetary defaults be cured before the debtor in bankruptcy can assume an unexpired lease. The court finds the wording of the statute to be ambiguous, finds no helpful legislative history, and agrees with most bankruptcy commentators who have written that such an interpretation is consistent with general bankruptcy policy. The court also indicates its disagreement with the contrary holding of the Ninth Circuit in *In re Claremont Acquisition Corp.*, 113 F.3d 1029 (9th Cir. 1997). Although the Supreme Court denied a petition for writ of certiorari, this issue was finally resolved in favor of the Claremont court's position by recent amendments to the Bankruptcy Code.

Authority of Lessee's Employee to Enter into Lease

Banc One Leasing Corp. v. Scat Recycling, L.L.C., 892 So.2d 98 (La.App. 2004)

Summary judgment in favor of a lessor is reversed by an appellate court finding material issues of fact regarding the actual and/or apparent authority of the lessee's accountant to sign a lease on behalf of the lessee. The lessee's operating agreement, a copy of which had been given to the lessor, indicated that only its two members (a

husband and wife) were authorized to incur such obligations. Evidence indicating that the accountant had forged documents stating that he was one of the owners of the lessee was one example of a number of contested issues of fact held to preclude summary judgment.

IOS Capital, LLC v. Allied Home Mortgage Capital Corporation, 150 S.W.3d 148 (Mo.App. 2004)

After the branch manager of an office of the purported lessee signed a lease (presented by the equipment vendor, but with an unaffiliated lessor) for a photocopy machine (and presumably after the lessor paid the equipment vendor for the machine), that particular office was closed by the lessee and the branch manager was terminated – a few days before the equipment was delivered to the office. In this action for breach of lease and for conversion (the whereabouts of the machine was unknown to both parties), the purported lessee successfully argues that the lessor was not justified in relying upon either actual or apparent authority of the employee to enter into the lease. The case does not indicate whether the lease contemplated the signing of a delivery and acceptance certificate before the lease was to commence.

Lease Proposals and Commitments

Fairbrook Leasing, Inc. v. Mesaba Aviation, Inc., 408 F.3d 460 (8th Cir. 2005)

This Circuit Court panel (with one dissent) finds in favor of a group of lessors that, notwithstanding the title “Term Sheet Proposal” regarding the acquisition and lease of certain aircraft, such document evidenced a binding preliminary agreement according to a series of factors established under New York law. Both the majority and dissenting opinions are instructive regarding the elements that can turn a non-binding proposal into a binding agreement.