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Is Your (Non-True) Lease a Sale?

By Edward Gross and Philip Livingston

Just in case the transaction you've just documented using your standard lease forms is not a "lease," you've included a granting clause in the form and filed UCC "notice" filings. So, you've protected the lessor from a re-characterization risk (*i.e.,* that the transaction is deemed not to create a "lease" under commercial law) — right? Well, maybe not.

A recent decision by the Federal District Court for the Western District of Wisconsin reminds us of the need to draft documents that protect against the possibility that a lease may be re-characterized as a "sale" to which Article 2 of the UCC applies. In *Key Equipment Finance, Inc. v. Pioneer Transportation, Ltd.*, 472 F. Supp. 2d 1131 (W.D. Wis. 2007), the court found that a transaction documented as a lease was instead a sale of goods with a reservation of a security interest and that Article 2 applied to the transaction. Although the court ultimately rejected the lessee's Article 2 defenses, it did consider them.

The *Key Equipment Finance* decision involved a fairly standard three-party equipment financing arrangement. The equipment to be financed was communication equipment supplied by the vendor. The communication equipment was installed on lessee's trucks. To finance the purchase, lessee entered into a Master Lease Agreement and associated equipment schedules with lessor, which purchased the equipment from the vendor for the purpose of leasing it to the lessee. The agreements were drafted as "leases." However, the court characterized the transaction as back-to-back "sales": "[lessor] acquired the T-Fleet Global Messenger Units from [vendor] and [lessee] acquired said units from [lessor]."

The equipment schedules were entered into in 2003 and 2004. Lessee accepted delivery of each unit without objection and the units initially functioned as represented. According to the opinion, in February 2005 the performance of the units became unreliable and then they stopped receiving messages altogether because the vendor lost access to the sub-carrier frequencies which it relied upon to transfer messages to this equipment. By April 2005, the vendor was not returning lessee's phone calls, and stuck with useless equipment, lessee stopped paying lessor under

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Anti-Suit Injunctions

Is the Best Defense A Strong Offense?

By Adam H. Friedman and Fredrick J. Levy

In a case of significance to the secondary loan and distressed claim market, a North Carolina state court has entered an "anti-suit injunction" barring a group of secondary, secured debt holders (the "Fund Defendants"), from commencing any actions against Wachovia Bank. The case, *Wachovia Bank, NA and Wachovia Capital Partners, LLC v. Harbinger Capital Partners, et al.*, Civ. Action No. 07-CVS-5097 is pending in the General Court of Justice, Superior Court Division (Mecklenburg, NC) (the "State Court Anti-Suit Action"), but its parties and the underlying facts arise from the Chapter 11 case of *In re Le-Nature, Inc.* pending in U.S. Bankruptcy Court, Western District of Pennsylvania (the "Bankruptcy Case").

The allegations in the Bankruptcy Case are lurid and filled with tales of fraudulent actions. Certain facts are clear. Shortly after Le-Nature and the Lender entered into the senior credit facility, court-appointed crisis managers discovered fraud and the bankruptcy followed soon thereafter.

In the Bankruptcy Case, the Fund Defendants and other secondary market purchasers not sued by the Lender formed an Ad Hoc Committee to, among other things, investigate possible claims

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the lease. Lessor sued for breach of contract, specifically relying on an "*Obligations Absolute*" (Hell or High Water) provision that read:

> NOTWITHSTANDING ANY CLAIM OR DEFECT OR ANY OTHER REASON WHATSOEVER, ALL RENTALS AND OTHER PAYMENTS UNDER EACH LEASE SHALL BE PAID BY LESSEE TO LESSOR OR ITS ASSIGNEES ABSOLUTELY AND UNCONDITIONALLY, WITHOUT ANY DEFENSE, SETOFF, CLAIM OR COUNTERCLAIM OF ANY NATURE …

SUMMARY JUDGMENT MOTION

Lessor moved for summary judgment on the basis of UCC §2A-407 (which makes the lessee's promises under a finance lease irrevocable and independent) and, alternatively, breach of the "*Obligations Absolute*" clause. Lessee also moved for summary judgment on the basis that the lease was, in fact, a sale, and that it was entitled to revoke acceptance of the non-conforming goods under UCC §2-608(1).

The court first determined, on the basis of UCC §1-203, that the lease created a security interest and was not a true "lease" for the following reasons: 1) lessee was not permitted to terminate its monthly payment option; 2) lessee was absolutely obligated to purchase the equipment; and 3) the purchase price was a nominal amount, $1. Because the lease was not a true lease, the lease was also not a "finance lease" (to qualify as a finance lease, a transaction must first qualify as a lease). This is important because a "finance lease," as defined in UCC §2A-103(l), is afforded automatic "Hell or High Water" treatment pursuant to UCC §2A-407(2). The decision underscores the importance of a "hell or high water" clause, as lessor was able to fall back on the "*Obligations Absolute*" clause and recover despite the court's finding that the lease was not a "finance lease" (or even a true "lease").

If a "lease" creates a security agreement, is it a sale to which Article 2 applies? The court applied Article 2 and answered this question with little discussion: "when a transaction purports on its face to be a lease, but is in fact a sale with reservation of a security interest in the vendor, it becomes subject to the law of sales." *Id.* (*citing Centurian Corp. v. A.L. Cripps*, 624 P.2d 706 (Utah 1981)).

However, *Centurian* involved only a two-party transaction, and in *Key Equipment Finance*, the security interest was not reserved by the vendor, but rather by the financier. Do those differences place the transaction outside the scope of Article 2?

Article 2 "applies to transactions in goods; it does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate *only* as a security transaction." UCC §2-102. The application of UCC §2-102 might be worth noting. In *General Electric Credit Corp. of Tennessee v. Ger-Beck Machine Co., Inc.*, 806 F.2d 1207 (3rd Cir. 1986), the court found that §2-102 prevented the application of UCC-2 to a lease in a similar three-party transaction because the lease was intended only to operate as a security transaction. However, the dissent argued that the transaction had elements of both a sale and a secured loan, and that Article 2 should apply. Because Article 2 could be found to apply to transactions documented as leases, but re-characterized as sales, lessors must be sure that the lease documents fully protect them from risks associated with the application of Article 2 to the transaction.

TWO UCC-2 DEFENSES

The *Key* court's decision to treat the lease as a sale to which Article 2 applied instead of a lease led it to consider two UCC-2 defenses raised by the lessee: 1) the goods were non-conforming and lessee had a right to revoke its acceptance under

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Toll Road Leasing Programs: Ready To Roll?

Part Two of a Two-Part Series

By Sven C. Hodges

Part One of this series discussed precedent transactions and standard terms and conditions in the toll road leasing market. The conclusion continues the discussion of terms and conditions and addresses legislative developments.

Capital Improvements

Toll Road leases often contain provisions addressing development and financing of capital improvements to the relevant toll facility during the lease term. With respect to the Chicago Skyway and the Indiana Toll Road, for instance, the concessionaire is required to make certain capital improvements at its own cost, while other capital improvements are to be undertaken at the cost of the state. Most concessions provide that the state will continue to use its powers of condemnation as necessary to acquire any additional land required to implement such capital improvements. In addition, lessees often negotiate for the right to undertake lessee-initiated capital improvements that the lessee believes will improve the operational functionality — and hence profitability — of the roadway in question.

As mentioned above, lease concessions often contain provisions regarding mandatory capital improvements. For instance, the lease concession for the Indiana Toll Road requires both the concessionaire and the Indiana Finance Authority to make certain capital improvements set forth in schedules to the concession agreement. In addition, the lease concession for the Pocahontas Parkway requires Transurban to construct a 1.58-mile, four-lane extension connecting the Parkway to the Richmond International Airport, subject to Transurban's ability to secure $150 million in credit assistance under the Transportation Infrastructure Finance and Innovation Act. Transurban is required to conduct a competitive bid process for a design-build contract for the airport connector road. The VDOT may cancel the construction of the airport connector road if the projected development costs exceed $45,200,000. If it does not exercise its cancellation option, the VDOT is required to reimburse Transurban for all development costs exceeding that threshold.

Guarantees/Letters of Credit

Concessionaires may also be required to establish guarantees or letters of credit with respect to their obligations under the relevant lease concession. For instance, the lease concession for the Pocahontas Parkway requires Transurban to establish a cash reserve fund or letter of credit each year in an amount equal to the cost of any extraordinary maintenance and repair work projected to be performed for the following five-year period. Transurban is also required to deliver a letter of credit in an amount equal to 110% of any shortfall projected for the following year's budget for ordinary operating, maintenance, and repair costs (less projected toll and other revenues). Letters of credit may also be required in order to ensure that the concessionaire will continue to maintain for relevant toll facility during the final years of the lease concession. For instance, 10 years prior to the expiration of the lease concession for the Chicago Skyway, SCC is required to establish a letter of credit in favor of the concession grantor in an amount equal to the highest gross revenues received in the preceding 10 years. Similarly, six years prior to the expiration of the lease concession for the Indiana Toll Road, the ITR Concession Company is required to establish a letter of credit in favor of the Indiana Finance Authority in an amount sufficient to cover the costs of capital improvements required to be performed by the concessionaire during the remainder of the lease term.

Events of Default And Termination Rights

The concession agreements for each of the Chicago Skyway, the Indiana Toll Road, and the Pocahontas Parkway contain substantially similar events of default. Under each concession agreement, events of default are triggered upon a material breach of any representation or of any payment or other obligation under the relevant lease concession (subject to certain cure periods). Certain customary insolvency events will also trigger an event in default. In addition, each concessionaire will trigger an event of default under the relevant lease concession upon an unauthorized transfer of the concessionaire's leasehold rights in the relevant toll facility. Upon a default under any lease concession, the non-defaulting party may, among other remedies, terminate the concession agreement and seek to recover any losses arising from the default. Concession grantors also have the right to attempt to cure any concessionaire default.

Upon termination of any concession agreement, possession of the relevant toll facility and any related improvements will revert to the relevant concession grantor. In addition, each lease concession requires the lessor to pay out the fair market value of the lessee's interest in the concession lease if the lessee terminates the concession agreement upon a default by the lessor or if the lease is terminated other than pursuant to its terms. The lease concession for the Pocahontas Parkway also grants the Virginia Department of Transportation the unilateral right to terminate the lease concession for public convenience upon payment of the fair market value of Transurban's interest in the Parkway.

Under each lease concession, an independent third-party appraiser determines the fair market value of any payout. However, lease concessions such as that for the Indiana Toll Road may also require any such

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Toll Road

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payout to be at least equal to the sum of outstanding indebtedness secured by the concession's leasehold interest in the relevant toll facility. The Indiana Finance Authority is also required to use its best efforts to lease or borrow against the Indiana Toll Road or its other assets in order to finance any such payout, with any deficiency to be appropriated from the state budget. Termination payouts may also include a guaranteed rate of return. For instance, any payout of the Pocahontas Parkway, whether upon an event of default or unilateral termination by the VDOT, is required to be at least equal to the sum of outstanding indebtedness secured by Transurban's interest in the Parkway, plus a guaranteed 10.5% rate of return for Transurban.

Adverse Legislative and Other State Action

Lease concessions may contain provisions protecting concessionaires against adverse legislative or other action taken by state legislatures or governmental authorities during the relevant lease term. For instance, with respect to the Chicago Skyway and the Indiana Toll Road, if any such action has a material adverse effect on the fair market value of the relevant concessionaire's interest in the toll road facility, the concession grantor may be required to compensate the concessionaire for any losses as they occur (including increased operating, capital, and maintenance costs as well as any lost toll road revenues). Alternatively, the concessionaire may terminate the lease concession and require the concession grantor to make a termination payout. The lease concession for the Pocahontas Parkway affords the concessionaire similar protections against adverse state action. Thus, the Virginia Department of Transportation is required to compensate Transurban for the adverse economic impact of discriminatory legislation and other state or local action (including any imposition or property taxes or license fee) or if the state expands the class of toll-exempt vehicles.

Third-Party Financing

Concession agreements may also contain provisions regarding the concessionaire's right to securitize any toll revenues or grant institutional lenders a security interest in its leasehold interest in the toll road. For instance, under the lease concession for the Indiana Toll Road, institutional lenders and beneficiaries of any securitization vehicle have a 30-day period to cure any default by the ITR Concession Company under the terms of the concession agreement. The concession agreement also grants such financing parties the right to foreclose on their interest in the toll road and to take possession of and manage the toll road upon a default under the terms of the relevant financing documentation. Upon foreclosure, the financing parties (or an approved transferee) will take the concessionaire's interest in the toll road subject to the concessionaire's obligations under the concession agreement. However, prior to the commencement of foreclosure proceedings, the Indiana Finance Authority has the right to purchase the interest of such financing parties in the toll road and any related revenues for the full amount secured by the toll road and related revenues. The Indiana Finance Authority will be able to secure funding for the purchase price through the appropriation process, by borrowing against the toll road or by re-leasing the toll road to a new concessionaire.

TOLL ROAD LEASE CONCESSIONS: LEGISLATIVE DEVELOPMENTS

Following the successful leasing of the Chicago Skyway, more than a dozen states enacted statutes authorizing public-private partnerships, including long-term leases of toll facilities. In addition to Indiana and Virginia, states that have enacted PPP legislation enabling the long-term lease of transportation facilities include Alabama, Alaska, Arizona, California, Colorado, Delaware, Georgia, Louisiana, Maryland, Minnesota, Missouri, Nevada, North Carolina, Oregon, Utah, and Washington. Similar legislation proposed in a number of other states, including New Jersey, remains subject to ongoing negotiation.

The U.S. Department of Transportation has prepared model legislation that identifies many of the key issues addressed in such enabling statutes, whether enacted or proposed. The model legislation sets forth provisions for the solicitation, evaluation, and selection of private sector PPP proposals, including lease proposals, as well as the evaluation and selection of unsolicited PPP proposals. After a solicited or unsolicited lease proposal has been selected, the winning contractor is required to enter into a public-private agreement with the state authority owning the relevant transportation facility. This agreement is required to contain certain mandatory provisions set forth in the model legislation, including provisions relating to the term of the lease, the nature of the contractor's operational or other responsibilities, actions the authority may take to ensure proper maintenance, toll fee determination and collection, and contract termination and amendment. Upon an event of default under the agreement, the model legislation permits the state authority to replace the operator or terminate the agreement. Additionally, the model legislation exempts any leased transportation facility from state property taxes and permits the authority to exercise state eminent domain powers to acquire the necessary property rights for the transportation facility.

California provides a representative example of PPP legislation authorizing toll road lease transactions. Under California Streets and Highway Section 143, the California Department of Transportation and certain regional transportation agencies have the sole right to "solicit proposals, accept unsolicited proposals, negotiate and enter into comprehensive development lease agreements" for toll facilities. The statute sets forth certain procurement approaches that may be utilized in selecting private entities for leasing arrangements. After a period for public comment, a negotiated lease agreement must be submitted to the

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Injunctions

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that the debtor's estate might have, including claims against the Lender. The Lender was a possible target because it, or affiliates, had also acted as Le Nature's financial adviser, underwriter for unsecured notes of the debtor, and investment banker to the debtor regarding a sale process. This relationship has led the Fund Defendants to label Lender as a "trusted advisor" to the Le Nature management team and an architect of the debtor's capital structure. The Fund Defendants maintain that no decision was made to commence any action, including against the Lender.

Anticipating a lawsuit by the Fund Defendants based upon news articles and other "public statements," the Lender executed a shock and awe preventive strike by commencing the State Court Anti-Suit Action and obtaining an *ex parte* TRO to bar the Fund Defendants from filing tort claims against the Lender. The Lender sought refuge in its home state to take advantage of North Carolina's champerty law, which Lender maintains bars the assignment of tort claims. The Fund Defendants opposed the preliminary injunction and filed a motion to dismiss for lack of jurisdiction. They also removed the State Court Anti-Injunction Action to the U.S. District Court for the Western District of North Carolina and sought dismissal or an order remanding the action to the U.S. District Court for the Western District of Pennsylvania, the district where the Bankruptcy Case is pending. The state court has granted the preliminary injunction. The district court has refused jurisdiction and remanded back to the state court.

The Preliminary Injunction And Forum Determination

Pending a full trial in North Carolina Superior Court, the Fund Defendants, and all others "acting in active concert or participation with them" as well as future assignees of claims are enjoined from pursuing virtually all tort claims (ranging from breach of fiduciary duty to racketeering) against Lender "with respect to [Lender's] role relating to the Credit Agreement."

The Preliminary Injunction Order provides that the Fund Defendants can only assert their tort claim against Lender in the Anti-Injunction Action as counterclaims. Finally, the court reserved decision as to whether personal jurisdiction had been obtained over the Fund Defendants.

Findings of Fact

The state court granted the Preliminary Injunction with 18 findings of fact and nine conclusions of law. What the court deemed of particular importance is of interest.

The findings of fact include the following:

- The Fund Defendants purchased their claims after Le Nature's fraud became widely known and after the Bankruptcy Case was commenced;
- The Commitment Transfer Supplements by which the Fund Defendants "became lenders" (the documentation entered into with Lender after taking the assignment of the claim from the assignor) and which Supplements explicitly provided for assignment of all tort claims provided for the application of North Carolina law as did the original Credit Agreement;
- The LSTA forms by which the Fund Defendants took assignment of their claims, but to which Lender was not a party, provided for application of New York law and "purport to override any contrary terms of the Supplements."
- "The Fund Defendants have taken actions making it clear that the Fund Defendants intend to assert and pursue tort claims, which the Fund Defendants assert have been assigned to them directly (or indirectly through intermediate assignments) by other members of the syndicate, against Wachovia … ";
- "Unless this Court enters this Preliminary Injunction to ensure that the Fund Defendants assert any assigned Personal Tort Claims against Plaintiffs only in this action, it will be impractical for the Plaintiffs to obtain the determination they seek [that the assignment of the tort claims is impermissible] in a reasonable and orderly manner consistent with the ends of justice. Further, unless this Court enters this Preliminary Injunction to ensure that any person or entity to which any Fund Defendant assigns any such Personal Tort Claims is bound by this Order and consents to be joined in this action, it will be impractical for the Plaintiffs to obtain the determination they seek in a reasonable and orderly manner consistent with the interests of justice."
- "The controversy presented for resolution in this action should be fully and solely resolved in this Court to prevent the Plaintiffs from being subjected to a multiplicity of lawsuits concerning the effectiveness and enforceability of the assignments and any future assignments of Personal Tort Claims against the Plaintiffs arising from or relating to the Credit Agreement. Any other proceedings instituted concerning these issues would be duplicative, wasteful, vexatious, and harassing. Injunctive relief should be entered here, on a preliminary basis, to prevent duplicative litigation, which might produce inconsistent results."

Conclusions of Law

The nine Conclusions of Law in the Preliminary Injunction are without citation to case law. There is only citation to the North Carolina preliminary injunction statute and its companion rule of civil procedure. The court concluded that: "Anti-suit injunctions have been recognized as appropriate to address a threat to a court's jurisdiction, to prevent the evasion of important public policy, to prevent a multiplicity of suits, or to protect a party from vexatious or harassing litigation. Such an injunction is warranted here."

Finally, the court also concluded that limiting the right of the Fund Defendants to bring their claims against Lender only as counterclaims in the Anti-Injunction Case "will not injure [Lender] and the Fund

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UCC §2-608 and then cancel the contract under UCC §2-711; and 2) that the "*Obligations Absolute*" clause left it with no remedy in violation of UCC §2-719.

The court's discussion of these defenses is a bit confused. For example, the court disposed of the first defense on the ground that the equipment was not "non-conforming," because the equipment worked but the service of transmitting the signals was defective. Because the equipment was "conforming," the lessee could not revoke acceptance under UCC §2-608(1). Arguably, this analysis was misdirected. Under UCC §2-106(2), goods are conforming "when they are in accordance with the obligations under the contract." Under the lease, which was the only contract between lessor and lessee, the goods were leased "AS IS." A reasonable argument seems to be that if the equipment which, by the express terms of the lease documents, is *leased* "AS IS," it can't be "non-conforming."

Lessee's second defense was that because of the "*Obligations Absolute*" clause, it had no remedy to address its receipt of defective equipment, and that UCC §2-719 requires that some remedy be available to a buyer. The official comment to UCC §2-719 provides, "it is of the very essence of a sales contract that at least minimum adequate remedies be available … there [must] be at least a fair quantum of remedy for breach of the obligations or duties outlined in the contract." Although the court considered this defense, it should have been irrelevant, unless the court determined that the lessor delivered non-conforming goods to the lessee. As mentioned above, "non-conformity" of the goods was deemed not to be an issue.

Nonetheless, the court found that an assignment from lessor to lessee of breach of warranty claims against the vendor under the lease was a sufficient remedy for the lessee. Interestingly, language intended to protect the lessee/buyer in a back-to-back sale transaction (by ensuring that lessee can maintain breach of warranty claims against the vendor) actually aided the lessor by convincing the court that lessee did have an adequate remedy.

Right Result

In the end, the court reached the right result and awarded damages to lessor under the "*Obligations Absolute*" clause. The practical application of this case for equipment lessors is to draft leases so as to protect their interests in the event that the lease is found to be something other than a lease. Many well-drafted lease documents already include provisions that cover the possibility that the lease will be subject to UCC-2 as well as UCC-9.

The *Key Equipment Finance* case is an excellent reminder of the stakes of failing to protect against an Article 2 re-characterization risk. The equipment's collateral value depended on the continuing reliability of the vendor and its communications services. In this case, the vendor was apparently insolvent, and the risk of this insolvency could have been re-allocated to the lessor. Specifically, the lessee was arguing that the transaction was really the second in a series of back-to-back "sales." So, if it was permitted to reject (per UCC-2) the delivery by the lessor of the equipment, the lessor would have to resort to the vendor (also per UCC-2) for some remedy; but without a credit-worthy vendor, the lessor would have been left with worthless collateral and worthless warranty claims.

To protect themselves, lessors should ensure that their lease documents disclaim all Article 2 Seller's warranties contained in §2-312 through §2-316 of the UCC, including the warranties of merchantability and warranty of fitness for a particular purpose.

Note that the *Key Equipment Finance* lease contained the following disclaimer:

> LESSEE LEASES THE EQUIPMENT ON AN 'AS-IS,' 'WHERE IS' BASIS. LESSOR MAKES NO REPRESENTATION OR WARRANTY OF ANY KIND WHATSOEVER, EXPRESS OR IMPLIED, REGARDING ANY EQUIPMENT, INCLUDING, WITHOUT LIMITATION, ANY IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE.

This language should have eliminated the need for the court's analysis of whether the equipment was "non-conforming" and whether lessee had a sufficient remedy. It does appear that it at least prevented lessee from making a breach of warranty claim against lessor.

Leases should limit lessee's (as buyer) remedies for defects or other breaches of warranty regarding the equipment, and should specifically exclude lessee's (as buyer) right to reject or revoke acceptance of non-conforming goods. However, a lessee should be given some recourse in that circumstance, but still maintain the "hell or high water" nature of the lease obligations. Under the *Key Equipment Finance* lease, lessee agreed "to look only to Supplier or the manufacturer for any defect or breach of warranty regarding the equipment." Although the court's overall analysis was misplaced, the court found this to be an enforceable limitation of remedy.

Lessors should also consider the possible tax, regulatory, and other consequences of a lease being re-characterized as a sale, and make sure that their documents contain proper protective provisions.

Obviously lessors should continue to ensure that their lease documents contain appropriate Article 9 protections in the event the lease is re-characterized as creating a security interest, as in *Key Equipment Finance*. As most equipment finance parties know, this re-characterization will impact the remedies which can be pursued by lessor and raises priority issues. So, lessors should continue to file precautionary financing statements under §9-505 to perfect the potential security interest. Among other things, lease forms should also continue to contain granting clauses, lien searches as closing conditions, lien removal provisions, usury and other loan-related regulatory protections, and other rights and remedies on which lessor may have to rely if its rights are to be governed by UCC-9 and not UCC-2A to create the security interest.

FTC and Texas AG File Suit Against IFC Credit

In yet another round of lawsuits stemming from the NorVergence telecommunications fraud, the Federal Trade Commission and the Attorney General of Texas filed simultaneous complaints in the U.S. District Court for the Northern District of Illinois and Harris County, TX, against Illinois-based commercial finance company IFC Credit for violating federal law by helping to finance the scheme and continuing to seek payment from defrauded NorVergence customers.

According to the FTC's complaint filed June 6, IFC Credit Corporation purchased NorVergence rental agreements valued at $21 million, with individual contracts ranging from $4439 to $160,672. The complaint alleges that despite making payments, no customers received telecommunications services from NorVergence for more than a short period of time, and many consumers received none. It further alleges that IFC continued to finance the fraudulent scheme by accepting new rental contracts, despite NorVergence's failure to provide the promised services and the resulting high rate of default among IFC customers. In addition, long after NorVergence entered bankruptcy in 2004, IFC continued to tell consumers they were obligated under the rental agreements because the payments are for the device, not for services.

Under the lawsuit, brought under the FTC Act, which prohibits unfair or deceptive business practices, the FTC charges IFC with misrepresenting that consumers have no defenses to payment on the NorVergence rental agreements; harming consumers by unfairly accepting and collecting on the rental agreements; and unfairly filing debt collection lawsuits in courts far from consumers' locations. The FTC is asking the court to order all rental agreements terminated and is seeking refunds for payments consumers made for services they never received. The FTC also is seeking a preliminary injunction to stop IFC from continuing any debt collection while the suit proceeds.

The petition, filed by the Consumer Protection Division of the Texas Attorney General's office, similarly seeks the dissolution of debts incurred by fraudulent means and the cancellation of wrongful contracts. The AG also asked the court to void lawsuits IFC has filed against debtors since 2004, given that the company misled business owners into thinking they had no defenses in debt collection cases and that the debts were enforceable.

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Defendants are entitled to assert their legal claims in some court of law."

Champerty and Home Court Advantage

At the core of Lender's pre-emptive strike is the legal doctrine of champerty and an apparent home court advantage, both of which date back centuries. Generally, champerty is a defense that prevents the assignment of claims made for the sole or primary purpose of pursuing litigation. Although the applicability of champerty to the facts at hand is hotly contested by the parties, it is beyond doubt that North Carolina interprets and applies the doctrine far more broadly than does New York, the other possible choice of law for the controversy, which the Lender asserted "has no meaningful limitations on champerty and does not void assignment of tort claims." Thus, the linchpin of the pre-emptive strike is the willingness of the North Carolina court to conclude: first, that, for the purposes of the Preliminary Injunction at least, it had personal jurisdiction over the Fund Defendants; and, second, that North Carolina law did in fact apply. Interestingly, in making the latter conclusion, the court chose to honor the choice of law provision contained in Lender-drafted Credit Agreement and the transfer Supplement between Lender and each Fund Defendant, rather than the standard LSTA assignment form between the assignors and each Fund Defendant as assignee, which contained New York as the choice of law.

Conclusion

Forum shopping is certainly not a new tactic to seek advantage in litigation. However, the prospect of pre-emptive, jurisdiction-grabbing lawsuits will not sit well with holders in the secondary market. If the ruling stands, it will likely become a more widely used strategy for parties looking for home court advantage to protect themselves against all manner of prospective plaintiffs' claims. Thus, parties must carefully consider which facilities and applicable choice of law provisions they invest in.

The broad interpretation of champerty, the broad exercise of personal jurisdiction, and rejection of the primacy of the universal LSTA assignment form would seem to undermine the strong public policy in favor of the free alienability of property necessary to our financial markets. This policy has contributed significant and generally accepted benefits to the credit markets. Indeed, it would seem that originating lenders have been primary beneficiaries of the secondary market, making this case even more interesting. Moreover, this tactic may have the unintended consequence of encouraging more litigation and creating a "race to the courthouse" mentality. Aggrieved parties may be forced to sue early and fast to beat the anticipated home court, pre-emptive strike. If this were to occur, parties in bankruptcy situations may need to consider jurisdictional provisions in DIP financing or similar orders.

Given this reality, it must be asked if this case is an aberrational struggle brought on by the specific facts, or is it a harbinger of an institutional rift between originating banks and secondary market participants.

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IN THE MARKETPLACE

Stroock & Stroock & Lavan LLP has announced that three partners from Brown Rudnick Berlack Israels LLP have joined the firm's New York office. **Boris Ziser** is joining the Structured Finance Practice Group. He focuses on public and private mortgage-backed and asset-backed securitizations, warehouse facilities, commercial paper conduits, and related transactions. His experience includes a variety of asset classes such as equipment leases, auto loans, and franchise loans. In addition, **Albert J. Pinzón** and **Thomas R. Weinberger** are joining Stroock's Insurance Practice Group. Pinzón has a particular focus on cross-border transactions, insurance-linked securities, and corporate restructurings and regularly develops and structures complex finance solutions for financial institutions that bridge traditional finance with structured finance. Weinberger focuses his practice on insurance and risk-linked securities, life insurance finance, and related capital markets transactions. He represents insurers, reinsurers, and investment banks, as well as both buyers and sellers in major transactions.

Troutman Sanders LLP has announced the addition of **Craig M. Kline** and **Philip H. Spector** as partners in the law firm's New York office. Kline joins the firm's Lending & Structured Finance and Energy practice groups, and Spector joins the Tax group. They join Troutman Sanders from the law firm of King & Spalding in New York City, where they worked together for six years, Kline as a partner since 2004 and an associate from 2001 to 2004, and Spector as a partner since 2001. They were responsible for the firm's equipment and facility leasing practice. At Troutman Sanders they will continue to focus their practice on representing banks and other capital providers as investors, lenders, and credit support providers in a wide variety of financial transactions. They bring a strong range of experience with tax-based asset finance, including domestic and cross-border leveraged leasing, operating leasing, and project finance, with an emphasis on renewable energy finance.

Dewey Ballantine LLP of New York has added two partners to the firm's structured finance group. **Patrick de Carbuccia** and **Alexander G. Fraser** are joining Dewey from the New York office of Reed Smith. This move follows the recent addition of two other partners from Reed Smith, **John J. Altorelli** and **Jeffrey A. Potash**, who also became Dewey structured finance partners. Both de Carbuccia and Fraser specialize in general corporate transactions, with a particular emphasis on private equity funds. Dewey is reportedly increasing its structured finance practice to accommodate an expected rise in "asset-backed buyouts," which are gaining favor with private equity groups.

Toll Road

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California state legislature, where the agreement will be deemed approved unless rejected by both houses within 60 days of submission. The statute also contains provisions regarding the terms of the lease concessions themselves that reflect many of the key issues identified above with respect to the concession agreements for the Chicago Skyway, Indiana Toll Road, and Pocahontas Parkway. Lease agreements are required to establish performance standards as well as specified toll or user fee rates, with any increase to be approved by the relevant state agency. Lessees are required to apply toll road revenues and user fees to capital and operation costs, expenses for state services, and a reasonable return on investment. Lease agreements may require any excess revenue to be applied to debt reduction or capital improvements or paid into the State Highway Account. The toll facility will revert to the relevant public agency upon any failure to comply with the lease agreement.

Conclusion

Although some commentators have called for a single national plan for leasing toll roads, states remain the primary incubators for toll road leasing programs. One advantage of this approach is to allow states to tailor their leasing programs to the highly specific physical, political, and economic factors applicable to each state roadway system. Lease terms that may make sense for an urban environment like Los Angles or Chicago may be inappropriate for more rural areas such as Texas. Single concession payment transactions such as those adopted in Illinois and Indiana may not be as attractive to some states as programs that provide for ongoing toll revenue sharing. Regardless of whether a truly uniform market in this area develops, or more of a state-by-state approach remains the norm, it seems likely that toll road leasing programs are gaining both traction and speed.

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