Leases

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Case Law Developments

This survey covers several 2017 cases involving parties to equipment financing transactions or with third parties, disputing aspects of the transaction or the related equipment. The courts in these cases considered many of the fundamental issues in establishing and enforcing the respective rights, obligations, interests, and remedies associated with equipment financing agreements. The issues covered in the following cases include whether a transaction documented as a lease creates a true "lease" or a security interest, a lessor's damages remedies, issues surrounding certainty of payment such as "hell-or-high-water" clauses, the rights of assignees of interests under a lease, end-of-lease-term issues, vicarious liability of a lessor, and issues relating to forum selection clauses.

True Leases

The characterization of a purported lease as creating either a true "lease" or a security interest is likely to have a significant impact on the respective rights, remedies, and responsibilities of the purported lessor and lessee. Accordingly, this issue is typically litigated in bankruptcy or enforcement cases, or priority disputes, with significant implications to the purported lessor's recovery of its investment by payment of the periodic or accelerated amounts or the related equipment. The case summarized below reflects the import of characterization on the parties to the referenced transaction.

In *In re Jack*,[1] the court in a Chapter 13 bankruptcy case was asked to consider a motion by Acceptance Now ("Acceptance"), the purported lessor, to compel Jeremy S. Jack (the "Debtor") to assume or reject an unexpired rental-purchase

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1. 579 B.R. 627 (Bankr. M.D. Fla. 2017).

agreement (the "Agreement") by which Debtor was acquiring bedroom furniture and a tool bench (the "Property"). Acceptance sought this relief from the court because, if granted, Acceptance was likely to achieve a greater recovery than was contemplated in the Debtor's Chapter 13 plan, which treated Acceptance as a secured creditor and provided for Acceptance's recovery of only $900 of the $5,892 owed by Debtor under the Agreement.[2]

When considering Acceptance's motion to compel, the court had to first determine whether the Agreement ought to be characterized as a true "lease" or a security agreement.[3] Under the Agreement, Debtor could become the owner of the Property by: "(1) paying the stated purchase price in full; (2) making monthly rental payments for 37 months; or (3) exercising an 'Early Purchase Option' at any time by paying the purchase price, together with any past due payments and additional charges associated with the 'Early Purchase Option.'"[4] The court noted that, although bankruptcy courts considering lease characterization issues typically focus on such factors as "whether title to the leased property is transferred to the lessee at the end of the lease term for nominal value,"[5] Florida's Rental-Purchase Agreement Act (the "Act")[6] "specifically provides that certain rental-purchase agreements are not security agreements."[7] Given this, the court analyzed whether the Agreement constituted a rental-purchase agreement under the Act,[8] and determined that it met the statutory factors,[9] as it was (1) a "contract for the use of personal property," (2) "entered into by Debtor, who is an individual," (3) that "involves the lease of property being used for household purposes," (4) "has an initial period of two months," (5) "is automatically renewed with each rental payment after the initial two month lease period," and (6) permits Debtor to "acquire ownership" of the Property.[10]

Because the Act expressly stated that a "rental-purchase agreement" (as defined in the Act) is deemed to be a lease and not a security agreement,[11] the court held the Agreement to be a true lease and granted Acceptance's motion to compel the Debtor to assume or reject the Agreement under section 365 of

2. *Id.* at 628 (noting the remainder of Acceptance's $5,892 claim was to be treated as unsecured under the Chapter 13 Plan and was "unlikely" to be paid).

3. *Id.*

4. *Id.*

5. *Id.* This factor is one of the four "bright line" factors listed in the two-part test in U.C.C. § 1-203(b), the starting point for most commercial and bankruptcy courts considering characterization of a purported lease. Among the pertinent factors specified in U.C.C. § 1-203(b) as being indicative of security interest characterization is that the lessee has an option to become the owner of the goods for no additional consideration or for nominal additional consideration. U.C.C. § 1-203(b)(4) (2011).

6. FLA. STAT. §§ 559.9231–559.9241 (2017).

7. *In re Jack*, 579 B.R. at 629.

8. *Id.*

9. *See id.* (citing FLA. STAT. § 559.9232(1)(e)) (noting that the Act "defines [a] 'rental-purchase agreement' as an agreement [(1)] for the use of personal property, [(2)] by a natural person, [(3)] for personal or household use, [(4)] for a period of four months or less, [(5)] that is automatically renewed with each rental payment following the initial period, and [(6)] that permits the lessee to acquire ownership of the property").

10. *Id.*

11. FLA. STAT. § 559.9232(2)(f).

the Bankruptcy Code.[12] However, prudent lessors should be aware that characterization of property in bankruptcy is state-law specific,[13] and in the absence of specific state statutory classifications such as those present in this case (or should the facts have failed to meet the definition of a "rental-purchase agreement" under the Act), a similar agreement is likely to be characterized as creating a security agreement.[14]

Lessor's Damages

Among the critical default remedies for the lessor is the right to demand that the lessee pay damages in a stipulated amount sufficient to compensate the lessor for the loss of its bargain as anticipated at the time of the lease's inception. The U.C.C. recognizes the enforceability of a liquidated damages remedy in a lease, by which a lessor may demand payment of a specified amount or an amount determined by a formula, after the occurrence of a default or other act or omission, "that is reasonable in light of the then anticipated harm caused by the default or other act or omission" giving rise to these damages.[15] Each of the courts in the two liquidated damages cases summarized below awarded acceleration damages to the lessor, but not the amounts payable under the liquidated damages formulas in the subject leases because the contracted amounts would have resulted in windfalls for the lessors. Neither of the opinions in these cases referenced any analysis of U.C.C. section 2A-504 or any other provision of the U.C.C. that might have pertained to the appropriate damages award.[16]

The court in *Quality Equipment Leasing, LLC v. Alabama Logistics, LLC*[17] granted the lessor's motion for summary judgment on a breach of contract claim against the lessee, but denied the lessor's request for liquidated damages without regard to the applicable provisions of the U.C.C. The lessee stopped paying rent under its four lease agreements with the lessor, and the lessor de-

12. *In re Jack*, 579 B.R. at 628.

13. *Id.* at 629 (citing *In re* Porterfield, 331 B.R. 480, 482 (Bankr. S.D. Fla. 2005)).

14. Per the U.C.C., "Whether a transaction in the form of a lease creates a 'security interest' is determined pursuant to Section 1-203." U.C.C. § 1-201(b)(35) (2011). As noted above, by the terms of the Agreement, one or more of the purchase or renewal options could have caused the transaction to be characterized as creating a security interest pursuant to U.C.C. § 1-203, but the court, without referencing the statutory or other authority for doing so, determined that the Act preempted the applicable provisions of the U.C.C. *In re Jack*, 579 B.R. at 628–29. The preemptive nature of another state law over the applicable provisions of the U.C.C. in that state has been frequently litigated in cases involving motor vehicle leases with terminable rental adjustment clauses (i.e., "TRAC" leases). *See* Edward K. Gross, Dominic A. Liberatore & Stephen T. Whelan, *Leases*, 72 Bus. Law. 1079, 1081–82 (2017).

15. U.C.C. § 2A-504(1) (2011).

16. *See, e.g.*, *id.* § 2A-504(2) (assuming each of the two leases were true "leases," a safety net provision would apply so that, if a liquidated damages formula in a lease does not comply with U.C.C. § 2A-504(1), or is an exclusive or limited remedy that circumstances cause to fail of its essential purpose, the lessor may rely on other remedies under U.C.C. Article 2A). Among the remedies available when a liquidated damages clause fails, the lessors could have relied on applicable statutory damage remedies. *See id.* §§ 2A-527, 2A-528, 2A-529.

17. No. 2:17-CV-00127-AKK, 2017 WL 4304626 (N.D. Ala. Sept. 28, 2017).

clared the leases to be in default and recovered the five trucks and (ultimately) four of the five flatbed trailers leased under those agreements.[18] Further, each of the lease agreements provided that, upon a default the lessor could "'[d]eclare [all] payments . . . due and payable by acceleration . . . as liquidated damages'; and require the payment of 'expenses incurred by Lessor in enforcing its rights . . . [including] reasonable attorney's fees.'"[19]

The lessor sought both actual damages and liquidated damages of $74,583.75 in its suit against the lessee.[20] The court upheld the lessor's claim for actual damages because the amount demanded was equal to the aggregate rentals the lessee was obligated to pay during the period from the default through the termination of each of the leases, "thereby placing the Plaintiffs in the position they would have occupied absent the breach."[21] As noted, the lessor's liquidated damages claim was for the same amount as its actual damages claim, because the accelerated rentals comprising each claim were for the period ending on the termination date.[22] Not surprisingly, the court refused to award the lessor both actual and liquidated damages because such an award "would amount to an impermissible double recovery for the same injury."[23]

Additionally, the court held that the liquidated damages provision was "unenforceable under Alabama Law" because it "qualif[ied] as a penalty."[24] As previously noted, the court relied on Alabama contract law, not U.C.C. Article 2A, when considering the enforceability of the liquidated damages provision in the lease.[25] The court relied on "the basic rule . . . in Alabama" that damages are awarded in an amount to return the non-breaching party to the position it would have had absent such breach occurring.[26] Under Alabama law, if a liquidated damages clause fails to meet any of the following three factors, it is characterized as a "penalty": "(1) the injury caused by the breach must be difficult or impossible to accurately estimate; (2) the parties must intend to provide for damages rather than for a penalty; and (3) the sum stipulated must be a reasonable pre-breach [estimate] of the probable loss."[27] The court found that the accelerated rent requested by the lessor failed both the first and third factors, and thus qualified as a penalty and was "void as against public policy" regardless of the

18. *Id.* at *2, *4–5.

19. *Id.* at *2 (quoting uniform provisions of the lease agreements).

20. *Id.* at *3.

21. *Id.*

22. The lessor's liquidated damages claim was for less than the amount payable as liquidated damages under the leases' required payment of the accelerated rentals through the scheduled expiration date of each lease. *Id.* at *4.

23. *Id.* at *3.

24. *Id.* at *3–4.

25. In fact, there was no discussion in the opinion as to whether the transactions constituted "leases" as defined in U.C.C. § 2A-103(1)(j) or under other Alabama law (e.g., a statute supporting true lease treatment of vehicle leases with terminal rental adjustment clauses). *See id.* at *3 (quoting HealthSouth Rehab. Corp. v. Falcon Mgmt. Co., 799 So. 2d 177, 183 (Ala. 2001) (addressing contract claims for damages)).

26. *Id.*

27. *Id.* (quoting Camelot Music, Inc. v. Marx Realty & Improvement Co., 514 So. 2d 987, 990 (Ala. 1987)).

parties' intent concerning characterization of the damages.[28] Interestingly, the court found that "Plaintiffs implicitly admit . . . by not seeking the recovery of all available liquidated damages under the contract, the sum stipulated is not 'a reasonable pre-breach [estimate] of the probable loss.'"[29]

The court also awarded the lessor the fair market value for the third trailer which was never returned to the lessor, because the lease terms obligated the lessee to return the "leased equipment to the [lessor] in the event of a default."[30] Again, returning to the core case law in Alabama, the court found that the fair market value of the trailer was the "amount necessary to place the [lessor] in the position [it] would have been in had the contractual obligation to return the trailer been performed."[31]

In a previously discussed case, *BA Jacobs Flight Services, LLC v. RutAir Ltd.*,[32] there have been additional proceedings regarding the final calculations of damages, finally closing out this case now familiar to our readers.[33] In our 2017 survey,[34] we discussed the court having held in the then-reported case that the liquidated damages formula in the related lease, on which the lessor's claim was based, was unenforceable. For the reasons explained in that survey, the court then held that "a liquidated damages provision that entitles a lessor to claim the remainder of rent due under a lease as damages irrespective of any repossession or other remedial action taken by the lessor is an unenforceable penalty."[35]

After refusing to uphold the lessor's liquidated damages claim, the court first considered evidence put forth by each of the parties regarding the actual damages to be awarded to the lessor with respect to the lessee's default under the

28. *Id.* at *4 (quoting *Camelot Music*, 514 So. 2d at 990). Had the court analyzed the enforceability of the liquidated damages remedy under the applicable provision of Alabama's U.C.C., ALA. CODE § 7-2A-504 (LexisNexis 2017), the formula might also have been deemed unenforceable for being unreasonable "in light of the then anticipated harm caused by the default or other act or omission" as shown by the court's finding that the third factor which the formula failed as being a "reasonable pre-breach [estimate] of the probable loss." *See Quality Equip. Leasing, LLC*, 2017 WL 4304626, at *4 (quoting *Camelot Music*, 514 So. 2d at 990).

29. *Quality Equip. Leasing, LLC*, 2017 WL 4304626, at *4 (quoting *Camelot Music*, 514 So. 2d at 990).

30. *Id.*

31. *Id.*

32. No. 12 C 2625, 2017 WL 277913 (N.D. Ill. Jan. 20, 2017).

33. Summarized and discussed previously in our 2016 and 2017 Surveys, this case relates to a decision in which the court granted the lessor partial summary judgment as to the defaulted aircraft lessee's liability despite the lessee's argument that, among other things, "it was not in default under the lease because a non-payment default would occur pursuant to the pertinent lease provision only if the lessee failed to 'make *any* payment of rent' within the proscribed period, and that the lessee had actually made *some* payments of rent each month." Edward K. Gross, Dominic A. Liberatore & Stephen A. Whelan, *Leases*, 71 BUS. LAW. 1263, 1277 (2016) (quoting BA Jacobs Flight Servs., LLC v. RutAir Ltd., No. 12 C 2625, 2015 WL 360758, at *4 (N.D. Ill. Jan. 27, 2015)); *see* Gross, Liberatore & Whelan, *supra* note 14, at 1091–93 (analyzing the case).

34. Gross, Liberatore & Whelan, *supra* note 14, at 1091–93.

35. *Id.* at 1092. That article also considered, rhetorically, why (assuming this transaction constituted a true lease) the court did not refer to the guidance provided by U.C.C. § 2A-504, but also noted that it was unlikely that section 2A-504 would have produced a different result. *Id.*; *see* U.C.C. § 2A-504(1) (2011); *see also* 810 ILL. COMP. STAT. 5/2A-504 (2016).

lease.[36] The court was unpersuaded by the evidence put forth by either party, including the lessor's claim because "its damages calculation starts from the premise that it should recover all of the monthly rent payments during the entire term of the Lease Agreement[,]" which acceleration was previously deemed by the court to be "a penalty and not enforceable."[37]

In lieu of accepting the calculation presented by either of the parties, the court ordered damages based on its own calculation.[38] First, at the time the lessor repossessed the aircraft, the lessee owed the lessor various fees, including pilot fees, airfare engine reserve fees, delivery charges, late fees, and maintenance.[39] Second, it was undisputed that there was eleven months of rent due and owed to the lessor by the time it repossessed and sold the aircraft.[40] Third, the lessor presented evidence of additional net operating losses based on efforts to mitigate its losses.[41] Despite the lessee's objections, the court looked favorably on the lessor's efforts to mitigate its damages and included this amount as part of the total damages awarded.[42] In the second reported case, the court confirmed the award to the lessor of late fees accruing on the unpaid damage amounts.[43]

The practice implication of the damages cases summarized above is that a lessor is more likely to achieve its exit strategy when enforcing a defaulted lease if amounts claimed represent the benefit of its reasonably anticipated bargain when entering into the lease, and not a windfall.

"Hell-or-High-Water" Clauses

In *Xerox Corp. v. RP Digital Services, Inc.*,[44] the lessor alleged that the lessee defaulted under a U.C.C. Article 2A finance lease that contained a "hell-or-high-water" clause. The lessee asserted that the lessor breached its obligations by providing defective equipment, and that it was fraudulently induced by the lessor to enter into the contract.[45] The court concluded that, pursuant to the "hell-or-high-water" clause, the lessee expressly had waived any claims or defenses under the lease, regardless of whether the lessor had failed to perform its obligations by providing a defective printer.[46] Next, the court declared that

36. *See BA Jacobs Flight Servs.*, 2017 WL 277913, at *2–3.
37. *Id.* at *2.
38. *Id.* at *3–4.
39. *Id.* at *3.
40. *Id.* at *4.
41. *Id.*
42. *Id.*
43. Discussion of calculations of attorney's fees, costs, and prejudgment interest can be found in the subsequent proceeding. *See* BA Jacobs Flight Servs., LLC v. RutAir Ltd., No. 12 C 2625, 2017 WL 2056193 (N.D. Ill. May 12, 2017). In that final proceeding, it is noteworthy that the court awarded prejudgment interest payable by each of the lessee and the guarantor and attorney's fees and costs payable by the lessee and guarantor, jointly and severally, as both the lease and guaranty specifically provided for recovery of such amounts in such a default scenario. *Id.* at *5.
44. 232 F. Supp. 3d 321 (W.D.N.Y. 2017).
45. *Id.* at 324.
46. *Id.* at 324–25.

the lessee's assertions that Xerox provided "extra-contractual assurances that the printer . . . was fit for a particular purpose" were "insufficient to overcome the clear language of [both] the 'hell-or-high-water' clause" and the contract's disclaimer of the implied warranty of "fitness for a particular purpose."[47] The court further noted that the "entire agreement" clause, along with the "hell-or-high-water" language, precluded the lessee from claiming fraudulent inducement or negligent misrepresentation.[48] Consequently, it is advisable to include disclaimer of warranties and "entire agreement" clauses, and not just rely on a "hell-or-high-water" clause to block a lessee's claims.

In *Construction Resources Group, LLC v. Element Financial Corp.*,[49] the lessee defaulted on its payments, alleging that excavation equipment suffered nineteen failures over an eleven-month period. The lessee claimed that the "hell-or-high-water" clause made the contract unconscionable, but the court declared that such clauses are not oppressive and "[t]here are significant policy reasons for upholding hell or high water clauses [in finance leases] where, as in the equipment leasing industry, the enforceability of the provision aids the parties in obtaining financing that would not otherwise be available."[50] The court further observed that the contract stipulated that it was a "finance lease" under U.C.C. Article 2A, thereby validating the "hell-or-high-water" clause,[51] and thus demonstrating the value for a lease to contain both a "hell-or-high-water" clause and an election to be treated as a U.C.C. Article 2A finance lease.

In *Lease Finance Group, LLC v. Qazi,*[52] the lessee allegedly failed to make payments under a lease agreement containing a "hell-or-high-water" clause. The lessee, whose first language was not English, claimed he was tricked into signing the lease agreement by a salesperson who purposefully neglected to mention that the lessee was signing an equipment lease in addition to a credit card processing services contract.[53] The court noted that thousands of lawsuits had been filed by the assignee and its related entities under similar circumstances, and that the New York Attorney General had filed a lawsuit against the assignee and these

47. *Id.* (citing Xerox Corp. v. Graphic Mgmt. Servs., Inc., 959 F. Supp. 2d 311, 318 (W.D.N.Y. 2013)).

48. *Id.* at 325.

49. No. CIV-14-1394-M, 2017 WL 2266894 (W.D. Okla. May 23, 2017).

50. *Id.* at *4 (quoting Colo. Interstate Corp. v. CIT Grp./Equip. Fin., Inc., 993 F.2d 743, 749 (10th Cir. 1993)) (alterations in original).

51. *Id.* at *3–4. U.C.C. § 2A-407 provides that:

> (1) In the case of a finance lease that is not a consumer lease the lessee's promises under the lease contract become irrevocable and independent upon the lessee's acceptance of the goods.
>
> (2) A promise that has become irrevocable and independent under subsection (1):
>
> (a) is effective and enforceable between the parties, and by or against third parties including assignees of the parties; and
>
> (b) is not subject to cancellation, termination, modification, repudiation, excuse or substitution without the consent of the party to whom the promise runs.

U.C.C. § 2A-407 (2011).

52. 59 N.Y.S.3d 281 (Civ. Ct. 2017).

53. *Id.* at 282.

related entities for allegedly engaging in a fraudulent scheme to ensnare unsophisticated business owners in equipment leases with "hell-or-high-water" clauses.[54] The court denied the assignee's motion for summary judgment because there were issues of material fact as to (a) whether the lessee was induced by the lessor's alleged fraud to enter into the contract,[55] and (b) whether the assignee was on notice of such fraudulent conduct, which would obviate its status as a holder in due course.[56] This decision demonstrates that an assignee or secured party, which has had frequent dealings with the original lessor, might not be able to enforce the "hell-or-high-water" clause where it "should have known at the time it acquired the lease . . . that the means by which the lease had been procured were of dubious integrity."[57]

Rights of Assignees

In *Blue Ridge Bank, Inc. v. City of Fairmont*,[58] the lessee sought a declaratory judgment that it could lower its monthly payments to the assignee under a lease purchase agreement, which contained a "hell-or-high-water" clause and was considered a U.C.C. Article 2A finance lease. The now-bankrupt assignor had applied only half of the amounts remitted to it by the assignee to pay the purchase price for the leased equipment, leaving the lessee to pay the remainder with its own funds. Citing U.C.C. section 9-404, the court concluded that the account debtor could assert against the assignee claims and defenses against the assignor that accrued before the lessee was notified of the assignment.[59] Because the lessee had purchased some of the equipment with its own funds, that equipment was not subject to the lease agreement and hence the assignee could not utilize the "hell-or-high-water" clause to compel payment of the purported rentals for that equipment. The assignee should have followed customary procedures for directing payment of its funds to the vendors for all of the leased equipment.[60]

In *Rapid Capital Financial, LLC v. Natures Market Corp.*,[61] a purchaser of receivables alleged that the seller defaulted under the underlying "Merchant Agree-

54. *Id.* at 282–83.

55. *Id.* at 283–84. "Defendant claims the vendor manipulated him into signing the lease by misrepresenting that 'this is just a paper which makes you responsible for damage or misuse of the equipment.'" *Id.* at 282 (quoting defendant's submission).

56. *Id.* at 283–84.

57. *Id.* at 284 (quoting Studebaker-Worthington Leasing Corp. v. New Concepts Realty, Inc., 887 N.Y.S.2d 752, 757 (App. Term 2009)).

58. 807 S.E.2d 794 (W. Va. 2017).

59. *Id.* at 798–800 (citing U.C.C. § 9-404(a) ("Unless an account holder has made an enforceable agreement not to assert defenses or claims . . . , the rights of an assignee are subject to any other defense or claim of the account debtor against the assignor which accrues before the account debtor receives a notification of the assignment.")).

60. *Id.* at 800–01 (internal quotations and footnotes omitted) ("It is well-established that . . . [t]he hell or high water clause is not . . . watertight . . . . [T]he comments to W. Va. Code § 46-2A-407 clarify that a 'hell or high water' provision is subject to the lessee's revocation of acceptance of goods, the lessor's obligation of good faith, and certain warranty obligations of the lessor.").

61. 66 N.Y.S.3d 797 (Sup. Ct. 2017).

ment" by blocking collection of the receivables. The seller claimed that the Merchant Agreement was actually a loan agreement rather than an agreement to purchase receivables, and as such, would result in imposition of a criminally usurious interest rate.[62] The court focused on two factors to ultimately conclude that the Merchant Agreement was an agreement to purchase receivables rather than a loan, and thus not criminally usurious.[63] First, the court noted that payments to the purchaser were contingent because the Merchant Agreement contained cash flow reconciliation provisions, which limited the purchaser to receiving only its specified percentage of the seller's receivables.[64] Second, the court noted that the agreement did not have a definite date at which repayment of the alleged "loan" would be required, because the time period for the collection of the sold receivables was contingent upon the merchant generating sales which resulted in collection of revenue.[65] The court further declared it was not dispositive that the purchaser had the ability to investigate the merchant's finances or that the purchaser had a security interest in all of the seller's accounts.[66]

In *United Leasing, Inc. v. Balboa Capital Corp.*,[67] the assignee of a vehicle lease alleged a breach of the assignment documents after it came to light during the lessee's bankruptcy that the lessee provided false financial statements to the assignor, the truth and accuracy of which the assignor represented and warranted in the assignment documents. The assignor successfully argued that language in the preamble to the representations and warranties section qualifying each statement to that of "[assignor]'s knowledge" relieved the assignor of any potential liability related to the false financial statements—unless the assignor had knowledge thereof.[68] The court bolstered its conclusion by citing language in the assignment agreement that the assignor was not vouching for the creditworthiness of the lessee or the collectability of the rentals, that the assignee would conduct its own credit review and underwriting of the rentals, and that the assignment was on a non-recourse basis.[69] The court also noted that the assignee had drafted the assignment documents and that any ambiguities would be construed against it.[70]

End-of-Term Issues

In *Midwest Railcar Corp. v. Everest Railcar Services, Inc.*,[71] lessee Everest Railcar Services, Inc. leased certain railcars from lessor Banc of America Leasing & Capital, LLC under a master lease agreement and six schedules. This case involved a

62. *Id.* at 798.
63. *Id.* at 800–02.
64. *Id.* at 800–01.
65. *Id.* at 801.
66. *Id.* In fact, U.C.C. sections 9-109(a)(3) and 1-201(35) require a purchaser of accounts to perfect its interest by filing a financing statement against the seller.
67. No. 3:17-cv-00023-RLY-MPB, 2017 WL 3674926 (S.D. Ind. Aug. 25, 2017).
68. *Id.* at *3.
69. *Id.* at *4.
70. *Id.* at *3–4.
71. No. 16 Civ. 604 (AKH), 2017 WL 1383765 (S.D.N.Y. Apr. 13, 2017).

lessee attempting to unilaterally change the lease-end options contained in the lease. All the lease schedules provided for an irrevocable option exercisable at lease end to either extend the schedules for a renewal period to be mutually agreed upon at a fair market value determined by lessor or to purchase the railcars at fair market value, again as determined by lessor.[72] The lessee exercised the option to do one or the other in a timely fashion pursuant to a letter, which stated "[t]his letter will serve as our written notice to either renew the lease at terms to be negotiated or exercise a purchase option at an amount to be negotiated."[73] Lessee later asserted that the letter exercising the option was merely an indication of "a willingness to either renew the Lease or to purchase the railcars upon receiving specific terms of the renewal or the purchase."[74]

Given that the schedules provided that each of the purchase price and the lease renewal price was to be "the amount equal to the then fair market value . . . as determined by Lessor[,]" the court found that the letter was an attempt to change the price to one to be negotiated, rather than the amount determined by the lessor as set forth in the lease.[75] The court held that such variation with the terms of the schedules had no legal effect and that the lessor was entitled to simply disregard lessee's attempt to change the process or the price.[76] The court concluded that "[lessor] ha[d] stated a claim for breach of contract as a result of [lessee]'s purported revocation of its exercise of the irrevocable option."[77]

In *Winthrop Resources Corp. v. Apollo Education Group, Inc.*,[78] the lessee attempted to prevent its lease with lessor for certain equipment from automatically renewing.[79] During the return process, lessee discovered that a small percentage (3 percent) of the leased equipment had been lost.[80] The lessee advised lessor of same and sent a check to lessor for the fair market value of the equipment as determined by a third party.[81] The lessor asserted that the lessee had renewed the entire lease (including the equipment that was returned) pursuant to a renewal provision that provided that the lease would be renewed automatically for four-month terms if the equipment was not returned as provided in the lease.[82]

The court found that lessee "adequately pleaded a claim for breach of the implied covenant of good faith and fair dealing."[83] The court found that lessor, in bad faith, hindered lessee's attempt to prevent the lease from automatically re-

72. *Id.* at *1.
73. *Id.* at *4 (quoting Everest's letter).
74. *Id.* at *2 (quoting Everest's countercomplaint).
75. *Id.* at *4 (quoting master lease agreement and schedules).
76. *Id.*
77. *Id.*
78. No. 17-1448 (DWF/SER), 2017 WL 3531516 (D. Minn. Aug. 16, 2017).
79. *Id.* at *1.
80. *Id.*
81. *Id.*
82. *Id.*
83. *Id.* at *3.

newing.[84] The court focused on the fact that lessor allegedly refused to explain why lessee's payment for the lost equipment was inadequate.[85]

The court further rejected lessor's argument that lessor was merely requiring lessee to strictly comply with the terms of the lease.[86] Again, the court stressed that lessor never explained why the amount sent by lessee was inadequate and that lessee was simply trying to comply with the lease terms but was prevented from doing so by lessor's bad faith in not explaining why lessee had paid too small an amount for the lost equipment.[87]

In *First Technology Capital, Inc. v. BancTec, Inc.*,[88] the court analyzed the various documents that comprised the lease transaction in order to determine the parties' intent regarding the intended lease term (sixty months versus sixty-one months).[89] The court found that "the entire suite of documents associated with the December 1, 2009, [lease] signing c[a]me into play,"[90] not simply the wording of the master lease and the applicable schedule. The court noted that:

> [Under] the parol evidence rule set forth in KRS 355.2-202, terms included in a writing intended by the parties to be a complete and exclusive statement of the terms of the contract may not be contradicted by any prior oral or written agreement or by any oral agreement entered into contemporaneously with the written agreement intended to be the final expression of those terms. *But two written documents executed contemporaneously may be considered together as evidence of the parties' agreement.*[91]

The court therefore found that "[t]he documents—including the signed quote, the signed assignment papers, and the attachments—were all part of the contemporaneous [lease] transaction."[92] When applying this framework, the court concluded that the issue was nonetheless ambiguous enough to require a jury.[93]

This case also analyzed whether a plaintiff lessor can recover on both a breach of contract theory and also on the theory of conversion in the context of the lessee not returning the equipment in light of the dispute between the parties.[94] At issue was whether the lessee paid rent for the full term (sixty months versus sixty-one months) and was therefore not in default, but would be liable for renewal payments.[95] Alternative issues included whether the lessee was in default and, if so, would this give rise to a claim for conversion.[96] The court noted that

84. *Id.*
85. *Id.*
86. *Id.*
87. *Id.*
88. No. 5:16-CV-138-REW, 2017 WL 4296339 (E.D. Ky. Sept. 26, 2017).
89. *Id.* at *5, *8.
90. *Id.* at *5.
91. *Id.* at *6 (emphasis added) (quoting Calumet Farm, Inc. v. N. Equine Thoroughbred Prods., Ltd. (*In re* Calumet Farm, Inc.), 150 B.R. 403, 409 (Bankr. E.D. Ky. 1992)).
92. *Id.*
93. *Id.* at *8.
94. *Id.* at *10.
95. *Id.*
96. *Id.*

"a plaintiff cannot maintain a conversion claim in addition to a breach of contract claim unless [it] can establish the existence of an independent legal duty separate and apart from the contractual obligation."[97]

The court summarized as follows:

> If [lessee] did not default on rental payments, the jury will meter purchase [option] liability under ¶ 5(B) [of the Lease] at FMV, and [lessee] will owe that amount, yielding title to it, and negating conversion. If [lessee] did default, then the Court anticipates the jury evaluating FMV as a conversion remedy, given that [lessee] would have neither renewed the lease, purchased the equipment, nor returned it to [lessor].[98]

Vicarious Liability

There have been no reported decisions successfully challenging the Graves Amendment[99] since last year's leasing law survey. However, there have been several noteworthy cases to report.

In *Chase v. Cote*,[100] the court highlighted that "protection of the Graves Amendment is limited to harm to persons or property that arises out of the operation of the vehicle 'during the period of the rental or lease.'"[101] In this case, the parties did not dispute that the defendant vehicle owner was engaged in the business of renting vehicles or that the owner initially rented the vehicle to the defendant driver.[102] However, at the time of the accident, it was not clear whether the rental agreement was still in effect. The agreement provided March 25, 2014, as the expiration date, whereas the accident at issue occurred June 6, 2014.[103] Defendant owner testified that an addendum to the agreement provided that, "If you wish to extend the rental period, you must return the vehicle to our rental office for inspection and written amendment of the due-in

97. *Id.* at *11 (alteration in original) (quoting Beacon Enter. Sols. Grp., Inc. v. MDT Labor, LLC, No. 3:12-CV-00759-H, 2013 WL 253134, at *4 (W.D. Ky. Jan. 23, 2013)).

98. *Id.* at *12. Note that this case was reconsidered in February 2018. First Tech. Capital, Inc. v. BancTec, Inc., No. 5:16-CV-138-REW, 2018 WL 662485 (E.D. Ky. Feb. 1, 2018). The court reviewed a motion filed by plaintiff lessor for reconsideration of a portion of the prior summary judgment opinion. *Id.* at *1. Plaintiff lessor contended that it should have been granted summary judgment for conversion liability because it was established that defendant lessee was in default of its non-payment obligations by virtue of having made unauthorized alterations to the hard drive of the underlying leased equipment. *Id.* at *1–2, *5. The court agreed with plaintiff lessor and held that plaintiff lessor was entitled to summary judgment for conversion liability, independent of a possible payment breach. *Id.* at *2, *5.

99. *See* 49 U.S.C. § 30106(a) (2012) ("An owner of a motor vehicle that rents or leases the vehicle to a person (or an affiliate of the owner) shall not be liable under the law of any State or political subdivision thereof, by reason of being the owner of the vehicle (or an affiliate of the owner), for harm to persons or property that results or arises out of the use, operation, or possession of the vehicle during the period of the rental or lease, if—(1) the owner (or an affiliate of the owner) is engaged in the trade or business of renting or leasing motor vehicles; and (2) there is no negligence or criminal wrongdoing on the part of the owner (or an affiliate of the owner).").

100. No. NNHCV 156053762, 2017 WL 3000739 (Conn. Super. Ct. June 12, 2017).

101. *Id.* at *2 (quoting 49 U.S.C. § 30106(a)).

102. *Id.*

103. *Id.* at *1–2.

date."[104] Unfortunately for the defendant owner, there was no such written amendment of the agreement, and it was unclear whether payments were still being made on the agreement.[105] The court therefore denied summary judgment.[106]

The rental agreement at issue here did not contain an automatic renewal clause and instead required an affirmative written amendment extending the expiration date. If the rental agreement had included an automatic renewal clause, subject to local law requirements, the result would likely have been different.

In *Peters v. Hertz*,[107] the court illustrated that, notwithstanding the protections afforded to vehicle owners from vicarious liability under the Graves Amendment, owners can still be found liable under an exception to the Graves Amendment, which exception relates to any negligence or criminal wrongdoing on the part of the owner.[108] The court held a "[defendant owner] may be liable for plaintiff's damages under a theory of negligent entrustment since said cause of action is based upon alleged affirmative negligence on the part of defendant [owner], which is separate and distinct from it being vicariously liable for [defendant driver]'s operation of the vehicle."[109] The court also held that plaintiff "sufficiently raised a triable issue of fact concerning whether defendant [owner] negligently entrusted the vehicle to [defendant driver] and therefore, defendant's motion for summary judgment [was] denied."[110]

In *Negri v. Murphy*,[111] the court analyzed a negligent entrustment claim. In this case, plaintiff sued the defendant driver and also the defendant owner of the motor vehicle for injuries sustained when the driver injured the plaintiff in an accident.[112] The defendant owner moved for summary judgment claiming liability is prohibited under the Graves Amendment, and that the negative entrustment claim fails, because the undisputed facts show the owner was not negligent.[113]

The court noted "[t]he elements of negligent entrustment of an automobile are (1) there is actual or constructive knowledge that the person to whom the automobile is lent is incompetent to operate a motor vehicle and (2) the injury resulted from that incompetence."[114] The court found that the evidence demonstrated the driver had been drinking alcohol the day of the collision.[115] However, the evidence also confirmed the owner rented the vehicle to the driver two days before the collision. The court agreed with the defendant owner that the fact that the defendant driver had been drinking two days after the rental agreement does not itself establish the driver was incompetent to drive the vehicle

104. *Id.* at *2 (quoting unsigned, additional page of rental agreement).
105. *Id.*
106. *Id.*
107. No. SC 3022-16, 2017 WL 3136388 (N.Y. City Ct. July 13, 2017).
108. *Id.* at *1.
109. *Id.* at *2.
110. *Id.*
111. No. NNHCV156054538, 2017 WL 1453894 (Conn. Super. Ct. Apr. 3, 2017).
112. *Id.* at *1.
113. *Id.*
114. *Id.* at *3.
115. *Id.*

on the date of the rental.[116] The court further indicated the defendant was competent to drive the motor vehicle because the driver produced a valid driver's license at the time of the rental.[117] The court further found the plaintiff had not demonstrated any duty by the defendant owner to do a background check on the defendant driver, or that had the defendant owner done so, that it would have discovered any information showing the defendant driver was not competent to drive a vehicle on the date of the injury.[118] The court therefore granted summary judgment in favor of the defendant owner.[119]

Forum Selection Clauses

In *Central Bank of St. Louis v. NEC Amarillo Emergency Center*,[120] the court considered the first-to-file rule in the context of a "floating jurisdiction" or "floating selection" clause. The lessee, under three equipment leases, filed a lawsuit in Texas against the originating lessor and two subsequent assignees of the originator alleging claims of fraud, breach of contract, unjust enrichment, and equitable estoppel regarding the underlying leases.[121] The ultimate assignee filed a special appearance in the Texas action objecting to personal jurisdiction, arguing that the leases include forum selection clauses and that such assignee did not have sufficient nexus to Texas.[122] Such assignee then also initiated its own action in the U.S. District Court for the Eastern District of Missouri claiming breach of the leases. The lessee filed a motion to dismiss the Missouri action or in the alternative a motion to transfer venue to Texas.[123]

The forum selection clauses in two of the assigned leases provided for jurisdiction in "ANY COURT OR COURTS IN THE STATE OF LESSOR'S OR ITS ASSIGNEE'S PRINCIPAL PLACE OF BUSINESS, OR ANY COURT OR COURTS IN THE LESSEE'S STATE OF RESIDENCE, OR IN ANY COURT HAVING JURISDICTION OVER THE LESSEE OR THE LESSEE'S ASSETS, ALL AT THE SOLE DISCRETION OF THE LESSOR."[124] The forum selection clause in the third lease provided: "You consent to jurisdiction and venue of any state or federal court in the state the Lessor or its assignee has its principal place of business and waive the defense of inconvenient forum."[125]

Lessee "argue[d] that the first-filed rule bars [the Missouri court] from considering th[e] case because the Texas Action involves the same dispute and origi-

116. *Id.*
117. *Id.*
118. *Id.* at *4.
119. *Id.*
120. No. 4:17-CV-02214 ERW, 2017 WL 4888981 (E.D. Mo. Oct. 30, 2017).
121. *Id.* at *2.
122. *Id.*
123. *Id.*
124. *Id.* at *1 (quoting two master equipment lease agreements).
125. *Id.* (quoting value lease agreement).

nated at an earlier date."[126] The court articulated the general rule that "the first court in which jurisdiction attaches has priority to consider the case."[127]

The court held that, if the Texas court finds it does have jurisdiction over the assignee, such jurisdiction would have attached at the time of the filing, which was prior to the assignee filing its action in Missouri.[128] On the other hand, if the Texas court finds it did not have jurisdiction over such assignee, jurisdiction would not have attached and the first-to-file rule would not be applicable.[129] The court therefore decided to stay the action until the Texas court rules on the assignee's objection to personal jurisdiction over assignee in Texas, at which point, the court would then conduct a hearing to consider lessee's motion to transfer venue or dismiss the Missouri action.[130]

In *XTRA Lease LLC v. 4D Daylight-To-Dark AG Services, LLC*,[131] the court analyzed whether one party to a lawsuit is precluded from objecting to venue in a given state court and removing the case to a federal court in light of another party having agreed to waive any objection to venue in such state.[132] In this case, the lessee waived any objection to venue in the Circuit Court of St. Louis County, Missouri.[133] On the other hand, the personal guarantors agreed to exclusive jurisdiction and venue of *either*: the Circuit Court of St. Louis County, Missouri, or the U.S. District Court, Eastern District, Missouri.[134] Defendants jointly argued that nothing in the lease expressly prohibits lessee from consenting to removal to a federal court.[135] The court held that "the [forum selection] clause plainly precludes a party from objecting to venue by removing a case to federal court once the suit is brought in a Missouri state court."[136] Although the forum selection clause did not specifically mention removal, the court held it was sufficiently clear the parties intended to restrict all litigation to the Missouri state court.[137] The court therefore held that, once the lawsuit was filed in the Circuit Court of St. Louis County, Missouri, the forum selection clause prohibited lessee from objecting to venue.[138]

The court then noted that, "[u]nder the 'rule of unanimity,' it is well established that . . . all defendants in a multi-defendant case must consent to removal, or the case will be remanded."[139] The court concluded that, "[e]ven if the [per-

126. *Id*. at *2.
127. *Id*. (quoting Orthmann v. Apple River Campground, Inc., 765 F.2d 119, 121 (8th Cir. 1985)).
128. *Id*. at *3.
129. *Id*.
130. *Id*. at *4.
131. No. 4:17-CV-02212 JAR, 2017 WL 4778588 (E.D. Mo. Oct. 23, 2017).
132. *Id*. at *2.
133. *Id*. at *1.
134. *Id*.
135. *Id*. at *2.
136. *Id*. at *3.
137. *Id*.
138. *Id*.
139. *Id*. (quoting Valspar Corp. v. Sherman, 211 F. Supp. 3d 1209, 1214–15 (D. Minn. 2016) (collecting cases)).

sonal guarantors] did not waive their right to removal under the Guaranty Agreement, this action must still be remanded because the rule of unanimity has not been satisfied; [lessee] contractually waived its right to join in or consent to removal."[140]

140. *Id.*