

On Site Sales-What Lessor's Counsel Should Know

By Anthony L. Lamm

When equipment lessors evaluate the risks of underwriting lease transactions for manufacturing equipment, one of the primary considerations in the credit decision is the resale value of the equipment in the event of default. In preparing for this risk, a key component of an underwriter's evaluation must be how to access and market the equipment in the event of a default. Therefore, it is critical to look at every transaction from the perspective of how much money a piece of equipment will bring in a sale, if there is an established market for the particular equipment, and also, how and where the equipment can best be marketed and sold if a liquidation is necessary. An often overlooked and significant factor in this analysis is whether the lessor will have unfettered access to remove the equipment to sell, refurbish, and/or prepare for liquidation at the location where it has been used.

If the lessee is cooperative and agrees to surrender possession of the equipment, there is said to be a "voluntary surrender" or a "friendly foreclosure". In this amicable setting, the equipment lessor's counsel can focus on pre-sale notices and negotiating terms for release and indemnity, insurance, an auctioneer's contract or the contract with a purchaser, and repayment of the deficiency by the lessee.

Sometimes, however, there will be an interim period after the lessee's default and prior to the sale by contract or auction where the lessee may be given an opportunity to cure the default and enter into a Forbearance Agreement with the Lessor. Under these circumstances, it is wise to secure the Lessee's consent to a Judgment for Possession in a form that is suitable for filing with the Clerk of Courts and delivery to the Sheriff. The most common form of Judgment for Possession traces its foundation to 9-609 (a)(1) which provides in pertinent part that, "After default, a secured party may take possession of the collateral" [If the governing contract is a true Lease, the statutory basis for a lessor to retake possession of its collateral is Article 2A-525 (6)].

In the majority of cases, the equipment lessor will want the Sheriff to secure access to the Lessor's equipment at the location where the equipment is found so the lessor's repossession and/or remarketing agent can remove the equipment from the lessee's location to a convenient site for the remarketing agency to prepare, store and/or show the equipment for sale. This is not always possible or practical, however. Certain equipment, like manufacturing equipment or equipment that constitutes a fixture, may be too expensive to remove and store, especially if the equipment is not so easily remarketed. If it is anticipated that the removal and storage of this type of equipment is impractical, it is reasonable that the lessor might decide that selling the equipment at the lessee's location itself is in the best interests of all concerned. Although a lessee is likely to resist an on-site sale, the best argument for forcing one can be found in Article 9.

The basis of disposing of collateral on a debtor/lessee's premises is 9-609 (a)(2) and 9-610 (b). 9-609 (a) (2) provides in pertinent part that, "After default, a secured party: (2)

without removal, may render equipment unusable and dispose of collateral on a debtor's premises under Section 9-610."Section 9-610 (b) Commercially Reasonable Disposition provides that "[e]very aspect of a disposition of collateral including the method, manner, time, place and other terms must be commercially reasonable. If commercially reasonable, a secured party may dispose of collateral by public or private proceedings, by one or more contracts, as a unit or in parcels and at any time and place and on any terms" (emphasis supplied).

In situations where the collateral involves manufacturing equipment, or equipment that is integral to the lessee's trade or business, selling the equipment at the lessee's place of business is not only commercially reasonable, but it is practical as well because it transfers the cost of removal to the buyer. Official Comment 6 to 9-609, "Secured Party's Right to Disable and Dispose of Equipment on Debtor's premises", explains that, In the case of some collateral, such as heavy equipment, the physical removal from the debtor's plant and the storage of the collateral pending disposition may be impractical or unduly expensive. This section follows former Section 9-503 by providing that, in lieu of removal, the secured party may render equipment unusable or may dispose of collateral on the debtor's premises".

In addition, if the leased equipment is only one part of a manufacturing process (but not necessarily unique), a higher sales price can be obtained if the buyer witnesses the equipment in operation, or together with the complete set of equipment that constitutes the manufacturing process. It should also be pointed out that from a standpoint of determining whether a commercially reasonable manner of sale was conducted, it is difficult to attack the price paid at a sale that demonstrated the equipment in operation, on-site, and for its intended use. Moreover, one can argue that the lessee's location is the truly ideal setting for inspection and sale because some of a buyer's questions and concerns can be answered only through an on-site inspection where there also may be an opportunity to ask the lessee or employees questions.

There is very little well-settled law interpreting 9-609 (a) (2) and 9-610 (b). However, *Spickler v. Lombardo*, 11 Pa. D&C 3d 627 (Pa. D&C 1978) and *Sierra Financial Corporation v. Brooks-Farrer Company, et al.*, 15 Cal. App. 3d 698, 93 Cal. Rptr. 422 (Cal, App. 1971) do suggest that non-repossession in a judicial disposition does not render invalid the transfer of title nor a sale commercially unreasonable. On direct point, footnote 12 in *Spickler*, supra emphasizes the Comment in the Uniform Commercial Code (9-609 (a) (2)) by clarifying the position on commercial reasonableness, as follows: "There are some factors in the instant case which might make the sale to plaintiff commercially reasonable despite nonpossession: the purchaser had opportunity to inspect the goods, the goods were heavy equipment and it was impractical or at least difficult to move them to a protected place, neither the debtor nor any other person had actual possession and there was no obstacle to plaintiff's taking actual possession promptly or within a reasonable time."

Of course, having a strong Article 9 argument is always a nice weapon in a lessor's arsenal, but as often is the case, being right and prevailing are not often the same. With this in mind, and with clear benefits to selling heavy certain equipment on-site, lessors may also want to strongly consider the benefits of negotiating an out of court, on-site sale with a lessee.

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