

# BEFORE YOU DO BUSINESS IN PENNSYLVANIA

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Although Pennsylvania is for the most part, a hospitable environment for out-of-state leasing companies, there are several aspects of Pennsylvania law that one should be aware of before entering into Pennsylvania's market. These include licensing and registration requirements, the procedures applied to suits brought in Pennsylvania, the challenges inherent in executing on a judgment, and several other miscellaneous rules relating to lessors.

## A. Licensing

Under Pennsylvania law, any company that maintains a place of business in the Commonwealth of Pennsylvania and leases services or tangible personal property that is subject to taxation is required to obtain a license from the Department of Revenue. *See* 72 P.S. §7208(a). The failure to obtain a license in accordance with this provision may result in the imposition a fine of \$300 - \$1,500, which if unpaid, could be followed by imprisonment of 5 – 30 days. *See* 72 P.S. §7208(c).

The language of this provision is deceptive, as a leasing company may be considered to be “maintaining a place of business in the Commonwealth” when it has an agent in the Commonwealth of general or restricted authority, even where such agent is located here temporarily. *See* 72 P.S. §7201(b). Because the obligation to pay tax is imposed irrespective of whether the leasing company procures a license, it is advisable for any leasing company that maintains an agent or office in Pennsylvania to register in accordance with this provision.

## B. Registration

For those out-of-state leasing companies that are incorporated, the Pennsylvania Business Corporation Law (“the Act”) may limit their access to the courts of Pennsylvania. *See* 15 P.S. §2014. Under the Act, foreign corporations that are transacting business” in Pennsylvania within the meaning of the Act, may not bring suit in Pennsylvania until they procure a Certificate of Authority (“Certificate”) to do business in Pennsylvania. *See* 15 P.S. §2014. It should be noted that, although foreign corporations that are “transacting business” in Pennsylvania without a Certificate may not bring suit in Pennsylvania, they do remain subject to suit in Pennsylvania courts.

Although there is no bright line rule as to what it means to be “transacting business” within the meaning of the Act, there are a number of activities that are specifically excepted from this definition. *See* 15 P.S. §2001. These include soliciting orders by mail or agent that require acceptance outside the state before becoming binding

contracts, creating security interests in personal property, and collecting debts and enforcing rights in property securing such debts. *See* 15 P.S. §2001.

It is worth noting that the failure to obtain a Certificate does not indefinitely bar the corporation from suing under a transaction entered into without the Certificate. *See e.g. A&A Waste Oil Service, Inc. v. C.H. Masland & Sons, Inc.*, 20 Pa. D.&C. 3d 154 (1981). The prohibition only remains until such time as the Corporation procures the Certificate. *See id.*

Although the fee for obtaining a Certificate is only \$180 and the application is a simple two-page form, out-of-state leasing companies must consider whether procuring a Certificate is in their best interests. Because a corporation seeking to obtain a Certificate must have a proposed registered office, or a commercial registered office provider, in Pennsylvania, compliance with this section could inadvertently establish the level of contacts with the state that would allow Pennsylvania courts to exercise personal jurisdiction over the corporation. Given that the failure to procure a Certificate can be cured before trial, there is little reason to obtain a Certificate upon entry into Pennsylvania's market.

### C. Bringing Suit

#### 1. Fact Pleading

Out-of-state lessors should also be aware that because Pennsylvania is a fact pleading state, bringing suit could be more costly in Pennsylvania than it is in many other states. While in a notice pleading state, the plaintiff is only required to make allegations in its pleadings sufficient to put the defendant on notice of the nature of the claims against him, in a fact pleading state such as Pennsylvania, the plaintiff also has the burden of "formulating the issues by summarizing those facts essential to support the claim." *Sevin v. Kelshaw*, 611 A.2d 1232, 1235 (1992). This requirement adds to the cost of litigation directly in the added time it takes to prepare pleadings, and indirectly, by subjecting pleadings to attack by Preliminary Objection on the grounds that the pleading fails to state a cause of action or lacks sufficient specificity. *See* Pa. R.C.P. §1028.

Often it is more cost effective to simply concede the Preliminary Objections and amend the pleading rather than contest the objections by filing a brief and requesting a hearing on the issue. However, even where the pleading is amended, subsequent Preliminary Objections can be raised against any defects that remain in the amended pleading.

The most effective means of limiting the costs associated with the fact pleading rules of Pennsylvania is to retain a firm that has a great deal of experience enforcing leases, and which understands the nuances of the laws applicable thereto. For such firms, striking the balance between providing enough information to immunize the pleading

from attack and not providing an excess of information that would drive up costs and distract the court from the strengths of your position, is an acquired skill.

## 2. Compulsory Arbitration

Also increasing the costs of bringing suit in Pennsylvania are the compulsory arbitration rules adopted by many courts. Under Pennsylvania law, many courts require that civil actions be submitted to a board of arbitrators before being heard by the court if the amount in controversy does not exceed \$25,000 or \$50,000 (depending on the district). *See* 42 Pa.C.S. §7361.

Although in theory this policy should limit unnecessary litigation and reduce costs for the parties, in practice, the result is often quite the opposite. Because the rules give the parties the right to appeal from a decision of the board of arbitrators and obtain a trial de novo in court, the effect of this rule is to often add a step to litigation, thus increasing the costs of bringing suit.

## 3. Confession of Judgment

An effective means of avoiding unnecessary expense in enforcing a lease is to require the lessee to execute an instrument, contemporaneously with the execution of the lease, which authorizes the lessor to confess judgment against the lessee in the event of a breach. *See* Pa. R.C.P. §2950, et seq. The instrument grants the lessor the authority to enter judgment against a lessee in breach simply by filing a Complaint in Confession (“Confession”), and supporting documents, with the court. *See* Pa. R.C.P. §2951.

Although the use of a Confession can significantly reduce the expenses associated with enforcing a lease, Confessions may not be used to enforce a lease “executed by a natural person in connection with a consumer credit transaction.” Pa. R.C.P. §2950. A “consumer credit transaction” is a transaction wherein a natural person is extended credit for the procurement of personal, family or household property or services. The limitation aside, Confessions are an effective means of expediting litigation and reducing the costs associated therewith.

## D. Execution

Once a valid judgment is obtained, the Plaintiff’s ability to execute on the judgment may be hindered in several ways. Pennsylvania courts afford a great deal of protection to marital property and a debtor’s wages. Where the debtor is married, or has limited assets and regular income, these protections can become a source of frustration for judgment creditors seeking to execute.

### 1. Marital Property

Pennsylvania, like many states, protects property owned by husband and wife from execution, levy, or sale by either spouse’s creditors. *See e.g. Wylie v. Zimmer*, 98 F.

Supp. 298 (1951). This protection covers not only real estate, but also extends to personal property that the spouses hold jointly. *See id.* Where a creditor seeks to execute on a judgment obtained against one spouse, the burden is on that creditor to prove that the property he seeks to levy upon is not marital property. *See e.g. In re Matson*, 542 A.2d 147 (1988).

If the creditor cannot satisfy this burden, he will only have a potential lien against the property based on the debtor spouse's contingent expectancy to survive and become the sole owner. *See, Zimmer, supra.* Even this expectancy, however, is limited, in that the creditor has no recourse if the property is conveyed during the life of the marriage. *See id.*

To avoid obtaining an unenforceable judgment, it is advisable to procure the signature of both spouses on any leases, personal guarantees and other controlling documents. Where both spouses are joint debtors, a judgment creditor may execute on their jointly held property. *See Klebach v. Mellon Bank*, 565 A.2d 448 (1989).

## 2. Garnishing Wages

Executing on a valid judgment in Pennsylvania is also made more difficult by the fact that Pennsylvania does not allow the garnishment of wages. *See* 42 Pa. C.S. §8127. The only exceptions to this rule apply to debts involving support or damages arising out of a residential lease. *See id.* The prohibition against garnishment, however, only applies to wages while in the hands of the employer. *See id.*

Because Pennsylvania's rules regarding the garnishment of wages only apply to wages in the hands of an employer, recovery may depend on the resourcefulness and persistence of the firm that is handling the execution. Where there is a judgment against an individual who earns a steady salary but has no assets, it is of critical importance to utilize a firm that is adept at tracing funds to bank accounts and that can move quickly to garnish the account before the funds are disposed of. Obviously, where the debtor has no assets and no bank accounts, recovery will be frustrated by this rule.

## E. Miscellaneous

### 1. Usury Laws

In Pennsylvania, because sellers, or lessors, "are free to contract with buyers as to the terms and conditions of sales," transactions involving the sale of merchandise by credit have never been subjected to usury laws or the regulations applied to banking and loan transactions. *See Equipment Finance, Inc. v. Grannas et al.*, 218 A.2d 81 (1966). Although Pennsylvania courts have likened sale or lease contracts to extending credit to the making of a loan, they have uniformly held that an increased charge for goods purchased on credit is included in the sales price of the goods, and thus not within the ambit of the usury laws. *See id.*

Notwithstanding the above, limits do exist on the rate of interest a lessor can charge on a lease of goods. Where the lessee agrees to pay an amount for the use of goods that exceeds or is equal to the value of the goods, and has an option to become the owner of the goods for little or no consideration, the maximum rate of interest that can be charged by the lessor is 18%. *See* 69 Pa. C.S. §1501(b)1.

## 2. Rental-Purchase Agreements

There are several rules relating to rental-purchase agreements (“RPAs”), of which out-of-state lessors should be aware. An RPA is defined as an “agreement for the use of personal property by an individual primarily for personal, family, or household purposes for an initial period of four months or less, that is automatically renewable . . . and that permits the lessee to acquire ownership of the property.” 42 Pa. C.S.A. §6902.

A lessor under an RPA is required to disclose, among other things: the total of all initial payments, rental payments and other charges necessary to acquire ownership of the property; the cash price of the property; and the cost of the lease services (the difference between the cash price of the property and the price the lessee would pay during the life of the lease to acquire ownership). *See* 42 Pa. C.S.A. §6903. By contrast, the RPA may not contain any provision that: grants a power of attorney; waives any defense, counterclaim or right the lessee has against the lessor or his agent; contains a provision authorizing a late fee in excess of 10%; or requires the lessee to pay a fee connected with the termination or rescission of the RPA. *See* 42 Pa. C.S.A. §6904.

Lessors under an RPA are also prohibited from charging an amount for lease services that exceeds the cash price of the property. *See* 42 Pa. C.S.A. §6905(a). Additionally, any time after making the first payment under an RPA, a lessee may acquire ownership of the property by tendering an amount equal to the cash price of the property less 50% of all rental payments made to date. *See* 42 Pa. C.S.A. §6905(b).

Another protection afforded lessees under an RPA is contained in 42 Pa. C.S.A. §6907(a), which provides that a lessee who has made 2/3 of the rental payments necessary to acquire ownership, and who experiences a reduction of 25% or more in income due to certain causes, must receive a deduction in the amount of each rental payment equal to the proportional deduction in the lessee’s income or 50%, whichever is less. *See* 42 Pa. C.S.A. §6907(a). When the payments are reduced under this section, the total dollar amount of payments needed to acquire ownership may not be increased, but the number of payments required to acquire ownership may be adjusted accordingly. *See* 42 Pa. C.S.A. §6907(b).

## 3. Evergreen Clauses

Outside of the area of Rental-Purchase Agreements, the Pennsylvania legislature has not enacted any legislation addressing clauses in leases that provide for the automatic renewal of the lease (“Evergreen clauses”) other than those found in leases involving real property. Despite the failure of the legislature to explicitly sanction Evergreen clauses in

non-real estate leases, these clauses survive scrutiny under Article 2A of Pennsylvania's Commercial Code ("Article 2A").

Under Pennsylvania law, a lease is effective and enforceable according to its own terms, unless otherwise provided by Article 2A. *See* 13 Pa. C.S.A. 2A301. Where a party is in default under a lease, the party seeking enforcement has all the rights and remedies provided in Article 2A, in addition to all of the remedies provided for in the lease that are not prohibited by Article 2A. *See* 13 Pa. C.S.A. 2A501(b); 13 Pa. C.S.A. 2A523(a)6. Therefore, because the legislature has not prohibited Evergreen clauses, such clauses are enforceable to the extent that they are bargained for and made part of an enforceable lease.

#### 4. Criminalizing Conversion of Secured Property

Pennsylvania also provides an additional level of protection for those lessors who have a security interest in, or a judgment lien upon, property of the lessee. Under 18 Pa., C.S.A. §4110, "a person commits a misdemeanor of the second degree if he destroys, removes, conceals, encumbers, transfers or otherwise deals with property subject to a security interest or levy ... with intent to hinder enforcement of such interest." 18 Pa. C.S. §4110. Although most lessees are unaware of this statute, it is an effective deterrence mechanism where counsel for the lessor references the statute in cautioning the lessee not to convey the property covered thereby.

#### 5. Repairman's Liens

Out-of-state lessors should also be aware of the ways in which Pennsylvania's laws governing repairman's liens could affect their security interests or ownership rights in personal property. Under Pennsylvania common law, a repairman's lien on property was created "whenever a workman or artisan, by his labor or skill, increase[d] the value of personal property placed in his possession to be improved . . . at the request of the owner or under circumstances from which [the owner's] assent [could] be reasonably implied." *Associates Financial Services Company, Inc. v. O'Dell*, 417 A.2d 604 (1980). Where a party had a prior security interest in the property, he was treated as an "owner" such that his consent was required to establish a repairman's lien. *See id.*

Following Pennsylvania's adoption of the new Uniform Commercial Code ("UCC"), however, courts no longer treat a secured party as an owner whose consent is required to create a repairman's lien. Rather, Pennsylvania courts have held that because the UCC governs the priority of a possessory lien vis-à-vis other security interests in the property, the consent of the secured party is no longer necessary to create a possessory lien in the property. *See Williamsport National Bank v. Shrey*, 612 A.2d 1081 (1992).

Under 13 Pa. C.S.A. §9333, a possessory lien takes priority over a perfected security interest "unless the [possessory] lien is statutory and the statute expressly provides otherwise." 13 Pa. C.S.A. §9333. Because a repairman's lien is a possessory

lien arising under common law, it takes priority over other perfected security interests. *See Williamsport, supra.*

The effect of a repairman's lien on a lessor's ownership interest in the property, however, is an issue that has yet to be definitively resolved under the cases interpreting the UCC. Under common law, a repairman's lien could not be created without the consent of the owner of the property. *See O'dell, supra.* Although the adoption of the UCC changed what it means to be an "owner" insofar as secured parties are concerned, it has yet to be held that the consent of a true owner is no longer required to establish a repairman's lien. Unfortunately, it is also true that there have been no cases subsequent to the adoption of the UCC that have suggested that the consent of the owner *remains* a requirement either.

Although Pennsylvania courts have yet to address the issue of whether the consent of an owner of property is still required to establish a repairman's lien in the property, the fact remains that the consent of an owner of property can be implied. *See O'Dell, supra.* Thus, it is advisable for leasing companies that are considering doing business in Pennsylvania to include in their leases provisions that expressly prohibit the lessee from creating any security interests in the property and which require the lessee to consult with the lessor before turning the property over to a third party for repairs. Additionally, the lease should provide that any violation of these provisions is grounds for immediately declaring the lessee in breach. This should discourage many lessees from turning the property over to third parties and inadvertently jeopardizing the lessor's ownership interests in the property. Until such time as the courts of Pennsylvania address the issue of whether an owner's consent remains necessary to create a repairman's lien, strict provisions limiting the lessee's authority to create such a lien remain the most effective means of protecting the owner's interests in the property from such liens.