

ARTICLE 9 – Ten Years Later

Ten years has now passed since Article 9 was revised. The upcoming Bank Alert notices will speak to some of the issues which are being resolved in the courts concerning the interpretation of Revised Article 9.

When taking possession of assets presumably secured to a lender, the lender is often confronted with equipment leases. A determination needs to be made whether the equipment lease is a “true lease” or a disguised security interest. True leases are not subject to Article 9 and there is no need to file a financing statement. An issue arises, however, when looking at the reality of the lease to determine whether that it is actually a disguised financing transaction. There is no bright line test for this determination and you are forced to look at all of the facts and circumstances concerning the “lease” arrangements.

Under the Uniform Commercial Code, certain transactions are always deemed secured transactions notwithstanding that they are styled as “leases”:

“A transaction in the form of a lease creates a security interest if the consideration that the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease and is not subject to termination by the lessee, and:

- (1) the original term of the lease is equal to or greater than the remaining economic life of the goods;
- (2) the lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods;
- (3) the lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or for nominal additional consideration upon compliance with the lease agreement; or
- (4) the lessee has an option to become the owner of the goods for no additional consideration or for nominal additional consideration upon compliance with the lease agreement.”

The issue that must be determined with respect to nominal consideration is whether, in essence, one can purchase the equipment for less than its fair market value.

Before taking possession of leased equipment or taking the position that the leased equipment does not fall within the ambit of your security interest, you must carefully review the facts and circumstances of the transaction supporting the lease.