

MARKS & WEINBERG, P.C.

In Re QDS Components, Inc.

292 B.R. 313, 50 U.C.C. Rep.Serv.2d 973 (Bankr. S.D. Ohio 2002)

In this case, the Court undertook an extensive analysis of the Uniform Commercial Code test used to determine whether a transaction designated as a "lease" constitutes a "true lease" or a "disguised security interest." In its opinion, the Court discussed true lease analysis under both the old and new version of § 1-201(37), which defines the term "Security Interest", including the Multiple Factor Approach, Percentage Test, The Option Price/FMV Test, the Economic Realities Test, and the new Bright-Line Test. The court detailed all of the tests and noted how different courts applied these tests, and the comments and criticisms of courts and commentators on each of these tests.

After its historical discussion, the Court applied the Bright-Line Test. According to the Court, this test contains two substantive prongs and satisfaction of these prongs would result in a transaction being characterized as a disguised security interest as a matter of law. Even if the Bright-Line Test was not satisfied, the Court noted that the UCC then allows for a facts and circumstances test which would result in a true lease only if, under the circumstances, the lessor still held some meaningful reversionary interest at the end of the lease term.

In this case the Court held that the first prong of the Bright-Line Test was satisfied since the lessee could not terminate its obligation to make payments for the entire term.



However, the court held that the party wishing to characterize the transaction as a disguised security interest did not satisfactorily prove the second prong of the Bright-Line Test since it did not present evidence of the reasonable expectations of the parties as to the cost of return or fair market value of the leased equipment at the end of the leases. The court also refused to apply other tests advanced to establish that the option price was nominal.

In holding that the lessors maintained a meaningful reversionary interest the court again focused on the challenging party's failure to submit sufficient evidence. This lack of evidence led the court to conclude that the lease agreements were true leases under UCC § 1-201(37).

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