UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF KENTUCKY
LONDON DIVISION

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Smith [redacted],	)	
	)	
Plaintiff	)	CASE NO. [redacted]
	)	
v.	)	
	)	
Our clients [redacted]	)	Motion to Dismiss Pursuant to Rule 12(b)(6)
	)	
	)	
	)	
	)	
Defendants	)	

*** *** *** ***

The Defendants, Our clients [redacted] ("Clients"), Our clients [redacted], and Our clients [redacted], LLC ("Clients"), move the court to dismiss this action pursuant to FED. R. CIV. P. 12(b)(6) for the following reasons:

INTRODUCTION

Mr. Smith claims ownership of one [redacted] Equipment (the "Equipment currently in the possession of Clients He further claims that Clients and Clients converted the Equipment and interfered with his contracts with Acme Inc. ("Acme"). He produces an impressive pile of paper in order to support his claims. The problem is that this particular pile proves the opposite: Mr. Smith does not own the Equipment he does not have a right to possess it, and Clients had the right to do everything about which Mr. Smith complains so vigorously.

When viewed under the bright light of the Uniform Commercial Code[1], the Complaint and its attachments demonstrate that (a) Acme owned the Equipment because its lease with Welsh **Equipment Finance**, Inc. ("Welsh was a very thinly disguised security interest and not a true lease (UCC §1-203), (b) Creditor Corp. ("Creditor (and Clients as its assignee) also had a properly perfected security interest in the Equipment (UCC § 9-203 & UCC § 9-310), (c) Creditor security interest in the Equipment became superior to Welsh (and Mr. Smith as its assignee) security interest when Welsh financing statements lapsed (UCC § 9-515), (d) Clients (as assignee of Creditor had the right to repossess and sell the Equipment because its interest was superior to that of Mr. Smith (UCC § 9-322), and (e) Clients acquired the Equipment free and clear of the interests of either Acme or Mr. Smith (UCC § 9-617).

STANDARD OF REVIEW

While "[t]he purpose of Rule 12(b)(6) is to allow a defendant to test whether, as a matter of law, the plaintiff is entitled to legal relief even if everything alleged in the complaint is true[,]" Mayer v. Mylod, 988 F.2d 635, 638 (6th Cir. 1993)(citations omitted), "'[i]n the event of conflict between the bare allegations of the complaint and any exhibit attached pursuant to [Fed.R.Civ.P. 10(c)], the exhibit prevails.'" Hudson v. Phillipson, 2008 WL 356884, 3 (W.D. Mich 2008) (quoting Fayetteville Investors v. Commercial Builders, Inc., 936 F.2d 1462, 1465 (4th Cir.

[1] There are three states whose law potentially applies here: 1. Kentucky, the present location of the Equipment 2. Pennsylvania, the former location of the Equipment and 3. Oregon, the place of Acme incorporation. To the extent that the Uniform Commercial Codes of these states do not vary, the official version will be cited. Comments to the official version will also be cited because (a) Kentucky has adopted the comments as authority for interpretation at KRS 355.1-103(c), (b) the comments are given "substantial weight . . . as evidencing the intended application of the Code" in Pennsylvania, In re Bristol Associates, Inc., 505 F.2d 1056, 1058 fn. 2 (3rd Cir. 1974), and (c) Oregon also relies on the comments in interpretation, See May Trucking Co. v. Northwest Volvo Trucks, Inc., 241 P.3d 729, 738 (Ore. Ct. App. 2010).

1991)).[2] Further, "[t]he Sixth Circuit has indicated that a District Court may consider matters of public record, orders and the like, without converting a motion under Rule 12(b)(6) into one of summary judgment under Rule 56."[3] Clarkco Landfill Co. v. Clark County Solid Waste Management Dist., 110 F. Supp.2d 627, 633 (S.D. Ohio 1999) (citing Nieman v. NLO, Inc., 108 F.3d 1546, 1554 (6th Cir. 1997)).

As occasionally happens in litigation, Mr. Smith "complaint is plagued not by what it lacks, but by what it contains," General Guaranty Ins. Co. v. Parkerson, 369 F.2d 821, 825 (5th Cir. 1966). "A plaintiff may plead himself out of court by attaching documents to the complaint that indicate that he or she is not entitled to judgment." Matter of Wade, 969 F.2d 241, 249 (7th Cir. 1992)(citation omitted); Mr. Smith has accomplished this feat. It is clear from the face of the documents that Mr. Smith attaches to his complaint and from his own allegations (a) that Clients had a security interest in the Equipment (b) that it had the right to repossess it, and (c)

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[2] See Consolidated Jewelers, Inc. v. Standard Fin. Corp., 325 F.2d 31, 36 (6th Cir. 1963) ("General averments of conclusions stated in the pleadings do not require the District Court to hear evidence, when the pleading are at variance and inconsistent with the clear and unambiguous language of the contract filed as an exhibit thereto and 'made a part here of as if fully copied here in.'"); Centers v. Centennial Mortgage, Inc., 398 F.3d 930, 933 (7th Cir. 2005) ("And while we accept well-pleaded allegations as true and draw all reasonable inferences in favor of the plaintiff, to the extent that the terms of the attached contract conflict with the allegations of the complaint, the contract controls.")(citations omitted); FED. R. CIV. P. 10(c) ("A statement in a pleading may be adopted by reference elsewhere in the same pleading or in any other pleading or motion. A copy of a written instrument that is an exhibit to a pleading is a part of the pleading for all purposes."); 5A CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1327 (3d ed.) ("It appears to be well settled that when a disparity exists between the written instrument annexed to the pleadings and the allegations in the pleadings, the terms of the written instrument will control, particularly when it is the instrument being relied upon by the party who made an exhibit.").

[3] See Nieman v. NLO, Inc., 108 F.3d 1546, 1554 (6th Cir. 1997) (citing 5A CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1357 (2d ed. 1990)); 5B CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1357 (3d ed.) ("Numerous cases . . . have allowed consideration of matters incorporated by reference or integral to the claim, items subject to judicial notice, matters of public record, orders, items appearing in the record of the case, and exhibits attached to the complaint's authenticity is unquestioned[.]")

that it had the right to sell it. Whatever Mr. [redacted] interest in the [redacted] was, that interest has come to an end.

ARGUMENT

I. [redacted] OWNED THE [redacted] [redacted] ONLY HAD A SECURITY INTEREST

The agreements with [redacted] as a matter of law, evidence a financing of [redacted] purchase of the [redacted] with [redacted] only retaining a security interest. The Uniform Commercial Code at §1-203[4] provides the following:

> Lease Distinguished from Security Interest
>
> (a) Whether a transaction in the form of a lease creates a lease or security interest is determined by the facts of each case.
>
> (b) 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:
>
> . . .
>
> (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.

[redacted] obtained its interest in the [redacted] via a Master Lease attached as Exhibit A to the Complaint. The terms of this document were supplemented by a Supplement to Master Lease (the "Supplement") also attached as Ex. A to the Complaint. The lease was already non-cancelable by its terms (See Plaintiff's Ex. A p. 2[5] at ¶ 21) and the Supplement allowed [redacted] to pay $1 at the end of the lease and take ownership of the [redacted] (See Plaintiff's Ex. A at p. 4 ¶ 1–2). Clearly, as a matter of law, because the [redacted] lease was non-cancelable and

[4] The older version of the UCC is to the same effect. See UCC § 1-201(37) (unrevised version).
[5] Page numbers referred to in exhibits mean the page numbers created by the Court's filing system.

provided a nominal purchase price at the end of the lease term, [redacted] had a security interest, not a lease. The Supplement even says that "Lessor will treat the lease as a sale," (Plaintiff's Ex. A at p. 4), and [redacted] did not even attempt to indicate a lessor/lessee relationship by checking the box on line 5 in its UCC filings, (See Plaintiff's Ex. D at p. 9). [redacted] perfected precisely the interest it had: an Article 9 security interest in the [redacted] When Mr. [redacted] took assignment from [redacted] all he got was all that [redacted] could give him: a security interest, not ownership. The assignment to Mr. [redacted] even acknowledges that the assignment was of "Loan Documents," not title to the [redacted] (See Plaintiff's Ex. E at p. 1). This Assignment of Loan Documents is also attached to this motion as Exhibit 1.

II. [redacted] HAD A SECURITY INTEREST IN THE [redacted]

Because [redacted] owned the [redacted] [redacted] security interest attached to it. [redacted] and [redacted] entered into a Financing Agreement on or about July 29, 2004. (See Complaint at ¶ 10). In the Financing Agreement, [redacted] granted [redacted] a security interest in all of its equipment. (See Plaintiff's Ex. C at pp. 33–34 § 6.1(e)). The [redacted] is equipment and is covered by this grant.[6] Under UCC 9-310(a), a security interest in equipment is perfected by filing. [redacted] just as [redacted] had done, filed a financing statement covering the [redacted] on August 18, 2004 and has remained continuously perfected since then. (See Defendant's Ex. 2 at pp. 2-6) (Oregon searches and filings reflecting an initial filing on August 18, 2004 (#6667771), an amendment to reflect a change in [redacted] name on August 15, 2005, and a continuation statement extending the lapse date to August 18, 2015). [redacted] is now the assignee of [redacted] interest. (See Complaint at ¶ 18)

[6] See UCC § 9-102(33) ("Equipment" means goods other than inventory, farm products, or consumer goods.")

The Financing Agreement's provision on "Excluded Property" does not change any of this. According to the Financing Agreement, "Excluded Property shall mean any contract, lease, license or other agreement[.]" (Plaintiff's Ex. C at p. 12). The Equipment is not a contract, it's not a lease, it's not a license, and it's not an other agreement; it's a Equipment The definition of "Excluded Property" clearly does not include the Equipment and, consequently, that definition does not adversely affect Clients security interest.[7]

III. MR. Smith SECURITY INTEREST WAS SUBORDINATE TO Clients

The security interest Mr. Smith obtained from Welsh became subordinate to Clients security interest when the Welsh financing statement lapsed. Under UCC 9-515(c), the lapse of a financing statement causes a security interest to become unperfected and "deemed never to have been perfected as against a purchaser of the collateral for value."[8] When this happens, the unperfected security interest becomes subordinate to any perfected security interests. See UCC 9-322(a)(2)("[a] perfected security interest or agricultural lien has priority over a continuing unperfected security interest or agricultural lien"). Welsh filed a financing statement; however, it was allowed to lapse by Mr. Smith (See Defendant's Exhibit 2 at pp. 2-3) (the search in Oregon does not show an effective financing statement filed by Welsh or Mr. Smith as of December 7, 2012 under either Leading-Edge Earth Products or

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[7] See also UCC § 9-401(b) ("An agreement between the debtor and secured party which prohibits a transfer of the debtor's rights in collateral or makes the transfer a default does not prevent the transfer from taking effect.")

[8] Creditor (and Clients as assignee) are purchasers of the Equipment for value. See UCC § 1-201(29) ("'Purchase' means taking by sale, lease, discount, negotiation, mortgage, pledge, lien, security interest, issue or reissue, gift, or any other voluntary transaction creating an interest in property."); UCC § 1-201(30) ("'Purchaser' means a person who takes by purchase"); UCC § 1-204 ("[A] person gives value for rights if the person acquires them: (1) in return for a binding commitment to extend credit or for the extension of immediately available credit, whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; . . . or (d) in return for any consideration sufficient to support a simple contract.")

Acme Inc.).[9] It appears from Plaintiff's Exhibit D that the latest Welsh financing statement covering the Equipment was filed September 20, 2004. Nothing was filed thereafter by either Welsh or Mr. Smith Consequently, the Welsh Smith financing statement lapsed after September 20, 2009. See UCC § 9-515(a).

Since Clients security interest was continuously perfected, Mr. Smith security interest became subordinate to that of Clients when it became unperfected.

IV. Clients HAD THE RIGHT TO REPOSSESS AND SELL THE Equipment

Clients had the right to repossess the Equipment and sell it. On default, a secured creditor has the right to repossess and sell collateral. See UCC 9-609(a)(1) ("After default, a secured party: may take possession of the collateral"); UCC 9-610(a) ("After default, a secured party may sell, lease, license, or otherwise dispose of any or all of the collateral"). Further, a secured creditor with a superior interest has the right to possess the collateral as against creditors with inferior interests. See UCC 9-609 cmt. 5 ("Conflicting rights to possession among secured parties are resolved by the priority rules of this Article"). Acme was in default of the Financing Agreement, Clients repossessed the Equipment and it sold it Clients (See Complaint at ¶ 19, 24, & 28); these were all actions Clients had the right to do under the Uniform Commercial Code. Further, it had the right to take these actions in spite of Mr. Smith protests because of Clients superior interest in the collateral.

[9] Oregon was the only proper place for the filing of a financing statement to perfect a security interest in the Equipment because Acme was incorporated there. See UCC § 9-301(1) (law of debtor's location governs perfection); UCC § 9-307(e) ("A registered organization that is organized under the law of a State is located in that State.")

V. [redacted] OBTAINED THE [redacted] FREE AND CLEAR OF MR. [redacted] INTEREST.

When a secured creditor sells collateral after default, UCC 9-617(a)(3) provides that any "subordinate security interest or other subordinate lien" is discharged. Mr. [redacted] security interest, being inferior to [redacted] was discharged when the [redacted] was sold to [redacted] Consequently, Mr. [redacted] has neither a right to possession of the [redacted] nor ownership of it.

VI. MR. [redacted] CLAIMS FAIL BECAUSE HE DID NOT HAVE OWNERSHIP OR A RIGHT TO POSSESS THE [redacted]

A. CONVERSION

To prove a claim for conversion under Kentucky law, a party must demonstrate (1) its ownership of the collateral and (2) possession or an immediate right to possession. See Kentucky Ass'n of Counties All Lines Fund Trust v. McClendon, 157 S.W.3d 626, 631–32 fn. 12 (Ky. 2005) (citing 90 C.J.S. *Trover and Conversion* § 4 (2004)); Meade v. Richardson Fuel, Inc., 166 S.W.3d 55, 58 (Ky. Ct. App. 2005) (citations omitted). Under Pennsylvania law, a party must prove either its ownership or right to possession. See 4 Std. Penn. Prac.2d § 23:104. As shown above, Mr. [redacted] has neither the right to possess the [redacted] nor ownership of it. This precludes his claims for conversion.

Further, Mr. [redacted] cannot show a right to possession of the [redacted] for an additional reason: he alleges that he leased it to [redacted] and that [redacted] did not have to return the [redacted] to him until November of 2013. (See Complaint ¶ 44, 46, 53 & 56). Under Kentucky law, the fact that Mr. [redacted] does not have an immediate right to possession precludes his claim. See 13 Ky. Prac. Tort Law § 8:1 (Concluding that an owner who entrusts

property to another for a period does not have a cause of action against a third party who converts the property until the period ends).

B. TORTIOUS INTERFERENCE

As for his tortious interference claim, Mr. Smith must demonstrate that Defendant's conduct was unprivileged. See RESTATEMENT (FIRST) OF TORTS § 766; Carmichael-Lynch-Nolan Advertising Agency, Inc. v. Bennett & Assoc., Inc., 561 S.W.2d 99, 102 (Ky. Ct. App. 1977); Birl v. Philadelphia Elec. Co., 167 A.2d 472, 474 (Pa. 1960). However, when a party is asserting superior rights to that of the alleged tort victim, that parties conduct is privileged. See In Re Quality Processing, Inc., 9 F.3d 1360, 1365–66 (8th Cir. 1993) ("Generally speaking, a secured party is justified in interfering to protect a superior security interest.")(citations omitted); US Claims, Inc., v. Flomenhaft, 519 F. Supp.2d 532, 539 (E.D. Penn. 2007) ("It is settled law in New York that '[p]rocuring the breach of a contract in the exercise of equal or superior right is acting with just cause or excuse and is justification for what would otherwise be an actionable wrong.'") (quoting Felsen v. Sol Cafe Mfg. Corp., 24 N.Y.2d 682, 687 (N.Y. 1969)); Spencer Companies, Inc. v. Chase Manhattan Bank, N.A., 81 B.R. 194 (D. Mass. 1987). Since Clients was asserting rights that were superior to that of Mr. Smith the actions of Clients and those taking from Clients cannot form the basis of a claim for tortious interference.

C. PUNITIVE DAMAGES

In order to state a claim for punitive damages, there must be an underlying tort asserted against Defendants. See Shibeshi v. Alice Lloyd College, 2011 WL 4970781, 5 (E.D. Ky 2011) (claim for punitive damages is not independent of the underlying tort). Since Mr. Smith fails to state any other claim, his claim for punitive damages must also fail.

CONCLUSION

Smith had a security interest, he failed to maintain perfection of that interest, and subsequently became subordinate to the rights of Clients Because of this, he may not complain of Defendants' possession of the Equipment nor any alleged interference with his agreements with Acme or others. Defendants are entitled to dismissal of Mr. Smith claims.

Respectfully Submitted,

/s/ D. Duane Cook
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And

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Co-Counsel for Defendants Our clients [redacted] Our clients [redacted] *and* Our clients [redacted] *LLC*

CERTIFICATE OF SERVICE

This is to certify that I have this day served the within and foregoing Motion via the CM/ECF system which will automatically send notification to the following attorneys for Plaintiff, who are participants in the CM/ECF system:

Welsh [redacted]

Counsel for Plaintiff, Welsh [redacted] Smith [redacted]

This 28th day of March, 2013.

/s/ D. Duane Cook
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