In the United States Bankruptcy Court

for the Northern District of Iowa

EMERSON MATTRESS INC. dba Lebeda Mattress Mfg. Lebeda Mattress Factory and Lebeda Mattress Sleep Factory *Debtor(s).*	Bankruptcy No. 95-12358KC Chapter 11
EMERSON MATTRESS INC. dba Lebeda Mattress Mfg. Lebeda Mattress Factory and Lebeda Mattress Sleep Factory *Plaintiff(s)* vs. ASSOCIATES LEASING INC. *Defendant(s)*	Adversary No. 99-9052-C

ORDER

On September 30, 1999, the above-captioned matter came on for hearing pursuant to assignment. Debtor Emerson Mattress, Inc. appeared by Attorney Dan Childers. Defendant Associates Leasing, Inc. appeared by Attorney Michael Jankins. Trial was held after which the matter was taken under advisement. All post-trial briefs are now submitted and this matter is ready for determination.

Statement of the Case

On December 4, 1995, Debtor Emerson Mattress, Inc. filed with this Court a voluntary petition for relief under Chapter 11 of the Bankruptcy Code. The Court confirmed Debtor's Plan of Reorganization on February 10, 1997. As part of its Plan, Debtor assumed three prepetition lease agreements it had with Defendant Associates Leasing, Inc. These leases involved motor vehicles used in Debtor's business. Debtor filed this adversary proceeding on April 19, 1999 asking the Court to determine its rights and obligations under these leases. Specifically, Debtor asserts that it is entitled to title to two vehicles. Associates denies that it is required to transfer title.

Core Proceeding

The administration of a debtor's estate is a core proceeding. 28 U.S.C. §157(b)(2)(A). In a Chapter 11 case, the property of the estate vests in the debtor upon confirmation, unless the plan provides otherwise. 11 U.S.C. §1141(b). The bankruptcy court, however, retains exclusive jurisdiction to determine the debtor's interest in property even after that property leaves the bankruptcy estate. 28 U.S.C. §1334(e); Abramowitz v. Palmer, 999 F.2d 1274, 1277 (8th Cir. 1993).

Debtor held interests in vehicle lease contracts on the date it filed bankruptcy. These interests became property of the estate. They remained in the estate until confirmation of Debtor's Chapter 11 plan. Under Abramowitz, this Court has jurisdiction to determine Debtor's interest in these contracts because they were once property of Debtor's bankruptcy estate. One Circuit Court has been asked to determine whether an action for the post-confirmation breach of a prepetition contract is a core proceeding. The opinion in In re St. Clare's Hosp. & Health Center, 934 F.2d 15, 18 (2d Cir. 1991), is consistent with the holding in this Circuit. The Court concludes that this matter is a core proceeding, pursuant to 28 U.S.C. §157, over which the Court has exclusive jurisdiction pursuant to 28 U.S.C. §1334.

Findings of Fact

On February 14, 1994, Debtor entered into a "master lease" agreement with Associates (the "Lease"), involving four vehicles. The lease was a TRAC lease. Under the TRAC lease, each vehicle contracted under the master lease was evidenced by a separate payment schedule. As part of its Chapter 11 plan, Debtor assumed three, and rejected one, of the lease agreements. Of the three assumed leases, only two are presently at issue. One vehicle is a 1994 Mac CH613 which was delivered to Emerson in April of 1994. The second is a 1994 Mitsubishi FUSO truck which was delivered to Emerson in February of 1994. The MAC truck had 48 scheduled monthly payments and the Mitsubishi had 60 monthly payments. The evidence establishes that all monthly rental payments required under both leases have been paid to Associates. The lease payments for both vehicles were completed in January and February, 1998. A third vehicle is also in possession of Debtor under the terms of the lease. At the time of trial, this vehicle had three monthly lease payments remaining. That lease is not directly at issue in this case.

Paragraph 8 of the lease agreement provides that the lessee (Debtor) is required to return the vehicle to the lessor (Associates) at the expiration of the lease in relation to that vehicle and that the lessee was to give the lessor at least 60 days and no more than 90 days notice of the return of any vehicle. It is uncontested that Debtor did not provide the notice under paragraph 8 of the lease and did not return the vehicle pursuant to the terms of the lease. It is also uncontested that at no time did Associates ask for return of the vehicles nor did it raise any issue concerning the failure to provide notice under paragraph 8 of the lease agreement.

Paragraph 9 of the lease provides for disposition of a vehicle after its return to the lessor by the lessee. Simply stated, it provides that the lessor (Associates) shall sell the vehicle by a public or private sale. The leases all contain a "residual value". This is a value for the vehicle upon the completion of the lease, as agreed upon in advance. If the sale was for an amount in excess of the residual value, the lessee would receive that amount after the payment of any costs associated with the sale. If the sale price was less than the residual value, the lessee would be required to pay the difference.

Associates did not notify the Debtor that it intended to enforce the notification requirements, nor did it notify Debtor that it intended to seek a return of the possession of the vehicles in question. Rather, Associates sent Debtor an "invoice" for the two vehicles indicating that Debtor owed Associates the "residual value" for each vehicle. Debtor paid the "residual value" reflected in the invoices in an amount of approximately $26,000. Associates accepted these payments without comment. Debtor never returned possession of the vehicles to Associates and Associates did not subsequently request possession of the vehicles. Rather, Debtor remained in physical possession of the vehicles and continued to drive them.

Debtor began a course of correspondence with Associates in an attempt to clarify the status of the title to the vehicles. Debtor was unable, however, to get any satisfactory explanation as to the position Associates was taking towards these vehicles. Eventually, Debtor asked for title to the vehicles with no response by Associates. Debtor filed this adversary proceeding seeking a forcible transfer of the titles to the vehicles.

Discussion

Associates's position in this adversary has been difficult to ascertain. Associates initially failed to file an answer in this case and a default was entered against it on May 25, 1999. Ultimately, Associates filed a Motion to Set Aside the Default on June 21, 1999 and filed an Answer which was a mere denial of Debtor's allegations without any specific theory of defense.

The default was set aside on June 23, 1999 and Associates was granted ten days within which to file a Recast Answer setting out the defenses. Associates filed its recast Answer on July 2, 1999. This Answer sets out, in general terms, Associates's theory of the case. The parties were to submit a Joint Pretrial Statement upon completion of discovery. Debtor timely submitted its portion of the Pretrial Statement. Associates, however, did not submit a Pretrial Statement prior to trial. Associates did submit what was designated as a Trial Brief on the morning of trial.

The parties were to submit a list of Exhibits prior to trial pursuant to Local Rule. Debtor timely submitted Exhibits. Associates did not submit Exhibits until the morning of trial. Associates did not submit any evidence at trial.

Based on the foregoing, the Court concludes that Associates raises two arguments in support of its contention that it is entitled to retain title to the vehicles in question: (1) Associates contends that under the terms of the lease, Debtor is only entitled to title to the vehicles if it turns over possession of the vehicles to Associates and buys them back at the "sale" that the lease purportedly contemplates; and (2) Associates contends that it is entitled to retain the proceeds of any sale under the lease until Debtor has fully performed under the lease as to all vehicles subject to its terms.

Choice of Law

The parties have not pled or proven the law of another forum. If the law of an alternate forum is sought to be given effect or enforced, it must be proven like any other fact. If the law of another forum is not pled or proven, the law of the forum, or the common law thereof, is ordinarily applied. Therefore, in the absence of an allegation of foreign law, the Court will apply the law of this forum in adjudicating this dispute. See Pellerin Laundry, Inc. v. Reed, 300 F.2d 305, 308 (8th Cir. 1962) (refusing to apply law of foreign state where parties failed to plead or prove the law of the foreign state).

Principles of Contract Construction

When construing a contract, Iowa courts focus on the parties' intent. Iowa R. App. P. 14(f)(14). Where possible, this intent is derived from the words of the contract. Id. The contract must be construed as a whole. Iowa Fuel & Minerals v. Board of Regents, 471 N.W.2d 859, 863 (Iowa 1991).

The Court will give effect to the practical interpretation the parties place on a contract. Village Supply Co. v. Iowa Fund, Inc., 312 N.W.2d 551, 555 (Iowa 1981); Miller v. Gerrlings, 128 N.W.2d 207, 213 (Iowa 1964). A party's method of performance under a contract is the best indication of the

interpretation that a party placed on the contract. Village Supply Co., 312 N.W.2d at 555; Miller, 128 N.W.2d at 213.

A contract will not be construed to work an unreasonably harsh result unless the terms of the contract clearly call for such a result. Iowa Fuel, 471 N.W.2d at 863. An unreasonable or harsh result will not be inferred; instead, the terms of the contract must specifically call for such a result. First Nat'l Bank v. Smith, 331 N.W.2d 120, 122 (Iowa 1983) (refusing to construe lien waiver to waive all liens where waiver is silent on the issue); Midwest Management Corp. v. Stephens, 291 N.W.2d 896, 913 (Iowa 1980) (clause giving party the "sole discretion" to determine conditions of subscription does not give the party the right to arbitrarily cancel the contract at will because such a result would put the other contracting party at the mercy of the first). Where the contract is susceptible to more than one reasonable interpretation, the Court will construe the terms of the contract against its maker. Village Supply, 312 N.W.2d at 555.

Failure to Return Vehicle as Breach of Contract

Associates first contends that even though it has received the full "residual values" for the two vehicles as well as all lease payments, it may nevertheless retain the titles because Debtor did not turn the vehicles over to Associates for sale under the terms of the Lease. Admittedly, the lease contains a provision which envisions a return of the vehicle upon completion of lease payments. The Lease is silent concerning whether Debtor may pay the "residual value" to Associates and receive a title in return. Paragraph 8 of the Lease requires Debtors to:

> "return each vehicle to Lessor, at Lessee's expense, at the expiration or termination of this Lease in relation to such Vehicle at the location where delivery was made or at such other location as is designated by Lessor in the same working order, condition and repair as when received by Lessee, excepting only wear and tear caused by normal usage.... After said return, Lessor shall cause such Vehicle to be sold at public or private sale, at wholesale, for the highest cash offer received and still open at the time of the sale." (emphasis added)

The Lease then requires Associates to return to Debtor the amount by which the "net sale proceeds" exceed the amount Debtor owes under the terms of the lease. (Lease ¶ 9.) Associates concedes that Debtor has paid all amounts to which Associates is entitled under the lease. It also concedes that Debtor has paid it the full "residual value" for the vehicles in question.

Associates, however, claims that Debtor is not entitled to title to the vehicles because Debtor did not observe the formality of giving notice and returning the vehicles for a sale under paragraph 8 of the Lease. Associates also contends, somewhat inconsistently, that having failed to receive the vehicles from Debtor, Associates treated the vehicles as stolen and considered the transaction a forced sale. Specifically, Associates's counsel stated at trial that "since there was no notice given, they [Debtor] were billed the residual amount. There are provisions in this lease agreement that state that if the vehicle is stolen, if the vehicle is not returned, that it's going to be treated as a sale having occurred."

Assuming that Associates treated the transaction as a sale of the vehicles, as Associates's counsel contends, Iowa law requires Associates to transfer title to Debtors. Iowa Code §321.45(3). Statutes existing at the time of contracting are implied terms in every contract. C & F Maintenance & Property Management v. Eliason & Knuth, 418 N.W.2d 44, 45 (Iowa 1988) (citing Koval v. Peoples, 431 A.2d 1284, 1285-86 (Del. Super. Ct. 1981) and implying local ordinances into construction contract).

Consequently, even if Associates was correct in treating this transaction as a "forced sale," it must relinquish title.

In addition to Associates's position that this transaction constitutes a sale, a reasonable construction of the Lease allows Debtor to purchase the vehicles from Associates without the formality of a turnover of possession. The Lease broadly allows Associates to sell the vehicle at a "public or private sale." (Lease ¶ 8.) Nothing in the Lease purports to prevent Associates from selling the vehicle to Debtor through a "private sale" for the "residual value." Viewing the contract and circumstances as a whole, Debtor could have reasonably interpreted the Lease to waive the formal turnover procedure if Associates agreed to sell the vehicles to Debtor.

Indeed, Associates's actions indicate that it interpreted the Lease to allow it to sell the vehicles to Debtor without the formality of a turnover. Debtor never returned the vehicles in question to Associates. Instead of sending Debtor a demand for possession of the vehicle, Associates sent Debtor an "invoice" for the vehicles, requesting payment of the "residual value" of each vehicle. (Debtor's Exs. 2, 5). An invoice is commonly used in conjunction with a sale. See, e.g., Webster's Collegiate Dictionary 617 (10th ed. 1993) (invoice is "an itemized list of goods shipped usu[ally] specifying the price and the terms of the sale") (emphasis added). This, together with Associates's failure to request return of the vehicles, would lead a reasonable person to conclude that Associates intended to sell the vehicles to Debtor for the "residual value." If Associates intended the Lease to allow a sale only when Debtor returned possession of the vehicle to Associates, it would have sent a demand for possession instead of an "invoice" for the "residual value" with language and terms indicating a sale. This conduct convinces the Court that Associates intended to allow Debtor to purchase the vehicles at the Lease's end without the formality of a turnover.

Iowa law provides that a party to a contract, who is entitled to performance, may waive the right to performance under the contract. This is known in contract terms as a waiver. A waiver may be shown by actions, or from a party's conduct and the surrounding circumstances. The essential elements of a waiver are the existence of a right, knowledge of that right, and the intention to give up enforcement of that right. See Terra Industries, Inc. v. Commonwealth Ins. Co., 981 F. Supp. 581, 601 (N.D. Iowa 1997) (applying Iowa law); Uniform Jury Instructions for Iowa, 2400.11.

In this case, Associates was authorized to seek return of the vehicles in question and sell them pursuant to the procedures set out in the lease. Based upon all of the circumstances presented in this case, however, it is clear to this Court that Associates waived the right to enforce those provisions by utilizing a procedure which was not set forth specifically in the lease. That procedure was the sending of an invoice for the residual value of the vehicles in question. In this Court's opinion, it is inconsistent for Associates to seek payment of the remaining value of these trucks, accept the same, and then subsequently complain that the procedures which Associates itself ignored now form the basis for a breach of contract claim.

Ultimately, this Court concludes that Associates waived the provisions requiring a return of the vehicle and a sale under paragraph 8. The conclusion that Associates waived those provisions is consistent with logic and the terms of the lease. Under the terms of the lease, Associates was entitled to all monthly rental payments as well as the residual value of the vehicles. Under the transaction which occurred, Associates received those benefits in their entirety. To conclude otherwise would require some explanation as to how Associates is entitled to both retain residual value payments of almost $26,000 as well as retain title to these vehicles.

Associates's counsel concedes that the Lease requires it to sell the vehicles once Debtor returns possession thereof. Counsel also concedes that Associates would have to relinquish title to the purchaser at that sale. Associates may only retain the "residual value" plus the amount of any default then existing from the proceeds of the sale. (Lease ¶¶ 8, 9.) It would be quite harsh for the Court to read the contract as allowing Associates the windfall of retaining both the "residual value" and title to the vehicles simply because Debtor did not observe the formality of a turnover. Absent clear terms in the Lease, the Court will not construe the contract to contemplate such a result.

The Court also rejects Associates's argument because the turnover and sale in this case would be a useless act. Associates suffers no harm by foregoing a formal turnover and sale. The record shows that Associates is not currently entitled to any further payments from Debtor for these two trucks. For this reason, Associates would not be entitled to retain any funds from the proceeds of a sale. Associates, therefore, has nothing to gain from the formality of a turnover and sale. The Court will not require a mere formality at the request of a party who has no interest in the performance.

Retention of Title

Associates alternatively contends that even if it "sold" the vehicles to Debtor, that it is entitled to retain title thereto until Debtor performs all of its obligations to Associates under other leases. This argument is without merit. Even if Associates does have a right to future offset under the Lease, that right only applies against proceeds of a sale. Paragraph 9 of the Lease, which Associates contends gives it the right to future offset applies only to "sums received as proceeds." Associates concedes that it treated the vehicles as sold under paragraph 8 of the Lease. Nowhere does paragraph 8, or any other provision of the Lease, allow Associates to sell the vehicles and retain title from the purchaser until Debtor has fully performed under all of its leases with Associates. Given the statutory mandate of Iowa Code sec. 324.45(3) to transfer title pursuant to the sale of a motor vehicle, the Court refuses to infer such a right from the terms of the lease.

Conclusion

It is the ultimate conclusion of this Court that Associates sold the vehicles to Debtor. This conclusion is rationally reached in two ways. Associates' apparent position is that this was treated as a forced sale under the theft provisions of the lease and Associates was, therefore, justified in seeking and retaining the residual value. From that position, the Court can conclude that the "forced sale" was a private sale under the lease agreement. This result is likewise reasonably reached by concluding that Associates waived the provisions requiring a return of the vehicle and a public sale, and privately sold the vehicle to Debtor for the residual value thereby getting the benefit of the bargain from this contract.

Under either theory, it is the conclusion of this Court that a sale of the two vehicles in question occurred when Associates tendered the invoice seeking the residual value and Debtor accepted this offer by tendering the entire residual value to Associates. Associates cannot now alter its position by denying a sale and arguing that it is not only entitled to the sale price but also entitled to retain the titles to these vehicles. This Court must, therefore, conclude that a sale did occur and that Debtor is entitled to the protections of the law provided when the sale of a motor vehicle occurs under Iowa law.

Title Transfer in Iowa

Iowa law provides that:

> Upon the transfer of any registered vehicle, the owner, except as otherwise provided in this chapter, shall endorse an assignment and warranty of title upon the certificate of title for such vehicle with a statement of all liens and encumbrances thereon, and the owner shall deliver the certificate of title to the purchaser or transferee at the time of delivering the vehicle except as otherwise provided in this chapter. The owner shall indicate to the transferee the name of the county in which the vehicle was last registered and the registration expiration date.

Iowa Code §321.45(3). The law also provides that:

> No person, except as provided in sections 321.23 and 321.45 shall sell or otherwise dispose of a registered vehicle or a vehicle subject to registration without delivering to the purchaser or transferee thereof a certificate of title with such assignment thereon as may be necessary to show title to the purchaser.

Iowa Code §321.67(1).

> Finally, the law provides that:
>
> It is a misdemeanor, punishable as provided in section 321.482 for any person to commit any of the following acts:
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> . . .
>
> (4) to purport to sell or transfer a motor vehicle, trailer, or semi-trailer without delivering to the purchaser or transferee a certificate of title or a manufacturer or importer certificate duly assigned to the purchaser or transferee as provided in this Chapter.

Iowa Code §321.104(4).

The law is clear that a buyer is entitled to receive title to a vehicle and that the duty is upon the seller to provide that title. Failure to do so is a violation of law. In Tim O'Neill Chevrolet, Inc. v. Forristall, 551 N.W.2d 611, 618 (Iowa 1996), the court holds that section 321.25 requires sellers of automobiles to transfer title. Failure to comply with the statute is negligence per se. Id. The court affirmed the award of damages for the buyer's loss of use of the car he purchased which was caused by the seller's failure to comply with the statute. Id.; see also Levin v. Nielsen, 306 N.E.2d 173, 184-85 (Ohio 1973) ("as a general rule, at law, a person aggrieved by the failure of another to perform a statutory duty imposed for the benefit of the public, or for the benefit of individuals, can assert a breach of that duty in a civil action").

The Court concludes Debtor is entitled to pursue civil remedies including remedies for damages and injunctive relief as a result of Associates' violation of its statutory duty. As the Court has concluded Associates sold the leased vehicles to Debtor, Associates has a statutory duty to transfer title to the vehicles to Debtor. The Court has equitable authority to compel Associates to take the necessary steps to correct its statutory violation. Associates is ordered to deliver to Debtor the certificates of title for the 1994 Mac CH613 truck and the 1994 Mitsubishi FUSO truck.

Damages

Debtor also requests damages in the total amount of $8,100.07. This amount includes repairs and maintenance as documented in Debtor's Exhibit 3. The Court is not convinced that these charges were

caused by Associates' refusal to turn over titles to the trucks. Rather, Debtor would likely be paying for repairs and maintenance, or monthly debt service, on replacement vehicles had it received the certificates of title and been able to trade the trucks for new ones.

Pre-judgment interest can be awarded from the initial date of demand in circumstances where a party has retained property to which it is not rightfully entitled. In re Hill, 174 B.R. 949, 953 (Bankr. S.D. Ohio 1994). Debtor paid Associates $19,225 as residual value on the Mac truck in April 1998. It paid $6,200 as residual value on the Mitsubishi truck in March 1999. The federal judgment rate of interest is currently approximately 5.4%. Interest on the $19,225 payment from April 1998 equals $1,712. Interest on the $6,200 payment from March 1999 equals $227. Debtor is entitled to total damages of $1,939 which is interest on the amounts Associates received from the sale of the trucks to Debtor for the residual values. Debtor has lost the use of these funds during the time Associates has withheld the certificates of title to the trucks.

WHEREFORE, Debtor's complaint is GRANTED.

FURTHER, Plaintiff has proven that Defendant, Associates Leasing, Inc., sold the leased trucks to Debtor.

FURTHER, Associates is ordered to transfer the certificates of title to the trucks, 1994 Mack Tractor, Model CH 613, Serial No. 1M2AA13Y1RW041798 and 1994 Mitsubishi Fuso, Model FK455MR, Serial No. JW6DNN1E5RL000162MW534A, to Debtor on or before November 29, 1999.

FURTHER, the Court awards Debtor Emerson Mattress, Inc. damages of $1,939.

FURTHER, Associates Leasing, Inc. shall transfer the certificates of title by December 2, 1999.

FURTHER, if Defendant, Associates Leasing, Inc., fails to transfer properly executed certificates of title by said date, it shall be assessed a penalty of $250 per day until Defendant is in full compliance with this order.

FURTHER, the costs of this action are assessed to Defendant, Associates Leasing, Inc.

FURTHER, judgment shall enter accordingly.

SO ORDERED this 19th day of November, 1999.

Paul J. Kilburg
Chief Bankruptcy Judge