STATE OF MINNESOTA
IN COURT OF APPEALS
A09-740

American Bank of the North,
Respondent,

vs.

Leonard Jelinski,
Appellant.

Filed May 4, 2010
Affirmed; motion granted
Hudson, Judge

Morrison County District Court
File No. 49-CV-07-2389

Stephanie A. Ball, Fryberger, Buchanan, Smith & Frederick, P.A., Duluth, Minnesota (for respondent)

G. Marlene Clark, G. Marlene Clark, P.A., Long Prairie, Minnesota (for appellant)

Considered and decided by Connolly, Presiding Judge; Hudson, Judge; and Johnson, Judge.

U N P U B L I S H E D O P I N I O N

HUDSON, Judge

On appeal from a judgment granting in part and denying in part respondent's claims for replevin of several items of personal property, appellant argues that the district court erred in holding that respondent had a valid security interest in the items because they were leased to, rather than owned by, respondent's debtor. On a notice of related

appeal, respondent argues that the district court erred by ordering return of the personal property based on a claim of replevin rather than allowing respondent to collect money damages. Because the district court did not err, we affirm. We also grant respondent's motion to strike.

FACTS

Appellant Leonard Jelinski is Gary Jelinski's father. Gary Jelinski was the president and sole shareholder of Northern United, a welding and fabrication business. Northern United entered into a small-business loan agreement with respondent American Bank of the North (Bank), which included a blanket security agreement covering all of Northern United's owned or after-acquired equipment. This security interest was perfected by filing financing statements with the Minnesota Secretary of State. Northern United eventually filed for bankruptcy and became insolvent, and Bank sought to collect its collateral. Bank sought an order enforcing its right to four items of personal property in appellant's possession: (1) a paint booth and powder-coating equipment, (2) a 1994 Hyster forklift, (3) a 1998 Dodge pickup truck, and (4) a 2004 PJ trailer. Bank claimed that these items were subject to a perfected security interest in its favor.

Appellant also provided financial assistance to Northern United and Gary Jelinski. While Northern United was in business, appellant, Clifford Jelinski, and Gary Jelinski discussed Northern United's business need for a paint booth and powder coating equipment. Appellant claims that he and Clifford Jelinski purchased the paint booth and equipment and leased them to Northern United. Bank asserts that Northern United owned the equipment subject to appellant's security interest in the items. Appellant and

Clifford Jelinski purchased the paint booth for $43,329.53 on July 1, 2005. Northern United and Gary Jelinski agreed to pay appellant and Clifford Jelinski for the paint booth over time. Once the purchase price of the paint booth was paid in full with interest, Northern United would own the paint booth outright. If more than three payments were missed, the parties agreed that appellant and Clifford Jelinski could remove the paint booth. Northern United made payments on the paint booth until January 2007. Appellant purchased Clifford Jelinski's interest in the paint booth at that time. After at least three payments were missed, appellant removed the paint booth in April 2007.

Appellant also asserted that in September 2004, he individually bought a 1994 Hyster forklift that he allowed Northern United to use and store. Bank asserted that appellant provided financing to Northern United for the purchase of the forklift. There is little documentation regarding the forklift. The forklift was removed by appellant from Northern United at approximately the same time as the paint booth.

A 1998 Dodge pickup truck and a 2004 PJ trailer were also the subject of dispute as to ownership and interest between Bank and appellant. The vehicles were primarily used by Northern United; but appellant insured both vehicles, had his name on the titles, and possessed the vehicles at the time of the dispute.

Bank filed a complaint against appellant seeking judgment in replevin, proceeds, wrongful detention, and conversion. Bank requested return of the four items of property that it claimed were subject to its security interest as well as damages. After a bench trial on October 27, 2008, the district court held that the paint booth and forklift were items owned by Northern United subject to security interests held by Bank and appellant.

Because Bank had perfected its security interest and appellant had not, the district court determined that Bank had priority and was entitled to possession of the paint booth and forklift or a money judgment if the items were not returned. The district court determined that appellant had a priority interest in the truck and trailer because he kept title to the vehicles in his name.

After trial, appellant sought to reopen the record to present additional evidence. That motion was denied. Appellant also sought a stay of the portion of the district court's order requiring him to return the equipment. The district court granted the stay. Bank also sought posttrial relief with respect to the district court's order that the paint booth and forklift be returned to Bank. Specifically, Bank sought to have the district court amend the order to provide an entry of money judgment rather than return of the equipment, claiming that, otherwise, the district court would effectively be allowing appellant to dictate the remedy. The district court declined to address the motion on its merits, stating that it could not address a claim of judicial error. This appeal and notice of related appeal follow.

D E C I S I O N

I

Appellant argues that the paint booth is owned by him and was leased to Northern United, rather than owned by Northern United subject to appellant's security interest. The district court determined that the agreement between appellant and Northern United was a loan secured by collateral rather than a lease.

Findings of fact, whether based on documentary or oral evidence, will not be disturbed unless clearly erroneous. Minn. R. Civ. P. 52.01. Due regard is given to the district court's credibility determinations. *Id.* But this court need not give deference to the district court's decision on a question of law. *Bondy v. Allen*, 635 N.W.2d 244, 249 (Minn. App. 2001).

A security interest is an interest in personal property or fixtures that secures payment or performance of an obligation. Minn. Stat. § 336.1-201(b)(35) (2008). Article 9 of the Uniform Commercial Code (UCC) applies to security interests created by a contract, including a lease intended as a security interest. *Id.* The UCC distinguishes leases from security interests. Minn. Stat. § 336.1-203 (2008). Whether a transaction in the form of a lease creates a lease or a security interest is determined by the facts of each case. *Id.* § 336.1-203(a). The court looks to the substance rather than the form of an agreement to determine whether it is a security interest or a lease. *James Talcott, Inc. v. Franklin Nat'l Bank of Minneapolis*, 292 Minn. 277, 282-83, 194 N.W.2d 775, 779 (1972).

A transaction that appears to be 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" one of four other factors is present, one of which is that "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." Minn. Stat. § 336.1-203(b).

Paint booth and related equipment

Here, there was no formal written lease agreement for the paint booth. Thus, no evidence was offered as to whether Northern United or Gary Jelinski could terminate the lease and, therefore, the district court could not apply section 336.1-203(b). Nevertheless, we agree with the district court that the substance of the transaction was a loan.

Appellant testified that once the purchase price money was paid to him for the paint booth, Northern United would own the paint booth outright. Gary Jelinski testified that "there was money borrowed on the paint booth," and that he "borrow[ed] money from [his] father." These statements indicate that the agreement is more properly characterized as a security interest and show that the transaction creates a security interest, rather than a true lease. *See FBS Bus. Fin. Corp. v. Edison Fin. Group, Inc.*, 464 N.W.2d 304, 305 (Minn. App. 1990) (stating that an agreement that upon compliance with lease terms, the lessee shall become or has the option of becoming the owner of the property for no consideration or nominal consideration makes the purported lease a security-interest agreement); *see also Chemlease Worldwide Inc. v. Brace, Inc.*, 338 N.W.2d 428, 432 (Minn. 1983) (concluding that a lease that allowed the lessee to own equipment at the end of the lease term for nominal consideration of one dollar is a security-interest agreement). And the terms used in the writing memorializing the agreement, such as "borro[w]s," "collateral," "interest," and "until equipment is paid in full," support the interpretation of the transaction as a loan.

Most importantly, appellant prepared a financing overview outlining what monies he had loaned to Gary Jelinski for Northern United. The financing overview summarized the extent of the various loans made by appellant to Gary Jelinski. The document clearly stated that the paint booth and powder-coating equipment were considered collateral for a $29,310 loan.[1] Therefore, the district court did not err in determining that the paint booth and related equipment were subject to Bank's perfected security interest.

Forklift

Appellant argues that he owns the forklift and simply stored it at Northern United and allowed Northern United to use it. The district court found that the forklift belonged to Northern United and was subject to a security interest by appellant. Because appellant's unperfected security interest was lower in priority than Bank's perfected security interest, the district court determined that Bank was entitled to possession of the forklift.

There was little evidence produced in the district court concerning the forklift. But the analysis applied to the paint booth may also be applied to the forklift. The forklift also appears on the financing overview prepared by appellant, and the overview indicates that the "1993 Hyster" forklift is collateral for a $5,325 loan accruing interest at

[1] Bank brought a motion to strike a document attached to appellant's reply brief entitled "Copy of Exhibit A - from Bankruptcy Court file," which purports to directly contradict the financing overview and state that the property in question was leased to appellant. Because that document is not part of the district court file, the motion to strike is granted and this court will not consider that document. *See* Minn. R. Civ. App. P. 110.01 (stating that the record on appeal consists of the papers filed in district court, and the exhibits and transcripts of the proceedings); *Thiele v. Stich*, 425 N.W.2d 580, 582-83 (Minn. 1988) (stating that an appellate court may not base its decision on matters not produced and received in evidence in district court).

a rate of 4%. Also relevant is appellant's status as a financier for Northern United. *See FBS Bus. Fin. Corp.*, 464 N.W.2d at 305. In that regard, appellant made many other loans to Northern United that also appear on the financing overview. Thus, the district court did not err in determining that, like the paint booth, appellant considered the forklift collateral for a loan, rather than equipment owned by him that he allowed to be used by Northern United.

Pickup truck and trailer

Appellant also appears to argue that Northern United does not have a security interest in the pickup truck and trailer. The pickup truck and trailer were also listed in the collateral column on the financing overview prepared by appellant. But the district court held that "[b]y maintaining title in his name, [appellant] employed a common but unofficial method of securing his interest in the vehicles. Northern United consequently owned the vehicles subject to [appellant's] interest." The district court also held that appellant's interest in the truck and trailer had priority over Bank's interest because Bank did not perfect its security interest in the vehicles. But the district court did not make any finding that Northern United has a security interest in the truck and trailer, and Northern United is not a party to this appeal. Therefore, we conclude that issue is moot because no actual controversy exists as to Northern United's potential security interest in the truck and trailer. *See In re McCaskill*, 603 N.W.2d 326, 327 (Minn. 1999) (stating that the mootness doctrine requires a court to only decide actual controversies and to avoid issuing advisory opinions). In any event, even if Northern United had a security interest

in the vehicles, it would be invalid because it did not record its interest or deliver a certificate of title. *See* Minn. Stat. § 168A.18 (2008).

II

Bank filed a notice of review[2] challenging the remedy provided to it by the district court. Bank claims that the district court erred in holding that it was entitled to immediate possession of the paint booth and forklift under a replevin theory and argues that it is entitled, instead, to money damages.

"Granting equitable relief is within the sound discretion of the [district] court. Only a clear abuse of that discretion will result in reversal." *Nadeau v. County of Ramsey*, 277 N.W.2d 520, 524 (Minn. 1979). Specific performance is an equitable remedy within the sound discretion of the district court. *Lilyerd v. Carlson*, 499 N.W.2d 803, 811 (Minn. 1993). A reviewing court will not disturb a damage award "unless its failure to do so would be shocking or would result in plain injustice." *Hughes v. Sinclair Mktg., Inc.*, 389 N.W.2d 194, 199 (Minn. 1986).

A conversion action seeks to recover damages, while a replevin action seeks to regain possession of the item itself. *Widgren v. Massie*, 352 N.W.2d 420, 424-25 (Minn. App. 1984). A replevin action is "to recover the possession of personal property." Minn. Stat. § 548.04 (2008). A replevin judgment "may be for the possession [of the personal property] or the value thereof *in case possession cannot be obtained*, and damages for the detention, or the taking and withholding." *Id.* (emphasis added). If possession of only a

[2] A notice of review is now called a "notice of related appeal." Minn. R. Civ. App. P. 106 (effective Jan. 1, 2010).

portion of the property may be obtained, a party may take possession of that portion and recover the value of the remainder. *Id.* The factfinder assesses the value of the property and the damages, if claimed in the complaint, that the prevailing party sustained "by reason of the detention, or taking and withholding, of such property." Minn. Stat. § 546.23 (2008).

Here, Bank pleaded alternative theories for recovery and remedies in its complaint, including both replevin and conversion. Replevin was the first count listed. The district court treated Bank's claim as one for replevin to prevent double recovery and because return of the property was possible. The district court stated that a replevin judgment would encompass the relief requested and that Bank was entitled to recover the property or its value if the property cannot be returned. The district court also noted that Bank should not receive more than it would have been entitled to recover directly from Northern United. The district court determined that Bank "is entitled to immediate possession of the paint booth and forklift. . . . [Appellant] shall return the paint booth and forklift to a location specified by [Bank] within twenty-one days of the entry of the Judgment herein." If appellant failed to return the items, the district court stated that judgment would be entered in favor of Bank and against appellant "in the amount of $50,739.30 plus interest since May 1, 2007."

But Bank alleges that it is entitled to elect its remedy; that it has elected conversion; and that the district court's ruling effectively allowed appellant to dictate the remedy. We are not persuaded by Bank's position. We first note that Bank did not amend its complaint at any time to dismiss the replevin claim, nor did it elect to

exclusively pursue a conversion claim during the proceedings. Moreover, Bank's closing arguments relating to the value of the property and potential damages could relate either to a conversion or replevin claim because damages may be ordered in replevin if the property cannot be returned. *See* Minn. Stat. § 548.04. And return of the physical property should be ordered whenever possible. *Widgren*, 352 N.W.2d at 425-26.

Here, the paint booth and forklift are available and in appellant's possession. Accordingly, Bank cannot elect to take a money judgment. Bank claims that it can elect a remedy but cites no authority to support its assertion. Indeed, neither appellant nor the district court dictated the remedy for Bank's replevin claim. Rather, the remedy—possession of the property—was dictated by the replevin statute. *See* Minn. Stat. § 548.04. Accordingly, the district court did not abuse its discretion by ordering return of the property.

Affirmed; motion granted.