High or Hell Water Clauses:
Understanding Equipment Finance Leases

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The sale of capital equipment has changed over the last decade to include the increased use of product leasing. As leasing grows, so do the questions concerning the liability of finance companies with regard to the quality of the product provided. Traditionally, product leasing has occurred when a purchaser selects capital equipment from a supplier, but instead of purchasing the equipment, the finance lessor buys the equipment and then leases it to the purchaser (now the lessee). The lease contract signed by the lessee commonly includes language whereby the lessee waives its right to withhold payment for any reason including defects, damage or unfitness of the equipment. Such payment provisions are called "hell or high water" clauses. A recent case decided by the Supreme Court of Georgia has clarified the Georgia courts' interpretation of these so-called "hell or high water" clauses. That case is Colonial Pacific Leasing Corporation vs. McNatt, et al.;Datronic Rental Corporation, et al. v. McNatt, et al., 268 Ga. 265 (Ga. 1997).

This case began when Linda and William McNatt, the owners of Quick Trip Printers entered into negotiations with a company called Itex Systems to purchase two computer printing systems. However, rather than purchasing the printers from Itex, the McNatts executed equipment finance leases with a company called Burnam Leasing Company, whereby Burnam agreed to purchase the equipment from Itex and then lease the equipment to Quick Trip for a monthly rental payment.

Prominently displayed on the front page of both leases signed by Quick Trip was Burnam's disclaimer of warranties as well as the "hell or high water" clause whereby the McNatts agreed that "[n]o defect, damage or unfitness of the equipment for any purpose shall relieve lessee of the obligation to pay rent or relieve lessee of any other obligation under this lease." Under the leases the McNatts further agreed to pay the total rent, not "abate, set off, deduct any amount, or reduce any payment for any reason," and not "assert against the lessor's assignee

any defense, counterclaim or setoff that Quick Trip may have against Burnam Leasing."

In the equipment leases signed by Quick Trip with Burnam, the McNatts authorized Burnam to assign its interest in the leases and also acknowledged that the equipment had been received "in good condition and repair, has been properly installed, tested, and inspected, and is operating satisfactorily in all respects for all of lessee's intended uses and purposes." Once the leases were executed with Burnam, Burnam assigned its interest in the leases to Colonial Pacific Leasing Corporation and Datronic Rental Corporation.

After the equipment was delivered to Quick Trip, they experienced problems with the printers and ultimately did not pay Colonial Pacific or Datronic under the assigned leases. After the lessors repossessed the equipment, Quick Trip filed suit against Itex and the lessors, seeking rescission of the leases and seeking damages for the lessors' negligent release of funds to Itex. The lessors Colonial Pacific and Datronic filed a counterclaim against the McNatts seeking payment under the leases and filed a motion for summary judgment on their claims. Prior to trial, the court entered an order granting the lessors' motion for summary judgment and finding in favor of the lessors against the McNatts.

On appeal, the Georgia Court of Appeals agreed with the McNatts that the trial court had wrongly granted summary judgment to the lessors when it failed to first determine the merit of the McNatts' rescission claim due to their problems with the equipment. The Appellate Court held that the lease's requirement that rental payments be made even if the equipment was damaged, defective or unfit, could not be enforced when it was alleged that employees of the equipment vendor, Itex, had fraudulently induced Quick Trip to acquire the equipment. The Court found "that McNatt took prompt action to rescind, never took action to affirm after it discovered the system was defective, and did not make a single payment under either lease." McNatt v. Colonial Pacific, et al., 221 Ga. App. 768, 770 (1996). The Court of Appeals rejected the lessor's effort to use the disclaimer provisions of the leases to defeat the McNatts' rescission claim, including the hell or high water clause.

The case was then appealed to the Georgia Supreme Court. The Supreme Court stated in its opinion the following:

"We express particular concern with whether the "hell or high water" clause in the equipment finance leases at issue insulated the assignees of the lessor from the lessee's claim of fraud allegedly perpetrated by agents of the supplier of the equipment. We conclude that a "hell or high water" clause does not insulate a lessor's assignee from a claim of fraud where an agency relationship can be established between the assignee and the perpetrators of the alleged fraud. "

The Court went on to state:

"In order for the purported fraud of the employees of the equipment supplier to authorize rescission of the finance lease, their actions must somehow be imputed to the assignee/lessors through the finance lessor. "

The court therefore concluded that as long as no evidence could be shown of a relationship between the equipment supplier and the finance lessor by which the alleged fraud could be imputed to the finance lessor, then the lease could not be rescinded and the hell or high water clause would be viable. The higher court's decision clearly strengthens the enforcement of such provisions when used in an equipment lease so long as the original representations used to lease the equipment are not fraudulent.

Certainly, where equipment manufacturers also finance leases of their equipment, the lines are not so clearly drawn, and the question remains if the arm of the company that finances the lease can insulate itself from the arm of the company that supplies the equipment. However, with respect to where there is independent financing of equipment, this Court's decision has clearly strengthened the use of such contract clauses as a means to protect the flow of money to companies that extend credit.