NADC
National Association of Dealer Counsel

DEFENDER

The National Association of Dealer Counsel Newsletter JULY / AUGUST 2010

In this Issue:

Save the Date:

Fall Workshop
October 3-4, 2010
Chicago, IL
Trump International Hotel & Tower

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Executive Director's Message

Erin K. Hussey
NADC Executive Director

I am pleased to present the July / August issue of the Defender as the new Executive Director of NADC. The management of NADC was transitioned to Association Management Strategies (AMS) on July 1, 2010. We are honored that the NADC has selected our group (AMS), and we look forward to working with NADC leadership and members in helping the association achieve its goals.

AMS is a full-service professional association management firm providing executive management and administrative support to industry trade associations, coalitions and professional societies. AMS was founded on the belief that an association management company should bring certain attributes to its client partnerships, including: strong leadership; an experienced and dedicated staff of professionals; the ability to keep pace with an ever-changing technology environment; sound financial management; and a vision for the future. Association Management Strategies has a record of successfully providing that leadership and vision to a number of organizations of varying size and interests.

The late summer and fall will be a busy time for NADC. We expect to launch the new and improved NADC Website on August 23, 2010. The new website will have an updated design and many new, useful features. We will have two separate web tutorials to show you how to best take advantage of all the enhanced features that the new website will offer. The website tutorials will take place on August 24th and 31st at 2:00 pm EST. Please watch your email for more details.

Also, please save the date for the Fall Workshop to be held October 3rd and 4th, 2010 at the impressive Trump International Hotel & Tower in Chicago, Illinois (http://www.trumpchicagohotel.com/). We will offer timely, useful sessions that will send attendees off with invaluable take home information. This Workshop promises to be a can't miss event! Please check the website for more information and to register for the event.

These are just a couple of the projects that NADC has on the horizon. We are always interested in hearing new ideas and suggestions from the membership. Your management team will be led by me (ehussey@dealercounsel.com) and Ben Bruno, Program Assistant, (bbruno@dealercounsel.com). I know I have only met a handful of the membership, but I look forward to meeting all of you in the very near future. In the meantime, please feel free to give us a call (202-293-1454) and introduce yourself. We look forward to starting a new and exciting Chapter in NADC's history book! ■

From the Editor:

It Pays to Remind Your Clients About the Basics Occasionally

Michael G. Charapp, Editor of the Defender

From time to time, I get calls from clients asking questions that surprise me. I generally assume that dealers are aware of the basics about what they must display in connection with the vehicles they sell. But when I get the call to the effect that "someone just told me that…" I realize that those of us representing dealers may assume too much about dealers' knowledge of the laws that affect them. Here are some basics on what must be displayed in connection with vehicles for sale about which you may want to remind your clients occasionally.

Fuel Economy Guides

Next time you are in a new car dealer client's showroom, ask where the fuel economy guide booklets are located. Chances are good that you will get a blank stare, followed by a stammering response that fuel economy numbers are on the factory (Monroney) sticker. However, federal law requires that new car dealers display EPA/DOE Fuel Economy Guide booklets at each location where new vehicles are offered for sale and to make them available to the public at no charge. The booklets and related information are available at http://www.fueleconomy.gov.

NHTSA Insurance Cost Information Booklets

In my experience, the booklets discussing collision costs for new cars are even more scarce. New car dealers must display NHTSA's most recent "Relative Collision Insurance Cost Information Booklet." This booklet compares differences in insurance costs for vehicles within a similar class on the basis of damage susceptibility, and it is updated each year. One booklet is generally mailed to each new car dealer annually. Or the booklet is available at http://www.nhtsa.dot.gov/. A dealer should reproduce and maintain a sufficient number of copies of the booklet so that it is available to prospective purchasers of new vehicles who request it.

Used Car Buyers Guides on Demonstrators

Under the FTC Used Car Rule, a buyer's guide must be affixed to a used motor vehicle available for sale to a consumer at retail by a dealer. A used motor vehicle is defined by the Rule as any vehicle driven more than the limited use necessary in moving or road testing a new vehicle prior to delivery to a consumer. That definition makes demonstrators used cars subject to the Rule.

Many dealers assume that a vehicle that may be sold as new under state law is not subject to the FTC Used Car Rule. As a result, they do not indentify demonstrators as vehicles that must have buyer's guides.

An FTC investigator who visits a dealership will look to see where the salespeople and managers part their demonstrators. If the vehicles do not have buyer's guides affixed, the dealer is looking at an FTC enforcement action. Remind dealers that they must spot check for buyer's guides occasionally, and that check should include a visit to the area where demonstrators are parked.

Warranties

The Magnuson-Moss Warranty Act requires the seller of a consumer product with a written warranty to make a text of the warranty readily available for examination by a prospective buyer. The requirement is satisfied if the dealer either displays the warranty in close proximity to the warranted vehicles or places signs, reasonably calculated to elicit the attention of prospective buyers, in prominent locations in the dealership advising prospective buyers of the availability of warranties upon request. If the dealer opts for the latter option, the dealer must furnish the warranty upon request.

Used Car Warranties

Many dealers assume that in selling a used car, the description of the warranty on the vehicle's buyer's guide is sufficient documentation for the buyer. That is not correct. The description of a warranty on the FTC window sticker is not the warranty itself. The Magnuson-Moss Warranty Act requires that a written warranty be provided to the buyer, and the buyer's guide does not contain the terms required in a warranty that complies with the Act. The actual warranty document must be delivered to the buyer in connection with the sale of a used car with an express warranty. ■

Michael G. Charapp is a lawyer in the Washington, D.C. metro area who represents car dealers and dealer associations. He is editor of the Defender. ***He encourages submissions for publication, and he can be reached at:*** *mike.charapp@cwattorneys.com.*

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Lien Priority between Motor Vehicle Floor Plan Lenders and Retail Lenders

Why Bank One v. Arcadia Financial is No Longer Good Law

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Introduction

In *Bank One v. Arcadia Financial*[1], the Fifth Circuit applied Texas law to give a floor plan lender priority over a retail purchaser's secured lender. The Court, in what many viewed as standing Article 9 of the Uniform Commercial Code ("UCC") on its head, ruled that the Texas Certificate of Title Act ("COTA") trumped the UCC.

Revised Article 9 exists in all states as do COTAs. Interpretation, and the language of the COTAs, however, can vary.

Bank One concerned whether the retail purchase of an automobile severed the security interest of the dealer's floor plan lender and gave priority to the retail lender's lien. Bank One argued that its security interest remained valid because the buyer did not receive the certificate of title (which it held) as required under COTA. Arcadia, the retail lender, argued that the buyer was a "buyer in the ordinary course of business" who took free and clear of Bank One's security interest. Accordingly, under the UCC, Arcadia's purchase money security interest took priority.

The Fifth Circuit held COTA controlled. Because the certificate of title was not transferred at the time of sale, the sale as between the dealer and buyer was void. Without a "sale" under COTA, the buyer's retail lender could not use the "buyer in ordinary course" defense, and the floor plan lender's lien remained in effect.

Though the Texas Supreme Court hasn't decided the issue, statutory analysis and recent case law suggest that *Bank One* is not, and perhaps never was, good law. This article analyzes the relationship between COTA and the UCC and reviews the case law of Texas and three other states.

I. Statutory Analysis

1. COTA Does Not Govern Completion of Dealer's Sale

Under COTA, a vehicle can be sold at a *subsequent* sale only when the *owner* transfers the certificate of title. COTA defines a "dealer" as "a person who purchases motor vehicles for sale at retail." "Owner" is "a person, *other than* a . . . *dealer*, claiming title to or having a right to operate under a lien a motor vehicle." Thus, a "dealer" is not an "owner" that must transfer a certificate of title to complete the sale of a motor vehicle. A dealer's failure to "deliver" or "transfer" a certificate of title to the purchaser does not affect the validity of the sale under COTA.

2. The UCC Controls

When there is conflict between COTA and the Texas UCC, COTA expressly defers to the UCC. Thus, Article 2 of the UCC determines when the sale is complete and Article 9 determines priority of security interests.

Under Article 2, a "sale" consists of the "passing of title from the seller to the buyer for a price." This occurs when the dealer has been paid and delivers the vehicle to the buyer. A buyer in the ordinary course takes free of a perfected security interest even though the buyer knows of the security interest, unless the buyer knows that the sale violates an agreement with the secured party.

If the secured party authorized the sale by express agreement or otherwise, then the buyer takes free of a security interest. Under UCC § 2.403(b), by entrusting its collateral to the dealer, the lender authorizes the dealer to transfer all rights the lender has in the vehicle to a buyer in the ordinary course. Because a sale from a dealer to a purchaser is authorized, the lender's security interest in the vehicle is extinguished.

Under UCC § 9.315, a perfected security interest in inventory purchased does not follow the collateral after it is sold in the ordinary course of business. It attaches to sale proceeds.

Neither COTA nor the UCC allows a lender to perfect a security interest in inventory by retaining the certificates of title. Under COTA, lien-holders whose liens are properly perfected by recordation on the certificate of title have the right to retain the original certificates in their possession until the lien is retired. COTA does not provide the same right to lien-holders in inventory.

Continued on page 4.

[1] *219 F.3d 494 (5th Cir. 2000).*

3. Retail Lender Trumps Floor Plan Lender

Under the UCC, the retail lender's security interest attaches and becomes enforceable against the debtor and third parties when (1) value has been given, (2) the debtor has rights in the collateral, and (3) the debtor has authenticated a security agreement with a description of the property. As a buyer in the ordinary course, the purchaser severs the floor plan lender's interest in the vehicle as inventory and enables the retail lender's security interest to attach and be perfected as a first priority lien.

II. Texas Case Law Since *Bank One*

In *In re Dota,* the Southern District of Texas addressed a suit between a bank as floor plan lender and the consumer purchaser. The buyer purchased two vehicles, but only received title to one. The seller did not pay the proceeds of the sale to the bank and the buyer filed bankruptcy. The bank demanded return of the untitled vehicle, arguing that the buyer was not a "buyer in the ordinary course of business" because he did not receive title.

The court found that the dealer was not covered under the specific terms of COTA because its definition of "owner" specifically excludes a "dealer." Because the buyer was a "buyer in the ordinary course …" the buyer took free of any security interest in inventory.

Further, neither the UCC nor COTA permits perfection of security interests in inventory by possession of certificates of title. The bank had no right to keep title once the buyer purchased the vehicle and the dealer had a legal obligation to transfer title to the buyer.

In *First National Bank of El Campo v. Buss*, the Corpus Christi Court of Appeals held that the UCC preempted COTA in the event of conflicts. Under facts similar to *Dota,* the court held that "buyers in the ordinary course of business" cut off the lender's security interest in inventory. The court held that because there was a conflict between COTA and the "buyer in the ordinary course" provision of the UCC, the UCC controls.

In *Vibbert v. Par, Inc.*, the El Paso Court of Appeals held that failure to transfer a certificate of title to a dealership as part of a trade-in did not void a sale. The vehicle's owner traded it in on the purchase of a new car but title was never taken out of the owner's name. Because the original contract on the trade-in was never paid, the prior seller sued the subsequent retail lender for conversion of the automobile.

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The court found that it was not the purpose of COTA to impede vehicle transfers. Under the UCC, title to a purchased vehicle passes upon its delivery, regardless of whether the seller transfers the certificate of title. Thus, the sale of a vehicle without transfer of a certificate of title is valid between the parties when the purposes of COTA are not defeated.

III. Inter-Jurisdictional Analysis

Ohio

In *First Merit Bank v. Angelini*, the Ohio Court of Appeals found that the Ohio COTA trumped the UCC, specifically relying on a recent Ohio Supreme Court decision. However, Ohio's COTA provides that it prevails over the UCC in the event of conflicts. Without a transfer of the certificate of title to the purchaser, dealer's floor plan lender took priority over subsequent purchasers and their lenders. The court refused to find the retail lender's interest superior to the floor plan lender's interest where title had not been transferred.

California

In *Brasher's Cascade Auto Auction v. Valley Auto*, the court held that California's COTA could not be used to void a sale between a middleman and a dealer. The middleman financed the purchase of 32 vehicles from an auction house and then sold them to a vehicle dealer. The auction house possessed a secured interest in the middleman's 32 vehicles and held the certificates of title. The auction house's lien would remain against the vehicles until the middleman sold the vehicles and paid the auctioneer. When the middleman escaped with the money, the auction house sued the dealer. The auction house argued that no sale had occurred because the dealer never received the certificates of title.

The court determined that if the dealer could show it adhered to reasonable commercial standards sufficient to qualify as a "buyer in the ordinary course," the dealer's purchase severed the auction house's liens on the vehicles. Under California law, the transfer of a vehicle is effective even if the parties have not complied with the COTA.

Colorado

In *Valley Bank & Trust Company v. Holyoke Community Federal Credit Union*, the floor plan lender sued the consumer's lender when the proceeds of the sale were not paid to the floor plan lender. The floor plan lender maintained control over the certificates of title.

The court found that after the vehicle was sold, the floor plan lender's security interest was extinguished and transformed into a security interest in the proceeds. Since the floor plan lender authorized the dealer to sell the vehicles without informing the buyers that it reserved its rights in the collateral, the floor plan lender did not maintain a security interest in the sold vehicles. The retail lender's lien prevailed.

IV. Conclusion

The Texas Certificate of Title Act does not control on the issue of priority between a floor plan lender and a retail lender. COTA does not apply to dealers, nor is its purpose to impede the transfer of vehicles. *Bank One*'s interpretation of COTA would impede the purchase of vehicles because retail lenders would not provide financing without a first priority lien. Lastly, in any potential conflict, Texas' COTA specifically defers to the UCC.

In states in which the UCC trumps the COTA, buyers in the ordinary course of business take free and clear of liens created by the seller. (In Ohio, the floor plan lender will prevail, since the Ohio COTA expressly trumps the UCC.) Because a dealer is authorized to sell inventory, a buyer's purchase will sever the floor plan lender's security interest, even when a certificate of title is not transferred. The floor plan lender will be left with a security interest in proceeds. The retail lender's purchase money security interest can then attach and be perfected as a first priority lien. ■

We are always looking for submissions to publish in the Defender.
Please send your contributions or proposals for articles to:
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