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DEFENDER

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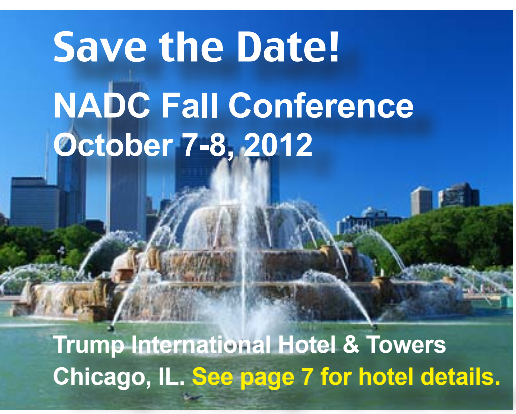

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Cars, Bankruptcy and Anna Nicole Smith

By Lawrence Young, HughesWattersAskanase

When the flamboyant Anna Nicole Smith passed away in 2007 she was survived by legal battles that began in 1995 in a California bankruptcy court. The court battles were triggered by a defamation claim brought by her opponent and stepson, E. Pierce Marshall, and Anna Nicole Smith's counterclaim against him for tortious interference. The battles raged across three venues for over sixteen years. They did not slow despite the death of both Anna Nicole Smith and E. Pierce Marshall.

The legal war was not resolved until June of last year. For the second time, the estates of Anna Nicole Smith and E. Pierce Marshall appeared before the United States Supreme Court. Only after the Court's ruling in *Stern v. Marshall* did the legal ramifications of Anna Nicole's final gift became clear.

Stern v. Marshall

In Stern, the Supreme Court found that bankruptcy courts possess the **statutory** authority to issue final judgments on private or state law counterclaims. They, however, lack the **constitutional** authority to do so.

> Article III of the United States Constitution provides in Section 1:
>
> The judicial Power of the United States shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish. The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behavior, and shall, at stated Times, receive for their Services a Compensation, which shall not be diminished during their Continuance in Office.

A primary purpose of Article III is to assure an independent judiciary, not subject to political influence by Congress or the Executive. The bankruptcy court's jurisdictional grant allows it to hear and issue final judgments on counterclaims "core" to the bankruptcy proceedings. However, the bankruptcy courts are legislative courts created to carry out a particular legislative scheme, the Bankruptcy Code, not Article III courts vested with the judicial power of the United States. Their compensation can be "diminished." They do not serve during "good Behavior" for life but instead have a limited term of 14 years. Without Article III protections for their salary and tenure, political pressure can be brought to bear on individual bankruptcy judges.

Accordingly, the Supreme Court found that allowing bankruptcy courts to issue final judgments on private or state law counterclaims would create an inherent conflict under the separation of powers doctrine in Article III. Ultimately, the Court's ruling indicates that a bankruptcy court can issue a final judgment only if a counterclaim arises under the express provisions of the Bankruptcy Code and is therefore a "public" right (one in which a claim derives from a federal regulatory scheme), not a private right under state law. As an example, the Court examined claims for tortious interference and fraudulent transfers. It concluded that each is a common law action "that simply attempts to augment the bankruptcy estate" and is thus a private right of action. Thus, both must be adjudicated only by an Article III (United States District Court) judge.

Why Does It Matter?

The rippling impact of *Stern v. Marshall* is being felt in every bankruptcy court. First, *Stern* has altered potential choices of venue. Now, if a trustee or debtor-in-possession wishes to assert, for example, a fraudulent transfer claim against a creditor, the debtor will no longer be able to bring the action in the same venue as the bankruptcy proceeding. Instead, the debtor must use a venue that would otherwise have jurisdiction over the creditor, most likely the state or federal court where the creditor is located.

Second, the threshold for determining consent to bankruptcy court jurisdiction has been elevated. One can consent to personal jurisdiction. The Supreme Court discounted the argument that by filing his proof of claim for defamation, E. Pierce Marshall impliedly consented to bankruptcy court jurisdiction to adjudicate Anna Nicole Smith's counterclaim for tortious interference. The counterclaim in the bankruptcy court would have been permissible only if E. Pierce Marshall had expressly consented to the bankruptcy court's jurisdiction.

Finally, since *Stern*, bankruptcy courts have conducted their proceedings in one of three ways:

1. First, the bankruptcy court will hear an arguably private or state law cause of action and provide a final ruling, but include a caveat that should the district court find the bankruptcy court lacked authority to enter the final ruling, the opinion is instead deemed the bankruptcy court's proposed findings of fact and conclusions of law.
2. Second, in accordance with 28 USC §157(c)(1), the bankruptcy court hears the private or state law cause of action but does not enter a final judgment. Instead, the bankruptcy court only provides recommendations on findings of fact and conclusions of law to the district court for its final judgment, much as a magistrate does.
3. Third, under the strictest interpretation of the *Stern* decision, the bankruptcy court finds that its authority is completely void to hear a private or state law cause of action because Article III goes to subject matter jurisdiction. Subject matter jurisdiction cannot be waived or conferred by consent. The reference to the bankruptcy court must be immediately withdrawn or the court must abstain or dismiss the case for lack of jurisdiction. The case must start anew in the United States District Court or another court that has jurisdiction.

In addition to the change brought to bankruptcy proceedings and counterclaims, *Stern's* effects have rippled into other areas of the judiciary. In March, the Fifth Circuit[1] considered the impact of *Stern* on the authority of magistrate judges to enter final judgments on state law causes of action. Ultimately, the Fifth Circuit did not broaden the holding of Stern, concluding that despite the parallels between magistrates and bankruptcy judges, *Stern's* limitation on authority applied only to bankruptcy proceedings. The Fifth Circuit's consideration suggests more courts will continue to ponder the jurisdictional implications of Stern in all areas touched by Article III.

The war of attrition between Anna Nicole Smith and E. Pierce Marshall has ended, as have their lives. But, the long term implications of *Stern v. Marshall* are just beginning.

BAPCA, 910 Vehicles, and a Debtor's Options

Since the enactment of the Bankruptcy Abuse Prevention and Consumer Act (BAPCA) in 2005, debtors have been forced to choose among surrendering automobile collateral, redeeming automobile collateral, or reaffirming the automobile secured debt within 45 days of the first date set for the first meeting of creditors. If the debtor fails to act, the automatic stay terminates and the property is no longer property of the estate. Automobile secured creditors can then proceed to exercise their rights under state law.

BAPCA brought many beneficial changes to automobile creditors' rights by removing most ride-through and lien stripping provisions. Significantly, BAPCA eliminated cram-down of automobile secured creditors' liens to the fair market value of vehicles purchased within 910 days of the bankruptcy filing.

Imaginative debtors, however, sought to erase any remaining debt on such vehicles. At first, the majority of courts held that

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surrendering any "910 vehicle" in this way would result in the full satisfaction of the debt, regardless of whether the car was worth less than the total amount of the debt. A minority of courts allowed creditors to pursue any remaining debt on a 910 vehicle if its value did not satisfy the entire debt.

By 2009, however, the majority view had been rejected by every circuit court of appeals that had examined the question, including the Fourth, Fifth, Seventh, Eight, Tenth, and Eleventh Circuits. All these circuit courts held that even if a debtor surrenders a 910 vehicle, a creditor has the right to pursue the remainder of the debt so long as the vehicle fails to fully satisfy the remaining debt. (e.g. *In re Miller,* 570 F.3d 633 (5th Cir. 2009)).

Starter Interrupt Devices

Once a debtor files for bankruptcy, the protection of the automatic stay prohibits the creditor from exercising control over the property of the estate. Any violations of the automatic stay are punishable by sanctions for contempt, which can include actual damages and attorney's fees.

A starter interrupt device prevents a debtor from starting his or her car for missing a scheduled payment. In bankruptcy, this violates the automatic stay because it exerts control over the debtor's and the estate's property. In *Hampton v. Yam's Choice Plus Autos, Inc.,*[2] the court held it was not the existence of the device on the car that violated the stay but instead the inaction of the creditor to nullify the device and make sure the debtor had use of the car during bankruptcy. The debtor had to call in each month to make a payment and receive the starting code, but the codes frequently failed to work and the dealer did not resolve the problem. Since *Hampton,*[3] courts have required dealers to prevent starter interrupt devices from disabling a bankruptcy debtor's vehicle.

In re Garner[4] heightened the stakes. "Intentionally" is always a bad word when the bankruptcy court applies it to a creditor. The bankruptcy court held that by refusing to promptly remove the starter interrupt device upon Garner's post-petition request, the dealer had intentionally: (1) exercised control over estate property because the dealer became the only source for the codes for the continuous use of the vehicle and (2) engaged in actions to collect a pre petition debt by requiring Garner to request a code every two weeks.

The Chapter 13 Trustee was making payments on the vehicle through the Chapter 13 plan. In bankruptcy, the only purpose of the starter interrupt device was to pressure Garner to remit payments on his pre petition debt. These intentional violations of the automatic stay entitled Garner to actual damages and attorney's fees. They also opened the dealer up to additional contempt sanctions.

Once you know the debtor has filed bankruptcy, it is prudent to give all the codes necessary to start the vehicle or disable the device. The better course is to disable the device. Any failure of the codes to operate will be at the creditor's peril.[5]

In the words of Bugs Bunny, "That's all, folks!" ■

Footnotes

[1] *Technical Automation Servs. Corp. v. Liberty Surplus Ins. Corp.,* 673 F.3d 399 (5th Cir. 2012).

[2] 319 B.R. 163 (Bankr. E.D. Ark. 2005).

[3] Id.

[4] 2010 WL 890406 (Bankr. M.D.N.C. 2010).

[5] *See also In re Peterkin,* 2009 WL 1076816, (Bankr. E.D.N.C.2009).

Larry Young is a partner in HughesWattersAskanase, Houston, Texas (email: lyoung@hwa.com; Tel: 713-328-2805). He is the First Vice President of NADC. He wrote part of the Bankruptcy Code and was involved in two U.S. Supreme Court cases challenging the constitutionality of the Bankruptcy Court and certain provisions of the Bankruptcy Code. Larry is a Fellow of both the American College of Consumer Financial Services Lawyers and the American College of Commercial Finance Lawyers. He is the Texas State Editor for ***CarLaw.***

President's Message

Patricia E.M. Covington
Hudson Cook, LLP
NADC President

I'm pleased to report that our eighth annual conference was yet another successful event! Sunny Scottsdale, Arizona, was the venue for our meetings and festivities. We had great member turnout with 140 members in attendance. Many came out early to do some golfing or to enjoy the hotel's resort offerings.

Our opening cocktail reception was the usual hit, during which members enjoyed food and drink and each other's company (*well past the close of the reception hour*). The next morning, the conference opened with a short annual meeting during which **Eric Chase**, **Johnnie Brown**, **Jeff Ingram** and **Stuart Rosenthal** were re-elected to second terms on the board of directors. Then, we were off to the races to listen to and participate in excellent programs.

For those who weren't able to join us in sunny Scottsdale, the following is a brief recap:

Eric Chase, of Bressler, Amery & Ross, P.C., and **Rob Cohen**, of Auto Advisory Services, Inc. and Arent Fox LLP, were our lead-off hitters, presenting on Eric's "2012 Top Twenty Legal Trends & Issues." Eric had 2 issues tied for number one: (#1) Dealer Rights vs. Franchisors' Initiatives, *along with* (#1) Economic and Regulatory Trends and Domestic Political Uncertainty.

The next presentation was the In-House Counsel Panel moderated by **Diane Cafritz**, of CarMax, Inc., **Kelly Baker**, of Asbury Automotive Group, Inc., **Rita Campanile**, of DCH Auto Group, **Harold Oehler**, of Lazy Days R.V. Center, Inc. and Diane shared their thoughts on the do's and don'ts for outside counsel. We learned what in-house counsel looks for when retaining outside counsel, which of our marketing efforts do and don't work, and mistakes that can damage outside counsel's relationship with in-house lawyers.

Len Bellavia, of Bellavia Gentile & Associates, LLP, **Chris DeVito**, of Morganstern, MacAdams & DeVito Co., L.P.A., and **Scott Silverman**, of Silverman Advisors, PC, then jumped right into one of the most timely topics of the year – manufacturer facility image upgrade programs. They discussed the factory's "carrot" and "stick" approaches, and shared strategies for countering manufacturer demands.

After lunch, we had another timely program – social media and the law. **Christopher Hoffman**, of Fisher & Phillips LLP, **Jami Jackson** of Farris, Parker Poe Adams & Bernstein LLP, and **James Hess**, of CarMax, Inc., discussed the use of social media in marketing, employee's use of social media *(the good and the bad)* and current litigation on this topic.

Day one ended with a discussion of the 2011 FTC's Dealer Roundtables. **Paul Metrey**, of NADA, moderated a panel of the following NADC members who were participants of the Roundtables: **Andy Koblenz** of NADA, **Tom Hudson** of Hudson Cook LLP, **Terry O'Loughlin** of Reynolds & Reynolds and

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Janet Buchanan
Automotive Management Services, Inc., *West Palm Beach, FL*

Mark S. Mulholland
Ruskin Moscou Faltischek, P.C., *Uniondale, NY*

Shawn Mercer of Bass Sox Mercer. Prior to the close of this session, each panelist shared his or her compliance recommendations.

Then we were off to visit and network at the evening cocktail!

Bright and early (7:45) after a hearty breakfast, day two started with **Erin Kerrigan**, of The Presidio Group, LLC, describing today's dealership M&A market. **Joe Aboyoun**, of Aboyoun & Heller LLC, followed with a discussion of the common problem he sees in M&A transactions.

NADA General Counsel **Andy Koblenz** has become a regular at NADC meetings, and for good reason. Andy's NADA update, delivered in his rapid-fire style, was filled with "insider baseball" stories of the goings-on in Washington.

Jeffrey Halbert, of Stewart & Irwin, P.C., and Christian Scali, of Arent Fox *(pinch hitting for Aaron Jacoby)* gave a rundown on current litigation in labor and employment, along with class action developments.

"Car Sales in the Cloud" was next with **Nicole Munro**, of Hudson Cook, LLP, and **Alan Wingfield**, of Troutman Sanders LLP. Nikki and Alan talked about the issues dealers must navigate through when engaging in transactions via the Internet.

Last at bat, but certainly not least, were, **Patrick L. Anderson** and **Lauren Branneman**, both of the Anderson Economic Group. They covered how dealership market territories get redrawn and why it matters.

The Annual Conference Planning Committee did a stellar job in selecting topics and recruiting skilled speakers with great depth on the issues. We can thank **Bruce Anderson**, **Diane Cafritz**, **Eric Chase**, **Patty Covington** *(oh, that's me)*, **Paul Metrey**, **Ken Rosenfield**, **Michael P. Shanahan** and **Oren Tasini** for their great work!

We had great participation from our Associate Members. Many had displays where members could get information about their products and services. Additionally, many Associate Members went the extra mile and sponsored conference events. **Portfolio General Management Group Inc.** sponsored the opening reception, while the **Anderson Economic Group** treated us to the second evening's cocktail. **The Fontana Group** and **CounselorLibrary** nourished us each morning by sponsoring our breakfasts. To make sure we kept bright eyed and bushy tailed, **Dixon Hughes Goodman** sponsored the snacks and drinks during breaks. We were again able to give attendees conference materials on flash drives, thanks to the sponsorship of **Rosenfield & Company**. And to make sure we could recall each others' names, **Cars Capital Automotive** sponsored the lanyards for our name badges.

If the on-site feedback we received is an accurate guide, our eighth annual meeting continued our tradition of great substantive programs, good networking and a lot of worthwhile visiting. If you missed this year's annual meeting, you shouldn't miss next year's.

While we're still selecting the dates and location for the 2013 Annual Conference, we do have them for this year's fall meeting. Our 2012 NADC Fall Conference will be held October 7th and 8th at the Trump International Hotel & Tower in Chicago, Illinois. We are planning a one-day program that will give you innovative ideas and valuable insight to meet the challenges of our constantly changing industry.

That's my Scottsdale report. If you weren't there, you missed a good one. Our founder, Jonathan Harvey, wasn't able to make this meeting, but I have to believe that it measured up to the vision Jonathan had for our organization years ago.

Plan to join us in the fall – I'll see you in Chicago. ■

Announcing the NADC Top Contributor Award Winner!

Russell McRory of *Robinson Brog Leinwand Greene Genovese & Gluck, P.C.* in New York, NY is the winner of the NADC Top Contributor Award.

We would like to thank Russell for his contributions to the organization over the past year!

Could Your Clients Pass an Audit?

Feature Article

By Jeffrey Ingram
Galese & Ingram, P.C.

The Consumer Financial Protection Bureau is quickly moving to investigate and regulate the industries under its jurisdiction. Its initial actions show that we should expect it to aggressively assert its authority. Why should we care? After all, new car dealers are exempt from its jurisdiction, right? At least three reasons come to mind: 1) Even if dealers are exempt, their financing sources are not. Regulations on those entities could easily be a back door into our clients' businesses. For example, a financing source might be prohibited from purchasing a contract from a business that does not meet certain requirements; 2) Many of our clients have separate used car or buy-here/pay-here dealerships that may be subject to the CFPB; 3) Finally, even if not regulated by the CFPB, our clients have to comply with many of the laws that the CFPB will enforce on other entities. How the CFPB does that could affect how those laws are applied and interpreted. For example, the CFPB is already filing amicus briefs in existing cases and will be bringing its own enforcement actions that could result in new interpretations of the law. In addition, the FTC, which does have jurisdiction to enforce laws applicable to car dealers, has begun a more aggressive enforcement course itself.

The CFPB published in October 2011 a Supervision and Examination Manual. That manual can be found at http://www.consumerfinance.gov/guidance/supervision/manual/. It provides important clues as to how we should expect the CFPB and potentially even the FTC to act. Additionally, it also provides a valuable tool that we can use in training our clients to comply with existing law.

The Guidelines make clear that business must "maintain effective systems and controls to manage their compliance responsibilities." Businesses must have the ability to "detect, prevent and correct practices that present a significant risk of violating the law and causing consumer harm."

Often times our clients want to know what forms to use to comply with the law. They get those forms from us or others. They give direction to their employees to use those forms and then all to often forget about their on-going responsibilities confident that they have complied with the law. How many of your clients implemented policies to comply with the red flags rule but then failed to monitor their employees' compliance with their rules or failed to update their rules on a periodic basis? No longer can that be accepted.

According to the Guidelines, our clients must have an effective Compliance Management System. That System is how a business actually insures that it complies with its legal responsibilities. It must have "four interdependent control components" consisting of 1) Board and management oversight; 2) A compliance program; 3) Responding to consumer complaints; and 4) A compliance audit. The Board must demonstrate clear compliance expectations to its employees and outside service providers. It must have clear policy statements regarding compliance. It must appoint an "appropriately qualified chief compliance officer with authority and accountability." It must allocate resources to compliance, address compliance issues and risks to consumers throughout its business and, finally, periodically audit its compliance matters.

The Compliance System must involve appropriate policies, training in those policies and ongoing monitoring and corrective action relating to those policies. The System must be a formal, written program. Can your clients show that they have audited their performance under their compliance programs? Can they show changes that they have made in their policies in response to their audits? Have they revised outdated content? If not, their Compliance Program is probably a dead program and an invitation to trouble.

The Training Program must provide training that is "current, complete, directed to appropriate individuals based on their roles, effective, and commensurate with the size of the entity and nature and risks to consumers." The training must be consistent with the business' written policies. The business must also be sure that its compliance personnel receive appropriate training to administer the business' compliance program. Our clients should therefore conduct training sessions and document that training including the content of the training. They should also document their plans for changes to the training over the next year. The actual training should match up to the plan.

Consumer complaints must also be treated appropriately. They should be "appropriately recorded and categorized." They should be "addressed and resolved promptly." If the complaints "raise legal issues involving potential consumer harm from unfair treatment or discrimination, or other regulatory compliance issues" they should be "appropriately escalated." These complaints should result in corrective action if necessary and adjustments to the business' policies. How many of your clients have written plans to accomplish any of this?

Our clients should have compliance audits and expect those audits to be reviewed. Is someone actually reviewing deal files to insure compliance with the applicable laws? Is someone reviewing the actions of third-parties who perform services for the business? When problems are found, are they corrected? Are policies adjusted to prevent problems from arising in the future?

How should we act in helping our clients? The Guidelines require the CFPB examination personnel "go onsite to observe, conduct interviews, and review additional documents and information." The examination personnel should interview senior managers, account personnel and compliance officers as well as observe how actual operations compare to the business' stated policies. Why should we do less? If we had to for our clients, could we justify doing less? To advise our clients properly, should we not be taking the same steps that the regulators may take?

The Guidelines also contain separate sections relating to specific legal issues. As just one example, there is a section on "unfair, deceptive, or abusive acts or practices." Such acts must: 1) be likely to cause substantial injury to consumers; 2) the injury must not be reasonably avoidable by consumers; and, 3) the injury to the consumer must not be outweighed to benefits to the consumers or competition. Even a small amount of monetary harm can be a substantial injury if the harm is to a large number of people. A significant risk of harm is all that is required. Actual harm may not be necessary. Although emotional harm is normally not sufficient, in some circumstances, such as unreasonable debt collection, it may be.

An act can be deceptive even if no one is misled. Instead, the act must only be "likely" to mislead a consumer when the consumer's interpretation of the representation is reasonable. The deceptive act must also be material. The act can be express or implied. Even written disclosures can be insufficient to correct such an act and subsequent truthful disclosures may not correct a deceptive act although exaggerated claims are considered puffery and are not deceptive "if the claims would not be taken seriously by a reasonable consumer."

A specific example of an unfair and deceptive practice listed in the Guidelines involves an action brought by the FTC against vehicle leasing companies who advertised the lease of a vehicle for "$0 down." The "blur" of "unreadable fine print" that appeared at the end of the commercial advertising these leases disclosed costs of at least $1,000. The FTC required these companies who advertised with "no money down" or "$0 down" must make an equally prominent disclosure of the total fees due at lease signing.

Are your clients scared? If not, they likely should be. Now, probably more than ever, we need to advise our clients of their legal responsibilities and provide to them ways that they can comply with those responsibilities. A review of the CFPB's Supervision and Examination Manual can be a good place to start. ■

Jeffrey Ingram is a shareholder in the firm of Galese & Ingram, P.C. in Birmingham, AL.

SAVE THE DATE for the

2012 NADC Fall Conference October 7-8, 2012

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The room block deadline for hotel reservations is September 17, 2012.
Space is limited so make your reservation today!

If you have any issues reserving your room please contact Erin Murphy at: emurphy@dealercounsel.com for assistance.

Topic Suggestions
Are there specific topics you would like to see covered at the NADC Fall Conference?
If so, please email Erin Murphy with your suggestions.

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