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2009 Volume I No. 28

Repossession Does Not Alter Debtor's Rights in Collateral

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INTRODUCTION

Does section 541(a)(1) of title 11 of the U.S. Code, which defines a debtor's bankruptcy "estate," include collateral which has been lawfully repossessed by secured creditors pursuant to Article 9 of the Uniform Commercial Code ("UCC") prior to the debtor's filing for bankruptcy? The courts have split in answering this pro-debtor issue by defining "estate" differently. Recently, in *Tidewater Fin. Co. v. Curry* (*In re* Curry), 509 F.3d 735, 735 (6th Cir. 2007), the Sixth Circuit Court of Appeals split with the Fourth and Eleventh Circuits and held that a secured creditor's repossession of collateral under the state's UCC prior to filing for bankruptcy does not alter the debtor's property rights or remove the collateral from the estate. The effect of this ruling is that a debtor may regain possession of his collateral by paying its value to the creditor, even if his redemption rights under state law requires payment in full of the secured obligation.

This article concludes that *Curry* was correctly decided because when resolving an issue that involves secured creditors, states should look to Article 9 of the UCC—the substantive law governing secured transactions—rather than state laws regarding redemption. Moreover, the Fourth and Eleventh circuits were wrong to not rely on the UCC, which would have led to the conclusion that the collateral does in fact remain in the estate. Part I of this essay will highlight the relevant statutes pertaining to this issue. Part II will discuss the *Curry* decision and elaborate on the positive case law it relied on to rule in favor of the debtor. Part III will discuss cases from

Cite as: *Repossession Does Not Alter Debtor's Rights in Collateral*, 1 ST. JOHN'S BANKR. RESEARCH LIBR. NO. 28, at 1 (2009), http://www.stjohns.edu/academics/graduate/law/journals/abi/sjbrl_main/volume/v1/Park.stj (follow "View Full PDF").

the Fourth and Eleventh cases that have ruled against the debtor. Part IV will analyze the Fourth and Eleventh cases' reasoning and argue that the Sixth Circuit correctly resolved this issue.

I. RELEVANT STATUTES

Pursuant to section 541(a)(1) of title 11 of the U.S. Code, an "estate is comprised of all the following property, wherever located and by whomever held … [including] … all legal or equitable interests of the debtor in property as of the commencement of the case." In turn, section 542(a) provides: "an entity … in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease … shall deliver to the trustee … such property … unless such property is of inconsequential value or benefit to the estate." A creditor who does not comply with turnover is subject to violation of automatic stay under section 362.

Pursuant to sections 9-609 and 9-610 of the UCC, secured creditors have the right after a debtor's default to "take possession of the collateral" or "sell … or otherwise dispose … the collateral." In turn, section 9-623 gives debtors the right to "redeem collateral" upon "fulfillment of all obligations secured by the collateral." Section 9-109(a)(1) states that Article 9 of the UCC applies to "a transaction, regardless of its form, that creates a security interest in personal property … by contract." Every state has adopted the UCC, with some modifications.

II. OVERVIEW OF *IN RE* CURRY

The issue in *Curry* was whether a debtor whose car has already been repossessed holds title to the car—thereby making it property of the estate under 11 U.S.C. § 541(a)(1) and subject to turnover under 11 U.S.C. § 542(a)—or merely an option to redeem it. The Bankruptcy Appellate Panel in the opinion adopted by the Sixth Circuit looked for guidance to *United States*

v. Whiting Pools, Inc., 462 U.S. 198 (1983), and answered that the debtor does hold title to a repossessed car. *In re* Curry, 509 F.3d at 735. Also, it relied on other Sixth Circuit cases, *TransSouth Fin. Corp. v. Sharon* (*In re* Sharon), 234 B.R. 676, 680 (6th Cir. 1999); *Nat'l City Bank v. Elliott* (*In re* Elliot), 214 B.R. 148, 150 (6th Cir. 1997), and an Eleventh Circuit case, *Motors Acceptance Corp. v. Rozier* (*In re* Rozier), 376 F.3d 1323, 1324 (11th Cir. 2004), that also relied on *Whiting Pools* for guidance.

A. FACTS AND RULING OF *IN RE* CURRY

In *In re* Curry, *In re* Curry, 347 B.R. 596, 598 (6th Cir. 2006), Laquita Curry, a consumer-debtor, purchased a car in Ohio and granted a security interest in the car to Tidewater Finance Company ("Tidewater"). When she defaulted on her monthly payments, Tidewater repossessed her car, but did not sell it. *Id.* A few weeks following the repossession, Curry filed for Chapter 13 bankruptcy and demanded that Tidewater return her car. *Id.* Tidewater refused, claiming that because it had lawfully repossessed her car prepetition under Ohio's UCC, Ms. Curry merely had a right to redeem rather than to possess it. *Id.* at 599–600. The Sixth Circuit Court rejected Tidewater's argument; it held that a bankruptcy "estate" includes property repossessed prepetition and therefore allowed Curry to keep the car while making monthly payments to Tidewater. *Id.* at 606–07.

B. POSITIVE CASE LAW 1: WHITING POOLS

Whiting Pools stands for the proposition that the definition of bankruptcy "estate" under 11 U.S.C. § 541(a) is broad and therefore includes collateral that has been repossessed by creditors prior to the bankruptcy filing. *Whiting Pools*, 462 U.S. at 209. In *Whiting Pools*, a corporation-debtor ("Whiting Pools") withheld approximately $92,000 in taxes from its employees. *Id.* at 199–200. It did not pay these taxes to the Internal Revenue Services ("IRS")

and did not respond to IRS's demands for payment. *Id.* The IRS seized Whiting Pools' equipment, vehicles, inventory, and office supplies pursuant to the Internal Revenue Code's levy and seizure provisions, but did not sell them. *Id.* at 200. A day after the seizure, Whiting Pools filed for Chapter 11 bankruptcy and demanded that IRS return its collateral. *Id.* The IRS sought to lift the automatic stay so that it could proceed with the tax sale. *Id.* at 200–201. The Court held that a business-debtor need not possess property prior to filing for bankruptcy to include it in its estate. *Id.* at 203. It reasoned that narrowly construing section 542(a) to include in the estate only the property which the debtor possessed prior to filing for bankruptcy would frustrate the legislature's intent "to facilitate the rehabilitation of the debtor's business"; in fact, allowing the debtor to continue his business was more financially beneficial for both parties than selling his collateral "for scrap." *Id.* Moreover, the Court reasoned that the IRS had more than enough adequate protection, including additional privileges specific to tax collector-creditors. *Id.* at 209. By stating that the "right to adequate protection … replace[s] the protection afforded by possession," *Id.* at 207, the Court viewed turnover as simply complying with bankruptcy procedures rather than a deprivation of IRS's right to get paid; in other words, there were methods other than possession to adequately protect its interest. *Id.* at 212.

C. POSITIVE CASE LAW 2: *IN RE* SHARON

In *TransSouth Fin. Corp. v. Sharon* (*In re* Sharon), 234 B.R. 676, 680 (6th Cir. 1999), Rosemary Sharon, a consumer-debtor, purchased a new car in Ohio and granted a security interest in the car to TransSouth Financial Corporation ("TransSouth"). When she inadvertently defaulted on a monthly payment—her check bounced because she was in the process of changing banks—TransSouth repossessed her car pursuant to Ohio's UCC, even though it previously assured her that it would not, so long as it received a new check. TransSouth did not sell the car.

Id. Ten days after the repossession, Ms. Sharon filed for Chapter 13 bankruptcy and repeatedly demanded that TransSouth return her car. *Id.* TransSouth refused, claiming that it lacked adequate protection, because the car was "too expensive." *Id.* at 680, 685. The court held that a repossessed car not yet sold prepetition is part of the debtor's "bundle of rights" and thus gets included in the estate. *Id.* at 682. It reasoned that the word "debtor" in section 542(a) gets replaced by "trustee," hence, all powers of a trustee become that of the debtor, including the power to possess any usable property that had been previously repossessed. *Id.* at 687. Notably, the dissent argued that the car, having only two seats, was not usable in *this* case because Ms. Sharon had two children and was pregnant with a third child; also, the new-model, luxury car cost more than her monthly rent. *Id.* at 690. Nonetheless, the majority opinion found that TransSouth violated the automatic stay by not returning the car even after Ms. Sharon's numerous requests, and affirmed the bankruptcy court's order to pay over $2,000 in attorney fees to Ms. Sharon. *Id.* at 681, 688.

D. POSITIVE CASE LAW 3: *IN RE* ELLIOT

In *Nat'l City Bank v. Elliott* (*In re* Elliot), 214 B.R. 148, 150 (6th Cir. 1997), Donald and Hazel Elliot, the consumer-debtors, purchased a car in Ohio and granted a security interest in the car to National City Bank ("National City"). When they defaulted on their monthly payments, National City repossessed their car and scheduled a date to sell it at a public auction. *Id*. Before the sale date arrived, the Elliots filed for Chapter 13 bankruptcy. *Id.* Subsequently, National City canceled the public sale, but claimed that the vehicle was not property of the bankruptcy estate. *Id*. The court held that a repossessed car, or any other usable property that is of some value to the estate, remains property of the estate if not sold prepetition and that "absolute title ownership" transfers to the secured creditor only after it has been lawfully sold. *Id.* at 152–53.

It reasoned that just because a secured creditor gains a right of redemption pursuant to Ohio's UCC does not mean that the debtor automatically loses his equitable interest in the vehicle. *Id.* at 151–52.

E. POSITIVE CASE LAW 4: *IN RE* ROZIER

In *Motors Acceptance Corp. v. Rozier* (*In re* Rozier), 376 F.3d 1323, 1324 (11th Cir. 2004), Derryl Franklin Rozier, a consumer-debtor, purchased a car in Georgia and granted a security interest in Motors Acceptance Company ("Motors Acceptance"). When he defaulted on his monthly payments, Motors Acceptance repossessed his car, but did not sell it. *Id.* at 1324. Shortly after, Mr. Rozier filed for Chapter 13 bankruptcy and demanded return of his car. *Id.* Motors Acceptance refused, claiming that it had lawfully repossessed it pursuant to Georgia's UCC. *Id.* The court held that ownership of a car repossessed prepetition remains with the debtor and, unless the creditor had lawfully sold it, it comes into the estate. *Id.* Additionally, the court found that Motors Acceptance violated automatic stay for refusing to comply with Mr. Rozier's demand to return his car. *Id.*

III. NEGATIVE CASE LAW FROM FOURTH AND ELEVENTH CIRCUITS

The *Curry* court distinguished cases cited by the creditor for the proposition that it owned the debtor's car because it repossessed it before she filed for bankruptcy. Those include two Eleventh Circuit cases, *Charles R. Hall Motors, Inc. v. Lewis* (*In re* Lewis), 137 F.3d 1280, 1281 (11th Cir. 1998); *Bell-Tel Fed. Credit Union v. Kalter* (*In re* Kalter), 292 F.3d 1350, 1351–52 (11th Cir. 2002), and a Fourth Circuit case, *Tidewater Fin. Co. v. Moffett* (*In re* Moffett), 356 F.3d 518, 520 (4th Cir. 2004).

A. NEGATIVE CASE LAW 1: *IN RE* LEWIS

In *Charles R. Hall Motors, Inc. v. Lewis* (*In re* Lewis), 137 F.3d at 1281, Elgin Lewis, a consumer-debtor, purchased a used car in Alabama and granted a security interest in the car to Charles R. Hall Motors ("Hall Motors"). When he defaulted on his monthly payments, he filed for Chapter 13 bankruptcy, which was dismissed. *Id.* After receiving notice of the dismissal, Hall Motors repossessed the car, but did not sell it. *Id.* Subsequently, Lewis re-filed for Chapter 13 bankruptcy and demanded that Hall Motors return his car, in exchange for paying 62 cents on the dollar for the outstanding balance. *Id.* at 1281–82. Hall Motors refused, claiming that under Alabama's common law of conversion, Lewis neither had title nor possession to a repossessed vehicle. *Id.* at 1282. The court accepted Hall Motors' argument, holding that a debtor does not have "title, possession or any other functionally equivalent ownership interest" in a car repossessed prepetition. *Id.* at 1284. It reasoned that under common law conversion principles, ownership automatically transfers to a party who has possession; thus, the debtor's right of redemption must be accompanied by some affirmative acts to change it into a "meaningful ownership interest." *Id.* The court did not believe that Lewis's paying 62 cents on the dollar was an affirmative act of redemption. *Id.* at 1285.

B. NEGATIVE CASE LAW 2: *IN RE* KALTER

In *Bell-Tel Fed. Credit Union v. Kalter* (*In re* Kalter), 292 F.3d 1350, 1351–52 (11th Cir. 2002), the consumer-debtors, Thomas Joh and Debra Marie Kalter and Matthew J. Chiodo, each purchased a car in Florida and granted a security interest to Bell-Tel Federal Credit Union ("Bell-Tel") and Tidewater Finance Company ("Tidewater"), respectively. When the Kalters defaulted on their monthly payments, Bell-Tel repossessed their car but did not sell it. *Id.* at 1351. A day after the repossession, the Kalters filed for Chapter 13 bankruptcy and demanded

return of their car, but Bell-Tel refused. *Id.* Similarly, Chiodo defaulted on the monthly payments of his used car. *Id.* Tidwater repossessed the car, but notified Chiodo of its intent to sell the car at a private sale. *Id.* Before the sale took place, Chiodo filed for Chapter 13 bankruptcy and demanded that Tidewater return his car. *Id.* Tidwater returned the car only after entering into an agreement with Chiodo that its interest would be adequately protected. *Id.* The court followed *Lewis*, holding that a debtor's right in repossessed car is a bare right of redemption rather than title. *Id.* at 1356. As in *Lewis*, the court did not look to the state's UCC, stating that "the statute is notably silent on the issue of ownership, proving this Court with no guidance as to who owned the Debtors' vehicles upon repossession." *Id.* at 1354. Therefore, it relied on the Florida Certificate of Title statute, which specifically deals with repossessed cars. *Id.* at 1356. The court reasoned that a creditor who has repossessed a car automatically owns it, because this statute assumes that title passes to the possessing party unless another party takes affirmative steps to block the automatic transfer of ownership. *Id.* at 1358. Like *Lewis*, the court in *Kalter* acknowledged that the right of redemption in and of itself is not enough to pull the actual car into the estate unless a debtor does something more affirmative to regain title. *Id.*

C. NEGATIVE CASE LAW 3: *IN RE* MOFFETT

In *Tidewater Fin. Co. v. Moffett* (*In re* Moffett), 356 F.3d 518, 520 (4th Cir. 2004), Moffett purchased a used car in Virginia and granted a security interest in the car to Tidewater Finance Company ("Tidewater"). When she defaulted on her monthly payments, Tidewater repossessed her car, but did not sell it. *Id.* On the same day as the repossession, Moffett filed for Chapter 13 bankruptcy and demanded that Tidewater return her car. *Id.* Tidewater returned the car (after its motion for relief was denied), but argued that because Moffett had no title as a result of its repossession, it should be allowed to sell it. *Id.* The court held that a debtor's right of

redemption is sufficient to pull a repossessed car into the estate. *Id.* at 522. However, it did not answer the question of whether the debtor holds title to the repossessed car. *Id.* at 523. It reasoned that addressing this issue was unnecessary because the debtor was able to redeem her only method of transportation to her job that was located 40 miles away, while the creditor was able to receive adequate protection under the reorganization plan that required Ms. Moffett to pay the full amount due under the original sales contract. *Id.* at 524.

IV. WHY NEGATIVE CASE LAW WERE WRONGLY DECIDED

Lewis, *Kalter*, and *Moffett* were wrongly decided because they did not rely on the state's enactment of Article 9 of the UCC, which is the substantive law governing secured creditors' rights. *See* U.C.C. § 9-109(a)(1). Had the UCC applied, the repossessed cars in these cases would have come into the estate. In *Lewis*, the court avoided the UCC, claiming that Alabama traditionally relied on common law principles of conversion, notwithstanding the fact that the state's UCC specifically dealt with security interest in personal property. 137 F.3d at 1283. It even acknowledged that Alabama's redemption statute is similar to that of Ohio's UCC in *Elliot*, *Id.* at 1285, but it merely dismissed the UCC, contending that if the legislature had intended to rely solely on the UCC, it would have changed the law a long time ago. *Id.* at 1284. Moreover, the court in *Kalter* avoided the UCC, claiming that another statute was more on point where vehicles were involved, specifically, the Florida Certificate of Title statute, which provides that a party who has repossessed a vehicle must obtain a certificate of title from the Department of Highway Safety and Motor Vehicles. 292 F.3d at 1356. However, it also went on to say that Florida courts have held that a certificate of title is not even necessary for ownership. *Id.* at 1358. Under this circular reasoning, the Florida Certificate of Title statute would not even be

persuasive authority. Furthermore, the court in *Moffett* avoided the UCC by choosing not to answer the issue of ownership of repossessed cars at all without fully explaining why it would not do so. 356 F.3d at 524. *Curry* distinguished *Moffett* by reasoning that it was not authority for the case at bar because it did not actually address the issue of ownership. 347 B.R. at 606.

CONCLUSION

In re Curry is an important case because it illuminates the current split among courts regarding the issue of whether a debtor whose car has already been repossessed holds title to the car or merely an option to redeem it. The Sixth Circuit tracks *United States v. Whiting Pools* and holds that because the debtor still has title to the car, she can seek turnover of the car and modify the secured debt in accordance with the Bankruptcy Code. The conflicting view that was adopted by the Eleventh Circuit holds that the debtor merely has a right of redemption, and can recover the car only by paying the entire secured debt. So when a debtor-client asks, "Can I get my car back?" the answer should be, "That depends on where you live."

Additionally, it is important to note that some states distinguish use of a car from title. *See* Posting of Grant F. Shipley to http://dizzy.abiworld.org/read/?forum=abi_ucc (Feb. 3, 2009, 09:32:00 EST). For example, under Indiana law, purchasing a car (and getting a certificate of title) merely gives the consumer a right to register the vehicle and drive it on public roads, not ownership. *See Madrid v. Bloomington Auto Co., Inc.*, 782 N.E.2d 386, 391 (Ind. 2003). Under such circumstances, it would be difficult to predict how the court will answer the issue of ownership.

Also, even if the repossessed car can be dealt with bankruptcy, meaning it comes into the bankruptcy estate, there is another issue to deal with, which is whether the car is subject to

turnover or cram down. *In re Curry* allowed the debtor a cram down (confirmation of a bankruptcy plan over a creditor's objection), *see* 347 B.R. 596 at 599, n.1., so she was allowed to keep her car while paying Tidewater a present value of the car, which was substantially lower than the contract price. 347 B.R. 596 at 599.