Handling Automobile Cases
Presented at State Bar Convention by Richard Tomlinson[1]
Consumer and Commercial Law Section Program
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If there is one theme to my presentation, it is this: consumer cases involving automobiles can be raised without utilizing the DTPA. As you will see, there are many other statutes that provide possible remedies such as the Uniform Commercial Code, the Truth-in-Lending Act, the Odometer Act and the Magnuson-Moss Warranty Act. Why should these other statutory claims be considered? First, you avoid the many procedural traps not found in the 1995 version of the DTPA. Second, many of these other statutory statutory claims provide for jurisdiction in federal court as an alternative to state court. If you are not happy with your local state courts, these other statutes give you the option of seeking out a different forum. What follows is a listing of common consumer claims involving automobiles.

A. Repossessions, Sales and Deficiencies

This is my first topic for a reason. In the past 5 years, I have noticed a change in the types of automobile cases that make it into my office. Fewer cases involving deception have appeared at my doorstop and many more repossession and deficiency cases have filled the vacuum. While I do not believe that dealers have become more honest and trustworthy, I do think that many consumers believe that going to an attorney is no longer an option in these matters, because consumers doubt that attorneys will handle such cases on a contingent basis, particularly given that many attorneys refuse to handle any cases that must be arbitrated. At any rate, given the declining economy, it appears that the rate of automobile repossession and the filing of automobile deficiency actions have both increased substantially.

1. Repossessions

To repossess an automobile, the secured creditor needs a security agreement authorizing repossession and a default. Virtually all retail installment sales contracts have security agreements, so the most common issue raised with repossessions relates to whether a default has occurred and exists at the time of repossession. Default is defined by the contract, and most retail installment contracts define default as the failure to make timely payments or the failure to maintain insurance coverage for the vehicle serving as collateral. Certainly, these are the most common examples of default used to justify repossession. What follows are several examples of default issues in repossession cases.

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a. Habitual Acceptance of Late Payments

By habitually accepting late payments, secured creditors waive the timely payment provisions of the contract unless such creditors send notice prior to repossession noting that late payments will no longer be accepted. *Ford Motor Credit Company v. Washington*, 573 S.W.2d 616, 617-618 (Tex. Civ. App. - Austin 1978, writ ref'd n.r.e.); *Cobb v. Midwest Recovery Bureau Company*, 295 N.W.2d 232, 236-237 (Minn. 1980). Secured creditors responded to these types of rulings by including non-waiver clauses in retail installment contracts that read like the following: "Acceptance of a late payment shall not operate as a waiver of any subsequent default by the debtor." In commercial cases, these non-waiver clauses effectively preclude any claim of waiver through acceptance of late payments. In consumer cases, however, the courts have generally found that such clauses can be waived as well. *Westinghouse Credit Corporation v. Shelton*, 645 F.2d 869, (10th Cir. 1981)(applying Oklahoma UCC); *Moe v. John Deere Company*, 516 N.W.2d 332, 336-338 (S.D. 1994)(applying S.D. UCC). While no Texas court has addressed the effect of non-waiver clauses in the context of the UCC, several Texas courts have found that such clauses can be waived through course of conduct in the real estate lease context. *Straus v. Kirby Court Corporation*, 909 S.W.2d 105, 107-108 (Tex. App. Houston [14th Dist.] 1995, writ denied); *Winslow v. Dillard Department Stores, Inc.*, 849 S.W.2d 862, 863-864 (Tex. App. - Texarkana 1993, writ denied); *Zwick v. Lodewijk Corporation*, 847 S.W.2d 316, 318 (Tex. App. - Texarkana 1993, no writ); *Regent International Hotels, Ltd. V. Las Colinas Hotels Corporation*, 704 S.W.2d 101, 104-105 (Tex. App. - Dallas 1985, no writ). If non-waiver clauses are subject to waiver, these clauses raise the bar for finding waiver or estoppel. In other words, courts are going to expect the acceptance of more late payments to overcome a non-waiver clause.

b. Existence of Credit Insurance

The sale of credit life, credit disability or credit unemployment insurance as a part of the retail installment contract for the sale of a vehicle is treated as an agreement to look to the relevant insurance policy in the even of the insured even, death, disability or unemployment. *Owens v. Walt Johnson Lincoln Mercury, Inc.*, 574 P.2d 642, 643-644 (Ore. 1978). Once the secured creditor is put on notice of a potential claim to be made against a credit insurance policy, the secured creditor is required to refrain from repossessing the collateral. *Id.*; *Carter v. United States National Bank*, 768 P.2d 930, 931-932 (Ore. 1989); *Wiley v. GMAC*, 624 So.2d 518, 521 (Ala. 1993); *Corbin v. Regions Bank*, 574 S.E.2d 616, 619-621 (Ga. App. 2002); *Entriken v. Motor Coach FCU*, 845 P.2d 93, 95-97 (Mont. 1992). See also *Bank One Milwaukee v. Harris*, 563 N.W.2d 543, 546 (Wis. App. 1997)(repossession of vehicle under these circumstances unconscionable). In short, if a secured creditor repossessed a vehicle after being informed that the buyer was disabled and the underlying contract provided for a purchase of credit disability insurance,

the repossession violated the implicit promise associated with the insurance purchase that the creditor would look first to the insurance to cover defaulted payments caused by disability.

c. Right to Withhold Payments to Cover Damages

Tex. Bus. & Com. Code § 2.717 provides that "[t]he buyer on notifying the seller of his intention to do so may deduct all or any part of the damages resulting from any breach of the contract from any part of the price still due under said contract." For example, after six months, title has not transferred and the buyer has been unable to obtain permanent registration, leading to several traffic tickets with substantial fines. Another example would entail a failing dealership taking a trade-in and failing to pay it off, even though current retail installment contracts provide that the seller will pay off the balance owed on the trade-in. A buyer would be free under section 2.717 to inform the seller or its assignee that the failure to transfer title or to pay off a trade-in has caused damages and that the buyer intends to apply its damages as a form of set-off or recoupment against future required payments.

d. Revocation of Acceptance

Under Tex. Bus. & Com. Code § 2.608, a buyer of an automobile may revoke acceptance when the automobile has a substantial non-conformity that substantially impairs its value to the buyer if discovery of the non-conformity was difficult, notice is given within a reasonable time, and the condition of the vehicle has not substantially changed. Under Tex. Bus. & Com. Code § 2.711, a consumer who justifiably revokes is entitled to cancel the transaction and to recover all payments made. In short, revocation is the UCC version of rescission. If a consumer revoked acceptance before a repossession occurred, it could be argued that there is no default to justify repossession. In addition, it could be argued that the revoking consumer has a security interest superior to the finance company assignee, because section 2.711(c) provides a justifiably revoking buyer "has a security interest in goods in his possession or control for any payments made on their price and any expenses reasonably incurred in their inspection, receipt, transportation, care and custody . . . ." In effect, such revoking buyers are entitled to hold the vehicle after revocation until the purchase price at least has been refunded. *Vista Chevrolet, Inc. v. Lewis*, 704 S.W.2d 363, 369 (Tex. App. - Corpus Christi 1985)(". . . after revocation of acceptance, the buyer has a security interest in the goods and may retain possession of the goods to secure repayment of any payments that may have been made by the buyer"), *aff'd in part and rev'd in part on other grounds*, 709 S.W.2d 176 (Tex. 1986).

Practice Pointer: I would not raise breach of express warranty made by the manufacturer as an impediment to repossession, relying upon the right to withhold

payments or revocation of acceptance. To raise one of these impediments to repossession, you need to show that the dealer-seller breached the contract. Breach of an express or implied warranty is hard to pin on a new-car dealer in Texas, because these dealers disclaim all warranties, express and implied, asserting that the buyer's warranty rights are limited to the express warranty afforded by the manufacturer. Dealers do retain certain duties that cannot ordinarily be disclaimed, such as the duty to transfer good title and to pay off trade-ins. To the extent the dealer affords an express warranty that has been breached, then the buyer may assert the right to withhold payments and revocation of acceptance to preclude a finding of default sufficient to justify repossession.

2. Sales Following Repossession

Secured creditors repossess vehicles to dispose of them in hopes pf paying off all or part of the balance owed. This right to sell or otherwise dispose of the vehicle does not mean the repossessing creditor has complete discretion. First, under Tex. Bus. & Com. Code § 9.623(c)(2), the buyer has an absolute right to redeem the repossessed vehicle at any time before sale. I am handling a case now where a secured creditor received a full payment of the redemption amount and then went ahead with the sale a few days later, rendering the sale wrongful and a form of conversion. Second, every aspect of the disposition of the collateral must be commercially reasonable to pass muster under Tex. Bus. & Com. Code § 9.610. For example, an attack on the commercial reasonableness of a sale could be based the failure to recondition the collateral before sale, the failure to publicize the sale, an unreasonably long delay in selling collateral and even unreasonably low price. National Consumer Law Center, *Repossessions and Foreclosures* (5th ed.) § 10.2.1. Third, after the sale, the secured creditor is supposed to send a notice of surplus or deficiency under Tex. Bus. & Com. Code § 9.616, but the failure to give such notice only entitles the debtor to a $500 penalty under Tex. Bus. & Com. Code § 9.625(e)(5) and (6).

3. Deficiencies

Under Tex. Bus. & Com. Code § 9.626, a secured creditor may sue a debtor for any deficiency remaining after a post-repossession sale. In the not too distant past, most lenders in this field, with the exception of credit unions, avoided filing deficiency actions, apparently viewing them as a waste of effort given the prohibition on wage garnishment in Texas. Most lenders, other than credit unions, would only sue debtors for a deficiency when a suit was filed to obtain a writ of sequestration when the collateral could not be located for repossession. That has changed in the past year or so. Ford Motor Credit Company has filed a number of direct suits in the past year to recover deficiencies, and, more importantly, debt buyers have begun to buy deficiency accounts from auto lenders and bring a vast number of lawsuits to recover the deficiencies. There are a number of defenses to these actions. What follows is a less than exclusive list.

First, to recover a deficiency arising out of a consumer transaction requires the sending of proper notice of intended disposition or sale that complies with Tex. Bus. & Com. Code §§ 9.611 through 9.614. In other words, Texas recognizes an absolute bar rule in cases in which either no notice or inadequate notice has been given. Tanenbaum v. Economic Laboratory, 628 S.W.2d 769 (Tex. 1982); State Bar Committee Comment following Tex. Bus. & Com. Code § 9.626. Since sections 9.613 and 9.614 provide form letters for giving such notice that serve as safe harbor protection for the form of the letter, this is not a difficult obligation to fulfill. Nevertheless, I have found on more than one of these letters that secured creditors fail to give at least 10 days' notice of intended disposition, even though at least that amount of time is required by section 9.612. In addition, most of my clients do not recall receiving such notice of sale and debt buyers are not always able to obtain such letters from original creditors or to prove that they were actually sent.

Practice Pointer: If a defendant raises lack of notice or an absence of commercial reasonableness in the sale in his/her answer, the burden of proving the sending of notice or the conduct of the sale in a commercially reasonable manner is placed upont the secured creditor plaintiff. Tex. Bus. & Com. Code § 9.626(a)(2); Greathouse v. Charter National Bank-Southwest, 851 S.W.2d 173 (Tex. 1992). In effect, if the defendant alleges lack of notice or an absence of commercial reasonableness, the burden of proof on these issues shifts to the plaintiff secured creditor.

Second, some of these deficiency claims are time-barred. The applicable statute of limitations is provided by Tex. Bus. & Com. Code § 2.725. Under this statute, the secured creditor or its assignee has four years from the date of breach. While the right to recover each payment is subject to limitations under this statute, the entire debt is barred if more than 4 years have expired since the date of repossession, because the debt is effectively accelerated on the date of repossession.

Third, debt buyers may be unable to prove up the amount of the deficiency in one of these suits. Much like the credit card debt suits filed by debt buyers, there may be little or no paperwork to support the amount of the claim. Even if the original creditor has retained such paperwork, the debt buyer may have to pay substantial sums to obtain it.

4. Possible Remedies

Wrongful repossession, no notice of sale and inadequate notice of sale claims should be brought, because the UCC provides for minimum damages on these claims in consumer transactions equal to 10% of the cash price and the entire finance charge. Tex. Bus. & Com. Code § 9.625(c)(2). In addition, repossessing when there has been no default or when there has been a failure to give proper notice may also be a breach of contract (depending on the language in the contract), entitling the consumer debtor to

attorney fees under Tex. Civ. Prac. & Rem. Code § 38.001. *First City Bank - Farmers Branch, Texas v. Guex*, 677 S.W.2d 25, 29-30 (Tex. 1984); *All Valley Acceptance Company v. Durfey*, 800 S.W.2d 672, 676-677 (Tex. App. - Austin, writ denied).

B. Deceptive Auto Sales: Odometer Rollbacks and Undisclosed Wreck Damage

1. Background

In my experience, two of the most common deceptive trade practices in the sale of automobiles involve misrepresentations regarding the mileage of an automobile and failures to disclose prior wreck damage. These commonly are issues in the sale of used automobiles, but the failure to disclose damage to automobiles can occur with new cars as well.[2] These are significant issues as well, because increased mileage and prior wreck damage, particularly when not fully remedied, have major impacts upon the fair market value of vehicles and may also render warranties void.

On an initial review, many attorneys may believe that the only responsible party in an odometer case is the party in the chain of title that rolled back the odometer. Upon further review, however, the law often holds parties up the chain of title to be liable in such cases, sometimes including the retail finance company.

With cases involving prior wreck damage, many defense attorneys representing dealerships will assert that their clients had no actual knowledge of the prior wreck damage and should therefore not be held liable. Dealers, and even retail finance entities, can be held liable in such cases.

2. Who is responsible when an odometer has been rolled back?

Imagine the following hypothetical facts based on one of my cases: Ms. Smith, a consumer, notices an advertisement for a vehicle in the Chronicle which claims a particular vehicle has "Low K," obviously an indication of low mileage. She calls the advertising dealer and is informed orally that the exact mileage is around 40,000, and she decides to go visit the dealership as a result. At the dealership, she is shown the advertised vehicle which has a sticker affixed to one of the side windows which affirmatively states the mileage to be around 40,000. After purchasing the vehicle and an extended warranty by way of a retail installment contract that is later assigned to a bank, she begins to notice that the vehicle seems to need constant repairs. Relying on a television story about odometer fraud, she runs a Carfax search and discovers that the odometer of her vehicle may have

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[2] For example, new cars sometimes fall off their transporters when being unloaded and sometimes new cars get into wrecks before they have ever been titled.

been rolled back, because the Carfax report notes an emissions test with a recorded mileage that is much more than what has apparently been recorded in the various title transfers visible in the title history of the vehicle. After sending a demand letter to the dealer, she is contacted by an adjustor for the dealer's insurance carrier who denied her claim, asserting that the emissions station had merely made a mistake on the inputing of the mileage. Upon contacting the first consumer owner of the vehicle and the dealer which accepted the vehicle as a trade-in, however, she discovered that the vehicle had over 100,000 miles on the odometer at the time of its trade-in after about 2 ½ years of use. The title history did not reflect the true mileage, because the initial entry at the time of trade-in and later sale by the trade-in dealer had been forged, as apparently the first digit of a 6-digit odometer reading entry had been turned into a upper-case "A" and this forgery hid the true mileage in subsequent sales. The issue is who is liable for this obvious fraud.

a. The party directly responsible for the roll-back

The party which rolled back the odometer and forged the mileage reading on the title was apparently a wholesaler which had purchased the vehicle at auction after the trade-in dealer had submitted the vehicle for sale at an auction. This wholesaler was able to forge the odometer reading in the first transfer of title paragraph on the back of the original certificate of title, because the trade-in dealer and the culpable wholesaler were not obligated, as licensed dealers, to apply for a new certificate of title, and thereby record for posterity the information regarding the odometer reading during each transfer, until a retail sale was made. In short, the wholesaler had the original certificate of title in hand and was able to forge the odometer reading in an effort to hide the roll-back of the odometer performed by the wholesaler. The cheating wholesaler engaged in this course of conduct to make a better profit on the vehicle, having purchased it at the low value reflected by its high mileage and then sold it for a much higher price which was based on a purported mileage reading which was far below the actual experience of the vehicle.

The cheating wholesaler that engaged in the roll-back and the forgery of the title is clearly liable under both the Texas Deceptive Trade Practices Act and the federal Odometer Act. The DTPA explicitly prohibits "disconnecting, turning back, or resetting the odometer of any motor vehicle so as to reduce the number of miles indicated on the odometer gauge. Tex. Bus. & Com. Code § 17.46(b)(16). See, e.g., *Houston v. Mike Black Auto Sales*, 788 S.W.2d 696, 697-699 (Tex. App. - Corpus Christi 1990, no writ) where a dealer was required to go to trial on this issue based on evidence that the dealer had replaced the odometer and failed to disclose that fact in a later sale. Likewise, the Odometer Act prohibits such tampering. 19 U.S.C. § 32703(2). See, e.g., *U.S. v. Whitlow*, 979 F.2d 1008 (5th Cir. 1992), an appeal regarding the sentence given to a Houston used car wholesaler who pleaded guilty to odometer tampering and was believed to have rolled back odometers in no less than 1500 automobiles. While both the DTPA and the Odometer Act would permit a private recovery of damages and attorney's fees

against such a party, this may be a waste of time, because the parties engaged in roll-backs are often judgment-proof. That does not mean, however, that consumers injured by such roll-backs are entitled to no relief.

b. The dealer which misrepresented the mileage or failed to disclose the true mileage of the vehicle

In the example set forth above, the dealer made a number of representations about the mileage that turned out to be false. First, the advertisement stated that the mileage on the vehicle was low when it was over 100,000 miles. Second, the dealer representative stated orally on the telephone that the mileage was around 40,000 which is clearly false. Third, the sticker on the car disclosed an exact mileage of around 40,000 when the true mileage was over 100,000. Obviously, this vehicle was represented to be a low mileage vehicle when, in fact, it had an excessive number of miles which clearly affected the value of the vehicle. As a result, the dealer clearly violated the DTPA, Tex. Bus. & Com. Code § 17.46(b)(5) and (7), by misrepresenting the characteristics and quality of the vehicle. There are numerous Texas cases where dealers have misrepresented the mileage of a vehicle with a rolled-back odometer and have been held liable under the DTPA for the misrepresentation. *Green Tree Acceptance, Inc. v. Holmes*, 803 S.W.2d 458, 460, 462 (Tex. App. - Fort Worth 1991, writ denied); *Houston v. Mike Black Auto Sales*, 788 S.W.2d at 699; *Jones v. Star Houston, Inc.*, 1988 Tex. App. LEXIS 827 (Tex. App. - Houston [14th Dist.] 1988, no writ); *Gallery Datsun, Inc. v. Metcalf*, 630 S.W.2d 853, 854 (Tex. App. - Houston [1st Dist. 1982, no writ); *Jack Criswell Lincoln-Mercury, Inc. v. Haith*, 590 S.W.2d 616, 617-619 (Tex. Civ. App. - Houston [1st Dist.] 1979, writ ref'd n.r.e).

One defense frequently raised in such cases is that the dealer did not know that the odometer reading that it was disclosing was false, and this fact can be relevant due to the fact that the odometer disclosures on the certificate of title are made based on the seller's "best knowledge." In *Preston II Chrysler-Dodge v. Donwerth*, 744 S.W.2d 142, 144-145 (Tex. App. - Dallas 1987), *rev'd on other grounds*, 775 S.W.2d 634 (Tex. 1989), the dealer represented that the mileage on the odometer of a vehicle was the accurate mileage "to the best of its knowledge," and the failure to prove actual knowledge that the mileage on the odometer was inaccurate doomed the DTPA misrepresentation claim. On the other hand, in *Green Tree Acceptance*, 803 S.W.2d at 459-460, a similar "to the best of its knowledge" representation was made, but there was enough evidence of actual knowledge that the odometer reading was false to uphold a DTPA verdict. In our example, however, the dealer made an affirmative statement about the mileage unconditioned by any limitation based on its knowledge, which imposes a duty on the seller to know whether its statements were true. *First Title Co. of Waco v. Garrett*, 860 S.W.2d 74, 76 (Tex. 1993)("when a seller makes an affirmative representation, the law imposes a duty to know whether that statement is true"); *Robinson v. Preston Chrysler-Plymouth, Inc.*, 633 S.W.2d

500, 502 (Tex. 1982)("When a seller makes representations to the buyer, he is under a duty to know if his statements are true."). Thus, the dealer in our example should be held liable for any misrepresentation, whether made with knowledge or not.

Like the DTPA, the Odometer Act also prohibits not only mileage misrepresentations on the prescribed odometer disclosure clauses on certificates of title, but also elsewhere in oral statements, advertising and other written statements. See 49 U.S.C. § 32705(a)(2); *Ryan v. Edwards*, 592 F.2d 756, 761 (4th Cir. 1979)(false representation of "low mileage" in newspaper advertising actionable, as our oral misstatements of mileage); *Hughes v. Box*, 814 F.2d 498, 501-502 (8th Cir. 1987). Under the Odometer Act, however, there is no private liability in a civil action unless the defendant is shown to have acted with "intent to defraud." 49 U.S.C. § 32710(a). Unlike the duty to establish a failure to disclose under the DTPA with actual knowledge, the "intent to defraud" element in an Odometer Act case can be established by constructive knowledge. In other words, a dealer making a false representation of mileage is liable under the Odometer Act if it reasonably should have known its statement was false or reasonably should have taken investigative steps which would have revealed the falsity of its statement. *Nieto v. Pence*, 578 F.2d 640, 642 (5th Cir. 1978). In further contrast with the DTPA, the Odometer Act provides that a prevailing consumer is entitled to an automatic award of three times the consumer's actual damages with minimum damages of $1,500. 49 U.S.C. § 32710(a).

c. The finance company that purchased the retail installment contract

Due to a clause in most retail installment contracts which provides that the holder of the contract is subject to all claims and defenses that the buyer has against the seller, assignee finance companies have vicarious liability for the odometer violations of dealers. See *Riggs v. Anthony Auto Sales, Inc.*, 32 F.Supp.2d 411, 415-417 (W.D. La. 1998). This vicarious liability is limited by the terms of the "holder clause," such that a consumer would be entitled to cancel the debt and recover affirmatively a sum not to exceed what has been paid under the contract.[3] *Id.*

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[3] Finance companies deal with the potential liability flowing from the "holder" clause by requiring dealers to agree to indemnify them should they be sued over a wrongful act performed by the dealer. This indemnification is usually a prominent part of the formal dealer agreement between the dealer and the finance company, which sets forth the terms of the relationship between them and the terms under which the finance company will purchase retail installment contracts. In lawsuits in which the lender has been added under a "holder clause" theory of vicarious liability, the finance companies often file cross-claims against the dealer seeking indemnification. In other cases, the dealer may agree to purchase the retail installment contract and assume all

3. Who is responsible when prior wreck damage has not been disclosed?

Imagine the following hypothetical facts based on one of my cases: Mr. and Mrs. Smith appear at a dealership and take their time looking over the available vehicles. Finding one late model vehicle with relatively low mileage, Mrs. Smith asked if there was anything wrong with the vehicle and whether it had been in a wreck, particularly in light of its low milage, and was told that there was nothing wrong with the vehicle and that it had only one owner before being traded-in to that dealer. As a result of these assurances, the Smiths purchased the vehicle. A few months after the purchase concluded, Mrs. Smith was informed by the service department that the vehicle had been in a serious wreck previously and that she might want to return it. After contacting the first and only owner, it was discovered that the first owner had been in a serious wreck, that the repairs had been performed by the same dealer which had later sold the car to the Smiths, and that he informed the salesman at the time of trade-in that the vehicle had been in a wreck previously, which fact reduced the trade-in allowance provided by this same dealer.

There is some specific Texas law which is intended to provide some protection against this sort of deception in automobile sales, but, in many cases, it does not appear to work. Under Tex. Transp. Code § 501.0911 through 501.0931, the Texas Legislature has set up a regulatory framework which requires vehicles which have suffered damages equal to 75% or more of their fair market value prior to an accident to have branded titles and those which have suffered damages equal to 95% or more of their prior fair market value to be used only as salvage. To avoid the loss in value associated with a branded title, however, insurance companies need merely estimate that the cost of repair following a serious wreck to be less than 75% of the prior fair market value. By manipulating either the estimate of repairs or the appraisal of the prior value, insurance companies can avoid the intended sweep of this statutory scheme. Despite the fact that the salvage title laws can be easily avoided, consumers can still receive some measure of protection through the DTPA.

a. Dealer liability

Under the foregoing facts, the dealer might well be liable both for an affirmative

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liability in an effort to save the finance company the expense and inconvenience of litigation.

Based on this inherent indemnification arrangement, the dealer is usually, but not always, the party which is ultimately responsible for covering the monetary cost of defensive attorney's fees, settlement, and judgment. The most common exception to this general rule is when the dealer is out of business or otherwise insolvent.

misrepresentation, in violation of DTPA § 17.46(b)(5) and (7), and a failure to disclose a material fact, in violation of DTPA § 17.46(b)(24). Many dealers have been liable for affirmatively misrepresenting the collision history of vehicles. *River Oaks L-M, Inc. v. Whalen*, 1998 Tex. App. LEXIS 5687 (Tex. App. [1st Dist.] 1998, no writ); *Grabinski v. Blue Springs Ford Sales, Inc.*, 136 F.3d 565 (8th Cir. 1998); *Torrance v. AS & L Motors, Ltd.*, 459 S.E.2d 67 (N.C. App. 1995). Likewise, many dealers have also been held liable for failing disclose the prior wreck history of vehicles. *Tandy v. Marti*, 213 F.Supp.2d 935 (S.D. Ill. 2002); *Bird v. John Chezik Homerun, Inc.*, 152 F.3d 1014 (8th Cir. 1998); *Parrott v. Carr Chevrolet, Inc.*, 965 P.2d 440 (Ore. 1998), *aff'd in part, rev'd in part*, 17 P.3d 473 (Ore. 2001). As mentioned previously, a failure to disclose violation requires proof of the dealer's knowledge of the prior wreck history as well as proof that this fact was not disclosed. Based on these violations, dealers in Texas would be liable for damages or rescission/revocation of acceptance/restoration of money or property under DTPA § 17.50(b)(3).

b. Finance company liability

As stated before, finance companies that purchase retail installment contracts are typically held liable for the wrongs of the dealers based on the "holder" clause. Even in those cases in which the "holder" clause is missing but should have been placed in the contract, recent amendments to the UCC have implied the existence of such a clause when it should have been present. See Tex. Bus. & Com. Code § 9.403.

4. Conclusion

Despite the weakening of the DTPA and the obvious impact of tort reform on Harris County juries, there remain many deceptive automobile sales cases worth taking to court. In particular, odometer rollbacks and undisclosed wreck damage provide strong bases for suit. Prior to suit, however, plaintiff's counsel must evaluate the facts and consider all of the risks associated with trial before taking on such cases. Given the conservative litigation climate, plaintiffs' counsel are advised to take those cases that even a conservative juror would consider to be fraud. In the automobile context, odometer rollbacks and failures to disclose wreck damage are the types of cases that all jurors would view as fraudulent and worthy of their time in the jury box.

C. Failed Yo-Yo Transactions

1. Background of Yo-Yo Sales, aka Spot Deliveries

A yo-yo or spot delivery is a very common sales practice with both new and used car dealers, and it is probably the most insidious practice affecting consumers with poor

credit histories. This is how it works. In response to advertising offering "second chance financing," a consumer with a less than sterling credit history appears at a dealership seeking to buy an automobile. After choosing a particular car to purchase and permitting his trade-in vehicle to be appraised, the consumer will be asked to provide a substantial cash downpayment, and sometimes a trade-in, and sign all of the usual paperwork, including a buyer's order, a retail installment contract, a title application, a promise to obtain insurance sheet and odometer disclosure documents, and, in addition, the consumer will be asked to sign a document usually referred to as a "bailment agreement" or "courtesy delivery agreement."[4]

In the bailment agreement, the dealer typically promises to seek financing on the terms set forth in the other documents, but, if the dealer is unable to obtain financing on those terms, then the consumer is obligated to return the vehicle upon request and the dealer can apply daily and mileage use charges against any cash downpayment provided by the consumer. Many of these bailment agreements even provide that the trade-in may be sold immediately, even if the dealer later claims the deal was not completed due to the failure to "obtain financing." Leaving his trade-in, if any, with the dealer, the consumer then drives away, often with a temporary dealer plate stating that a sale occurred that day, but often the consumer is only allowed to retain a copy of one document, the bailment agreement. Frequently, consumers in these transactions are told that they will receive a copy of the retail installment contract in the mail or when they come to pick up their permanent license plates. Most of these consumers drive away assuming that the deal is final.

After driving off in a new vehicle, the dealer attempts to sell the retail installment contract, and the right to receive the monthly payments, to a sub-prime finance company. If the dealer is unable for any reason to sell the contract or at least not on the terms set forth in the contract, the dealer will usually call the consumer and ask for either the car to be returned or the consumer to sign a new retail installment contract, frequently back-dated to the date of delivery, with terms less favorable to the consumer, such as a higher downpayment, a higher interest rate and consequently higher monthly payments, or the addition of a co-signor. In fact, sometimes dealers ask consumers to return and sign several different retail installment contracts. When the retail installment contract is not sold or renegotiated and sold, the dealer takes the position that no sale was ever consummated, as it has not transferred title (which only occurs when the dealer is paid in full by a finance company). Instead, because no financing has occurred, the argument

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[4] Some wags refer to these documents as "MacArthur agreements." This is based on General Douglas MacArthur's famous promise that "I shall return" after he was forced to depart the Philippines in World War II. The relevance of this moniker will soon become apparent.

goes that the transaction was merely a form of rental and an objecting consumer will have daily and mileage rental charges assessed against their downpayment. When such a deal goes south and a consumer demands the return of the trade-in and cash downpayment, the dealer frequently says the trade-in has already been sold and that the consumer is not entitled to any refund due to significant use, relying on the "bailment agreement." (Marvin Zindler calls this process "dehorsing" when consumers are denied the return of their trade-in.) To avoid arguments over the existence of a sale on specific terms, dealers have alternated between providing no copies of the retail installment contract until after funding at the time of assignment and providing a copy of the retail installment contract with no dealer signature (based on the feeble argument that it was not a final agreement without such a signature).

Not surprisingly, the dealer will typically assert that the retail installment contract was consummated on the day the consumer signed when it is able to sell that contract and obtain funding from a finance company, but, on the other hand, the dealer will assert that no sales transaction was ever consummated if it was not able to sell the finance contract even though the consumer has already signed. Talk about a one-sided agreement! This is one of the best examples of a "tails I win/heads you lose" transaction.

2. Are such transactions even subject to challenge?

The legal effect of the "bailment agreement" and the eventual failure to sell the retail installment contract turns largely on whether there is a "condition precedent" or "condition subsequent" contractual transaction. If this is a "condition precedent" deal, the dealer must retain title, the plates must be dealer use license plates and the dealer must provide the insurance coverage. In a "condition precedent" deal, the transaction is not consummated until the dealer sells the retail installment contract. In short, with a condition precedent contract, no agreement exists until the condition is met. If this is a "condition subsequent" deal, the dealer would be entitled to rescind the contract if the subsequent condition of contract sale is not met. With a "condition subsequent" deal, title should pass immediately, temporary dealer sale plates are permissible and the consumer-buyer is responsible for insuring the vehicle. Thus, if a condition is not met, one or both of the parties are entitled to cancel an agreement that has already been consummated.

It is hard to determine whether the "spot delivery" transactions are either "condition precedent" or "condition subsequent," because dealers set up the deals using elements of both types of transactions. For example, dealers typically retain title and do not apply for a new certificate of title showing ownership in the name of the consumer-buyer until the deal is funded following the sale of a retail installment contract to a finance company, and

this suggests the transaction is a "condition precedent" transaction.[5] On the other hand, dealers typically provide temporary license plates that can only be used when a vehicle has been sold according to Tex. Transp. Code § 503.603, and they require the consumer-buyer to maintain insurance on the vehicle. Moreover, under Tex. Fin. Code § 348.101(b)(4), a retail installment contract for the purchase of a vehicle can only be tendered for signature when it is "complete as to all particulars," which suggests that the contract must be binding when tendered for signature. Also, if these are "condition precedent" transactions, the trade-in should not be sold until the condition of contract sale has occurred, but dealers frequently sell the trade-ins very quickly, or at least represent that to the consumers caught in the web of these transactions. In addition, if these are "condition precedent" transactions, no interest can be earned until the condition of contract sale occurs, and yet dealers *always* allege that interest can be earned from the date the first contract was signed and delivery of the vehicle was made. Finally, the execution of a retail installment contract with an entirety clause and no language on the sale being conditional could render invalid all other documents with contrary language.[6]

a. Attacks on "condition subsequent" yo-yo's

I believe that these transactions should ordinarily be considered "condition subsequent" transactions, which means that there has been a consummated transaction.[7] From that conclusion, a number of consequences follow. First of all, the failure to provide copies of the retail installment contract to the sub-prime consumers in these transactions

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[5] Under Tex. Bus. & Com. Code § 2.401, however, it can be argued that title passes immediately upon delivery of the vehicle and that retention of the certificate of title only means the dealer has retained a security interest. See, e.g., *In re Johnson*, 230 B.R. 466, 468-469 (Bkrtcy.D.D.C. 1999).

[6] For example, many retail installment contracts used in Houston have language indicating that the contract "contains the entire agreement between you and us relating to this contract."

[7] For TILA purposes, the transaction is consummated when the consumer is obligated and, according to the only two courts of appeals to rule on the issue, that is when the consumer signs the retail installment contract. *Nigh v. Koons Buick Pontiac GMC, Inc.*, 319 F.3d 119, 123-124 (4th Cir. 2003), *cert. granted on other grounds*, 2004 U.S. LEXIS 677 (2004); *Bragg v. Bill Heard Chevrolet, Inc.*, 374 F.3d 1060, 1066-1068 (11th Cir. 2004).

constitutes a violation of the Truth-in-Lending Act.[8] *Polk v. Crown Auto, Inc.*, 221 F.3d 691, 692 (4th Cir. 2000); *Lozada v. Dale Baker Oldsmobile, Inc.*, 197 F.R.D. 321 (W.D. Mich. 2000); *In re Williams*, 232 B.R. 629 (Bkrtcy.E.D. Pa.), *aff'd as corrected*, 237 B.R. 590 (E.D. Pa. 1999). See Revisions to Official Staff Commentary to Regulation Z, 67 F.R. 16980, 16982-16983 (April 9, 2002). Unfortunately, consumers can only recover for this type of violation if there are "actual damages." *Baker v. Sunny Chevrolet*, 349 F.3d 862 (6th Cir. 2003). Second, dating the contract on a date before it was actually signed can render the APR disclosure inaccurate, entitling the consumer buyer to recover statutory damages under TILA. See *Rucker v. Sheehy Alexandria, Inc.*, 228 F.Supp.2d 711 (E.D. Va. 2002). Third, representing a right to repossess the automobile subject to spot delivery and/or a right to retain the downpayment and the trade-in or the proceeds from its sale may violate the DTPA, and in particular § 17.46(b)(12), if the contract had been consummated and the consumer had not defaulted. Fourth, because in a "condition subsequent" transaction ownership has already passed to the consumer, the dealer is required to comply with Article 9 of the UCC when it repossessed and disposed of the vehicle following repossession. If the repossession was not performed in a peaceable manner or no notice of sale was given after repossession, the dealer will be subject to minimum statutory damages under Tex. Bus. & Com. Code § 9.625(c)(2).[9]

b. Attacks on "condition precedent" yo-yo's

Even if a court finds a "spot delivery" to be a "condition precedent" transaction, consumers may still challenge the dealer's conduct. First, a consumer can sue under the DTPA for a misrepresentation if he was told that financing had been approved when it turned out otherwise. See *Taylor v. Butler*, 2003 Tenn. App. LEXIS 308 (Tenn. App. 2003). This is a fraud in the inducement claim. Second, if the consumer complied with his obligations under the bailment agreement after being informed that the retail installment contract could not be sold, the consumer may have a breach of contract claim if the downpayment is not returned. See *Violette v. P.A. Days, Inc.*, 2002 U.S. Dist. LEXIS 23246, * 13-14 (S.D. Ohio 2002). Third, the failure to return the trade-in when a spot delivery fails may well be an unconscionable act, entitling the consumer to relief under the DTPA. Fourth, if the dealer relies on the absence of its signature on the retail installment

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[8] The finance company which is the assignee on the retail installment contract probably has no liability for this TILA violation, because it is not apparent from the face of the contract paperwork which followed the assignment. See 15 U.S.C. § 1641(a).

[9] Failure to give notice or to sell the vehicle in a commercially reasonable manner will further preclude the dealer from seeking a deficiency judgment. See Comment 4 following Tex. Bus. & Com. Code § 9.626, the State Bar Comment following § 9.626, and *Tanenbaum v. Economic Laboratory, Inc.*, 628 S.W.2d 769 (Tex. 1982).

contract to argue the absence of consummation and to support its right to keep all or a portion of the downpayment, the dealer may have violated Tex. Fin. Code § 348.101(b) by tendering a retail installment contract for signature by the consumer when it was not "completed as to all essential provisions." See, e.g., *Cannon v. Metro Ford, Inc.*, 242 F.Supp.2d 1322, 1332-1333 (S.D. Fla. 2002). As such, the consumer would be entitled to statutory damages and attorney's fees under Tex. Fin. Code § 349.003(a) equal to three times the actual loss caused by the violation (conceivably three times the amount of the downpayment being withheld).

c. Possible changes in the regulatory environment

In the "spot delivery" context, the risk of loss associated with a failed transaction could fall on either the consumer or the dealer. There are indications, however, that the regulatory landscape in this area may possibly change, because, on October 22, 2004, the Finance Commission authorized the Office of the Consumer Credit Commissioner to publish a proposed rule on this issue. Specifically, the Commissioner sought leave to publish a proposed rule on the issue in the Texas Register to solicit comments from the public and the affected industry. The proposed rule would legitimize yo-yo sales under state law, but it would explicitly prohibit some of the biggest abuses. For example, no trade-in could be sold by a dealer until the underlying retail installment contract was actually sold to a third-party lender. Likewise, the dealer is stuck with the retail installment contract unless the contract is rescinded or sold to a third-party lender within 10 days. On the other hand, the dealer is entitled to recover for loss of use from the consumer's down payment if the bailment agreement so provides and the transaction is rescinded within 10 days. That could mean that many consumers in yo-yo deals will have lost their entire cash downpayment. That proposed rule was never promulgated, but a bill to prohibit these transactions entirely was introduced in the last session of the Texas Legislature in 2007.

3. What yo-yo cases are worth taking?

In my practice, I have agreed to represent consumers in these matters only where the consumer has suffered a concrete loss. This happens when a dealer has retained the consumer's cash downpayment, sold a trade-in owned outright by the consumer and/or repossessed the new car. When the consumer has lost no cash and the trade-in was worth less than the amount still owed (this is referred to in dealer parlance as being "over-under"), I am usually reluctant to take the case. In addition, I am more likely to accept this kind of case if the consumer has returned a number of times to sign new contracts, especially when the subsequent contracts impose progressively worse terms upon the consumer. Moreover, I am more likely to accept such a case when the dealer has repossessed the spot delivered vehicle and violated some UCC provision during the repossession or later sale of the vehicle. Given the prevalence of the practice and the frequent unfairness in the dealer's conduct, attorneys willing to represent consumers

should consider handling these types of cases. Acceptance of such cases in the future, however, must depend upon the effect of any OCCC rule that may be promulgated to legitimize and regulate the practice.

D. Car Title Disputes Arising Out of Sales Out of Trust

In the typical automobile sales transaction, there are a number of parties that serve particular roles. First, whether the transaction involves a new or used vehicle, there is a floorplanner which provides financing for the dealer to put the automobile on the lot for sale, secured by a purchase money security interest (PMSI) in the dealer's inventory. Second, there is the dealer that is offering to sell the vehicle. Third, there is the consumer who agrees to purchase the vehicle off the lot of the dealer. Finally, there is the retail finance source which ultimately provides the funding for the purchase of the automobile from the dealer by the consumer, secured by a PMSI in the vehicle which is the subject of the sale. This retail financing usually comes in one of two forms. A retail lender can provide direct financing to consumers who seek their own funding or indirect financing by purchasing a retail installment contract executed by the dealer and the consumer.

What happens when a vehicle is sold by a dealer without payment of the inventory lender's PMSI? This is commonly known as a "sale out of trust." Such sales out of trust are very common, especially with failing used car dealers who must steal from Peter to pay Paul. The law must determine who must suffer or share the risk of loss when such a sale out of trust occurs. Attorneys representing consumers can make at least modestly decent money in such cases, as long as careful case selection analysis is conducted before offering to be retained. On the one hand, consumers in these cases are sympathetic even to very conservative judges and jurors, because they are often truly innocent and yet have suffered a loss of title or even possession of a vehicle that they had purchased. On the other hand, there can be substantial risk in these cases as well, however, because there may be no deep pocket defendant that can afford to pay damages or afford other relief. Before agreeing to represent a consumer in a sale out of trust case, consumer attorneys must be sure that their prospective consumer is innocent and that there is a target defendant with the resources to pay damages. With the right facts, the right client and the right defendant, an attorney representing an innocent consumer can do well for his client and himself. This paper endeavors to survey how the law has addressed the burden of risk in sales out of trust and, thereby, to give consumer advocates the tools to identify those cases which are worth handling.

1. Background of sales out of trust

Many dealers need financing to purchase their inventory of automobiles, whether they are offering new cars or used cars for sale. When dealers need such financing, they usually sign floorplan agreements with their lenders. In the case of new car dealers, they

frequently get this financing from the finance subsidiaries of the manufacturers, such as GMAC or Ford Motor Credit. With used car dealers, such financing may come from a local bank or an individual or group of individuals. Under these floorplan agreements, dealers receive funds from the lender to purchase new cars from a manufacturer or used cars from a wholesale source, such as an auction or another dealer. In return for providing a line of credit to purchase inventory, for example at an auction, the dealer will agree to grant a security interest to the lender on all of its inventory. In practice, this means that, when a floorplanned vehicle is sold off its lot, the dealer is obligated to use the proceeds first to pay off the principal and interest owed to its floorplanner, leaving any remainder as its gross profit. To further protect themselves, floorplanners will commonly retain possession of the titles or manufacturer's certificates of origin to automobiles purchased with their credit until the money that they have advanced, together with interest or other applicable fees, is paid off by the dealer.

Not infrequently, dealers, especially in the used car context, sell floorplanned vehicles to consumers by execution of a retail installment contract, receive a payment from a finance company for the sale and assignment of the contract, and then fail to use these proceeds to pay their floorplanner. (The reasons for this failure to pay can run the gamut from excessive spending on drug or gambling addictions, payment of other demanding creditors before the floorplanner to simple business incompetence.) What is a floorplanner to do? At a minimum, the injured floorplanner will usually refuse to release the title it has retained as security. More assertive floorplanners have even arranged for the repossession of the floorplanned vehicle from the innocent consumer-buyer. Even when a consumer does not find the automobile repossessed in the middle of the night by the floorplanner, the dealer's failure to obtain title and registration for the consumer will prevent the consumer from lawfully operating the vehicle. In effect, floorplanners usually try to assert that the consumer-buyer and the finance entity that financed the sale should bear the entire risk of loss from the dealer's failure to pay.

To obtain a license to sell vehicles, used car dealers are required to have a $25,000 bond in place to cover damages incurred by buyers and others when title does not pass. See Tex. Transp. Code § 503.033. As currently construed, this law permits consumers, retail finance entities and wholesalers to sue what are often defunct dealers and obtain judgments and then to recover the amount of these judgments against the applicable dealer bond of $25,000. *Old Republic Surety Company v. Reyes*, 2002 Tex. App. LEXIS 5649 (Tex. App. - Dallas 2002, pet. pending)(consumer); *Grammercy Ins. Co. v. Arcadia Financial Ltd.*, 96 S.W.3d 320, 323-326 (Tex. App. - Austin 2001, pet. denied)(retail finance company); *Grammercy Ins. Co. v. Auction Finance Program*, 52 S.W.3d 360, 363-368 (Tex. App. - Dallas 2001, pet. denied)(auction house); *Grammercy Ins. Co. v. Arcadia Financial Ltd.*, 32 S.W.3d 402, 407 (Tex. App. - Houston [14th Dist.] 2000, no pet.)(retail

finance company); *Lawyers Surety Co. Royal Chevrolet*, 847 S.W.2d 624, 626-627 (Tex. App- Texarkana 1993, no writ)(wholesaler); *Geters v. Eagle Ins. Co.*, 834 S.W.2d 49, 50 (Tex. 1992)(consumer). Interestingly enough, floorplanners would usually have no claim to recovery under the bond. *Grammercy Ins. Co. v. MRD Investments, Inc.*, 47 S.W.3d 721, 727 (Tex. App. - Houston [14th Dist.] 2001, pet. denied); *Lawyers Surety Corporation v. Riverbend Bank*, 966 S.W.2d 182, 185-187 (Tex. App. - Fort Worth 1998, no pet.).

Problems frequently arise, however, because a $25,000 bond will usually only cover the loss associated with one or two automobiles. Additionally, the bond covers only claims occurring during the 12-month term of the bond which has been reduced to judgment. Sureties most often pay claims in order of presentment. Thus, the surety bond is paid out on a first-come-first serve basis with the first claimant recovering up to the amount of the $25,000 face value of the bond and with each claim reducing the value of the bond until fully depleted. When a dealer sells out of trust, however, it is not unusual for the dealer to sell a whole raft of vehicles out of trust before it is discovered. When the minimal dealer bond is not enough to cover the potential loss, the question of who bears the risk of loss must be addressed head-on. Unfortunately, in these circumstances, the law in Texas is as not clear on the placement of the risk of loss as I wish it was.

2. Who should bear the risk of loss?

As support for the position that the consumer and the retail finance entity should bear the full risk of loss, the floorplanner will usually argue that the purported sale of the vehicle to the consumer-buyer by the dealer was void due to the failure of the dealer to possess title or to transfer title at the time of sale. Floorplanners rely specifically on Tex. Transp. Code § 501.071(a) which provides that "[a] motor vehicle may not be the subject of a subsequent sale unless the owner designated on the certificate of title transfers the certificate of title at the time of sale" and Tex. Transp. Code § 501.152 which provides that it is an offense to sell or offer to sell a motor vehicle registered in this state when the seller "does not possess the title receipt or certificate of title for the vehicle." Thus, since Tex. Transp. Code § 501.073 provides that "[a] sale made in violation of this chapter is void and title may not pass . . . ," floorplanners argue that no title passes when they are holding the title and the dealer did not transfer title at the time of the purported sale. In a number of cases in which floorplanners, wholesalers and other sellers were paid with drafts that bounced, several Texas appellate courts have accepted this Certificate of Title Act ("COTA") argument and have found subsequent sales by dealers to be void. *Bank One Texas N.A. v. Arcadia Financial Ltd.*, 219 F.3d 494, 497-498 (5th Cir. 2000); *Allstate Insurance Company v. Troy's Foreign Auto Parts*, 2001 Tex. App. LEXIS 5029 (Tex. App. - Dallas 2001); *Gallas v. Car Biz. Inc.*, 914 S.W.2d 592, 594-595 (Tex. App. - Dallas 1995, pet. denied); *Everett v. United States Fire Insurance Company*, 653 S.W.2d 948, 950 (Tex.

App. - Fort Worth, no writ); *Boswell v. Connell*, 556 S.W.2d 624, 625-626 (Tex. Civ. App. - Beaumont 1977, writ ref'd n.r.e.). What does this mean in practice? The floorplanner retains title, is entitled to possession of the vehicle sold out of trust, and the innocent consumer must bear the entire risk of loss. The practical result places every consumer in peril. Giving legal significance to the mere possession of a certificate of title provides the floorplanning lender the best of both worlds: permitting its inventory collateral to be exposed to sale to the public from which proceeds are generated for the dealer to pay the secured debt, and empowering that lender to render void, retroactively, any sale of which it does not approve.

a. Agency Exception

In an effort to ameliorate the harshness of this rule, other courts have found an agency exception. Initially, these courts cite to the recognized rule that a sale of an automobile may still be valid as between a buyer and a seller despite non-compliance with COTA. *Phil Phillips Ford, Inc. v. St. Paul Fire & Marine Insurance Co.*, 465 S.W.2d 933, 937 (Tex. 1971); *Hudson Buick, Pontiac, GMC Truck v. Gooch*, 7 S.W.3d 191, 197 (Tex. App. - Tyler 1999, pet. denied); *Tyler Car v. Empire Fire & Marine Ins. Co.*, 2 S.W.3d 482, 485 (Tex. App. Tyler 1999, pet. denied); *Jarrin v. Sam White Oldsmobile Co.*, 929 S.W.2d 21, 24 (Tex. App. - Houston [1st Dist.] 1996, writ denied); *Najarian v. David Taylor Cadillac*, 705 S.W.2d 809, 811-812 (Tex. App. - Houston [1st Dist.] 1986, no writ). If proven that the dealer was acting as the agent of the floorplanner in selling the vehicle, a number of courts have recognized that the innocent consumer who purchased from the dealer is entitled to retain possession and to receive title, even if COTA was violated in the process. *Morey v. Page*, 802 S.W.2d 779, 784 (Tex. App. - Dallas 1990, no writ); *IFG Leasing Co. v. Ellis*, 748 S.W.2d 564, 566 (Tex. App. Houston [1st Dist.] 1988, no writ); *Cash v. Lebowitz*, 734 S.W.2d 396, 398 (Tex. App. - Dallas 1987, writ ref'd n.r.e.); *Jim Stephenson Motor Co., Inc. v. Amundson*, 711 S.W.2d 665, 669 (Tex. App. - Dallas 1986, writ ref'd n.r.e.); *Pfluger v. Colquitt*, 620 S.W.2d 739, 743 (Tex. Civ. App. - Dallas 1981, writ ref'd n.r.e.). These courts recognize that if A (the dealer), as agent of B (e.g., the floorplanner), was authorized to sell a vehicle to C (the buyer), the sale would be effective as between B, the actual seller, and C, the buyer. *Morey*, 802 S.W.2d at 784. Under these circumstances, the floorplanner would bear the risk of loss associated with its own agent's faithlessness. *Cash*, 734 S.W.2d at 399; *Pfluger*, 620 S.W.2d at 743. In other words, the floorplanner then would bear the loss of the money that the dealer failed to pass on to the floorplanner following the sale.

This agency exception to the general rule requiring compliance with COTA gives some protection to innocent consumer-purchasers, but not always. In *Morey v. Page*, for example, the Dallas Court of Appeals found inadequate evidence of agency. In that case,

Page consigned a 1967 Bentley for sale by Yardley under the stipulation that he recover a $20,000 net profit. Yardley then negotiated the sale of the Bentley to Morey for only $9,000, and Yardley absconded with these funds. The Dallas Court of Appeals found no express authority for the sale due to the failure to meet the consignment condition of a $20,000 net return and no apparent authority due to the fact that Yardley never disclosed that he was acting on behalf of Page. *Morey*, 802 S.W.2d 782-785. Given the fact that the strength of the evidence in favor of agency will vary greatly from case, this exception provides at best an uncertain lifeline to innocent purchasers. If the innocent purchaser is buying from a licensed dealer, in a transaction that has the appearance of a sale in the ordinary course of the dealer's business, why should the validity of the sale be dependent upon a prior transaction between the dealer and an undisclosed principal? The Texas Uniform Commercial Code provides rules of priority that protect buyers in the ordinary course of business in such circumstances.

b. UCC Alternative

If the UCC applies in the context of a sale out of trust by a dealer, an innocent purchaser would be accorded title and the risk of loss associated with the dealer's defalcation would be placed squarely upon the floorplanner. In a majority of the states, the UCC prevails over the applicable COTA in cases involving out of trust sales. See, e.g., *Madrid v. Bloomington Auto Company, Inc.*, 782 N.E.2d 386, 391-397 (Ind. App. 2003); *Jones v. Mitchell*, 816 So.2d 68, 69-72 (Ala. App. 2001); *Cherry Creek Dodge, Inc. v. Carter*, 733 P.2d 1024, 1027-1029 (Wyo. 1987); *Dartmouth Motor Sales, Inc. v. Wilcox*, 517 A.2d 804, 806-807 (N.H. 1986); *Big Knob Volunteer Fire Company v. Lowe & Moyer Garage, Inc.*, 487 A.2d 953, 956-959 (Pa. Super. 1985); *Atwood Chevrolet-Olds, Inc. v. Aberdeen Mun. School Dist.*, 431 So.2d 926, 927-929 (Miss. 1983); *Martin v. Nager*, 469 A.2d 519, 522-526 (N.J. Super. 1983); Roger D. Billings, *Floor Planning, Retail Financing & Leasing in the Automobile Industry* §§ 5.36 - 5.41 (West 1998). Interestingly enough, the Texas Transportation Code specifically provides that it is to yield to the Texas Uniform Commercial Code where there is a conflict between these two bodies of law. Tex. Transp. Code § 501.005. Several Texas courts have recognized the U.C.C. as an alternative source of law which, unlike the agency rule, provides a bright line rule.

Innocent buyers are entitled to receive title in "out of trust" sales under two theories based on the U.C.C. First, under Tex. Bus. & Com. Code § 2.403(a), a person "with voidable title has power to transfer a good title to a good faith purchaser for value," and "[w]hen goods have been delivered under a transaction of purchase the purchaser has such power even though . . . the delivery was in exchange for a check which is later dishonored . . . or the delivery was procured through fraud punishable as larcenous under the criminal law." In effect, the courts construing these provisions have held that a

purchaser who procured a good, such as a vehicle, with a check or draft that was dishonored nevertheless had voidable title to pass and that a good faith buyer from such a fraudulent purchaser was entitled to receive title. *Prestige Ford v. Dallas Postal Credit Union*, 2002 Tex. App. LEXIS 974, * 11-13 (Tex. App. - Dallas 2002)(dishonored draft); *Perry v. Breland*, 16 S.W.3d 182, 190 (Tex. App. - Eastland 2000, pet. denied)(dishonored check); *Villa v. Alvarado State Bank*, 611 S.W.2d 483, 487-488 (Tex. App. - Waco 1981, no writ)(dishonored check); *Leif Johnson Ford, Inc. v. Chase National Bank*, 578 S.W.2d 792, 794 (Tex. Civ. App. - Beaumont 1978, no writ)("Section 2.403(a) gives good faith purchasers of even fraudulent buyers-transferors greater rights than the defrauded seller can assert.").

Second, under Tex. Bus. & Com. Code § 2.403(b), the "entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in the ordinary course of business." Under Tex. Bus. & Com. Code § 1.201(9), a "'buyer in the ordinary course of business' means a person who in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interest of a third party in the goods buys in ordinary course from a person in the business of selling goods of that kind but does not include a pawnbroker." Under Tex. Bus. & Com. Code § 2.401(b), title to goods passes when the seller completes physical delivery of the goods, even if a document of title is to be delivered at a different time and place.

Under an amendment to COTA passed in 1971 and intended to be a reversal of the ruling in *Phil Phillips* (see above) on the inapplicability of the UCC to automobile title issues, the provisions of the UCC are supposed to prevail over the Certificate of Title Act in the event of any conflict. Tex. Transp. Code § 501.005. This amendment should have established that §§ 2.401 and 2.403 control over the Act's provisions which purport to void the sale of an automobile absent possession of title by the seller at the time of sale or absent a transfer of title at the time of sale. *Hudson Buick*, 7 S.W.3d at 198; *In re Bailey Pontiac, Inc.*, 139 B.R. 629, 633 n.3 (Bkrptcy. N.D. Tex. 1992).

While the conflict between the UCC good faith buyer provisions and the Certificate of Title Act is clear, the Dallas Court of Appeals and a few other courts have attempted to "harmonize" the statutes and thereby avoid the resulting UCC control in the event of a conflict. *Gallas*, 914 S.W.2d at 594-595; *Morey*, 802 S.W.2d at 783-784; *Everett v. U.S. Fire Ins. Co.*, 653 S.W.2d 948, 950 (Tex. App. - Fort Worth 1983, no writ); *Pfluger*, 620 S.W.2d at 741-742; *Bank One Texas N.A.*, 219 F.3d at 497 n. 3 (5th Cir. 2000). The existence of a conflict between §§ 2.401 and 2.403 of the UCC and COTA, however, is clear and the UCC should govern title disputes arising out of "out of trust" sales. The Tyler Court of Appeals and the U.S. Bankruptcy Court for the Northern District of Texas have

recognized the conflict and have given full effect to the UCC. *Hudson Buick*, 7 S.W.3d at 198; *In re Bailey Pontiac, Inc.*, 139 B.R. at 633 n. 3. Likewise, two dissenting justices on the Dallas Court of Appeals have recognized the conflict and opined that § 2.403(b) should be given full effect. *Gallas*, 914 S.W.2d at 595-601; *Pfluger*, 620 S.W.2d at 744-748.

c. Recent cases finding that COTA is inapplicable

In 2003, U.S. District Judge Sim Lake of the United States District Court for the Southern District of Texas concluded that a dealer was not an "owner" for purposes of Trans. Code § 501.071 and, therefore, the failure to transfer title did not render a sale from a dealer to a retail buyer invalid under Trans. Code § 501. 073. *In re Dota*, 288 B.R. 448, 455-458 (S.D. Tex. 2003). Judge Lake further held that neither the Transportation Code nor the UCC permitted a floorplanner to assert a security interest to a vehicle held as inventory by merely retaining possession of the title. *Id.* at 458-460. Then, Judge Lake applied the UCC to find that a cash buyer was a buyer in the ordinary course of business under Tex. Bus. & Com. Code § 1.201(9) and, thereby, free to take title to a vehicle, despite having failed to demand a transfer of title at the time of sale. *Id.* at 460-461. This decision was appealed to the Fifth Circuit, but the appeal was dismissed on jurisdictional grounds.

More recently in August of 2004, the Corpus Christi Court of Appeals took a different tack to rule for an innocent consumer buyer. In a classical sale out of trust involving the same dealer as in the *Dota* bankruptcy case, this appellate court, unlike the Dallas Court of Appeals and the 5th Circuit Court of Appeals, found a conflict between the COTA and the UCC and then applied the UCC. Finding the consumer to be a "buyer in the ordinary course of business," the Court thereby affirmed the trial court's finding that the consumer should receive title free of the bank's inventory lien. *First National Bank of El Campo v. Buss*, 143 S.W.3d 915, 919-923 (Tex. App. - Corpus Christi 2004, pet. denied). Given the Texas Supreme Court's denial of the petition for review, the principles espoused by *Dota* and *Buss* appears close to full acceptance.

Based on the *Dota* and *Buss* rulings, COTA would never apply to cases involving dealers who made "out of trust" sales. Under *Dota*, there is no need to argue that there is a conflict between COTA and the UCC, so that the preemption provision in COTA becomes effective. By contrast, under *Buss*, there is a conflict between COTA and the UCC and this means that the UCC prevails. In short, if the *Dota* and *Buss* cases are followed, the bright line of the UCC will apply to all "out of trust" cases involving dealers, and the cases applying COTA to such issues in the past can be ignored. I certainly hope this is where the law shakes out, as the UCC provides a rule which is both more fair and more clear than COTA.

All of the Texas cases since 2004 have followed the rulings in both *Dota* and *Buss* that the UCC governs the issue of automobile title. *One Ford Mustang v. State of Texas*, 231 S.W.3d 445, 452 (Tex. App. - Waco 2007, no pet.)("In determining the respective rights of parties to vehicle transactions in which the parties did not comply with the terms of the Title Act, courts have uniformly held that the terms of the UCC control over the terms of the Title Act . . . . "); *Vibbert v. PAR, Inc.*, 224 S.W.3d 317, 321-324 (Tex. App. - El Paso 2006, no pet.).

Even if *Dota* and *Buss* are not followed in the future, practitioners should expect a change in the law nevertheless. The Conference on Uniform Laws is considering proposals for changes in the uniform COTA that would recognize the BFP rule now solely recognized in the UCC. Should such proposed amendments to our COTA be passed by the Texas Legislature, innocent consumer-purchasers will be protected, even if our courts fail to recognize that the UCC should apply.

2. Conclusion

In any sale out of trust case, attorneys considering representation of an injured consumer buyer should closely evaluate the facts. First, does the dealer which sold the vehicle at issue out of trust still possess an untouched dealer bond of $25,000? If so, has anyone else already filed and how close are they to a judgment, default or otherwise? Second, how did the floorplanner act after discovering the default by the dealer? Did it merely hold the title or did it act more aggressively by, for example, repossessing the vehicle at issue? If so, is the floorplanner a deep pocket or merely a small business entity? Third, is there a consumer finance party that purchased the dealer's retail installment contract? If so, you should consider whether the duty to obtain title is imposed upon the assignee of the retail installment contract, thereby allowing a consumer to sue its consumer finance lender for breach of the warranty of title under Tex. Bus. & Com. Code § 2.312 and recover damages or rescission/revocation of acceptance plus attorney's fees. In the right case, an attorney representing a consumer buyer in a sale out of trust case can not only obtain good results for the client but recover a decent fee as well.