No. 08-3192

IN THE UNITED STATES COURT OF APPEALS

FOR THE TENTH CIRCUIT

JOHN WESLEY FORD, SR.
CYNTHIA DAWN FORD

Debtors/Appellants,

vs.

FORD MOTOR CREDIT COMPANY, LLC

Appellee.

AMICUS CURIAE BRIEF OF AMERICAN FINANCIAL SERVICES ASSOCIATION IN SUPPORT OF APPELLEE FORD MOTOR CREDIT COMPANY, LLC SUPPORTING AFFIRMANCE OF BANKRUPTCY COURT

APPEAL FROM THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS
HON. ROBERT E. NUGENT, BANKRUPTCY JUDGE

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Corporate Disclosure Statement

The American Financial Services Association is a trade association. It does not have a parent company and there are no publicly held companies holding 10% or more of an interest in the organization.

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PRIOR OR RELATED APPEALS

Comes now *Amicus Curiae* pursuant to 10th Cir. R. 28.2(C)(1) and advises the Court that there are no prior or related appeals involving the same parties and facts as the present case. However, the legal issue presented in this appeal is pending before this Court in *Wells Fargo Bank, N.A. v. Hunt*, Case No. 07-3297. The *Hunt* case was argued on May 14, 2008 (Judges McConnell, Seymour and Holmes, presiding).

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IDENTITY AND INTEREST OF AMICUS CURIAE AND SOURCE OF AUTHORITY TO FILE

I.
IDENTITY AND INTEREST OF AMICUS AMERICAN FINANCIAL SERVICES ASSOCIATION

The American Financial Services Association (AFSA) is the national trade association for the consumer credit industry protecting access to credit and consumer

choice. The Association encourages and maintains ethical business practices and supports financial education for consumers of all ages. AFSA has provided services to its members for over ninety years. The Association's officers, board, and staff are dedicated to continuing this legacy of commitment through the addition of new members and programs and increasing the quality of existing services.

The AFSA membership has a vital interest in the outcome of this case. AFSA members primarily represent motor vehicles installment sale financers. The 2005 amendments to section 1325(a) of the Bankruptcy Code added an unenumerated, hanging paragraph at the end of the section that deals with certain claims secured by motor vehicles. The effect of this paragraph has been widely debated by creditors, debtors, counsel, and commentators, and there is a split of authority in the courts. This case affords the Court an opportunity to address this debate as it pertains to whether a creditor's claim is covered by the hanging paragraph where a portion of the financing is used to pay off negative equity from a trade-in vehicle.

II.
SOURCE OF AUTHORITY TO FILE AMICUS CURIAE BRIEF

Pursuant to FED R. APP. P. 29(a), AFSA requested consent of the parties to this appeal to file an amicus curiae brief in support of Ford Motor Credit Company, LLC ("Ford Credit"). Such consent has been received from Thomas J. Lasater, counsel for Appellee. Counsel for AFSA has not heard from Michael J. Studtmann, counsel for

Appellants, concerning his position. Therefore, pursuant to FED R. APP. P. 29(a), AFSA seeks leave of court to file this Amicus Curiae Brief. AFSA submits this brief in conjunction with its Motion for Leave to File.

STATEMENT OF ISSUES

AFSA adopts the Statement of the Issue in the Brief for Appellee, Ford Motor Credit Company, LLC filed with this Court on September 22, 2008. The defined terms used in Ford Credit's brief filed with this Court are used with the same meaning in this Amicus Curiae Brief.

SUMMARY OF ARGUMENT

The question raised on appeal is whether the Bankruptcy Court erred in finding that Ford Credit's security interest in the Fords' vehicle was a "purchase-money security interest" as that term is used in Section 1325(a) of the Bankruptcy Code, to the extent the seller advanced sums to pay off the unpaid indebtedness on the Fords' trade-in vehicle. Amicus Curiae AFSA believes that the Bankruptcy Court correctly held that Ford Credit's security interest was a "purchase-money security interest" in its entirety and was therefore not subject to bifurcation and cramdown in the Fords' Chapter 13 wage earner plan. AFSA urges this Court to affirm the decision of the Bankruptcy Court.

This case is a byproduct of the 2005 amendments to the Bankruptcy Code. Those amendments are titled the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 and are known to bankruptcy disciples as "BAPCPA." Prior to BAPCPA, a debtor who owed $15,000 on a car worth only $10,000 could, in a wage earner's plan under Chapter 13, keep his car by paying only $10,000 to his secured creditor. In a procedure inelegantly known as a "cramdown," the debtor could divide his creditor's claim into a $5,000 unsecured claim and a $10,000 secured claim. He would then keep the car by paying $10,000 over time to his creditor on the secured obligation and give the creditor little or nothing on the $5,000 unsecured claim.

BAPCPA restricted this right to cramdown. For vehicles financed within 910 days of bankruptcy, the debtor was denied the power to divide his debt into secured and unsecured portions. To keep his car, the debtor had to pay the full amount to his creditor even if the value of the collateral (the car) was acknowledged to be less than the remaining balance on the debt.

This inartfully drafted provision of BAPCPA reflects a balancing of the interests of consumer creditors who specialize in secured credit (car creditors) and those other consumer creditors who specialize in unsecured credit (credit card issuers).

The issue in this case and in similar cases elsewhere is whether the entire debt secured by the new car is to be treated as a "purchase-money security interest." To the

extent that the security interest is not purchase-money, the creditor does not enjoy the protection of the new provision and the debtor may cramdown. If the entire security interest is "purchase-money," cramdown is prohibited. As noted above, the issue has caused a significant split among courts and commentators. To date only one federal circuit court has ruled on this issue, and this ruling favors the position Ford Credit has taken. *In re Graupner*, 537 F.3d 1295 (11th Cir. 2008). As pointed out in Ford Credit's brief in this case, the majority of the appellate courts have ruled in the same way, and this appears to be the national trend. *See* Brief for Appellee Ford Motor Credit Company, LLC at pp. 14-17.

So what is so hard about the term "purchase-money security interest?" Quite a bit, it turns out. Like many things in the Bankruptcy Code and in commercial law generally, there is more than meets the eye. In recent times it has become commonplace for debtors to pay for their cars over five or even seven years. Typically cars depreciate more quickly than the principal balance of the debt is paid down. When that happens, the debtor is said to have a "negative equity" in his car or to be "upside down;" he owes more on the debt than the car is worth.

The problem in this case comes when the debtor returns for a new vehicle before he has paid off the debt on the old one. When he buys the new car, he incurs a new debt that includes not only the sticker price on the new vehicle, but also payments

for dealer-provided products and services (such as extended service contacts), license fees, assorted taxes, ***and*** an amount to cover the "negative equity." The "negative equity" is the amount by which his debt against the trade-in exceeds the value of the trade-in. This secured transaction only works if the price paid to acquire the new vehicle covers the expense incurred to satisfy the negative equity.

Now there is a problem. Is a security interest that secures both the sticker price on the new car and the remaining balance on the old car regarded as a "purchase-money security interest?" The Fords, of course, say "no." Ford Credit says "yes." The Bankruptcy Court held that the security interest covering the Fords' vehicle was a purchase-money security interest in its entirety and was therefore entitled to the new protection in BAPCPA against cramdown.

Although it is stuffed with definitions, the Bankruptcy Code has no definition of "purchase-money security interest." It seems likely that Congress intended the term to have a federal law meaning drawn from the language, from inferences about Congressional intent, from commercial practice, and by analogy to state law and to other federal law. It is also possible that Congress intended to use state law definitions. Whether one regards the words as federal or state, the outcome is the same. Even if Congress intended a federal definition, that definition would have to

lean heavily on state statutes that define the term. If Congress wanted to adopt state law definitions, those same statutes would be applied directly.

ARGUMENT AND AUTHORITIES

I.
THE LANGUAGE OF THE STATUTE AND THE CONGRESSIONAL PURPOSE FAVOR FORD CREDIT

A. Congress' Purpose

As its name proclaims ("Bankruptcy Abuse Prevention") the 2005 Act was designed both to make it more difficult for consumers to cancel their debt and to require debtors with means to repay their bills. It came at the end of a twenty-year spike in bankruptcy filings from 250,000 in 1978 to more than 1,500,000 filings in 2004. All but a small number of these filers were consumer debtors.

That is not to say that the birth of the Act was easy or quick. The original form of BAPCPA was first introduced in 1998. In the succeeding years it passed the House six times, passed the Senate four, and cleared both houses of Congress in the same form twice. Once it even reached the President's desk, only to suffer President Clinton's pocket veto.

The opponents in Congress were as persistent and clever in opposition to the Act as the proponents were determined and united in support. Among the principal

creditor advocates for the bill were credit card companies.[1] By 2005 it was claimed that the credit card industry had spent over $100 million in lobbying and other activity to promote the bill. In general, credit card companies make unsecured loans and fare poorly in Chapter 7 consumer liquidations. Many consumer Chapter 7s are "no asset" cases. A "no asset" debtor shields all of his assets by smart use of the exemption laws and so makes no distribution to any unsecured creditor. To attempt to get something from some of the Chapter 7 debtors, the credit card companies and other unsecured creditors hoped to force some of those debtors into Chapter 13 where they would be required to give up a part of their wages for up to five years.

To the extent that changes in bankruptcy law take assets that the debtor would have kept for himself under the old law, the changes have the potential to benefit all creditors. But to the extent that a change in the law leaves the debtor with the same assets as he would have had under the old law, the change merely improves one creditor's lot at the expense of another creditor. Since, by hypothesis, most debtors in bankruptcy are insolvent, any change in an existing bankruptcy law has the high probability of taking from one creditor and giving to another without any change in the debtor's status. The provision in Section 1325 that is the subject of this case was

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[1] Timothy Egan, *Newly Bankrupt Raking in Piles of Credit Offers*, N.Y. TIMES, Dec. 11, 2005, at Section 1.

most likely intended to protect ***secured*** consumer creditors from the loss that they might otherwise suffer from debtors' migration from Chapter 7 to Chapter 13.

The secured creditors, particularly the auto creditors, must have feared that their interests would be injured by a bill that would move many debtors from Chapter 7 (liquidation), into Chapter 13 (wage earner plans). Secured creditors' concerns would arise principally because of the probability of a cramdown in Chapter 13. In Chapter 7, by comparison, debtors frequently sign "reaffirmation" agreements under which they are obliged, even after the bankruptcy, to pay the full amount due on their cars, whatever its value. So a large-scale move out of Chapter 7 and into Chapter 13 ─ of the kind hoped for by the credit card issuers ─ would favor the credit card companies (by giving them a 5-year share of the debtor's future wages) and would injure the auto creditors (by substituting low-pay cramdowns for high-pay reaffirmation agreements).

When one considers the parties to the Congressional debate (unsecured creditors who would benefit from Chapter 13 growth vs. secured creditors who would suffer), the goals of the principal creditor advocates (credit card issuers who openly advocated expansion of Chapter 13) and the evolving language of the Act (see Section I.B. below), it is unmistakable that Congress intended to protect creditors who finance consumer vehicle purchases from cramdowns in Chapter 13. Congress appears to have been persuaded by the auto financiers' argument that, unless the anti-cramdown

provision was added to the law, the increased costs of cramdown would ultimately be borne by consumers – including, in particular, some who would be priced out of the market as a result. (*See Bankruptcy Abuse Prevention and Consumer Protection Act of 2001: Hearings Before the Committee on the Judiciary, House of Representatives*, 107th Cong. 371-72 (2001)). That Congressional purpose is best served by a decision in favor of Ford Credit.

B. Congress' Language

The earliest response in the history of BAPCPA to secured creditors' concern is a provision in the 1998 House bill. That provision barred cramdowns, but it was quite narrow. It was not limited to motor vehicles, but it covered only:

> the unpaid principal balance of the purchase price of the personal property acquired [within 180 days of the filing] and the unpaid interest and charges at the contract rate . . .

H.R. 3150, 105th Cong. §128 (1998).

That provision would not have protected from cramdown much of the debt that is covered by a purchase-money security interest on a car. It would not have protected amounts attributable to title and taxes or negative equity on trade-ins, and, of course, it would not have touched any secured transaction that was completed more than six months before the bankruptcy filing.

Meanwhile an amendment proposed by Senator Abraham of Michigan, inserting a different anti-cramdown provision, was adopted by the Senate Judiciary Committee. This amendment prohibited cramdowns for all security interests of whatever kind and whenever incurred. S. REP. No. 105-253, at 7 (1998) (prohibiting cramdown of "an allowed claim [in a Chapter 13 case] that is secured under applicable non-bankruptcy law. . .").

Contemporary press reports made the unsurprising claim that Senator Abraham was responding to the interests of the "industry." The language proposed by Senator Abraham was presumably intended to protect the interests of an important group of constituents – the auto companies and their auto finance arms.

By 1999, the Senate version covered a claim where the debt that is the subject of the claim was incurred within the 5-year period preceding the filing of the petition and the collateral for that debt consists . . . of a motor vehicle . . . acquired for the personal use of the debtor . . . S. REP. No. 106-49, at 224 (1999). Note that the 1999 Senate version does not refer to a "purchase-money security interest" and that one infers that the legislation deals with the ***purchase*** of a motor vehicle only from the use of the verb "acquired," but the provision is now limited to motor vehicles bought for personal use.

The purchase-money language appears for the first time in 2000 when the section covers:

> a claim . . . if the creditor has a purchase-money security interest securing the debt that is the subject of the claim, the debt was incurred within the 5-year period preceding the filing of the petition, and the collateral for that debt consists of a motor vehicle . . . acquired for the personal use of the debtor . . .

H.R. REP. No. 106-970, at 57 (2000) (Conf. Rep.).

As finally enacted, the Abraham amendment is an unnumbered "hanging paragraph" attached to Section 1325(a), sometimes now labeled 1325(a)(*):

> For purposes of paragraph (5), section 506 shall not apply to a claim described in that paragraph if the creditor has a purchase-money security interest securing the debt that is the subject of the claim, the debt was incurred within 910-day preceding the date of the filing of the petition, and the collateral for that debt consists of a motor vehicle . . . acquired for the personal use of the debtor, or if collateral for that debt consists of any other thing of value, if the debt was incurred during the one year period preceding that filing.

C. Both The Language and Congress' Purpose Support a Reading Favorable to Ford Credit

There are two notable insights buried within Congress' choice of words and in the progression from the early House language to the words that are now part of Section 1325(a). First, is the probability that Congress chose the current language to exclude a certain kind of secured creditor from the Section's protection, and not to deal

with the scope of "purchase-money." Second, is the breadth of the traditional purchase-money security interest.

1. Excluding Certain Secured Creditors

The drafters may have chosen the purchase-money language to exclude non-purchase-money security interests in vehicles already owned by the debtor. Non-purchase-money security interests in property already owed by consumer debtors are frequently disfavored under the law. (*See* 16 C.F.R. § 444.2(a)(4), where taking a non-purchase-money security in certain household goods is an unfair trade practice, and Bankruptcy Code § 522(f)(1)(B), avoiding nonpossessory non-purchase-money security interests against certain consumer goods).

After the original House language, which referred to "purchase-money," was replaced with the 1999 version of the Abraham amendment, a non-purchase-money secured creditor who took a security interest in a car that the debtor had purchased outright within five years of the filing could have claimed the benefit of the provision. The automobile financiers – purchase-money creditors – had no interest in enriching non-purchase-money secured creditors who take security interests in property already owned by a consumer debtor, nor would the consumer advocates have wished to benefit these creditors. So, it is plausible that the purchase-money language was inserted only to deprive these non-purchase-money creditors from using the Section,

not to draw any distinction between parts of a secured debt incurred in the acquisition of the collateral. If that is the purpose of the language, i.e. to exclude a class of secured creditors, its presence does not justify the omission of negative equity from its protection against cramdown.

2. "Purchase-money Security Interest" Is Broader Than "Principal Balance"

By using the generic term "purchase-money security interest" instead of the original House term "unpaid principal balance of the purchase price attributable" to property acquired within 180 days, Congress must have intended to include some parts of the debt that would have been omitted by the original House language. The House language, "unpaid principal balance . . . attributable to the goods purchased," identifies the particular type of ***debt*** that is covered, whereas "purchase-money security interest" refers to a type of ***security interest***.

No purchase-money security interest is limited to the principal balance and unpaid interest. At a minimum, fees and taxes owed on the purchase of a motor vehicle would be covered and secured by any "purchase-money security interest." *See, e.g.*, UCC § 9-103, cmt. 3. But it would be easy to find that a claim for fees, taxes, and negative equity was not part of the "unpaid principal balance" or "interest." So, the words of the House and Senate versions are different, and the words of the

Senate version bar cramdowns on more kinds of debt than the words of the House would bar.

Conceding that the Senate language is broader than the House language, can one infer that the Senate intended to treat negative equity amounts as covered by "purchase-money security interests?" Yes. Representatives of the debtors and creditors must have known of the practice of rolling negative equity amounts from trade-ins into debts secured by purchase-money security interests on new cars. By 2005, as many as 38 percent of all new car purchasers rolled some part of the exiting debt on a trade-in into the new debt incurred to buy the new car.[2] This is not an obscure practice; it is commonplace and would have been well known to any informed debtor or creditor representative. By 2004, the practice was specifically permitted in the Motor Vehicle Sales Acts of at least 36 states.

It cannot be said that the cramdown provision on motor vehicles traveled below the Congress' radar. The topic was controversial; as shown in Section I.B. above, the provision was modified several times in different ways.[3] And, while it was one of the continuing points of dispute between the debtor and the creditor interests between

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[2] *See, e.g.,* FDIC Supervisory Insights*, The Changing Landscape of Indirect Automobile Lending,* June 23, 2005.

[3] *See., e.g.,* H.R. REP. No. 107-617 (2002) (Conf. Rep.).

1998 and 2004, ultimately, the language adopted reflected a compromise worked out over several years to gain the secured lenders' support.

Most importantly, the language chosen by Congress has a meaning found in practice and in state law (*see* Section III below). That law and practice show that a "purchase-money" interest reaches not only a car's cash price but also other amounts that may be folded into the total purchase price. That this language was chosen in lieu of the more restrictive language of the House buttresses the argument for a broad definition of "purchase-money." That Congress was apparently adopting Senator Abraham's approach to help car creditors gives further support for the broad reading as a federal definition. As recently stated by the United States Court of Appeals for the Sixth Circuit: "Based upon the legislative history, there is little doubt that the 'hanging-sentence architects intended only good things for car lenders and other lien holders.'" *In re Long*, 519 F.3d at 294 (6th Cir. 2008); *See also*, *GMAC v. Peaslee*, 373 B.R. 252, 261 (W.D.N.Y. 2007) ("By its terms, the hanging paragraph prohibits the bifurcation of any claim if the debt is secured by a PMSI. To adopt the Trustee's position would in effect undo [BAPCPA]").

II.
THE DEFINITIONS IN FEDERAL TRUTH IN LENDING LAW AND REGULATIONS SUPPORT FORD CREDIT

When Congress enacted BAPCPA in 2005, it is presumed to have known about other pertinent federal law governing purchase-money financing of motor vehicles.[4] The Truth in Lending Act (TILA) (15 U.S.C. §1600, *et seq.*) and the Act's regulation, Regulation Z (12 C.F.R. § 226), deal generally with the disclosures that are required in both consumer credit card debt (open ended credit) and purchase-money debt for items of personal property (closed end credit). Although that law does not give a definition as such of "purchase-money security interest," the law does explain the kind of disclosures that must be made in a purchase-money transaction that generates a purchase-money security interest.

In 1999, the Federal Reserve Board amended the Official Staff Interpretations of Regulation Z to clarify how purchase-money vehicle financers should disclose negative equity. Those amendments direct creditors to incorporate negative equity as a part of the "total sale price" of a new vehicle in a single financing transaction. 64 Fed. Reg. 16614-01, 16617 (adopting revisions to 12 C.F.R. Pt. 226, Supp. I, ¶ 18(j)-

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[4] *See Quality Tooling v. United States,* 47 F.3d 1569, 1584 (Fed. Cir. 1995) ("When Congress enacts legislation, it is presumed to know the pertinent law.").

3). The Staff Interpretations define the Total Sale Price to include negative equity as follows:

> *18(j) Total sale price.*
>
> 3. *Effect of existing liens.* When a credit sale transaction involves property that is being used as a trade-in (an automobile, for example) and that has a lien exceeding the value of the trade-in, the total sale price is affected by the amount of any cash provided. (See comment 2(a) (18)-3.) To illustrate, assume a consumer finances the purchase of an automobile with a cash price of $ 20,000. ***Another vehicle used as a trade-in has a value of $ 8,000 but has an existing lien of $ 10,000, leaving a $ 2,000 deficit that the consumer must finance.***
>
> *i.* ***If the consumer pays $ 1,500 in cash, the creditor may apply the cash first to the lien, leaving a $ 500 deficit, and reflect a down payment of $ 0. The total sale price would include the $ 20,000 cash price, an additional $ 500 financed under § 226.18(b) (2), and the amount of the finance charge.*** (emphasis added) Alternatively, the creditor may reflect a down payment of $ 1,500 and finance the $ 2,000 deficit. In that case, the total sale price would include the sum of the $ 20,000 cash price, the $ 2,000 lien payoff amount as an additional amount financed, and the amount of the finance charge.
>
> ii. If the consumer pays $ 3,000 in cash, the creditor may apply the cash first to extinguish the lien and reflect the remainder as a down payment of $ 1,000. The total sale price would reflect the $ 20,000 cash price and the amount of the finance charge. (The cash payment extinguishes the trade-in deficit and no charges are added under § 226.18(b) (2).) Alternatively, the creditor may elect to reflect a down payment of $ 3,000 and finance the $ 2,000 deficit. In that case, the total sale price would include the sum of the $

> 20,000 cash price, the $ 2,000 lien payoff amount as an additional amount financed, and the amount of the finance charge.

The highlighted portions of the quoted paragraphs show that the Federal Reserve intended that any negative equity amount be added to the cash price on the new vehicle to be shown as a single amount in the "total sale price" disclosure. Elsewhere, the Regulation (12 C.F.R. § 226.18(b)) requires that negative equity amounts be shown as part of the "Amount Financed." The implication to the buyer and to the creditor from this single disclosure of the "total price" and "amount financed," (i.e. amount secured) is that the negative equity will have the same status as the cash price of the new vehicle. Since the seller's security interest for the cash price of the new vehicle is indisputably a "purchase-money security interest," it follows that the Federal Reserve's direction to bundle the negative equity with the cash price is a direction to secure it with a "purchase-money security interest." By reference, Kansas has adopted this view as to the treatment of negative equity in automobile sales and financing transactions. *See* KAN. STAT. ANN. § 16a-6-117 and KAN. ADMIN. REGS. § 75-6-26 (adopting provisions of TILA and Regulation Z).

III.
STATE LAW, COMMERCIAL PRACTICE AND PUBLIC POLICY AFFIRM FORD CREDIT'S POSITION IN THIS CASE

A. The Uniform Commercial Code

Whether Congress intended a federal definition or a state definition, the state law is a rich source of help. First consider the breadth of the "purchase-money" umbrella under Article 9 of the UCC. Article 9 is the law of every state. The provisions at issue here have not been modified by Kansas or any other state. It is, therefore, tantamount to uniform federal law on this issue.

The Kansas UCC provides that "[a] security interest in goods is a purchase-money security interest . . . to the extent that the goods are purchase-money collateral with respect to that security interest." KAN. STAT. ANN. § 84-9-103(b)(1). "Purchase-money collateral" is defined as "goods . . . that secur[e] a purchase-money obligation incurred with respect to that collateral." *Id*. § 84-9-103(a)(1). A "purchase-money obligation" is defined, in turn, as "an obligation … incurred as all or part of the price of the collateral or for value given to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used. *Id*. § 84-9-103(a)(2).

Comment 3 to KAN. STAT. ANN. § 84-9-103 explains that "purchase-money obligation" reaches more than just the listed price of the item purchased:

> As used in subsection (a) (2), the definition of "purchase-money obligation," the "price" of collateral or the "value given to enable" includes ***obligations for expenses incurred in connection with acquiring rights in the collateral***, sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, administrative charges, expenses of collection and enforcement, attorney's fees, and other similar obligations.

> The concept of "purchase-money security interest" requires a close nexus between the acquisition of collateral and the secured obligation.

(Emphasis added). Notably, the phrase, "obligations of expenses incurred in connection with acquiring rights in the collateral" stands by itself; it is not followed by limiting words like "including" or "such as." It must, therefore, be regarded as a separate and independent obligation that may be part of the price of the collateral and therefore included in the purchase money obligation and purchase money security interest.[5]

The federal district court in *Peaslee* found the phrase "obligations for expenses incurred in acquiring rights" to be broad enough to include negative equity. As stated by the court:

> (I)n addition to the specific items listed in Comment 3, the comment also includes "obligations for expenses incurred in connection with acquiring rights in the collateral." Since the items following that term - sales taxes, duties, etc. - are not set off by the words "such as," "including," or a similar phrase, they are apparently not listed as examples of such

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[5] This is further illustrated by the fact that the list ends with the catch-all phrase, "and other similar obligations." This drafting convention demonstrates that the first item in the list—obligations for expenses incurred—is not limited to obligations that are similar to the listed items that follow. Otherwise, the first and last items in the list would be redundant. *See Smith v. Midland Brake, Inc.*, 180 F.3d 1154, 1161 (10th Cir. 1999) (in interpreting statutes, courts will "avoid a reading which renders some words altogether redundant" or "makes any part superfluous") (quoting *Gustafson v. Alloyd Co.*, 513 U.S. 561, 574 (1995) and *Fuller v. Norton*, 86 F.3d 1016, 1024 (10th Cir.1996)).

> expenses, but as additional components of the "price" of the collateral, or of "value given" by the debtor. It is not apparent why a refinancing of rolled-in negative equity on a trade-in as part of a motor vehicle sale could not constitute an "expense[ ] incurred in connection with acquiring rights in" the new vehicle. If the buyer and seller agree to include the payoff of the outstanding balance on the trade-in as an integral part of their transaction for the sale of the new vehicle, it is in fact difficult to see how that could ***not*** be viewed as such an expense.

373 B.R. at 258-59 (emphasis in original).

Comment 3, quoted above, adopts a "close nexus" test in determining whether charges and expenses are "purchase-money obligations" under Section 9-103. Current commercial practices, discussed below, recognize negative equity owed on a trade-in as a routine "expense incurred in connection with acquiring" the new vehicle, and the financing of the remaining debt on the trade-in has more than a "close nexus" to the acquisition of the new vehicle. Since buyers with negative equity on their trade-ins seldom have cash to pay off the amount owed, inevitably that amount must be financed by the creditor on the new vehicle or by some other creditor. So, in many cases, the "nexus" is so close that the new car cannot be acquired without financing from the new purchase-money creditor to retire the negative equity. As stated by the 11th Circuit in *In re Graupner*:

> We believe there is such a "close nexus" between the negative equity in Debtor's trade-in vehicle and the purchase of his new vehicle. The financing was part of the

> same transaction and may be properly regarded as a "package deal." Payment of the trade-in debt was tantamount to a prerequisite to consummating the sales transaction, and utilizing the negative equity financing was a necessary means to accomplish the purchase of the new vehicle. As the district court held in affirming the bankruptcy court, the negative equity was an "integral part of," and "inextricably intertwined with," the sales transaction. To hold otherwise would not be a fair reading of the UCC.

537 F.3d at 1295, 2008 WL 2993570, at 7.

B. Commercial Practice and Public Policy

Since all decisions interpreting commercial law have the capacity to facilitate or impair commercial activity, courts should be sensitive to commercial practice when they are interpreting federal and state statutes. The commercial practice, in this case, supports the proposition that including negative equity into a new contract creates a purchase-money security interest. So far as one can tell from reading the cases, the law review literature, and the contracts, the consumer and creditor parties to these transactions treat the negative equity portion of the new debt in exactly the same way as every other part of the debt. They regard it as secured by the newly sold vehicle in exactly the same way as every other part of the debt. Presumably, the Fords chose this mode of financing their debt over other alternatives because the 3.9% rate they were

charged in the transaction was far below the rate they would have paid had they borrowed the money on an unsecured basis from a bank or finance company.

In evaluating the commercial practice that underlies these cramdown cases, one should remember that these debtors are always employed (otherwise they would not be in Chapter 13), and are always the owners of vehicles. These cases do not involve powerless consumers who must accept anything a creditor offers. Here, the dealer's financing offer was knowingly, and quite understandably, accepted by the Fords.

The Fords traded in their used vehicle on a new 2007 Ford Pickup truck; they bought the new vehicle just 4 months before they filed in Chapter 13. The dealer's willingness to finance the negative equity of $7,200 on their used vehicle enabled them to complete the deal as they chose. It undoubtedly enabled them to finance the $7,200 advance at a better annual percentage rate than they could have obtained elsewhere. In any case, it facilitated their purchase of the new vehicle that they were under no obligation to purchase.

It is a basic principle of American commercial law – learned from Karl Llewellyn, father of the Uniform Commercial Code – that the law should follow practice, not the other way around. This principle is particularly powerful where the practice appears to have been freely chosen by parties who had other alternatives. *See* KAN. STAT. ANN. § 84-1-102(1) and (2)(b) ("UCC to be liberally construed to promote

its underlying purposes and policies including "to permit the continued expansion of commercial practices through custom, usage and agreement of the parties").

CONCLUSION

The words, the statutory history, the Congressional intent, the analogies to the federal Truth in Lending law, and the breadth of the "purchase-money" umbrella under Kansas Uniform Commercial Code direct this Court to affirm the decision of the Bankruptcy Court.

Respectfully submitted,

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As required by FED. R. APP. P. 32(a)(7)(C), I certify that this brief is proportionally spaced and contains 5,596 words.

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DATED September 30, 2008

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