

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION

ENTERED
DEC 15 2003
U.S. BANKRUPTCY COURT
MDNC - YHP

IN RE:)
)
Richard Shane Ware, d/b/a) Case No. 02-12262C-7G
Ware Racing Enterprises,)
)
Debtor.)
_____)
)
Everett B. Saslow, Jr.,)
Trustee in Bankruptcy for)
Richard Shane Ware,)
)
Plaintiff,)
)
v.) Adversary No. 03-2003
)
Porsche Financial Services,)
)
Defendant,)
)
and)
)
Foreign Cars International,)
LLC,)
)
Intervenor.)
)

MEMORANDUM OPINION

This adversary proceeding came before the court on August 19, 2003, for hearing upon cross-motions for summary judgment filed by the Plaintiff and the Defendant. Everett B. Saslow, Jr. appeared on behalf of the Plaintiff, Christopher L. White appeared on behalf of the Defendant and John H. Small appeared on behalf of the Intervenor. Having considered the motions, the materials submitted in support of and in opposition to the respective motions, the briefs filed by the parties and the arguments of counsel, the court

finds and concludes as follows:

JURISDICTION

The court has jurisdiction over the subject matter of this proceeding pursuant to 28 U.S.C. §§ 151, 157 and 1334, and the General Order of Reference entered by the United States District Court for the Middle District of North Carolina on August 15, 1984. The motions for summary judgment which are now before the court are matters which this court may hear and determine.

PROCEDURAL BACKGROUND

On July 29, 2002, a petition for involuntary bankruptcy was filed against the Debtor, Richard Shane Ware. On August 30, 2002, an order for relief under Chapter 7 was entered. However, on September 11, 2002, Debtor's case was converted to one under Chapter 11 upon the motion of the Debtor. The case remained under Chapter 11 until March 17, 2003, when an order was entered converting the case to Chapter 7 and appointing Everett B. Saslow, Jr. as Chapter 7 Trustee ("the Trustee").

On January 13, 2003, while this case was proceeding as a Chapter 11 case, the Debtor filed a complaint against the Defendant, Porsche Financial Services, seeking to avoid a security interest claimed by the Defendant in a 2002 Porsche automobile owned by the Debtor. On April 21, 2003, following the conversion of this case to one under Chapter 7, an order was entered substituting the Trustee as Plaintiff and allowing an amendment to

the complaint. The complaint, as amended, alleges that the Defendant's security interest in the 2002 Porsche automobile was not perfected until September 5, 2002, and that such perfection occurred during the pendency of Debtor's bankruptcy case and without obtaining relief from the automatic stay. The Plaintiff alleges that the security interest and lien claimed by the Defendant therefore is avoidable under § 362 and under § 544 and § 549 of the Bankruptcy Code as having been perfected post-petition and without obtaining relief from the automatic stay or court approval.

FACTUAL BACKGROUND

On June 29, 2002, the Debtor entered into a retail installment sales contract ("the retail contract") with Foreign Cars International, LLC ("Foreign Cars") for the purchase of a 2002 Porsche automobile from Foreign Cars. Under the retail contract, the Debtor made a down payment of \$1,000.00 and financed the sum of \$158,546.80 at 9.75% which the Debtor agreed to repay by means of 59 consecutive monthly payments of \$2,315.95 each and a final payment of \$81,799.20. The retail contract also granted a security interest in the Porsche to Foreign Cars in order to secure the Debtor's obligation to make these payments. The retail contract was immediately assigned by Foreign Cars to Porsche Financial Services pursuant to a dealer agreement between Porsche Financial Services and Foreign Cars.

On June 29, 2002, Foreign Cars also prepared and had the Debtor sign a Division of Motor Vehicle title application form known as a MVR-1, another document known as a retail order and invoice and an odometer disclosure statement. The title application listed the Debtor as owner of the Porsche, listed Porsche Financial Services as the first lienholder and contained a request signed by the Debtor that the Division of Motor Vehicles issue a certificate of title for the Porsche.

At the time of the transaction involving the 2002 Porsche, Foreign Cars was a participating dealer under an Electronic Dealer Agreement for the N.C. On-Line Program with the North Carolina Division of Motor Vehicles. This agreement authorized Foreign Cars to deliver title applications and to pay registration and title fees to the Division of Motor Vehicles by transmitting such applications and fees electronically into the Division's database in Raleigh. According to Foreign Cars, its representative attempted to transmit the application for the 2002 Porsche to the Division by electronic means on July 11, 2002, but was unable to do so because of a block or stop that was in place with respect to the Debtor which prevented access to the Division's database. Actual delivery of the application and required fees did not occur until September 5, 2002, when the application and fees, in fact, were transmitted electronically to the Division of Motor Vehicles by Foreign Cars. Thus, although the sale transaction occurred on

June 29, 2002, and all of the documents are dated June 29, 2002, the title application and the other title registration documents and required fees were not received in Raleigh by the Division of Motor Vehicles until September 5, 2002. Upon receipt of the title registration documents, the Division of Motor Vehicles issued a certificate of title for the Porsche showing the Debtor as owner and Porsche Financial Services as first lienholder. The certificate of title is dated September 14, 2002, and the date of the lien is shown on the certificate of title as being September 5, 2002, the date on which the title registration documents were received in Raleigh by the Division of Motor Vehicles. The issuance of the certificate of title and the entry of the lien on the certificate of title occurred while Debtor's bankruptcy case was pending and without obtaining authorization from the bankruptcy court or relief from the automatic stay which was in effect pursuant to § 362 of the Bankruptcy Code.

THE MOTIONS FOR SUMMARY JUDGMENT

The Plaintiff contends that it is undisputed that the application for notation of security interest was not delivered to the Division of Motor Vehicles until September 5, 2002, which was more than 20 days after June 29, 2002, the date of the security agreement. Based upon N.C. Gen. Stat. § 20-58.2, the Plaintiff contends that a security interest in a motor vehicle is perfected as of the date the application for notation of security interest is

delivered to the Division of Motor Vehicles unless the application for notation of security interest with the required fee is delivered to the Division of Motor Vehicle within 20 days after the date of the security agreement. Since the September 5 delivery date in the present case was more than 20 days after the date of the security agreement, the Plaintiff concludes that the lien in favor of the Defendant was not perfected until September 5, and, therefore, is avoidable as a matter of law pursuant to § 544 and § 549 of the Bankruptcy Code.

In opposing the Plaintiff's motion for summary judgment and arguing that it is entitled to summary judgment, the Defendant relies upon the fact that Foreign Cars was a participating dealer under an Electronic Dealer Agent Agreement for the N.C. On-Line Program with the Division of Motor Vehicles. The Defendant contends that under the Electronic Dealer Agent Agreement Foreign Cars was a title service agent for the Division of Motor Vehicles and that receipt of the application for notation of security interest and the required fees by Foreign Cars from the Debtor on June 29, 2002, amounted to delivery of the application and the fees to the Division of Motor Vehicles since Foreign Cars was a title service agent for the Division. Defendant concludes that perfection of its security interest under N.C. Gen. Stat. § 20-58.2 therefore occurred on June 29, 2002.

DISCUSSION

I. The Perfection of the Security Interest Occurred on September 5, 2002.

The record before the court includes a copy of the certificate of title record on file at the Division of Motor Vehicles for the 2002 Porsche involved in this case. This record reflects that according to the records of the Division of Motor Vehicles, the title application from the Debtor for the 2002 Porsche and the required fees and tax were received by the Division of Motor Vehicles on September 5, 2002. The fact that the title application and fees were received by the Division of Motor Vehicles on September 5, 2002, is confirmed by the affidavit of Diane Johnson, Director of Vehicle Registration for the North Carolina Department of Motor Vehicles. According to Ms. Johnson's affidavit, "[p]er the North Carolina Division of Motor Vehicles' records, the required application and fees for the issuance of a title and the notation of a security interest in favor of Porsche Financial Services on the 2002 996 Porsche Turbo, Vehicle Identification Number WP0AB29952S687138, were not submitted to the Division of Motor Vehicles until September 5, 2002." It is undisputed that following the receipt of the application and fees on September 5, 2002, the Division of Motor Vehicles processed the application and issued a certificate of title for the Porsche. A copy of this certificate of title also is a part of the record before the court. The certificate of title lists Porsche Financial Services as the

first lienholder on the Porsche and shows the date of the lien as being September 5, 2002.

In showing the date of the lien as being September 5, 2002, the Division merely followed the mandate of N.C. Gen. Stat. § 20-58.2, the statute which is controlling in North Carolina in determining the date on which a lien on a motor vehicle is perfected. N.C. Gen. Stat. § 20-58.2 provides:

§ 20-58.2. Date of perfection.

If the application for notation of security interest with the required fee is delivered to the Division within 20 days after the date of the execution of the security agreement, the security interest is perfected as of the date of the execution of the security agreement. Otherwise, the security interest is perfected as of the date of delivery of the application to the Division.

It is undisputed that the date of the execution of the security agreement in the present case was June 29, 2002. Since the application was not delivered to the Division of Motor Vehicles until September 5, 2002, it follows that the application was not delivered to the Division of Motor Vehicles within 20 days after the execution of the security agreement and that there would be no relation back to the date of the Security Agreement under the statute. Instead, under the statute, the security interest of Porsche Financial Services was perfected as of the date of delivery of the application to the Division, i.e., September 5, 2002. See Bank of Alamance v. Isley, 74 N.C. App. 489, 492-93, 328 S.E.2d

867, 870 (1985). See also In re Millerburg, 61 B.R. 125, 127 (Bankr. E.D.N.C. 1986). Contrary to Defendant's assertion, none of the foregoing facts are in dispute. The affidavits of Deborah E. Norris, an employee of Foreign Cars, which are relied upon by the Defendant and the Intervenor, do not dispute the fact that the application and fees were not received by the Division of Motor Vehicles until September 5, 2002. The affidavits of Ms. Norris state only that she attempted to transmit the application and fees electronically on July 11, 2002, i.e., that she "initialized" a transmission. However, her second affidavit reflects quite clearly that her effort to deliver the application and fees to the Division of Motor Vehicles on July 11, 2002, was not successful because, according to Ms. Norris, there was a "block" in place "that prevented any registration or titling for Mr. Ware" The result is that it is undisputed that the application regarding the Porsche was first received by the Division of Motor Vehicles on September 5, 2002, some 68 days after the execution of the security agreement.

Contrary to Defendant's assertion, September 5, 2002, as the date of delivery of the application and fees to the Division of Motor Vehicles is not altered by the fact that Foreign Cars was a participating dealer under an Electronic Dealer Agent Agreement for the N.C. On-Line Program with the Division of Motor Vehicles. Such an agreement allows a dealership to be on-line with the Division of

Motor Vehicles in Raleigh and to transmit their own applications to Raleigh electronically rather than having to submit them to a local License Plate Agency. As explained by the Division's Director of Vehicle Registration, the On-Line Program allows a participating dealership to have license plates and stickers stocked in their office and to enter the title information into the Division's database in Raleigh, after which the hard copy of the application is forwarded to the Division's Raleigh office for retention and quality checks. However, nothing in the Agreement suggests that certificates of title no longer will be issued in Raleigh or that a participating dealer is not required to submit title applications and fees to Raleigh for the issuance of certificates of title and the registration of security interests. In fact, the Electronic Dealer Agent Agreement specifically provides that standards for operation as a Participating Dealer have been established by the Division which "include all rules, regulations and procedures established by the Division as well as those established by Executive Order and are to be considered a part of this Agreement." The affidavit of Diane Johnson discusses some of the procedures and guidelines established by the Division for participating dealers. According to these procedures, participating dealers in the On-Line Program are not authorized to process applications where a block prevents the dealer from entering the application electronically into the Division's database. If such a block is in place and the

application cannot be delivered in Raleigh electronically, the proper procedure is for the participating dealer to take the application to a local License Plate Agency for processing by the License Plate Agency or, if the application cannot be processed locally, to have the local License Plate Agency place a dated refusal stamp on the application reflecting that it was submitted but could not be processed. Defendant's affidavits reflect that Foreign Cars failed to comply with the required procedures. According to these affidavits, Foreign Cars attempted to deliver the application to the Division's Raleigh office electronically but was unable to do so because a block was in place that prevented delivery of the application into the Division's database. At that point, Foreign Cars International knew or should have known that the application for the Porsche had not been delivered to the Division of Motor Vehicles as required in order to obtain the issuance of a certificate of title and the registration of the security interest of Porsche Financial Services that would relate back to the date of the security agreement. The procedure required at that point in order to register a security interest that would relate back was to take the application and required fees to a local License Plate Agency for processing, which admittedly was not done by Foreign Cars. Instead, Foreign Cars delayed for some 68 days in order to transmit the application and fees to the Division's Raleigh office electronically. The result was that the

application was received by an authorized office of the Division of Motor Vehicles for the first time on September 5, 2003. The affidavits of Ms. Norris do not create an issue as to any of the foregoing facts. While her affidavit does state that the Division of Motor Vehicle never informed Foreign Cars that Foreign Cars was not authorized to process a lien application where stops or blocks were in place or that the Division ever instructed Foreign Cars that such applications were to be submitted to the local License Plate Agency for processing or further instructions, such statements do not create a material issue of fact. Under the agreement between Foreign Cars and the Division of Motor Vehicles, Foreign Cars agreed that the regulations and procedures established by the Division are part of the agreement and Foreign Cars further agreed to abide by all such regulations and procedures. If, as stated by Ms. Norris in her affidavit, the manuals in the possession of Foreign Cars did not contain adequate instructions on what Foreign Cars was to do when a block or stop was encountered, it was incumbent upon Foreign Cars to ascertain the proper procedure and to follow such procedure. The failure of Foreign Cars to do so does not alter the undisputed fact that such procedure was in place and that under its agreement Foreign Cars was obligated to follow such procedure if it wished to register the security interest of Porsche Financial Services in a manner in which it would relate back to the date of the security agreement.

The undisputed facts in the record establish that Foreign Cars failed to do so and that as a result, the Division of Motor Vehicles, in accordance with its procedures, determined that the application and fees were first delivered to the Division on September 5, 2002, and that September 5, 2002, therefore was the date of the perfection of the security interest.

II. The Lien Is Avoidable.

Under § 362(a)(4) of the Bankruptcy Code, an involuntary petition filed under § 303 operates as a stay of "any act to create, perfect, or enforce any lien against property of the estate. . . ." The involuntary petition against the Debtor was filed on July 29, 2002, and was followed by an order for relief that was entered on August 30, 2002. Hence, when Foreign Cars transmitted the title application to the Division of Motor Vehicles on September 5, 2002, in order to perfect the security interest of Porsche Financial Services, the automatic stay was in effect and prohibited any act to perfect a lien against the 2002 Porsche which had been purchased by the Debtor and was property of the estate in his bankruptcy case. Consequently, perfection of Porsche Financial Service's lien on September 5, 2002, was in violation of the automatic stay. See In re Prine, 222 B.R. 610, 612 (Bankr. N.D. Iowa 1997).

There is a split of authority as to whether action that is taken in violation of the automatic stay is void or merely

voidable, although it appears that the weight of authority holds that such action is voidable rather than void. See Khozai v. Resolution Trust Corp., 177 B.R. 524, 526-27 (E.D. Va. 1995). See also Winters v. George Mason Bank, 94 F.3d 130, 136 (4th Cir. 1996) (noting the split in authority and declining to address the issue). The bottom line in this proceeding is that the Plaintiff is entitled to a judgment in his favor because he is entitled to prevail under either line of authority, i.e., the security interest and lien of Porsche Financial Services was either void ab initio or is voidable and should be adjudged void as a result of having being perfected in violation of the automatic stay.¹

Defendant's reliance upon § 362(b)(3) and § 546(b) of the Bankruptcy Code is misplaced. Under § 362(b)(3), the automatic

¹The Plaintiff also is entitled to prevail under § 544 of the Bankruptcy Code. Under § 544(a)(1), one of the positions occupied by the Plaintiff as a Chapter 7 bankruptcy trustee is that of judicial lien creditor. Prior to Plaintiff's appointment as Chapter 7 Trustee, the Debtor, as a Chapter 11 debtor-in-possession likewise occupied the position of a judicial lien creditor pursuant to § 544(a)(1). See § 1107(a) and 7 COLLIER ON BANKRUPTCY ¶ 1107.03[4] (15th ed. rev. 2003) ("As of the commencement of the case, the debtor in possession has the power to avoid the kinds of transfers that a trustee may avoid pursuant to the avoiding powers."). Under North Carolina law, a judicial lien creditor has priority over an unperfected lien on personal property. See In re Millerburg, 61 B.R. 125, 128 (Bankr. E.D.N.C. 1986). Since the security interest of Porsche Financial Services was unperfected prior to September 5, 2002, the hypothetical judicial lien under § 544(a)(1) which attached prior to that date, takes priority over the subsequently perfected security interest of Porsche Financial Services. Id. See also First Nat. Bank of Denver v. Turley, 705 F.2d 1024, 1027 (8th Cir. 1983) ("we conclude that a creditor must have a perfected security interest in its collateral at the time of a bankruptcy in order to defeat the interest of the trustee").

stay does not apply to "any act to perfect, or to maintain or continue the perfection of an interest in property to the extent that the trustee's rights and powers are subject to such perfection under § 546(b)." Section 546(b)(1), in turn, provides that the rights and powers of a trustee under sections 544, 545 and 549 are subject to any generally applicable law that (A) permits perfection of an interest in property to be effective against an entity that acquires rights in such property before the date of perfection; or (B) provides for the maintenance or continuation of perfection of an interest in property to be effective against an entity that acquires rights in such property before the date on which action is taken to effect such maintenance or continuation. However, "[t]he legislative history of § 546(b) clearly states that the 'rights granted to a creditor under this subsection prevail over the trustee only if the transferee has perfected the transfer in accordance with applicable law, and that perfection relates back to a date which is before the commencement of a case.'" In re Ridley, 50 B.R. 51, 53 (Bankr. M.D. Tenn. 1985) (citing H.R. Rep. No. 95-595, at 371 (1979)). In the present proceeding, the title application and fees were not delivered to the Division of Motor Vehicles until September 5, 2002, which was more than the twenty days allowed under N.C. Gen. Stat. § 20-58.2. Since the Defendant did not comply with the relation back provision of the North Carolina statute, § 546(b) is not operative and the Trustee's

rights under § 362 and § 544 therefore are not subject to the post-petition perfection by the Defendant. See In re Baxter, 2002 WL 485643, 3 (Bankr. N.D. Iowa).

CONCLUSION

In accordance with the foregoing, the court concludes that the Plaintiff's motion for summary judgment should be granted, that Defendant's motion for summary judgment should be denied and that a summary judgment should be entered in this adversary proceeding adjudging that the security interest and lien of Porsche Financial Services is void and of no effect and that the Plaintiff is entitled to the proceeds realized from the sale of the 2002 Porsche automobile referred to in the complaint.

This 15 day of December, 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION

ENTERED
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IN RE:)
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Richard Shane Ware, d/b/a)
Ware Racing Enterprises,)
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Debtor.)

Case No. 02-12262C-7G

Everett B. Saslow, Jr.,)
Trustee in Bankruptcy for)
Richard Shane Ware,)
)
Plaintiff,)

v.)

Adversary No. 03-2003

Porsche Financial Services,)
)
Defendant,)

and)

Foreign Cars International,)
LLC,)
)
Intervenor.)

JUDGMENT

In accordance with the memorandum opinion filed contemporaneously herewith, it is ORDERED, ADJUDGED AND DECREED as follows:

- (1) Defendant's motion for summary judgment is denied;
- (2) Plaintiff's motion for summary judgment is granted and judgment is hereby entered in favor of the plaintiff;
- (3) The security interest and lien asserted by Porsche Financial Services in and upon the 2002 Porsche automobile

referred to in the complaint is adjudged to be void and of no effect; and

(4) Plaintiff shall have and recover the proceeds realized from the sale of the 2002 Porsche automobile.

This 15 day of December, 2003.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge