The Record System, Perfection of a Security Interest and Subsequent Purchasers or Creditors

Leon R. Hetherington

Follow this and additional works at: https://scholarship.law.uwyo.edu/wlj

Recommended Citation
Leon R. Hetherington, The Record System, Perfection of a Security Interest and Subsequent Purchasers or Creditors, 18 Wyo. L.J. 269 (1964)
Available at: https://scholarship.law.uwyo.edu/wlj/vol18/iss3/10

This Comment is brought to you for free and open access by Law Archive of Wyoming Scholarship. It has been accepted for inclusion in Wyoming Law Journal by an authorized editor of Law Archive of Wyoming Scholarship.
THE RECORD SYSTEM, PERFECTION OF A SECURITY INTEREST AND SUBSEQUENT PURCHASERS OR CREDITORS

The motor vehicle record system in Wyoming is based principally on three statutes. These are the registration, certificate of title, and Wyoming Uniform Commercial Code Statutes.¹

The registration statute is primarily a revenue measure whereby owners of motor vehicles are required annually to register their vehicles, pay the registration fees and obtain registration (license) plates. A certificate of title is a prerequisite to registration.² A registration receipt is presented to the owner showing his name, the manufacturer or dealer and a description of the vehicle. No liens or encumbrances are noted on the receipt.³ Registration is not required of non-resident owners until the vehicle has been in the state for ninety (90) days, with certain enumerated exceptions.⁴

The certificate of title statute provides in substance that every owner of a motor vehicle must obtain an official certificate of title from the state board of equalization or any county clerk before the motor vehicle can be registered in Wyoming and that all registered motor vehicles must have a certificate of title prior to operation on the highways. The application must set forth any liens or encumbrances upon the vehicle and must be under oath.⁵ Upon being satisfied that the applicant is the owner of the vehicle, the county clerk will issue the certificate of title which will show among other things all liens or encumbrances on the vehicle.⁶ The certificate is good as long as the vehicle is owned by the same person⁷ and is required to be recorded by the county clerk and open to public inspection.⁸

Upon passage of the original Uniform Commercial Code provision,⁹ considerable confusion arose as to whether or not filing of a security agreement or financing statement¹⁰ was necessary to perfect a security interest in motor vehicles. This was due in part to the wording of Wyo. Stat. Sec. 34-9-302 (1957) (Supp. 1963), Laws 1961, ch. 219, Sec. 9-302, and in part to other statutes which were not repealed when the Uniform Commercial

---

The 1963 legislature attempted to eliminate the ambiguity by amending several statutes and repealing others. Wyo. Stat. Sec. 31-37 (f) (1957) of the certificate of title statutes which required filing of an encumbrance instrument concurrently with delivery of the certificate of title with the encumbrance noted thereon was repealed, but nearly the same language and procedure was included in the Uniform Commercial Code provision which was passed. Wyo. Stat. Sec. 10-104, Laws 1961, Ch. 219, Sec. 10-104, which was redundant, was repealed and Wyo. Stat. Sec. 31-40 (1957) of the certificate of title statutes pertaining to duplicate certificates was rewritten.

The mechanics for perfecting a security interest in a motor vehicle required to be licensed are provided by Wyo. Stat. Sec. 34-9-302 (4) (1957) (Supp. 1963). In general, the secured party must file a financing statement or security agreement in the county clerk’s office and the security interest must be endorsed by the clerk on the certificate of title. If the vehicle is new and is sold, the dealer must deliver the security agreement and the other necessary papers for a certificate of title to the county clerk’s office. The clerk will file the security agreement, make out a certificate of title, and endorse the security interest on the certificate of title.

Of primary importance is the relationship of the certificate of title statutes to the Uniform Commercial Code in regard to perfecting a security interest and the effects on subsequent purchasers or creditors.

In *Sterling Acceptance Co. v. Grimes*, the plaintiff brought an action in replevin against purchasers of a new automobile which was purchased in the ordinary course of business from the inventory of an auto dealer. Prior to the sale, a security agreement had been entered into between the plaintiff and the dealer covering new and used vehicles and proceeds from the sale thereof. The security agreement was filed pursuant to the Pennsylvania Uniform Commercial Code statutes. Under the Motor Vehicle Code, no regular certificate of title could come into being for a new vehicle until a sale thereof, but a dealer was permitted to obtain a dealer’s certificate of title. Such a dealer’s certificate of title was obtained for the new automobile involved and the encumbrance was noted thereon pursuant to a Vehicle Code statute which provided for notation of liens on certificates of title and, as such, would be notice to creditors, subsequent mort-

---

gagees and purchasers. The dealer, upon sale of the vehicle to the defendant, did not remit the proceeds to the plaintiff. The defendant purchaser contended that, under the Uniform Commercial Code, Section 9-307, a purchaser in the ordinary course of business takes free of perfected security interests. Although not clear, the plaintiff's contention apparently was that the Uniform Commercial Code did not apply because of the notation on the dealer's certificate of title. The court held that where the Uniform Commercial Code and the Vehicle Code deal with the same subject matter and the statutes are in pari materia they should be considered concurrently whenever possible and effect should be given to both. With this basis, the court went on to say that inventory lienors cannot defeat rights of buyers in the ordinary course of business by noting the encumbrance on a dealer's certificate of title which was not required to be obtained and that upon sale of a new auto by a dealer in the ordinary course of business, the buyer takes free of perfected security interests even if the buyer knows of the terms of the security agreement.

In Wyoming, like Pennsylvania, a certificate of title for a new car does not come into existence until the new car is first sold. Apparently then, under Wyo. Stat. Sec. 9-302 (4) (1957), (Supp. 1963), it would be sufficient in order to perfect an inventory security interest in a new car to merely file the financing or security agreement.

Taylor Motor Rental, Inc. v. Associates iDiscount Corporation, Inc. is another case where the contention of a buyer in the ordinary course of business was asserted. Here, the defendant perfected a security interest according to the then existing provisions of the Uniform Commercial Code in an auto purchased by McCurry Motors, Inc. McCurry Motors in turn sold the auto to the plaintiff corporation (appellant). The defendant, not being paid for the auto from the proceeds of the sale, seized the auto from the plaintiff and the plaintiff sued to replevy. The facts disclosed that the plaintiff was a corporation with interlocking officers, shareholders, and directors with McCurry Motors and that Fred McCurry managed both corporations and acted for both in applying for the certificate of title in the name of the plaintiff. This relationship was sufficient to deny the plaintiff the status of a purchaser in the ordinary course of business.

Three Wyoming problems concerning the 1963 procedure for perfecting a security interest are apparent. First, it is not a uniform provision. Wyoming has departed completely from the official alternative of Section 9-302 of the 1958 Uniform Commercial Code's official text, resulting in

non-uniformity, a primary purpose of the Code, which will probably lead to anomalous decisions causing more trouble than cure.\textsuperscript{24}

Second, the system requires a dual filing which is cumbersome, non-uniform, and provides a further chance for error. Simplicity in the law of security transactions plus uniformity among the states are the two main reasons for having uniform laws. The purpose behind a certificate of title law is to reach the point where reliance can be had upon the certificate of title as to the rights of various persons in the vehicle.

The Uniform Commercial Code's 1958 official text in substance provides two alternatives to filing a financing statement for states which have enacted certificate of title laws requiring the indication of all security interests on the certificate of title. The second alternative\textsuperscript{25} made an exception to notation on the certificate of title for inventories held for sale. The reason for such an exception is that to require the notation on each certificate for every motor vehicle would be an unreasonable burden. Filing the financing statement would be sufficient for motor vehicles held in inventory. The Wyoming legislature in adopting Wyo. Stat. Sec. 9-302 (4) (1957) (Supp. 1963), has made no mention of situations involving a dealer's inventory.

A preliminary question is whether a motor vehicle held in the inventory of a dealer for sale is a “motor vehicle required to be licensed,” as Wyo. Stat. Sec. 9-302 (4) (1957) (Supp. 1963), pertains only to such vehicles. No specific definition for this phrase is present in either the Uniform Commercial Code or the Wyoming Motor Vehicle Code. No attempt will be made to speculate as to what the Wyoming courts will hold if this question is presented, but several Motor Vehicle Code statutes do exist which may be used to judicially interpret this phrase.\textsuperscript{26}

If a motor vehicle held by a dealer in inventory is one not “required to be licensed,” then apparently Wyo. Stat. Sec. 9-302 (1) (1957) (Supp. 1963), will control, in which case filing alone without notation on the certificate of title will be sufficient to perfect the security interest unless the particular arrangement comes within one of the specifically enumerated

\textsuperscript{24} See article, Does Article 9 of the Uniform Commercial Code Achieve its Purpose? Coogan and Albrecht, Uniform Commercial Code Co-ordinator, Annotated, p. 631, Matthew Bender & Company (1963).

\textsuperscript{25} Wyo. Stat. § 34-9-302 (3) (1957) (Supp. 1963) provides “The filing provisions of this Article do not apply to a security interest subject to a statute. (a) . . . Alternative B-(b) of this state which provides for central filing of security interests in such property, or in a motor vehicle which is not inventory held for sale for which a certificate of title is required under the statutes of this state if a notation of such a security interest can be indicated by public official on a certificate or a duplicate thereof.”

exceptions to filing.\textsuperscript{27} If a motor vehicle held by a dealer in inventory is deemed to be a motor vehicle "required to be licensed," then the statute\textsuperscript{28} says that both filing and notation on the certificate of title is necessary for perfection of a security interest and no exception is made for the dealer-inventory situation. Kentucky and Pennsylvania courts have indicated their feeling on this question in the cases of Lincoln Bank and Trust Co. v. Queenan\textsuperscript{29} and Howarth v. Universal C.I.T. Credit Corporation.\textsuperscript{30}

In the Lincoln Bank case,\textsuperscript{31} the court by its holding, created a dual filing system for Kentucky similar to the method which Wyoming arrived at by legislation\textsuperscript{32} but made an exception to filing in the case of a dealer's inventory. At the present time, Kentucky and Wyoming are the only Code states requiring a dual filing system to perfect a security interest in a motor vehicle. The Kentucky case is important in Wyoming, not because the case required a dual filing system, but because of the dicta discussed after the conclusion that a dual system was established. The court said, "We may judicially notice that the inventory of any dealer in motor vehicles is likely to include used vehicles. . . . Literally, therefore, KRS 186.195\textsuperscript{33} (statute requiring liens to be noted on registration receipt held to be equivalent to a certificate of title) would apply. . . . However, one of the important reforms effected by the Code in the field of security financing is the concept of a floating lien on shifting collateral, whereby a security interest may be created by one agreement and perfected by one notice covering a changing inventory. Each item of the inventory is automatically freed of the security interest as it goes into the hands of a buyer in the ordinary course of business." The court then said that a statute requiring dual filing is incompatible where the financing statement covers an inventory of vehicles that are not required by the Code to be identified individually and that notation of a lien was not required to perfect a security interest in a dealer's inventory.

The Howarth case\textsuperscript{34} involved an action by Howarth, a trustee in bankruptcy of a car dealer, to recover from a finance company the value of property transferred to it within four months of bankruptcy. Among other automobiles, there were eleven used vehicles covered by a Trust Receipts agreement and a filed financing statement. The trustee contended that the security interest was not perfected unless the lien was noted on the certificate of title to the used cars. Section 203 (b) of the Pennsylvania

\begin{itemize}
\item \textsuperscript{29} 344 S.W. 2d 383 (Ky. 1961); 60 Mich. L. Rev. 242; Annot., Boston College Ind. and Com. L. Rev. 43 (Fall, 1961) and Uniform Commercial Code Cordinator, Annotated, p. 311, Matthew Bender & Co. (1963); Whiteside & Lewis, Kentucky's Commercial Code—Some Initial Problems in Security, 50 Ky. L.J. 61-85 (1961).
\item \textsuperscript{30} 203 F. Supp. 279 (W.D. Pa. 1962).
\item \textsuperscript{31} Lincoln Bank & Trust Co. v. Queennan, 344 S.W. 2d 383 (Ky. 1961).
\item \textsuperscript{33} Ky. Rev. Stat. § 186-195 (1962).
\item \textsuperscript{34} Howarth v. Universal C.I.T. Credit Corp., 203 F. Supp. 279 (W.D. Pa. 1962).
\end{itemize}
Motor Vehicle Code provided a method whereby a person could show a lien on the certificate of title. Section 207 (c) provided that a dealer was not required to apply for a certificate of title for cars in inventory. The court in holding for the finance company said, "We cannot perceive any good reason why a lender engaged in wholesale financing cannot perfect a valid security interest in used cars by the same method he employs to perfect a valid security interest in new cars." As to new cars, a security interest could be perfected by filing only, as no certificate of title for a new car came into existence until the sale thereof. In striking down such a dual filing requirement as contended for, the court further commented that such a dual filing arrangement would require a dealer's prospective creditor to demand an inspection of the dealer's certificate of title to each used car in inventory as well as a search of the filed records and that such an arrangement would also require that a lender who engages in wholesale financing of used cars would have to insist that the dealer obtain a new certificate of title for each used car acquired.

The third problem, and a good example of the results of a departure from the suggested Code provisions, is the place of filing requirements. Wyo. Stat. Sec. 9-302 (4) (1957) (Supp. 1963), says to perfect a security interest in a motor vehicle required to be licensed, filing must be in the office of the county clerk of the county in which said vehicle is located. Wyo. Stat. Sec. 9-401 (c) (1957) (Supp. 1963), the general place of filing statute, says that the proper place to file in order to perfect a security interest is in the office of the county clerk for the county in which the debtor has his principal place of business, if any, otherwise his residence. If the debtor is not a resident, then the place to file is in the office of the secretary of state of the state of Wyoming. Although Wyo. Stat. Sec. 9-302 (4) (1957) (Supp. 1963), pertains to a specific type of goods and would probably control, the provisions are ambiguous and should be cleared up. In the Matter of Babcock Box Co. illustrates the problem created where a filing is required in two places. Here, the Massachusetts statute covering the place of filing requirements to perfect a security interest required dual filing, first in the office of the state secretary and second in the office of the clerk of the town where the debtor had his place of business. The secured party filed a financing statement with the secretary of state, but did not file with the city clerk. This error was held to be sufficient to defeat the

39. Finance Company not dealer must properly record lien, Joel Strickland Enterprises, Inc. v. Atlantic Discount Co., 137 So. 2d 627 (Fla. 1962); see also Matter of Shepler, 58 Lanc. L.R. 43, 54 Berks L.J. 110.
secured party’s status as a holder of a perfected security interest. Further, only actual knowledge\textsuperscript{42} of the contents of the financing statement could help the petitioner in his assertion that a good faith filing in an improper place is nevertheless effective as provided by Wyo. Stat. Sec. 9-401 (2) (1957) (Supp. 1963).\textsuperscript{43}

More filing provisions are set forth in the situation where a debtor changes his place of business or residence.\textsuperscript{44} In this event, after four months, the secured party must refile his security agreement in the proper county to keep his filing effective. This rule applies to both changes of residence or business by the debtor within the state and to the situation where a debtor moves from another state to a Uniform Commercial Code state.\textsuperscript{45} 

\textit{Churchill Motors, Inc. v. A. C. Lohman, Inc.}, involved a motor vehicle sold by a conditional vendor to a conditional vendee in Rhode Island.\textsuperscript{46} The conditional sales contract was perfected in Rhode Island and no certificate of title law existed for notation of liens thereon. Several days later, the conditional vendee drove the auto to Pennsylvania and sold it to an auto dealer without knowledge of the security interest. The auto dealer secured a certificate of title pursuant to the Pennsylvania statutes and sold the auto to the defendant in Pennsylvania who in turn took it to New York and sold it to the plaintiff, warranting title. All transactions in Pennsylvania took place within four months from the time when the auto was brought into the state. The Uniform Commercial Code was not in effect in New York the time of the transactions within that state. After nearly a year, the original conditional vendor, who perfected his security interest in Rhode Island, located the auto in the possession of the plaintiff and took possession from him. Upon judgment for the plaintiff for recovery of the purchase price, the court held (1) that the plaintiff never acquired title superior to the conditional vendor, hence the defendant was liable for his breach of warranty; (2) the court will look to the state where the contract was made to determine if the conditional sales contract was perfected; (3) the four months is not a grace period for filing in the new location, but is an absolute period of protection designed to give a vendor adequate time to make an investigation and to locate the property. The protection of the security interest ceases upon expiration of the four month period; and (4) issuance of the clean certificate of title to the auto dealer did not

\textsuperscript{42} See Uptown National Bank of Chicago v. Purvis, 26 Ill. App. 2d 473, 168 N.E.2d 791 (1960), for dicta as to actual knowledge; see In re German, 285 F.2d 740 (Cir. Ill., 1961), as to constructive notice.

\textsuperscript{43} The good faith argument of the petitioner was based upon the U.C.C. § 9-401 (2), which states that: "A filing which is made in good faith in an improper place or not in all of the places required by this section is nevertheless effective with regard to any collateral as to which the filing complied with the requirements of this Article and is also effective with regard to collateral covered by the financing statement against any person who has knowledge of the contents of such financing statement." "Good faith" filing discussed in 68 Com. L.J. 253 (Sept. 1963); "good faith" argument rejected in In the Matter of Lux’s Superette, Inc., 206 F. Supp. 368 (E.D.Pa. 1962).


\textsuperscript{46} 229 N.Y.S.2d 570, 16 A.D.2d 560 (1962).
give him any right superior to that of the conditional vendor. Two propositions are clear from this case. First, a motor vehicle may be brought into Wyoming from a state which does not require notation of a lien on the certificate of title and sold to a purchaser who may take subject to a pre-existing perfected security interest; and second, upon removal of collateral to another state having the Uniform Commercial Code, or to another county, the secured party may have to refile his security interest before the expiration of four months to retain a continuing perfected status.47

The rules of priority between unperfected security interests and persons who take priority over the same, including lien creditors, are provided by Wyo. Stat. Sec. 9-301 (1957) (Supp. 1963).48 As to security interests created in Wyoming, a subsequent purchaser of a used or new motor vehicle will take free of security interests which are not perfected by filing and notation on the certificate of title.49 Upon compliance with the two required steps,50 the security agreement will take effect and be in force as to all creditors and subsequent purchasers.51

A number of situations may exist where there will be conflicting security interests in the same motor vehicle. The most common will involve dealers, manufacturers, financing institutions who engage in inventory financing, and takers of chattel paper.52 Priorities among conflicting security interests are generally governed by Wyo. Stat. Sec. 34-9-312 (1957) (Supp. 1968) and the sections cited. They will not be individually discussed due to the variety of facts which control their application.

Another problem which was foreseen and apparently alleviated by the 1963 legislators is in regard to duplicate certificates of title. Under the old Wyo. Stat. Sec. 31-40 (1957), it was a relatively simple procedure to obtain a duplicate certificate of title from the county clerk upon payment of $1.00. It was thereby possible for a dishonest person to borrow on his vehicle, deliver a clean original title to the lender in compliance with the old Wyo. Stat. Sec. 31-37 (f) (1957), and in the five day interval before the original was submitted to the county clerk for notation of the encumbrance, apply for and immediately receive a clean duplicate which could again be

used as collateral for a second loan.\textsuperscript{53} \textit{Union National Bank and Trust Co. v. Geyer Auction}\textsuperscript{64} is a case involving such a fraudulent use of a duplicate certificate of title.\textsuperscript{55} In this Pennsylvania case the owner of an original "clean" certificate of title, Meyers, applied and received a "clean" duplicate certificate of title by representing the loss of his original when in fact it was not lost. Meyers then used the original for a loan from the plaintiff. The plaintiff followed the statutory requirements necessary under the Vehicle Code to secure his loan. Later, Meyers secured a second loan from a bank using the "clean" duplicate certificate of title which was assigned to the defendant. The question considered by the court was "does the improper issuance of a duplicate certificate of title render the original certificate of title void when the original certificate of title has been pledged to an innocent lender"? The court held that the original was not void when given to the innocent plaintiff who had no knowledge of the fraud. "Where two innocent persons are the victims of the fraud or mistake of a third person, and neither victim could have been reasonably expected to take steps to detect or to prevent the fraud or mistake, the victim who first acquired the muniments of title should prevail, for precedency in time, where the equities are in other respects equal, gives priority in law."

Wyo. Stat Sec. 31-40 (1957), was amended in 1963 to prevent situations as above.\textsuperscript{56} Upon loss of a certificate of title, the owner must submit an affidavit requesting a duplicate which, in the discretion of the county clerk, can be issued on the eleventh day after the affidavit is filed. An alternative of posting an indemnity bond is permitted for a duplicate certificate requested to be issued prior to the eleventh day. Further, a capital letter notation is written on the face of the certificate as notice that it is a duplicate and may be subject to the rights of persons under the original certificate. This notation would apparently permit a secured party to prevail over a subsequent bona fide purchaser or creditor who relied upon the clean duplicate when purchasing or lending as they would be on notice that other prior rights may exist. Such a purchaser or lender should proceed with extreme caution and should at least forestall their transaction for a minimum of ten days. Although the legislature has closed many of the avenues for fraud by the use of two certificates of title, it is still possible for two clean certificates to be obtained and both later used to obtain serve as notice. A suggested improvement by legislation is to proceed on the premise that it is rare when an honest person actually loses his original loans within a few days time before anything appears on the records to

\textsuperscript{53} The requirement in Wyo. Stat. § 31-37 (f) (1957), repealed by Laws 1963, ch. 185, § 4 but substantially re-enacted in Wyo. Stat. § 34-9-502 (4) (1957) (Supp. 1963), that an encumbrance be recorded within five days does not apply until the owner has been issued an original or substitute certificate. General Credit Corp. v. First Natl. Bank of Cody, 74 Wyo. 1, 283 P.2d 1009 (1955).
\textsuperscript{55} Certificate of title procured by false representations is void ab initio, Hertz Corp. v. Hardy, 197 Pa. Super. 466, 178 A.2d 893 (1962).
certificate of title; hence such a person should bear the risk and expense of posting an indemnity bond for the duration of time that a duplicate certificate of title is outstanding.67

**Leon R. Hetherington**