No. 07-3962

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In re Faith Ann Peaslee

GEORGE M. REIBER,
Trustee/Appellant

v.

GMAC, LLC, et al.,
Creditor/Appellee

Brief of *Amicus Curiae* National Association of Consumer Bankruptcy Attorneys in Support of Appellant and Reversal of the District Court Decision

On appeal from the United States District Court for the
Western District of New York

Lewis W. Siegel (LS9161)
Attorney for
National Association of
Consumer Bankruptcy Attorneys *Amicus Curiae*
355 Lexington Avenue - Suite 1400
New York, NY 10017
(212) 481-1300

Tara Twomey, Esq., Of Counsel On Brief

December 10, 2007

CORPORATE DISCLOSURE STATEMENT

George M. Reiber v. GMAC, LLC, et al. - No. 07-3962

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure *Amicus Curiae* the National Association of Consumer Bankruptcy Attorneys makes the following disclosure:

1) For non-governmental corporate parties please list all parent corporations. **NONE.**

2) For non-governmental corporate parties please list all publicly held companies that hold 10% or more of the party's stock. **NONE.**

3) If there is a publicly held corporation which is not a party to the proceeding before this Court but which has a financial interest in the outcome of the proceeding, please identify all such parties and specify the nature of the financial interest or interests. **NONE.**

4) In all bankruptcy appeals counsel for the debtor or trustee of the bankruptcy estate must list: 1) the debtor, if not identified in the case caption; 2) the members of the creditors' committee or the top 20 unsecured creditors; and, 3) any entity not named in the caption which is an active participant in the bankruptcy proceedings. If the debtor or trustee is not participating in the appeal, this information must be provided by appellant. **NOT APPLICABLE.**

s/ Lewis W. Siegel
Lewis W. Siegel, Esq. (LS9161)
Attorney for the National Association of Consumer Bankruptcy Attorneys

Dated: December 10, 2007

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Legislative History

Regulations

Other Authorities

STATEMENT OF INTEREST OF NACBA

Incorporated in 1992, the National Association of Consumer Bankruptcy Attorneys ("NACBA") is a non-profit organization of more than 2500 consumer bankruptcy attorneys nationwide. Member attorneys and their law firms represent debtors in an estimated 500,000 bankruptcy cases filed each year.

NACBA's corporate purposes include education of the bankruptcy bar and the community at large on the uses and misuses of the consumer bankruptcy process. Additionally, NACBA advocates nationally on issues that cannot adequately be addressed by individual member attorneys. It is the only national association of attorneys organized for the specific purpose of protecting the rights of consumer bankruptcy debtors. NACBA has filed *amicus curiae* briefs in various courts seeking to protect the rights of consumer bankruptcy debtors. *See*, *e.g.*, *Kawaauhau v. Geiger*, 523 U.S. 57 (1998); *In re Scarborough*, 461 F.3d 406 (3rd Cir. 2006); *In re Tanner*, 217 F.3d 1357 (11th Cir. 2000).

The NACBA membership has a vital interest in the outcome of this case. NACBA members primarily represent individuals, many of whom own motor vehicles. The 2005 amendments to section 1325(a) 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. This case 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. The answer to that question will determine whether many debtors are able to keep, or will have to surrender, their vehicles.

SUMMARY OF ARGUMENT

The 2005 amendments created a narrow exception to the general rule under which debtors are permitted to modify the right of creditors. The exception created by the "hanging paragraph" at the end of section 1325(a) is carefully limited in time, by type and use of the goods, and by the type of claim protected. Specifically, one requirement is that the creditor must have a purchase money security interest securing the debt that is the subject of the claim.

An upside-down car is one in which in which the value of the car is less than the amount owed on it. It is not unusual for owners with longer-term loans, low or no down payments, and/or cars that are depreciating rapidly to be "upside-down." When an owner of an upside-down car wants to trade-in that car and buy a new car, not only must he pay the purchase price of the new car, the negative equity on the old car must also be paid off. While it is common for debtors to finance the payoff of the negative equity, funds advanced to pay off negative equity for a trade-in vehicle do not constitute a purchase money obligation under the Uniform Commercial Code. Such funds are not part of the cash price of the vehicle, nor are they obligations for expenses incurred in connection with acquiring right in the collateral. The financing of negative equity may be convenient but it is not necessary to acquire rights in the new collateral.

The District Court, however, expanded the very narrow exception created by Congress far beyond its intended scope—by converting the unsecured negative equity from a trade-in vehicle into a purchase money obligation that is protected from bifurcation. The District Court's decision paves the way for creditors to manipulate transactions in ways that would permit the creditor to transform an otherwise unsecured debt into one that could not be modified in bankruptcy, by simply insisting that refinancing the additional unsecured debt is a condition of granting a purchase money loan. Furthermore, the District Court erroneously relies on definitions contained in consumer protections statutes and nonexistent legislative history to support its conclusion.

This Court should hold that the financing of negative equity does not constitute a purchase money obligation and that the creditors' claims are not protected by the hanging paragraph. The decision of the District Court should be reversed.

ARGUMENT

I. In light of longstanding bankruptcy policies, the provisions of the "hanging paragraph" of section 1325(a) should be construed narrowly.

The two main objectives of the Bankruptcy Code are to provide a fresh start for the debtor and the fair and orderly repayment of creditor to the extent possible. To foster a debtor's fresh start, the Bankruptcy Code generally permits debtors to modify the rights of secured and unsecured creditors to reflect what they would receive in a liquidation of the debtor's assets. 11 U.S.C. § 1322(b)(2). To ensure the fair repayment of creditors, longstanding bankruptcy policy favors equality of distribution among like creditors. *See* 11 U.S.C. §§ 1322(a)(3); 1322(b)(1).

Debtors frequently modify the rights of secured creditors by splitting, or "bifurcating," the creditor's claim into two parts: the secured portion which is equal to the value of the collateral and an unsecured portion represented by any amount owed over the value of the collateral. 11 U.S.C. § 506. The 2005 enactment of the "hanging paragraph" at the end of section 1325(a) arguably[1] created an exception to this common method of dealing with secured creditors. The exception at issue in this case, however, is carefully limited 1) in time, 2) by

[1] Courts have significantly disagreed on the meaning of the hanging paragraph, which makes section 506 inapplicable to certain claims. *See, e.g.*, *In re Carver*, 338 B.R. 521 (Bankr. S.D. Ga. 2006)(910 car claims not "allowed secured claims"); *In re Brooks*, 344 B.R. 417 (Bankr. E.D.N.C. 2006)(910 car claims are allowed secured claims in the full amount of the debt); *In re Wampler*, 345 B.R. 730 (Bankr. D. Kan. 2006)(910-car creditor does not have an "allowed secured claim" but has an allowed claim for the entire prepetition debt without post-petition interest).

type and use of the goods, and 3) by the type of claim protected. Specifically, for motor vehicles, the debt must have been incurred within 910 days of the filing of the petition, 2) the collateral must be a motor vehicle acquired for personal use of the debtor and 3) the creditor must have a purchase money security interest securing the debt that is the subject of the claim. 11 U.S.C. § 1325(a).

As an exception to the general rules favoring equal treatment of creditors and permitting debtors to modify claims, the elements of the hanging paragraph should be construed narrowly. *See Howard Delivery Serv., Inc. v. Zurich Am. Ins., Co.,* 126 S. Ct. 2105, 2116 (2006)(equal distribution objective underlying the Bankruptcy Code requires that preferences be tightly construed)(citations omitted); *Trustees of Amalgamated Ins. Fund v. McFarlin's Inc.,* 789 F.2d 98 (2d Cir. 1986)("Because presumption in bankruptcy is that the debtor's limited resources will be equally distributed among his creditors, statutory priorities are narrowly construed."). Exceptions to general bankruptcy rules, including those related to dischargeability,[2] priority payments,[3] and the automatic stay,[4] have all been

[2] *See, e.g., In re Kaspar,* 125 F.3d 1358, 1361 (10th Cir. 1997)("[e]xceptions to discharge are to be narrowly construed, and because of the fresh start objectives of bankruptcy, doubt is to be resolved in the debtor's favor), *citing In re Hunter,* 780 F.2d 1577, 1579 (11th Cir. 1986).
[3] *See, e.g., Trustees of Amalgamated Ins. Fund v. McFarlin's Inc.,* 789 F.2d 98 (2d Cir. 1986); *In re HLM Corp.,* 183 B.R. 852 (D. Minn.)(presumption exists favoring equal distribution of debtor's limited resources and statutory priorities within the Bankruptcy Code should be narrowly construed), *aff'd,* 62 F.3d 224 (8th Cir. 1995).
[4] *See, e.g., In re Miller,* 454 F.3d 899 (8th Cir. 2006)("Section 549(c) serves as an exception to the automatic stay imposed when a bankruptcy petition is filed, and as such, it should be construed narrowly").

narrowly construed to promote the fundamental underlying purposes of the Bankruptcy Code. Similarly, the hanging paragraph's preference in favor of a certain class of creditors should be strictly interpreted since granting protection under the paragraph necessarily reduces funds available to pay unsecured creditors and may diminish the recovery of other secured creditors.[5] *See Howard Delivery*, 126 S. Ct. at 2116.

The language of the hanging paragraph, with its clearly defined time frame and specification of covered claims, indicates that Congress was concerned with the rapid initial depreciation of motor vehicles and other personal property securing debts incurred to purchase that property. Presumably, Congress felt that the limited class of creditors identified in the hanging paragraph should not be subject to a cramdown shortly after the purchase. Creditors, however, seek to expand the very narrow exception created by Congress far beyond its intended scope—by converting the unsecured negative equity from a trade-in vehicle into a purchase money obligation that is protected from bifurcation. Despite the District Court's suggestion to the contrary, there is simply no legislative history with respect to the hanging paragraph that supports the creditors' position that it should receive a windfall from financing unsecured antecedent debt along with the

[5] Distribution of the debtor's assets in bankruptcy is almost always a zero-sum game because the claims against the debtor typically far exceed the value of the estate.

purchase price of the new vehicle.[6] *See* Section III, *supra.* Indeed, a ruling in favor of the creditors would "transform knowingly refinanced unsecured negative equity debt into secured debt not supported by collateral value, and then require it to be paid in full to the detriment of other unsecured creditors."[7] It would also allow a creditor to manipulate a transaction in a way that would permit the creditor to transform an initially unsecured debt into one that could not be modified in bankruptcy, by simply insisting that refinancing of additional unsecured debt is a condition of granting a purchase money loan.

II. Terms used in consumer protection statutes, such as the federal Truth In Lending Act and the New York MVRISA, enacted for entirely different purposes than the UCC, should not control the meaning of "purchase money obligation.

A. Funds advanced to pay off negative equity for a trade-in vehicle do not constitute a purchase money obligation.

The majority of courts considering whether funds advanced to pay off negative equity on a trade-in vehicle constitute a purchase money obligation have

[6] The legislative history merely mirrors the language of the statute. For example, the House Committee Report concerning the hanging paragraph summarizes the change as follows: Section 306(b) adds a new paragraph to section 1325(a) of the Bankruptcy Code specifying that Bankruptcy Code section 506 does not apply to a debt incurred within the two and one-half year period preceding the filing of the bankruptcy case if the debt is secured by a purchase money security interest in a motor vehicle acquired for the personal use of the debtor within 910 days preceding the filing of the petition. Where the collateral consists of any other type of property having value, section 306(b) provides that section 506 of the Bankruptcy Code does not apply if the debt was incurred during the one-year period preceding the filing of the bankruptcy case. H.R. Rep. 109-31, Pt. 1, at 72, 109th Cong., 1st Sess. (2005).

[7] *In re Peaslee*, 358 B.R. 545, 556 (Bankr. W.D.N.Y. 2006).

concluded that they do not. [8] In New York, as in most other states, the definition of a purchase money security interest is contained in § 9-103 of the Uniform Commercial Code. N.Y. U.C.C. § 9-103. The starting point for defining a "purchase money security interest" is a "purchase money obligation" which means "an obligation of an obligor incurred as all or part of the price of the collateral or for given value to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used." N.Y. U.C.C. § 9-103(a)(2), (b). The terms "price" and "value given" in § 9-103 are nearly synonymous. The former is used in credit sales transactions in which the seller extends credit to the buyer and the latter is used in loan transactions in which a third-party lender loans funds to the buyer to purchase goods from the seller. *See* N.Y. U.C.C. § 9-103; former § 9-107 (1962)(clearly delineating the difference between seller financed transactions and those financed by third parties). Because each of the transactions at issue in these appeals is a credit sale the only issue is whether the financed negative equity is part of the part of the "price" of the collateral. There is no need to consider the related,

[8] *See Citifinancial Auto v. Hernandez-Simpson*, 369 B.R. 36 (D. Kan. 2007)(excess trade-in balance is an unsecured antecedent debt which is not entitled to purchase money treatment under § 1325(a)); *In re Mitchell*, 2007 WL 3378229 (Bankr. M.D. Tenn. Nov. 13, 2007); *In re Hayes*, 376 B.R. 655 (Bankr. M.D. Tenn. Nov. 1, 2007); *In re Sanders*, 2007 WL 3047233 (Bankr. W.D. Tex. Oct. 18, 2007); *In re Acaya*, 369 B.R. 564 (Bankr. N.D. Cal. 2007); *In re Bray*, 365 B.R. 850 (Bankr. W.D. Tenn. 2007)(financing of negative equity not included within creditor's purchase money security interest); *In re Westfall*, 365 B.R. 755 (Bankr. N.D. Ohio 2007); *In re Price*, 363 B.R. 734 (Bankr. E.D.N.C. 2007); *In re Peaslee*, 358 B.R. 545 (Bankr. W.D.N.Y. 2006). Even the *Graupner* court in Georgia noted the "seemingly obvious conclusion" that Creditor "does not hold a purchase money security interest". *In re Graupner*, 356 B.R. 907, 917 (Bankr. M.D. Ga. 2006), *aff'd, Graupner v. Nuvell Credit Corp*., 2007 WL 1858291 (M.D. Ga. June 26, 2007)

but distinct inquiry into whether value was given to enable the debtor to purchase the collateral.[9]

Clearly, payments to pay off a debtor's prior loan do not constitute part of the cash price for the vehicle. Instead both creditors and the District Court below relied solely on an expansive reading of the comment to § 9-103 to find that payoff of negative equity constituted an obligation for expenses incurred in connection with acquiring rights in the collateral. *See* N.Y. U.C.C. § 9-103 (Comment 3). Specifically, "price" for purposes of defining a "purchase money obligation" may include obligations for expenses incurred in connection with acquiring right in the collateral, sales taxes, duties, finance charges, freight charges, costs of storage interest, demurrage, administrative charges, expenses of collection and enforcement, and attorney's fees. N.Y. U.C.C. § 9-103 (Comment 3). Price may also include other obligations that are similar to those items on the enumerated list. *Id.* The pay off of antecedent debt is not included in this list, nor is it an obligation similar to those provided. [10]

The District Court's suggestion that negative equity fits squarely within the term "expenses" because it is a "package transaction" is not only against the overwhelming weight of authority, it is also absurd. Paying off negative equity is

[9] Some courts have mistakenly attempted to apply both tests without regard to whether the transaction is a credit transaction or loan transaction. *See In re Conyers*, 2007 WL 3244106 (Bankr. M.D.N.C. Nov. 2, 2007).
[10] *See* cases cited, *supra* note 8.

no more closely related to the purchase price than funds advanced to the borrower to pay off, for example, credit card debts to satisfy a creditor's underwriting requirements. Does the payoff of $10,000 in unrelated consumer debt become an "expense incurred in connection with acquiring rights in the collateral" if the creditor both requires the debt to be paid off as a condition of extending financing and offers to give the debtor the funds for that purpose? Of course not. *See, e.g., Laubach v. Fidelity Consumer Finance Co.,* 686 F. Supp. 504 (E.D. Pa. 1988)(describing a car finance transaction in which lender required Mr. Copin, a 75-year old borrower, to pay off home mortgage and liens against home and financed the entire transaction), *rev'd* 898 F.2d 907 (3d Cir. 1990)(reversed on preemption grounds). Similarly, a creditor's acceptance of a trade-in vehicle on the condition that the negative equity be paid off and the creditor's willingness to extend the funds to do so does not make it an "expense incurred" to acquire rights in a new vehicle. The creditor's requirement that the debtor retire an existing obligation and providing the debtor the means to do so, does not change the "price" of the new vehicle debtor seeks to purchase. The financing of negative equity may be convenient but it is not necessary to acquire rights in the new collateral.

B. The definition of "total sale price" under the federal Truth In Lending Act has no bearing on the definition of "purchase money obligation" under the UCC.

In 1968, Congress enacted the Truth In Lending Act ("TILA") as part of the Consumer Credit Protection Act. Pub. L. No. 90-321 (May 29, 1968). TILA is primarily a disclosure statute that compels creditors extending credit to consumers to disclose the cost of the credit using a standardized format and terminology defined by the Act itself and by the Federal Reserve Board. The primary goal of TILA is to promote the informed use of credit and encourage comparison shopping by prescribing a uniform standard for disclosing the true cost of credit. In order to achieve this goal, TILA adopts an expansive view of the cost of credit, which includes negative equity, insurance products, and any other cost associated with borrowing money.[11]

i. "Total sale price" describes the amount a buyer would pay in exchange for the ability to pay an obligation over time, not the actual price of the item purchased.

The "total sale price" is not, and has never been, a term that defines a "purchase money security interest" or "purchase money obligation" under the

[11] The cost of credit under TILA is referred to as the finance charge, and it includes "any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or condition of the extension of credit. It does not include any charge of a type payable in a comparable cash transaction." 12 C.F.R., § 226.4(a). To determine the cost of credit, all amounts in a transaction must be categorized as either finance charges or amounts that are financed. It is for that purpose that TILA and similar state statutes discussed below, sometimes include amounts used to pay off of additional debts with the price of the item purchased.

UCC. *See In re Pajot*, 371 B.R. 139, 150 (Bankr. E.D. Va. 2007)(TILA disclosure statute does not presume to address the nature or extent of security interests under state or federal law or serve to define the relative priorities of creditors). Rather, it is used expansively to advise consumers of the true cost of credit in credit sale transactions. Under the original version of TILA, credit sellers were required to disclose the "deferred payment price" which represented the total amount the borrower would pay in return for the ability to pay the obligation in installments. 12 C.F.R. § 226.8(c)(8)(ii)(1980). *See McGowan v. King, Inc*., 569 F.2d 845 (5th Cir. 1978)(failure to use term "deferred payment price" violated Old. 12 C.F.R. § 226.8(c)(8)(ii)). The term "deferred payment price" was later changed to "total sale price" but the meaning remains the same. The "total sale price" is defined as the sum of 1) the cash price; 2) amounts that are financed by the creditor and are not included in the finance charge (e.g., title fees, credit insurance premiums); and, 3) the finance charge. 12 C.F.R. § 226.18(j). Notably this definition distinguishes between the "cash price" and the "total sale price." Under the Federal Reserve Board's Official Supplemental Staff Commentary the financing of negative equity on a trade-in vehicle is included in the "total sale price," (i.e., the true amount being financed), but it is not included in the cash price of the new automobile. *See* Official Staff Commentary § 226.2(a)(18)-3 (Supp. 1 to Part 26)(describing how to

calculate the "total sale price" for a vehicle with a "cash price" of $20,000, negative equity from a trade-in of $2,000, a down payment of $1500).

ii. Creditors are permitted to choose the method by which "total sale price" is determined, with one method resulting in a higher "total sale price."

In 1999, the Federal Reserve Board issued Commentary to address situations in which the borrower makes a down payment and trades in a vehicle with negative equity.[12] The Federal Reserve Board's Supplemental Staff Commentary allows the creditor to use either a "netting" or "non-netting" approach when dealing with negative equity and down payments.[13] The "netting" method results in a lower "total sale price" than if the netting was not performed. Based on the example in

[12] Official Staff Commentary § 226.2(a)(18)-3 (Supp. 1 to Part 26) provides: *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 downpayment 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. Alternatively, the creditor may reflect a downpayment 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 downpayment 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 downpayment 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.

[13] Netting" means that the cash down payment would be applied, or "netted" against the negative equity.

the Staff Commentary the netting approach would yield a "total sale price" of $23,500 and the non-netting approach would yield a "total sale price" of $25,000.[14]

The Official Staff Commentary makes clear that purchase money obligations under the UCC cannot depend on the "total sale price" as used in TILA where the creditor can choose whether the "total sale price" should be higher or lower in transactions involving the trade-in of vehicles with negative equity.

iii. The term "total sale price" only applies to credit sale transactions and not to enabling loans which may be considered purchase money obligations under the UCC.

In a credit sale, a transaction in which the seller extends the credit, the "total sale price" must be disclosed using that term. Disclosure of the "total sale price" is not required, and is not relevant, to loan transactions. 12 C.F.R. § 226.2(a)(16). That is, under § 9-103 a seller can obtain a purchase money obligation by financing all or part of the price or a third-party may obtain a purchase money obligation by giving value that enables the debtor to acquire rights in the collateral. N.Y. U.C.C. § 9-103. The term "total sale price" as used in the Truth In Lending Act applies only in the former type of transaction, not the later. Consequently, "total sale price" could only be used in determining "purchase money obligations" in seller financed transactions. The result would be significant asymmetry in defining

[14] The "total sale price" is the sum of the "cash price" [$20,000] plus other charges [$500 prior lien pay-off in the "netted" approach] or [$2,000 lien payoff in the non-netted approach] plus the finance charge. *See* 12 C.F.R. § 226.18(j).

"purchase money obligations" in credit sales and loan transactions, which would run counter to the policies underlying the protections that the U.C.C. gives to all holders of purchase money security interests.[15]

C. Similarly, Motor Vehicle Sales Financing Acts are a wholly inappropriate standard for defining "purchase money obligations" and "purchase money security interests."

Like the Truth In Lending Act, the New York Motor Vehicle Retail Instalment Sales Act (MVRISA) is a consumer protection statute that was primarily designed to require sellers to disclose costs of credit sales transactions involving motor vehicles. In addition, MVRISA substantively limits the cost of such transactions. The New York MVRISA was originally enacted in 1956.[16] From its enactment until today, no New York court has ever suggested that provisions of the UCC should be interpreted based on the definition of terms used in this consumer protection statute which was enacted to promote disclosure of the true cost of credit and limit finance charges.

Across the country during the late 1950s and 1960s, states enacted laws regulating the use of retail sales contracts out of concern for protection of

[15] The transactions covered by the MVRISA and the TILA do not generally include private sales. So while under the U.C.C. a private seller may have a purchase money security interest such a seller would not be covered by these consumer protection statutes. It simply makes no sense to borrow definitions from these consumer protections statutes when they only apply to a subset of transactions covered by the U.C.C. and the hanging paragraph.

[16] N.Y. Laws 1956, c. 633 § 1.

consumers from unconscionable business practices.[17] Historically, general usury statutes applied only to loans, not to sales of goods on credit.[18] As a result, lenders were avoiding usury restrictions by buying consumer paper at a discount from retailers rather than issuing loans for the purchase of goods. Retail installment statutes, such as the New York MVRISA, addressed this loophole that allowed lenders to exploit unwary consumers. These special usury laws set limits on the charges assessed in credit sale transactions typically required disclosure of the cost of credit.[19]

Like the New York MVRISA, many of these state laws provide a definition of "cash sale price" and "time sale price," the former being the price which would be paid if the buyer used cash or its equivalent, and the latter being the invariably higher price which the buyer would pay in return for the ability to pay in

[17] *See* Retail Instalment Sales Legislation, 58 Colum. L. Rev. 854, 855 (1958)("there have recently been expressions of concern over the rising quantity of consumer credit, deterioration in the qualify of consumer credit, and the oppressive business practices form which consumers need protection").

[18] *See, e.g., Thomas v. Knickerbocker Operating Co.*, 108 N.Y.S. 2d 234 (N.Y. Sup. Nov. 19, 1951)("mere fact of variation between cash price and time selling price which was greater than 6 per cent did not render transaction usurious"; usury must be founded on loan or forbearance of money; installment agreement did not constitute forbearance of money); *Bryant v. Securities Inv. Co.*, 102 So. 2d 701 (Miss. 1958)(fact that time price shown in conditional sales contract for sale of automobile and cash price exceeded percentage of interest permitted by usury laws did not render contract usurious).

[19] As originally enacted the New York MVRISA established three classes of motor vehicles and established a maximum credit service charge for each class. The 1980 amendments to the Act substituted the rate or rates agreed to by the retail seller and the buyer for the previous schedule of rates. N.Y. Laws 1980, c. 883 § 73.

installments.[20] Traditionally, the difference between the time price and the cash price was not legally recognized as interest, but was instead considered a "time-price differential." Many state statutes define the difference between the cash sale price and the time sale price as the "finance charge."[21]

In 1994, New York amended its MVRISA to provide that the "cash sale price" (and concomitantly the "time sale price") could include amounts used to pay off negative equity on a trade-in vehicle.[22] This amendment, which allows sellers to treat negative equity as part of the cash or time sale price, parallels the 1999 Supplemental Staff Commentary to TILA. It permits credit sellers to finance such negative equity and like TILA, instructs how such negative equity should be included in determining the cost of the credit. There is no indication in the statute or the legislative history that the 1994 amendment to the term "cash sale price" in the MVRISA was intended to modify the traditional understanding of a purchase money obligation under the UCC. *Cf. In re Sanders*, 2007 WL 3047233 at *8-10 (finding Texas Finance Code, which regulates Motor Vehicle Instalment Sales contracts, inapplicable to determining purchase money obligations under the UCC); *In re Acaya*, 369 B.R. at 568 (same with respect to California law).

[20] *See* N.Y. Pers. Prop. Law § 301(4) (Time sale price is the cash sale price plus insurance, official fees, and the credit service charge).
[21] *See, e.g.*, Ga. Code Ann. § 10-1-33 (Georgia's Motor Vehicle Sale Finance Act limits the finance charge in certain transactions)
[22] N.Y. Laws 1994, c. 1, § 45.

The New York MVRISA is also an inappropriate standard by which to measure purchase money security interests because the MVRISA applies only to a limited subset of property covered by the hanging paragraph. Importing any definition from the MVRISA would necessarily require the court to apply the same standard to other property such as appliances purchased within one year of a bankruptcy filing. Under the District Court's ruling, if the debtor purchased a stereo on a credit card, and thereafter the auto lender required the debtor to pay off the $500 credit card debt as a condition of financing an auto, then the $500 would be transformed from unsecured debt to secured debt not subject to cramdown. The reasoning of the District Court that this "package deal" entitles the lender to greater protection gives all lenders a tremendous incentive to manipulate transactions in order to achieve preferential treatment under the Bankruptcy Code.

III. By its plain language the hanging paragraph at the end of section 1325(a)(9) only applies when the creditor holds a purchase money security interest with respect to the entire debt.

The starting point for the court's inquiry should be the statutory language itself. *See Lamie v. U.S. Trustee*, 540 U.S. 526, 534, 124 S.Ct. 1023, 1030 (2004); *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 241-42, 109 S.Ct. 1026, 1030-31 (1989); *United States v. Steele*, 147 F.3d 1316, 1318 (11th Cir.1998) (*en banc*) ("In construing a statute we must begin, and often should end as well, with the language of the statute itself."). In interpreting the statutory language, the court

must assume that Congress said in the statute what it meant and meant in the statute what it said. *See Connecticut Nat'l Bank v. Germain*, 503 U.S. 249, 253-54 (1992). Thus, it has been well established that when the "statute's language is plain, the sole function of the court, at least where the disposition required by the text is not absurd, is to enforce it according to its terms." *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6 (2000)(internal quotations omitted). A result will be deemed absurd only if it is unthinkable, bizarre or demonstrably at odds with the intentions of its drafters. *See In re Spradlin*, 231 B.R. 254, 260 (Bankr. E.D. Mich. 1999), *citing Public Citizen v. Dept of Justice*, 491 U.S. 440, 109 S. Ct. 2558, 105 L.Ed.2d. 377 (1989). A plain reading of the statutory language makes clear that the hanging paragraph only applies when the creditor holds a purchase money security interest in the entire debt. *See In re Mitchell*, 2007 WL 3378229 at *5-6; *In re Sanders*, 2007 WL 3047233 at *17-21.

The new paragraph added to the end of section 1325(a)(9) (hereinafter the "hanging paragraph") states in relevant part:

> 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 the 910-day preceding the date of filing of the petition, and the collateral for that debt consists of a motor vehicle (as defined in section 30102 of title 49) acquired for the personal use of the debtor…

The word "debt" appears five times in the hanging paragraph. On none of those occasions is the word modified by language such as "to the extent" or "portion of." *See Sanders*, 2007 WL 3047233 at *18. Congress could easily have provided that the hanging paragraph applied to the extent that debt was secured by a purchase money obligation, but it did not do so. By contrast, in other sections of the Code, Congress specifically used the words "to the extent" or "any portion" to indicate applicability to all or part of a debt, claim, payment, property or lien at issue. *See, e.g.*, 11 U.S.C. § 329 ("return of any such payment, **to the extent** excessive,…"); 11 U.S.C. § 365(j)("recovery of **any portion** of the purchase price…"); 11 U.S.C. § 506(b)("**To the extent** that an allowed secured claim is secured by property…"); 11 U.S.C. § 506(d)("**To the extent** that a lien secures a claim…"); 11 U.S.C. § 522(o)(3)("**to the extent** such value is attributable to **any portion** of any property…"). "Where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is presumed that Congress acted intentionally and purposely in the disparate inclusion or exclusion." *Rusello v. United States*, 464 U.S. 16, 23 104 S. Ct. 296, 300 (1983)(citation and quotation omitted). Also, "[w]here Congress knows how to say something but chooses not to, its silence is controlling." *In re Griffith*, 206 F.3d 1389, 1394 (11th Cir. 2000)(citation and quotations omitted).

Indeed, the legislative history of the bankruptcy amendments demonstrates that Congress specifically rejected language that would have limited bifurcation if creditor's claims were attributable, in whole or in part, to a purchase money obligation. For example, section 122 of the Bankruptcy Reform Act of 1999 provided that "subsection (a) [of § 506] shall not apply to an allowed secured claim to the extent ***attributable in whole or in part to the purchase price*** of personal property acquired by the debtor within 5 years of filing of the petition."(emphasis supplied). *See also* Bankruptcy Reform Act of 1998, H.R. 3150, 105th Cong. § 128 (1998). Similarly, the 1997 version of the bill provided that "Subsection (a) [of § 506] shall not apply to an allowed secured claim to the extent ***attributable in whole or in part to the purchase price*** of personal property acquired by the debtor during the 90-day period preceding the date of filing of the petition."(emphasis supplied). Consumer Bankruptcy Reform Act of 1997, S. 1301, 105th Cong. § 302(c) (1997). Surely, had Congress intended to prevent the bifurcation of claims for which creditors held a partial purchase money security interest, it could have easily done so. The change from the prior version shows that Congress did not intend for the hanging paragraph to apply to debts that consist of non-purchase money obligations. *Transcontinental & W. Air, Inc. v. Civil Aeronautics Bd.,* 336 U.S. 601, 696 (1949)(relying on legislative history to prior unenacted bill for clarification of language used in bill that was ultimately enacted). In this case, the

result of applying the plain language does not produce a result that is absurd, bizarre, or demonstrably at odds with Congressional intent. If, however, Congress "enacted into law something different from what it intended, then it should amend the statute to conform to its intent." *Lamie*, 540 U.S. at 1034.

If this court effectively rewrites the statute so that the word "debt" in the phrase "purchase money security interest securing the debt" applies to "any portion of the debt" or "the debt, in whole or in part" then each other occurrence of the word "debt" in the section must be similarly construed. *See Ratzlaf v. U.S.*, 510 U.S. 135, 143 S. Ct. 655 (1994)("a term appearing in several places in a statutory text is generally read the same way each time it appears"). Such judicial revisionism would potentially expand the applicability of the hanging paragraph far beyond the plain language of the statute. A broad construction of the hanging paragraph would also violate principles of statutory construction and longstanding bankruptcy policy which dictate that exceptions to general rules be construed narrowly.

IV. The court's best guess as to legislative intent is insufficient to overcome the plain language of the statute.

Despite the dearth of legislative history on the hanging paragraph, creditors have routinely argued in hanging paragraph cases that Congressional intent in enacting the provision was solely to benefit creditors. *See In re Kenney*, 2007 WL 1412921 (Bankr. E.D. Va. May 10, 2007)("Creditors argue that the hanging

paragraph should always be read to provide heightened protection to 910 secured creditors, as that was the intent of Congress"); *In re Brown*, 346 B.R. 868 (Bankr. N.D. Fla. 2006)("Wells Fargo contends that the absurdity of the result originates from the fact that the changes in the Code wrought by BAPCPA were enacted to enhance the rights of secured creditors in bankruptcy"). One court recently summarized the creditor's argument on the hanging paragraph as follows:

> The crux of Ford Motor Credit's argument is that § 1325 was amended to protect the interests of the 910 creditor and thus the statute should be interpreted to give the interests of the secured 910 creditor increased protection. Ford Motor Credit is in essence requesting this Court to find that the statute on its face is contrary to the intent of the drafters.

In re Williams, 2007 WL 2122131 (Bankr. E.D. Va. Jul. 19, 2007). Several courts, including the District Court below, have adopted the creditors' argument despite the absence of supporting legislative history. These courts have given significant weight to what they perceive as Congress' intent. For example the District Court below, without any citation, stated that "the so-called 'hanging paragraph' of § 1325, was obviously intended to protect the interests of automobile dealers who provide financing for customers." District Court Op. at 16; *see also In re Wright*, 492 F.3d 829, 832 (7th Cir. 2007); *In re Zehrung*, 351 B.R. 675, 678 (W.D. Wis. 2006)(basing its decision on what it found to be the "likely" and "extremely unlikely" intent of Congress). But what makes this intent "obvious"? Certainly,

the legislative history reflects no such intent. *See In re Quick*, 371 B.R. 459, 463 n.10 (B.A.P. 10th Cir. 2007)(" Specifically, we do not agree that BAPCPA amendments that appear to benefit creditors must be interpreted in such a way as to benefit only creditors. In fact, many of the supposedly "pro-creditor" amendments appear reflective of the normal give and take of the legislative process.") To the extent such beliefs are based on the role of private groups advocating for the legislation, the Supreme Court has specifically counseled against inferring any such intent. Courts should not attribute to Congress an official purpose based on the motives of particular groups that lobbied for or against certain provisions. *See Circuit City Stores v. Adams*, 532 U.S. 105, 120, 121 S. Ct. 1302, 149 L.Ed 234 (2001)(private interest groups' roles in lobbying for or against legislation provide a dubious basis from which to infer intent); *see also Garcia v. United States*, 469 U.S. 70, 76, 105 S. Ct. 479, 83 L.Ed.2d 474 (1984)(courts should look only to Committee Reports that "represent[] the considered and collective understanding of those [legislators] involved in drafting and studying the proposed legislation."). This Court should reject the reasoning of the District Court which would lead to the unsupportable conclusion that creditors should always win in cases related to the 2005 amendments simply because creditors lobbied for the passage of the bill.

The language of the hanging paragraph should not be "interpreted" to match a court's determination of what Congress "meant" to say. Rather the plain

language of the statute should be conclusive, except in rare cases in which the literal application will produce a result *demonstrably* at odds with the intentions of the drafters.

CONCLUSION

For the reasons stated above, this Court should hold that the financing of negative equity does not constitute a purchase money obligation and reverse the decision of the District Court below.

Dated: December 10, 2007

Respectfully submitted,

s/ Lewis W. Siegel
Lewis W. Siegel (LS9161)
Attorney for
National Association of
Consumer Bankruptcy Attorneys
amicus curiae
355 Lexington Avenue - Suite 1400
New York, NY 10017
(212) 481-1300 telephone
(212) 696-4064 fax
LWS@LWSEsq.com email

Tara Twomey, Esq. , Of Counsel On Brief

CERTIFICATE OF COMPLIANCE

This brief, exclusive of the certifications, tables of contents and authorities and the identity of counsel at the end of the brief, is 6,771 words in text and footnotes as counted by Microsoft Word, the word processing system used to prepare this brief. This brief has been prepared in a proportionally spaced typeface using Microsoft Word in Times New Roman 14-point font.

The text of the electronic brief and the hard copies are identical.

A virus check was performed on the electronic brief using Norton software and no virus was detected.

I certify under penalty of perjury that the foregoing is true and correct.

s/ Lewis W. Siegel_____
Lewis W. Siegel (LS9161)
Attorney for *amicus curiae*
355 Lexington Avenue - Suite 1400
New York, NY 10017
(212) 481-1300 telephone
(212) 696-4064 fax
LWS@LWSEsq.com email

Date: December 10, 2007