

11 U.S.C. § 1325(a)
11 U.S.C. § 1325(a) (5)
O.R.S. § 79.0103
O.R.S. § 79.0201(2)
O.R.S. § 83.510
O.R.S. § 83.680
Cramdown
Hanging paragraph
Negative equity
PMSI
Price
Purchase money obligation
"Value given to enable"

Michael Lloyd Johnson and
Jennifer Dawn Johnson, Case No. 07-31717-rld13

12/19/2007 RLD

Published

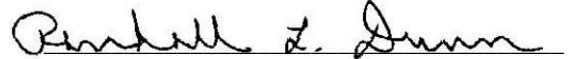
Chapter 13 debtors proposed a plan which attempted to cram down the value of a vehicle they purchased within 910 days of filing their bankruptcy petition, asserting that the Hanging Paragraph, added to 11 U.S.C. § 1325(a) by BAPCPA, did not prevent bifurcation of the secured creditor's claim into secured and unsecured components, because the claim included financed negative equity. The secured creditor objected, asserting that the financed negative equity constituted value given to enable the debtors to acquire rights in the vehicle, and as such, constituted a purchase money obligation under O.R.S. § 79.0103, which in turn supported a purchase money security interest ("PMSI") in the vehicle.

The court held that, for purposes of § 1325(a)'s Hanging Paragraph, a security interest based on debt arising from financed negative equity, paying off antecedent debt, cannot be a PMSI. The court applied the "dual status" rule and held that the Hanging Paragraph protected the secured creditor from cramdown of the PMSI portion of its claim.

NOTE: This is an amended opinion; the amendment highlights that Article 9 of the UCC as adopted in Oregon is subject to the retail installment contract provisions of O.R.S. §§ 83.510 to 83.680. See O.R.S. § 79.0201(2).

P07-16(28)

Below is an Opinion of the Court.



RANDALL L. DUNN
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In Re:) Bankruptcy Case
Michael Lloyd Johnson and) No. 07-31717-rld13
Jennifer Dawn Johnson,)
Debtors.) **AMENDED MEMORANDUM OPINION**

The issue before me requires that I plunge further into the semantic briarpatch generally referred to as the Hanging Paragraph, added to § 1325(a) of the Bankruptcy Code by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA").¹ Specifically, I must decide whether a creditor holds a purchase money security interest ("PMSI") for purposes of the Hanging Paragraph, where a portion of its

¹Unless otherwise indicated, all chapter, section and rule references are to the Bankruptcy Code, §§ 101-1532, and to the Federal Rules of Bankruptcy Procedure, Rules 1001-9036, as enacted and promulgated as of October 17, 2005, the effective date of most of the provisions of BAPCPA (Pub. L. 109-8, April 20, 2005, 119 Stat. 23).

1 debt represents financing of negative equity² in a vehicle traded in by
2 the debtors at the time the debtors purchased their new car.

3
4 BACKGROUND

5 On January 4, 2006, Michael and Jennifer Johnson ("the
6 Johnsons") purchased a 2005 Chrysler Sebring ("Vehicle") from Gresham
7 Chrysler Jeep, Inc. ("Dealer"). Daimler Chrysler Services Americas LLC
8 ("DaimlerChrysler") financed the purchase of the Vehicle. The amount
9 financed was \$26,078, an amount which the parties agree included \$8,990
10 in negative equity in the 2003 Chevrolet Cavalier ("Trade In") that the
11 Johnsons traded in as part of the transaction in purchasing the Vehicle.

12 The Johnsons filed their voluntary petition for relief under
13 chapter 13 of the Bankruptcy Code on May 1, 2007 ("Petition Date"), a
14 date within the 910-day period after their purchase of the Vehicle. As
15 set forth in the proof of claim ("Claim") filed by DaimlerChrysler, to
16 which the Johnsons have not objected, the Johnsons owed DaimlerChrysler
17 \$24,869.06³ as of the Petition Date in connection with DaimlerChrysler's
18 financing. In their chapter 13 plan dated May 4, 2007 ("Plan"), the

19
20 _____
21 ²"Negative equity is the amount by which the outstanding loan
22 balance exceeds the value of the trade-in vehicle." In re Lavigne, No.
23 07-30192, 2007 WL 3469454 at *1 n.1 (Bankr. E.D. Va. Nov. 14, 2007).

24 ³In its Memorandum in Support of DaimlerChrysler's Objection to
25 Confirmation, DaimlerChrysler states that the total amount financed was
26 \$26,975 and that the current debt is \$25,191.81. DaimlerChrysler's
Claim, supported by a copy of the Retail Installment Contract, reflects
the amount financed as \$26,078. The Claim further reflects the amount of
the debt as of the Petition Date as \$24,869.06. It is this amount that
DaimlerChrysler contends should be treated as a secured claim under the
Plan.

1 Johnsons propose to treat \$13,800 of the Claim as secured, and the
2 balance of the Claim as unsecured. The Plan estimates that unsecured
3 creditors will receive an approximate 40% distribution on their claims.

4 DaimlerChrysler contends that its finance of the negative
5 equity in the Trade In constitutes "value given to enable the [Johnsons]
6 to acquire rights in or the use of the [Vehicle]." Accordingly,
7 DaimlerChrysler objects to the Plan on the basis that because it holds a
8 PMSI in the Vehicle, purchased by the Johnsons within 910 days preceding
9 the Petition Date for their personal use, the Hanging Paragraph prevents
10 the Johnsons from using § 506 to bifurcate the Claim into secured and
11 unsecured components. DaimlerChrysler asserts that the Plan must provide
12 for the payment of the Claim in the amount filed, i.e., \$24,869.06, in
13 equal monthly installments. The Johnsons counter that DaimlerChrysler's
14 financing of negative equity does not constitute a purchase money
15 obligation, and therefore cannot give rise to a PMSI. It is their
16 position that because DaimlerChrysler does not hold a PMSI in connection
17 with that portion of the Claim relating to the finance of negative
18 equity, DaimlerChrysler is not entitled to the protection afforded by the
19 Hanging Paragraph.

20 On October 18, 2007, I heard argument on DaimlerChrysler's
21 objection to confirmation of the Plan, after which I took the matter
22 under submission. This Memorandum Opinion constitutes my findings of
23 fact and conclusions of law, which I make pursuant to Fed. R. Civ. P.
24 52(a), applicable in this contested matter pursuant to Fed. R. Bankr. P.
25 9014. I have core jurisdiction to resolve plan confirmation issues
26 pursuant to 28 U.S.C. §§ 1334(b), 157(a), 157(b)(1), and 157(b)(2)(L).

1 DISCUSSION

2 A. Treatment of DaimlerChrysler's Claim Under the Plan.

3 In order to have the Plan confirmed, the Johnsons must provide
4 one of three alternative treatments with respect to any allowed secured
5 claim of DaimlerChrysler: (1) DaimlerChrysler must consent to its
6 treatment under the Plan; (2) the Johnsons may retain the Vehicle and
7 provide a stream of payments to DaimlerChrysler; or (3) the Johnsons must
8 surrender the Vehicle to DaimlerChrysler. See § 1325(a)(5). Because the
9 Johnsons have elected to retain the Vehicle, and to provide
10 DaimlerChrysler with a stream of payments, § 1325(a)(5)(B) requires,
11 among other things, that the Plan distribute to DaimlerChrysler the
12 present value of its allowed secured claim as of the Petition Date, and
13 provide for equal monthly payments in an amount sufficient to provide
14 adequate protection to DaimlerChrysler.

15 DaimlerChrysler contends it has additional rights with respect
16 to its treatment under the Plan; under the Hanging Paragraph,
17 DaimlerChrysler asserts the present value of its allowed secured claim
18 must be the full amount of its debt, i.e., the amount of the Claim, as of
19 the Petition Date.

20 Effective in cases filed on or after October 17, 2005, BAPCPA
21 added the Hanging Paragraph to § 1325(a). As relevant to the matter
22 before me, the Hanging Paragraph provides:

23 For purposes of paragraph [1325(a)](5), section 506 shall not
24 apply to a claim described in that paragraph if the creditor
25 has a purchase money security interest securing the debt that
26 is the subject of the claim, the debt was incurred within the
910-day [period] preceding the date of the filing of the
petition, and the collateral for that debt consists of a motor

1 vehicle (as defined in section 30102 of title 49) acquired for
2 the personal use of the debtor. . . .

3 The Hanging Paragraph has been the subject of substantial
4 litigation and disputes regarding its interpretation. It is now settled
5 in this circuit, through decisions of the Bankruptcy Appellate Panel,⁴
6 that the Hanging Paragraph applies to § 1325(a)(5) to preclude debtors
7 from using cramdown⁵ of a secured claim with respect to a vehicle
8 purchased within 910 days prior to a bankruptcy petition, provided that
9 the secured creditor's claim satisfies the criteria set by the Hanging
10 Paragraph. To fall within the protection of the Hanging Paragraph, the
11 secured claim must meet the following conditions:

12 The creditor must have a purchase-money security interest; and
13 The purchase-money security interest must secure the debt that
14 is the subject of the claim; and
15 That debt must be incurred no more than 910 days before the
16 date of the debtor's filing; and
17 The collateral for the debt must be a "motor vehicle"; and
18 That motor vehicle must have been acquired for the personal use
19 of the debtor.

17 In re Trejos, 352 B.R. 249, 264 (Bankr. D. Nev. 2006).

18 The only issue in the dispute before me is whether
19 DaimlerChrysler has a PMSI in the Vehicle. The issue arises because the
20 financing which forms the basis of the Claim includes funds provided both
21 / / /

23 ⁴See Wells Fargo Financial Acceptance v. Rodriguez (In re
24 Rodriguez), 375 B.R. 535 (9th Cir. BAP 2007); Trejos v. VW Credit, Inc.
(In re Trejos), 374 B.R. 210 (9th Cir. BAP 2007).

25 ⁵For a brief explanation of the concept of cramdown and its
26 operation, see In re Sanders, No. 07-50783-C, 2007 WL 3047233 at *4-5
(Bankr. W.D. Tex. Oct. 18, 2007).

1 for the Johnsons' purchase of the Vehicle and for payoff of the Johnsons'
2 negative equity in the Trade In.

3
4 B. Whether a PMSI Exists is Determined By State Law.

5 The Bankruptcy Code does not define the term "purchase money
6 security interest." It is lifted from the Uniform Commercial Code
7 ("UCC"), which has been enacted with variations among the states as state
8 code law.

9 At least one bankruptcy court has suggested that a uniform
10 federal definition or interpretation of "purchase money security
11 interest" should be developed and applied. See In re Westfall, 365 B.R.
12 755, 759 n.4 (Bankr. N.D. Ohio 2007) ("Westfall I"), with further
13 elaboration in In re Westfall, 376 B.R. 210, 212-20 (Bankr. N.D. Ohio
14 2007) ("Westfall II"). In addition, Official Comment 8 to § 9-103 of the
15 UCC ("Official Comment 8"), promulgated pre-BAPCPA, indicates that usage
16 of the term "purchase money security interest" under Article 9 of the UCC
17 is not meant to preempt the definition or characterization of the term
18 under other statutes, including the Bankruptcy Code.⁶

19
20 _____
21 ⁶Official Comment 8 states:

22 . . . This section addresses only whether a security interest
23 is a "purchase-money security interest" under this Article . . .
24 . In particular, its adoption of the dual-status rule,
25 allocation of property rules, and burden of proof standards for
26 non-consumer-goods transactions is not intended to affect or
influence characterizations under other statutes. Whether a
security interest is a "purchase-money security interest" under
other law is determined by that law. For example, decisions
under Bankruptcy Code section 522(f) have applied both the

(continued...)

1 I can appreciate the irony in developing federal common law to
2 interpret a state law code term to aid in the interpretation of a federal
3 law code provision. However, I find it inappropriate to do so. I join
4 with most other courts that have considered the issue and look to state
5 law to determine whether DaimlerChrysler holds a PMSI. See, e.g., Trejos
6 v. VW Credit, Inc. (In re Trejos), 374 B.R. 210, 215 (9th Cir. BAP 2007);
7 In re Lavigne, No. 07-30192, 2007 WL 3469454 at *5 (Bankr. E.D. Va.
8 Nov. 14, 2007); In re Pajot, 371 B.R. 139, 147 (Bankr. E.D. Va. 2007).

9 Under Oregon's version of the UCC, DaimlerChrysler's security
10 interest is a PMSI "to the extent" the Vehicle is "purchase-money
11 collateral with respect to that security interest." O.R.S.
12 § 79.0103(2)(a). The Vehicle constitutes "purchase money collateral" if
13 it represents "goods or software that secures a purchase-money obligation
14 incurred with respect to that collateral." O.R.S. § 79.0103(1)(a). In
15 order for DaimlerChrysler to have a PMSI as a result of financing
16 negative equity, the negative equity must be a purchase money obligation
17 incurred with respect to the Vehicle. Oregon law defines a purchase
18 money obligation to be an "obligation of an obligor incurred as all or
19 part of the price of the collateral or for value given to enable the

20 / / /

21 _____
22 ⁶(...continued)
23 dual-status and the transformation rules. The Bankruptcy Code
24 does not expressly adopt the state law definition of "purchase-
25 money security interest." Where federal law does not defer to
26 this Article, this Article does not, and could not, determine a
question of federal law.

(emphasis in original).

1 debtor to acquire rights in or the use of the collateral if the value is
2 in fact so used." O.R.S. § 79.0103(1)(b).

3
4 C. DaimlerChrysler's Finance of Negative Equity Does Not Constitute a
5 Purchase Money Obligation.

6 O.R.S. § 79.0103(1)(b) imposes an alternative test for a
7 purchase money obligation: the debt must have been incurred as "all or
8 part of the price of the collateral," or it must have been incurred "for
9 value given to enable the debtor to acquire rights in or the use of the
10 collateral if the value is in fact so used."

11
12 1. Price of the collateral.

13 Courts have reached different conclusions on whether the "price
14 of the collateral" includes negative equity. "The case law grappling
15 with this issue has reached opposite conclusions, when trying to decide
16 whether the term ["price of the collateral"] could include the negative
17 equity paid off by part of the loan." In re Sanders, No. 07-50783-C,
18 2007 WL 3047233 (Bankr. W.D. Tex. Oct. 18, 2007).

19 Courts that have held that financing extended to cover negative
20 equity constitutes part of the "price of the collateral" rely primarily
21 on Official Comment 3 to § 9-103 of the UCC ("Official Comment 3"), or on
22 the doctrine of in pari materia⁷ to conflate the definition of cash sale
23 price contained in state automobile sales and finance laws with the term
24 "price of the collateral" in UCC § 9-103, or both.

25
26 ⁷Statutes in pari materia are to be construed together, as dealing
with the same subject matter.

1 Although the term "price" is not defined in the UCC, Official
2 Comment 3 provides some guidance as to its meaning. Official Comment 3
3 provides:

4 [T]he "price" of collateral or the "value given to enable"
5 includes obligations for expenses incurred in connection with
6 acquiring rights in the collateral, sales taxes, duties,
7 finance charges, interest, freight charges, costs of storage in
transit, demurrage, administrative charges, expenses of
collection and enforcement, attorney's fees, and other similar
obligations.

8 In analyzing "price of the collateral" in light of Official Comment 3,
9 one court has stated that "it is not apparent why a refinancing of
10 rolled-in negative equity on a trade-in as part of a motor vehicle sale
11 could not constitute an 'expense incurred in connection with acquiring
12 rights in' the new vehicle." GMAC v. Peaslee (In re Peaslee), 373 B.R.
13 252, 259 (W.D.N.Y. 2007) ("Peaslee II"). The court continues: "If the
14 buyer and seller agree to include the payoff of the outstanding balance
15 on the trade-in as an integral part of their transaction for the sale of
16 the new vehicle, it is difficult to see how that could *not* be viewed as
17 such an expense." Id. (emphasis in original).

18 Official Comment 3 further requires that for a PMSI to arise,
19 there must be a "close nexus between the acquisition of the collateral
20 and the secured obligation." Some courts have found this close nexus in
21 the financing of negative equity because the parties have agreed to a
22 "package transaction."

23 The trade-in of the vehicle was an integral part of the sales
24 transaction. The value of that trade-in along with its
25 accompanying debt affected the ultimate price that was paid for
26 the new pick-up truck. The negative equity is inextricably
intertwined with the sales transaction and the financing of the
purchase. This close nexus between the negative equity and
this package transaction supports the conclusion that negative

1 equity must be considered as part of the price of the
2 collateral.

3 Graupner v. Nuvell Credit Corp. (In re Graupner), Case No. 4:07-CV-37CDL,
4 2007 WL 1858291 at *2 (M.D. Ga. June 26, 2007).

5 Further, some courts which have found that the price of a
6 vehicle includes financed negative equity rely on the doctrine of in pari
7 materia to incorporate the definition of "cash sale price" from state
8 automobile sales and finance laws. In some states, the definition of
9 "cash sale price" explicitly includes negative equity financed as part of
10 the sale transaction. See Peaslee II, 373 B.R. at 260 (under New York's
11 Motor Vehicle Retail Installment Sales Act, the "cash sale price . . .
12 may include the unpaid balance of any amount financed under an
13 outstanding motor vehicle loan agreement"); Graupner, 2007 WL
14 1858291 at *2 n.1 (under the Georgia Motor Vehicle Sales Finance Act,
15 cash sales price includes negative equity); In re Petrocci, 370 B.R. 489,
16 501 (Bankr. N.D.N.Y. 2007)(the term "price" as used in New York's UCC
17 § 9-103 must be given the meaning set forth in the New York Motor Vehicle
18 Retail Installment Sales Act's definition of "cash sales price," which
19 includes negative equity).

20 Other courts, using various arguments directly contrasting with
21 the analyses discussed above, hold that negative equity is not a
22 component of the "price of the collateral".

23 One line of reasoning refutes the idea that negative equity
24 constitutes one of the "expenses incurred in connection with acquiring
25 rights in the collateral" contemplated by Official Comment 3. See, e.g.,
26 In re Pajot, 371 B.R. at 149-50 (list of expenses to be included in the

1 price of the collateral as set forth in Official Comment 3 does not
2 contemplate the inclusion of negative equity); In re Price, 363 B.R. 734,
3 741 (Bankr. E.D.N.C. 2007)(advances to pay off balance of debt on vehicle
4 that was traded in are not part of the purchase price; they are
5 "significantly and qualitatively different from the fees, freight
6 charges, storage costs, taxes, and similar expenses that are typically
7 part of an automobile sale.").

8 A second line of reasoning disagrees that inclusion of negative
9 equity in a single package financing agreement constitutes a sufficient
10 nexus between the acquisition of the collateral and the secured
11 obligation to transform negative equity into part of the price of the
12 vehicle financed. Rather, in that circumstance, there are simply "two
13 separate financial transactions memorialized on a single retail
14 installment contract document. . . ." In re Price, 363 B.R. at 741-42;
15 see also In re Mitchell, No. 07-02913, 2007 WL 3378229 (Bankr. M.D. Tenn.
16 Nov. 13, 2007); Citifinancial Auto v. Hernandez-Simpson (In re Hernandez-
17 Simpson), 369 B.R. 36 (D. Kan. 2007).

18 Those courts which refuse to use in pari materia to incorporate
19 a definition of "cash sale price" from state automobile sales and finance
20 laws do so for several reasons.

21 First, some courts hold that because the term "price of the
22 collateral" is not ambiguous, in pari materia, a doctrine of statutory
23 interpretation, is not available to incorporate definitions of "cash sale
24 price" under state automobile sales and finance laws. See In re
25 Blakeslee, No. 07-1019-3F3, 2007 WL 3133937 (Bankr. M.D. Fla. Sept. 19,
26 2007)(term "price of the collateral" in Florida's version of UCC § 9-103

1 is clear on its face; it "has the same meaning that it has always had in
2 connection with transactions for the acquisition of any collateral,
3 including a motor vehicle, which is the actual price of the collateral
4 being acquired." (quoting In re Peaslee, 358 B.R. 545, 556 (Bankr.
5 W.D.N.Y. 2006) ("Peaslee I"), rev'd, Peaslee II, 373 B.R. 252 (W.D.N.Y.
6 2007)); In re Acaya, 369 B.R. 564, 570 (Bankr. N.D. Cal. 2007) (concluding
7 that financing used to pay negative equity does not constitute part of
8 the price of the collateral as contemplated by UCC § 9-103; "[t]here is
9 no indication in the [California Automobile Sales Finance Act or its
10 legislative history] that . . . "cash price" was intended to effect a
11 departure from the traditional understanding of a purchase money security
12 interest.").

13 Other courts decline to use the in pari materia doctrine to
14 graft the definition of "cash sale price" from state automobile sales and
15 finance laws onto the term "price of the collateral" as used in the
16 definition of a purchase money obligation under the UCC because the two
17 statutes do not relate to the same subject matter or do not have the same
18 purpose. See, e.g., In re Lavigne, 2007 WL 3469454 at *7.

19 At least one court has applied in pari materia to conclude that
20 negative equity is not part of the "price of the collateral" because the
21 state automobile sales and finance law definition of "cash sale price"
22 does not expressly include negative equity. In re Conyers, No. 07-50855,
23 2007 WL 3244106 at *4-5 (Bankr. M.D.N.C. Nov. 2, 2007).

24 In another vein, one court advocates a "straightforward,"
25 contextual reading of the phrase "price of the collateral" within the
26 UCC, and rejects the proposition that "price of the collateral" includes

1 negative equity.

2 Context thus bolsters the conclusion that "price of the
3 collateral" need not be given some exotic meaning or treated as
4 some peculiar argot to sweep up more than the common
5 understanding of the phrase is intended to convey. One may
6 borrow money to buy something (e.g., a new vehicle), and also
7 borrow additional money for some other purpose (e.g., to pay
8 off the balance of a loan for the trade-in vehicle). The part
9 used to buy something is purchase money obligation. The part
10 used for some other purpose is not. We can tell what part was
11 used to buy something by simply looking at the price of the
12 thing purchased.

13 In re Sanders, 2007 WL 3047233 at *12.

14 I agree that "price of the collateral" does not include negative
15 equity. Negative equity is not similar in nature or scope to the other
16 "expenses incurred in connection with acquiring rights in the collateral"
17 contemplated by Official Comment 3. More importantly, I agree with the
18 Lavigne court that the liability for negative equity is not an expense
19 "incurred in connection with acquiring" the Vehicle; it is an antecedent
20 debt.

21 That liability necessarily preceded the acquisition. The pre-
22 existing indebtedness was simply rolled into the new car loan.
23 As the court observed in Pajot, "the substance of the
24 transaction, although instantaneous, is that the second
25 creditor is paying off the debtor's unsecured deficiency debt
26 on the first vehicle." Pajot, 371 B.R. at 154.

27 Lavigne, 2007 WL 3469454 at *8.

28 DaimlerChrysler requests that I utilize the doctrine of in pari
29 materia to incorporate into the UCC term "price of the collateral" the
30 definition of "cash sale price" from Oregon's automobile sales and
31 finance law, found at O.R.S. § 83.510(1). Doing so, however, does not
32 advance DaimlerChrysler's argument. In fact, O.R.S. § 79.0201(2)
33 specifically provides that Article 9 of the UCC as adopted in Oregon is

1 subject to the retail installment contract provisions of O.R.S. §§ 83.510
2 to 83.680.

3 O.R.S. § 83.510(1) provides:

4 "Cash sale price" means the price for which the motor vehicle
5 dealer would sell to the buyer, and the buyer would buy from
6 the motor vehicle dealer, the motor vehicle that is covered by
7 the retail installment contract, if the sale were a sale for
8 cash instead of a retail installment sale. The cash sale price
may include any taxes, registration, license and other fees and
charges for accessories and their installation and for
delivering, servicing, repairing or improving the motor
vehicle.

9 This definition of "cash sale price" does not explicitly include negative
10 equity, as do similar statutes in New York, Georgia, and California.
11 Nevertheless, DaimlerChrysler asserts that the omission is immaterial,
12 because the list of additional items O.R.S. § 83.510(1) says may be
13 included in the cash sale price does not exclude negative equity.

14 DaimlerChrysler's reasoning fails for two reasons. First,
15 because the "cash sale price" is the price the Johnsons would have paid
16 the Dealer in a cash transaction, it logically cannot include negative
17 equity. The Johnsons never would have paid the amount of the negative
18 equity to the Dealer in an all cash transaction; instead, they would have
19 paid the lender which financed the Trade-In directly.

20 Second, automobile finance transactions are subject to
21 Regulation Z of the Federal Reserve Board, which, beginning in 1998,
22 added disclosure requirements concerning the financing of negative
23 equity. Thereafter, numerous states, including Oregon, enacted
24 legislation to address negative equity disclosures at the state level.
25 See Kenneth J. Rojc & Thomas K. Juffernbruch, Negative Equity in Trade-In
26 Vehicles: Regulation Z and State Law Developments, 55 Bus. Law. 1295

1 (2000). Oregon's version of Regulation Z is contained in the Oregon
2 Motor Vehicle Retail Installment Sales Act, 1999 Or. Laws 525, codified
3 at O.R.S. § 83.520(3)(d), which mandates the form and content of a motor
4 vehicle retail installment contract in Oregon, and specifically requires
5 that any amount "actually paid or to be paid by the motor vehicle dealer
6 pursuant to an agreement with the buyer to discharge a security interest,
7 lien or lease interest on property traded in" is to be listed separately
8 from the "cash sale price of the motor vehicle which is the subject
9 matter of the retail installment contract." Compare O.R.S.
10 § 83.520(3)(a) with O.R.S. § 83.520(3)(d). If anything, O.R.S. § 83.520
11 indicates that negative equity is not a part of the "cash sale price" of
12 the Vehicle.

13 The doctrine of in pari materia is available for interpretation
14 of Oregon statutes.

15 In interpreting a statute, our task is to discern what the
16 legislature intended. That inquiry begins with the text of the
17 statutory provision itself, because the text is the best
18 evidence of the legislature's intent. Also pertinent at that
19 first level of analysis is the context of the statute under
20 consideration. Context includes other related statutes.

21 State v. Carr, 877 P.2d 1192, 1194 (Or. 1994) (en banc).

22 I find that in the context of deciding whether under Oregon law,
23 negative equity can be part of the "price of the collateral" and
24 therefore a purchase money obligation with respect to a consumer's
25 purchase of a vehicle, the legislative intent can be gleaned from the
26 text and context of the Oregon Motor Vehicle Retail Installment Sales
Act. Accordingly, I find it appropriate, under the doctrine of in pari
materia, to use O.R.S. §§ 83.510(a) and 83.520(3) as aids in determining

1 what constitutes "price of the collateral" for purposes of O.R.S.
2 § 79.0103(1)(b).

3 For the reasons stated above, I conclude that negative equity
4 does not constitute part of the purchase price of the Vehicle under
5 Oregon law.

6
7 2. Value given to enable debtor to acquire rights in the
8 collateral

9 A purchase money obligation also can arise based on "value given
10 to enable the debtor to acquire rights in or the use of the collateral if
11 the value is in fact so used."⁸ O.R.S. § 79.0103(1)(b). Not
12 surprisingly, there is considerable overlap in the analyses courts have
13 used in interpreting the phrase "value given to enable the debtor to
14 acquire rights in or the use of the collateral if the value is in fact so
15 used" and in determining the meaning of "price of the collateral." That
16 overlap principally occurs in the application of Official Comment 3.

17 For instance, many courts evaluate the Official Comment 3 phrase
18 "value given to enable" to determine whether negative equity can be
19 / / /

21 ⁸While a purchase money obligation based on "price of the
22 collateral" and a purchase money obligation based on "value given to
23 enable the debtor to acquire rights in or the use of the collateral" both
24 give rise to a PMSI, the UCC recognizes a greater need to protect the
25 PMSI which is based on the "price of the collateral" than the PMSI based
26 on the enabling loan. See O.R.S. § 79.0324(7) ("A security interest
securing an obligation incurred as all or part of the price of the
collateral has priority over a security interest securing an obligation
incurred for value given to enable the debtor to acquire rights in or the
use of collateral."), and Official Comment 13 thereto.

1 considered an expense "incurred in connection with acquiring rights in
2 the collateral."

3 The Sanders court ruled that financed negative equity was not
4 value given to enable debtors to acquire rights in a vehicle because it
5 did not represent an obligation for an expense incurred in acquiring
6 rights in the collateral. In re Sanders, 2007 WL 3047233 at *13.

7 The [expense] items listed [in Official Comment 3] are closely
8 connected with the purchase of the vehicle itself - compensating
9 the seller for the cost of delivering the vehicle, repaying the
10 seller for sales taxes realized from the sale of the vehicle,
11 paying for such administrative charges as title costs and license
fees associated with transferring ownership of the vehicle from
seller to buyer, and the like. In addition, the list includes
costs normally associated with the enforcement of the security
interest once granted. . . .

12 Id. See also In re Conyers, 2007 WL 3244106 at *5 (payment of
13 preexisting debt is not similar to other enumerated items); In re Pajot,
14 371 B.R. at 152 (that negative equity payoff is neither necessary nor
15 compelled "cuts against" its inclusion with the list of expenses
16 contained in Official Comment 3).

17 Given that financing negative equity is increasingly common, it
18 was not an oversight that the legislature did not include negative equity
19 in the list of "expenses incurred in connection with acquiring rights in
20 the collateral" set forth in Official Comment 3. In re Blakeslee, 2007
21 WL 3133937 at *3. Further, negative equity is not of the same "type" or
22 "magnitude" as the expenses listed in Official Comment 3. Id.

23 There is greater division among courts on the question of
24 whether "value given" in the form of financing negative equity creates a
25 close nexus with the acquisition of collateral.

26 / / /

1 Some courts have found the requisite close nexus based on the
2 package transaction itself. For instance, in finding that "[t]he phrase,
3 'value given to enable the debtor to acquire rights in' purchase money
4 collateral is broad enough to include the 'negative equity' financed by a
5 lender," the court in In re Cohrs found the required "close nexus"
6 between the acquisition of the property and the secured obligation
7 existed where the financed negative equity was "part of a single
8 transaction and all components of the obligation incurred [were] for the
9 purpose of acquiring the property securing the new obligation." In re
10 Cohrs, 373 B.R. 107, 110 (Bankr. E.D. Ca. 2007). See also In re Brei,
11 No. 4:07-BK-01354-JMM, 2007 WL 4104884 at *1 (Bankr. D. Ariz. Nov. 14,
12 2007)(deciding, without analysis, that "the entire amount which was lent
13 was for the purpose of acquiring a vehicle, regardless of whether some
14 portion thereof was used to pay off a previous lien on the trade-in.");
15 In re Petrocci, 370 B.R at 499 (negative equity constitutes "value given
16 to enable the debtor to acquire rights in the collateral" where
17 "[n]egative equity financing is inextricably linked to the financing of
18 the new car. It is clear that one would not take place without the
19 other.").

20 Other courts have determined that negative equity financing does
21 not provide the direct assistance for purchasing a vehicle that the
22 standard "for value given to enable the debtor to acquire rights in . . .
23 the collateral" requires. For example, the Sanders court recognized a
24 distinction between facilitating a transaction and enabling a debtor to
25 acquire rights in a new vehicle. "The fair implication of this
26 [condition that the value given be 'in fact so used'] is that the value

1 must be used to acquire *rights* in the collateral, as opposed to, for
2 example, *enabling the transaction* that ultimately results in the
3 borrowers acquiring rights in the collateral." Sanders, 2007 WL 3047233
4 at *14 (emphasis in original). In re Blakeslee, 2007 WL 3133937 at *3
5 (The court observed that it did not find "the requisite close nexus
6 between the payoff of negative equity and the acquisition of the new
7 vehicle."). See also In re Pajot, 371 B.R. at 154 (because the substance
8 of the transaction whereby negative equity is financed is that the second
9 creditor is paying off the debtor's unsecured deficiency debt on the
10 first vehicle, "it is not clear that there is a close nexus between the
11 negative equity payoff and the acquisition of the new vehicle.").

12 It is not enough that value be given to acquire rights in the
13 vehicle; the value given must be "in fact so used." Sanders, 2007 WL
14 3047233 at *14.

15 Still other courts look to the language "value given to enable"
16 in an effort to determine whether the finance of negative equity
17 qualifies as a purchase money obligation. Starting with the Black's Law
18 Dictionary definition of enable, the Conyers court concluded that the
19 financing of negative equity was not required for the debtor to purchase
20 a new vehicle. Rather, the loan of additional money was "a convenience
21 and an accommodation to the Debtor." In re Conyers, 2007 WL 3244106 at
22 *5.

23 The court in Acaya found the words "value given to enable the
24 debtor to acquire rights in or the use of the collateral if the value is
25 in fact so used" to be ambiguous in the context of the Hanging Paragraph.
26 In re Acaya, 369 B.R. at 569. Applying Matthews v. Transamerica Fin.

1 Servs. (In re Matthews), 724 F.2d 798 (9th Cir. 1984), which held that a
2 refinance destroyed the purchase money character of an obligation, as
3 part of its rationale, the Acaya court concluded that "the amount used to
4 pay the negative equity does not constitute . . . value given to acquire
5 rights in the collateral" In re Acaya, 369 B.R. at 570.

6 In Matthews, the Ninth Circuit addressed the character of an
7 enabling loan in deciding a motion to avoid a non-PMSI in debtor's
8 property under § 522 of the bankruptcy code. Matthews, 724 F.2d at 799-
9 801. While Matthews arises in the context of lien avoidance and predates
10 the enactment of Revised Article 9, it is nevertheless instructive for
11 this case. Prior UCC § 9-107 defined a PMSI as a security interest taken
12 by a person who "gives value to enable the debtor to acquire rights in or
13 use of collateral if such value is in fact so used." This is essentially
14 the same phrase as used in current O.R.S. § 79.0103(1)(b), except that in
15 the current version the article "the" is inserted before "collateral."
16 Matthews articulates that a refinance constitutes value to enable debtors
17 to pay off a loan, not to acquire rights in collateral. Speaking to the
18 apparent harshness of the loss of a PMSI through a refinance, the
19 Matthews court stated:

20 The argument that form should not be elevated over substance
21 has merit in some settings, but not here. We are dealing with
22 a statutory scheme that governs the priorities among creditors.
23 Purchase money security is an exceptional category in the
24 statutory scheme that affords priority to its holder over other
25 creditors, but only if the security is given for the precise
26 purpose as defined in the statute. And we should not lose
sight of the fact that the lender chooses the form.

25 Id. at 801.

26 / / /

1 In the matter before me, the financed negative equity is nothing
2 more than a refinance of the pre-existing debt owed on the Trade-In.
3 Accordingly, it does not create the requisite close nexus between "value
4 given" and the Johnsons' acquisition of rights in the Vehicle. I
5 previously have determined that financing of negative equity is not an
6 expense incurred as part of the "price of the collateral." Neither is it
7 value given and used to enable a debtor to acquire rights in the
8 collateral.

9

10 3. Financed negative equity is not a purchase money obligation.

11 Because financed negative equity is neither an obligation
12 incurred as "all or part of the price of the collateral" nor an
13 obligation incurred "for value given to enable the debtor to acquire
14 rights in or the use of the collateral if the value is in fact so used,"
15 for purposes of O.R.S. § 79.0103(1)(b), financed negative equity is not a
16 purchase money obligation.

17

18 D. Applicability of the Hanging Paragraph

19 Having determined that the financed negative equity portion of
20 DaimlerChrysler's Claim is not covered by a PMSI, I now must decide what
21 effect that determination has on treatment of the Claim under the Plan.

22 Most courts concluding that financed negative equity is not a
23 purchase money obligation then apply one or the other of two interpretive
24 rules, developed under state UCC law, for dealing with the secured
25 creditor's PMSI: the "transformation rule" or the "dual status rule."
26 "The 'transformation rule' provides that when a transaction contains both

1 purchase money and non-purchase money obligations, the entire transaction
2 is transformed into a non-purchase money obligation." In re Burt, No.
3 07-23193, 2007 WL 4087071 n.34 (Bankr. D. Utah Oct. 24, 2007). The dual
4 status rule "allows a security interest to have both the status of a
5 PMSI, to the extent that it is secured by collateral purchased with loan
6 proceeds, and the status of a general security interest, to the extent
7 that the collateral secures obligations unrelated to the purchase." In
8 re Petrocci, 370 B.R. at 504.

9 Those courts which have applied the transformation rule
10 generally hold that the Hanging Paragraph does not afford any protection
11 against cramdown of the secured creditor's claim. See In re Blakeslee,
12 2007 WL 3133937 at *5 (court is unwilling to "unwind the manipulations"
13 applying the dual status rule would require of it); In re Price, 363 B.R.
14 at 746 ("[G]enerally when negative equity is involved, the appropriate
15 rule is the transformation rule.").

16 Those courts which have applied the dual status rule have
17 allowed protection against cramdown under the Hanging Paragraph only for
18 the portion of the secured creditor's claim that is a purchase money
19 obligation. See Hernandez-Simpson, 369 B.R. at 46 (under Kansas law,
20 dual status rule applies even to consumer transactions); In re Lavigne,
21 2007 WL 3469454 at *1 n.1 (adopting dual status rule unless a negative
22 equity transaction is "structured such as to obfuscate transaction
23 details or otherwise abuse the dual status rule," in which case the court
24 would "not hesitate to discretionarily apply the more stringent
25 transformation rule"); In re Conyers, 2007 WL 3244106 at *6 (applying
26 dual status rule preserves congressional intent in enacting the Hanging

1 Paragraph); In re Hayes, 376 B.R. 655, 676 (Bankr. M.D. Tenn.
2 2007)(applying dual status rule such that a secured creditor holds a PMSI
3 "within the scope of the hanging sentence to the extent of its claim less
4 . . . the payoff of negative equity. . . ."); Westfall II, 376 B.R. 210
5 (applying dual status rule, but not as a matter of state law); In re
6 Honcoop, No. 07-1358, 2007 WL 3133936 (Bankr. M.D. Fla. Sept. 19,
7 2007)(in a case finding that GAP insurance was not purchase money
8 obligation, court applied dual status rule to reduce secured claim by
9 amount of non-purchase money obligation; balance of secured claim was not
10 subject to bifurcation under the Hanging Paragraph); In re Pajot, 371
11 B.R. at 163 (applying dual status rule, but "not without reservation");
12 In re Acaya, 369 B.R. at 571 (applying dual status rule; finding no
13 impediment to easy allocation of prepetition payments given traceability
14 resulting from compliance with California's automobile sales and finance
15 laws).

16 Two recent decisions have turned immediately from the analysis
17 of whether the secured creditor has a purchase money obligation based on
18 financing negative equity to application of the Hanging Paragraph,
19 without first determining the impact of the secured creditor's non-
20 purchase money obligation under state law. In re Mitchell, 2007 WL
21 3378229 at *5; In re Sanders, 2007 WL 3047233 at *17-18. The Mitchell
22 and Sanders courts focused on the phrase "if the creditor has a purchase
23 money security interest securing the debt that is the subject of the
24 claim." Their reasoning is that Congress' use of the conditional "if"
25 rather than more flexible language such as "to the extent," coupled with
26 the omission of any quantifying modifier to the word debt, e.g. "part of"

1 the debt, requires an absolute result, mandating application of the
2 transformation rule rather than the dual status rule.⁹

3 In yet another analytical variation, the Westfall II court
4 utilized the "excluded purpose" doctrine¹⁰ of federal statutory
5 interpretation in concluding that it was not appropriate to look to state
6 law to ascertain whether the transformation rule or the dual status rule
7 should apply to determine the impact on a PMSI when part of the subject
8 debt is not a purchase money obligation. Westfall II, 376 B.R. at 216-
9 17. In reaching this conclusion, the Westfall II court observed, as
10 noted above, that Official Comment 8 expressly provides that the state
11 law definition of PMSI was not meant to apply to bankruptcy law. Without
12 analyzing the language of the Hanging Paragraph, the court "adopted" the
13 dual status rule because "[s]imply, application of the transformation
14 rule is too severe." Id. at 219.

15 I now turn to the task of applying these concepts to the matter
16 before me.

17 / / /

18 / / /

19

20

21 ⁹But see In re Hayes, 376 B.R. 655, 676 (Bankr. M.D. Tenn.
22 2007) ("The hanging sentence mixes state and federal legal principles in
23 the complicated manner discussed above. Overlaying a federal
24 transformation rule produces a wobbly three-legged stool anchored by no
obvious congressional policy choice in this context.").

25 ¹⁰"Excluded purpose means that a state statute should not serve as a
26 federal rule of decision if the federal purpose was excluded from the
state law. That is the case in the state law definition of purchase
money." Westfall II, 376 B.R. at 216.

1 Oregon's Revised Article 9¹¹ adopted the dual status rule for
2 non-consumer transactions, so that even if purchase money collateral also
3 secures an obligation that is not a purchase money obligation, the PMSI
4 does not lose its status as such for any portion of the debt. O.R.S.
5 § 79.0103(6)(a). Oregon's dual status rule has broader implications
6 however, because it provides, again in non-consumer transactions, that a
7 PMSI does not lose its status even if the purchase money obligation is
8 renewed, refinanced, consolidated, or restructured. Id. Whether to
9 apply the dual status rule in consumer transactions is left to the
10 discretion of the courts without further guidance from the statute.

11 The limitation of the rules . . . of this section to
12 transactions other than consumer-goods transactions is intended
13 to leave to the court the determination of the proper rules in
14 consumer-goods transactions. The court may not infer from that
15 limitation the nature of the proper rule in consumer-goods
16 transactions and may continue to apply established approaches.

17 O.R.S. § 79.0103(8).

18 In light of that discretion, I return to the language of the
19 Hanging Paragraph to examine it in context in the Bankruptcy Code, as
20 modified by BAPCPA. That is appropriate because in interpreting the
21 language of a code provision, it is essential to consider "the language
22 itself, the specific context in which that language is used, and the
23 broader context of the statute as a whole." Robinson v. Shell Oil Co.
24 519 U.S. 337, 341 (1997). Statutory interpretation is a "holistic
25 endeavor." United Sav. Ass'n of Texas v. Timbers of Inwood, 484 U.S.

26 ¹¹For a discussion of the transformation rule and the dual status
rule under former Article 9 and Revised Article 9, see Keith G. Meyer, A
Primer on Purchase Money Security Interests Under Revised Article 9 of
the Uniform Commercial Code, 50 U. Kan. L. Rev. 143, 155-161 (2001).

1 365, 371 (1988). If the interpretation of statutory language is not
2 clear from the plain meaning of the words used, the statute's context
3 within the overall statutory framework should be examined, with
4 appropriate consideration of the legislative history. Davis v. Michigan
5 Dept. of Treasury, 489 U.S. 803, 809 (1989) ("[S]tatutory language cannot
6 be construed in a vacuum. It is a fundamental canon of statutory
7 construction that the words of a statute must be read in their context
8 and with a view to their place in the overall statutory scheme.")
9 (citation omitted).

10 With those principles in mind, the relevant language of the
11 Hanging Paragraph is "[f]or purposes of paragraph [1325(a)](5), section
12 506 shall not apply to a claim described in that paragraph if the
13 creditor has a purchase money security interest securing the debt that is
14 the subject of the claim. . . ." (emphasis added). Congress did not
15 state specifically that the Hanging Paragraph applied to a claim or debt
16 "or any part or portion" of either. Neither did Congress specify that
17 the Hanging Paragraph could be applied only to the "entire" claim or
18 debt. I do not find the "plain language" of the Hanging Paragraph
19 dispositive as to whether the "dual status" or the "transformation" rule
20 should apply in this instance.

21 However, from the language of the Hanging Paragraph itself and
22 its limited legislative history,¹² it is clear that the Hanging Paragraph
23 was designed to combat a particular perceived abuse by debtors in chapter
24

25 ¹²For an exhaustive review of the legislative history of the Hanging
26 Paragraph, see the Addendum to Judge Lundin's decision in In re Hayes,
376 B.R. at 676-684.

1 13: purchasing a car shortly before a chapter 13 bankruptcy filing and
2 taking advantage of the substantial depreciation that occurs immediately
3 when a new car is driven off the lot to cram down the secured creditor's
4 collateral interest.

5 Prior to BAPCPA, vehicle financiers could be harmed by a debtor
6 who acquired a vehicle in the months leading up to bankruptcy,
7 then filed bankruptcy and crammed the creditor's claim down to
8 the collateral value on the date of filing. Due to the rapid
9 depreciation of motor vehicles the moment they leave the
10 dealer's lot, debtors could often reap a benefit by cramming
11 down the debt, only paying a secured claim equal to the
12 depreciated value of the car...In enacting the hanging
13 paragraph, Congress fixed this disparity to ensure that debtors
14 could not load up on vehicle-secured debt pre-petition only to
15 cram it down to the collateral value in bankruptcy.

16 In re Pajot, 371 B.R. at 159. See In re Lavigne, 2007 WL 3469454 at *11.

17 In light of that clear purpose behind the Hanging Paragraph, it
18 does not make sense to apply the transformation rule and deprive the
19 creditor of the benefit under BAPCPA of its vehicle PMSI entirely because
20 the creditor has financed some negative equity in its transaction with
21 the debtor. I find that applying the dual purpose rule is more
22 consistent with congressional intent, as reflected in the Hanging
23 Paragraph. Accordingly, I find that § 506 does not apply to the portion
24 of the Claim that is not a debt for negative equity financing, and
25 cramdown does not apply to that portion of DaimlerChrysler's Claim. I
26 will sustain Daimler Chrysler's objection to the Plan in part, and I will
deny confirmation of the Plan and enter a 28-day order for the Johnsons
to file a modified plan.

27 / / /

28 / / /

29 / / /

1 CONCLUSION

2 Financed negative equity is neither part of the "price of the
3 collateral" being purchased, nor is it "value given to enable the debtor
4 to acquire rights in or the use of the collateral" being purchased. It
5 must be one or the other in order to be a purchase money obligation under
6 O.R.S. § 79.0103(1)(b). Because a debt must be a purchase money
7 obligation in order to give rise to a PMSI, a security interest based on
8 debt arising from financed negative equity, paying off antecedent debt,
9 cannot be a PMSI. However, applying the "dual status" rule, as allowed
10 in the court's discretion under O.R.S. § 79.0103(8) and consistent with
11 the language and intent behind Congress's adoption of the Hanging
12 Paragraph, I hold that the protection of the Hanging Paragraph against
13 cramdown applies to the PMSI portion of DaimlerChrysler's Claim and
14 sustain DaimlerChrysler's objection to the Johnsons' Plan, in part. I
15 will deny confirmation of the Plan and enter a 28-day order for the
16 filing of a modified chapter 13 plan by the Johnsons.

17
18 cc: Todd Trierweiler
19 Lee M. Hess
20 Brian D. Lynch, Trustee
21 U.S. Trustee
22
23
24
25
26