

Michigan Law Review

Volume 52 | Issue 2

1953

Securities - Rights of Used Car Purchasers Under Trust Receipt Financing

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Recommended Citation

Walter H. Weiner S.Ed., *Securities - Rights of Used Car Purchasers Under Trust Receipt Financing*, 52 MICH. L. REV. 276 (1953).

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SECURITIES — RIGHTS OF USED CAR PURCHASERS UNDER TRUST RECEIPT FINANCING—The recent enactment of the Uniform Trust Receipts Act¹ by the Michigan legislature² was an important and much needed revision in the Michigan law of chattel security. Although the UTRA has been referred to as a “. . . perplexing maze of technical phrases . . . ,”³ it is submitted that the act contains a clear presentation of the changes which are to be effected, and should go far in freeing the financing of goods in the flow of commerce from some anachronistic shackles. The particular intent of this comment is to explore the impact of the UTRA and other recent legislation on the position of purchasers of used cars in the ordinary course of business. It is in this narrow field that the consumer seems most in jeopardy because of the effects of the Certificate of Title Act. Therefore, there will be only slight coverage of the effect of the UTRA on the financing of *new* cars, and no attempt to explore the financing of other goods, documents, or instruments. Since the UTRA specifically excludes from its operation the financing of purchases by the ultimate consumer,⁴ there will likewise be no coverage of the conditional sale contract.⁵

I. *The Situation at Common Law*

A history of the relatively new security device known as the trust receipt may be found in almost every case in which the validity or effect of the device has been in issue. Trust receipts were first used

¹ 9a U.L.A. 274 (1951).

² Mich. Pub. Acts (1952) No. 19, effective Sept. 18, 1952, Mich. Comp. Laws (1952 Supp.) §§555.401 to 555.419.

³ McColloch, J., in re Chappell, (D.C. Ore. 1948) 77 F. Supp. 573 at 575.

⁴ UTRA §1, Mich. Comp. Laws (1952 Supp.) §555.401, specifically excludes conditional sales vendors and purchase money mortgages. Cf. Commissioners' Prefatory Note, 9a U.L.A. 278 (1951).

⁵ For a discussion of consumer credit in the automobile industry see 61 YALE L.J. 718 (1952). See also Motor Vehicle Sales Finance Act, Mich. Comp. Laws (1952 Supp.) §§492.101 to 492.140, discussed by Cudlip and Tindall, "The Michigan Motor Vehicle Sales Finance Act," 31 MICH. S.B.J. 14 (Jan. 1952).

in the financing of imports, as a means of ensuring payment to the exporter and receipt of the goods by the importer who was unable or unwilling to advance the full price of the goods. A bank would pay the exporter who would transfer title to the bank and send the goods to the importer who had already executed a note and trust receipt to the bank. By substituting manufacturer or distributor for exporter, and dealer for importer, the arrangement was adapted to the domestic automobile industry and soon spread to other "heavy" goods.⁶ It was not long before the position of the bank was taken over by finance companies which specialized in "floor-planning" automobiles on trust receipt security and very often the financier was a subsidiary of the manufacturer. The proposition that the trust receipt was *sui generis* and so not subject to the recording requirements of chattel mortgages and conditional sales contracts received a varied reception in the courts. The tripartite transaction was variously interpreted by some courts as a consignment, or a conditional sales contract, or a pledge, or a chattel mortgage, or a bailment.⁷ However, many courts did recognize the trust receipt as a new and valid method of security to which the chattel mortgage and conditional sales contract requirements did not apply.⁸

The courts that recognized the tripartite trust receipt based their decisions for the most part on the fact that there were three parties involved and that the new mass merchandising methods that were being developed necessitated a new type of financing. This reasoning *a fortiori* limited the use of the trust receipt to the three-party transaction, since it was the acquisition of newly acquired goods by the dealer which distinguished the trust receipt from the more conventional types of security. The requirement of a three-cornered deal ensured the existence of new goods which prior creditors had no right to rely upon to satisfy their debts.⁹ Therefore, the test for a valid trust receipt was a tripartite transaction, in which the financier's (entruster's) security interest came from the manufacturer, distributor, or exporter,

⁶ For an excellent description of the mechanics of tripartite trust receipt financing, see *Singletary v. General Motors Acceptance Corp.*, (5th Cir. 1934) 73 F. (2d) 453 at 454.

⁷ 20 VA. L. REV. 689 at 691 (1934); 15 ORE. L. REV. 171 at 173 (1936).

⁸ Michigan, adhering to its practice of calling chattel security devices chattel mortgages, refused to recognize trust receipts as *sui generis*. *Motor Bankers' Corp. v. C.I.T. Corp.*, 258 Mich. 301, 241 N.W. 911 (1932); *C.I.T. Corp. v. Wiseman*, 287 Mich. 689, 284 N.W. 609 (1939).

⁹ VOLD, *CASES ON SALES*, 2d ed., 394 (1949), offers as another reason for distinguishing trust receipts from other forms of chattel security the fact that when trust receipts are used the borrower is not usually in such a pressing situation and the relative inequality between borrower and lender is not so pronounced, and therefore there is less reason for protecting the borrower.

and not from the dealer or importer who came to be known as the trustee. At this point it should be noted that the common law trust receipt transaction, while it logically prevented reliance by prior creditors, did not prevent reliance by subsequent creditors who had no notice that the goods in the trustee's possession were in any way encumbered. In this way the common law trust receipt was practically identical with a purchase money mortgage. Therefore, some doubt was cast upon the tripartite test when it was used to validate the trust receipt as against subsequent creditors and purchasers without notice. The recording requirements of the UTRA solve the problem of protecting subsequent creditors.

Since the very justification for the trust receipt was the tripartite arrangement, the courts would scrutinize the facts of each case and would invalidate the trust receipt unless this requirement was strictly adhered to. If trust receipts were used to secure loans on existing stocks of goods, this would completely avoid the chattel mortgage recording requirements and leave creditors with no protection against secret liens. It was felt that only the tripartite requirement prevented this result.¹⁰ To many this requirement seemed artificial, since title might accidentally have passed to the dealer before passing to the financier, while as a practical matter the requirement that the dealer receive new goods was being met. The courts that had seen the necessity of looking through the form of security devices and establishing the validity of the trust receipt were once again being bound by a new formal requirement of their own creation.¹¹ However, all agreed that the acquisition of new goods was the reason for excluding trust receipts from the recording requirements,¹² and it was the general confusion and appearance of new technicalities which led to the adoption of the UTRA by thirty states in twenty years.¹³

¹⁰ For an expression of this view see 31 MICH. L. REV. 558 (1933).

¹¹ There was often difficulty in determining whether a tripartite or a bipartite transaction was involved. On this point see Bacon, "A Trust Receipt Transaction: I," 5 FORDHAM L. REV. 17 at 42, n. 98 (1936); Commissioners' Prefatory Note, 9a U.L.A. 276 (1951); VOLD, CASES ON SALES, 2d ed., 418n. (1949).

¹² On common law trust receipts generally, see Frederick, "The Trust Receipt As Security," 22 COL. L. REV. 395, 546 (1922); Zane, "A Modern Instance of Zenothemis v. Demon," 23 MICH. L. REV. 339 (1925) (tracing trust receipts back to the practices of the ancient Greek traders); Hanna, "Trust Receipts," 19 CALIF. L. REV. 257 (1931); Bacon, "A Trust Receipt Transaction: I," 5 FORDHAM L. REV. 17 (1936); Lusk, "Trust Receipts," 12 TEMPLE L.Q. 189 (1938); MCGOWAN, TRUST RECEIPTS (1947); 17 MINN. L. REV. 790 (1933); 20 VA. L. REV. 689 (1934); 49 A.L.R. 267 (1927); 87 A.L.R. 304 (1933); 101 A.L.R. 447 (1936).

¹³ The UTRA was adopted by the Commissioners on Uniform State Laws in 1933. The current list of states which have enacted the UTRA appears in 9a U.L.A. (1952 Cum. Supp.) at 80.

II. *Floor Financing of Used Cars*

To appreciate the effect of the UTRA on the financing of used cars, it is necessary to understand the various methods by which used car dealers acquire and finance their stock in trade.¹⁴ The dealer may acquire used cars from a wholesaler. This is similar to a new-car dealer's acquiring his stock from a manufacturer or distributor, and would involve the tripartite transaction that was recognized at common law and is still recognized under the UTRA.

Another method is to accept the used car as partial payment for the purchase of a new car or another used car, the common "trade-in" transaction. The problem raised by this means of acquisition is whether the trade-in is subject to the same encumbrance as was the car purchased.

The third and most frequent manner in which used cars are acquired by dealers is through purchase from private individuals, one at a time. The dealer will pay for the car immediately and will then approach the financier for the purchase money. It is this manner of acquisition and financing which falls outside the common law trust receipt since only two parties are involved, and as yet no case has determined the validity of trust receipts in this transaction under the UTRA.

III. *Validity of Trust Receipts in Used-Car Financing Under the Uniform Trust Receipts Act*

The first method of acquisition and financing of used cars would clearly seem to be within the scope of the term "trust receipt" as it is defined by section 2(1)(a) of the UTRA.¹⁵ Here the wholesaler, a

¹⁴ For a concise discussion of various means of automobile dealer financing, see 43 MICH. L. REV. 605 (1944).

¹⁵ Mich. Comp. Laws (1952 Supp.) §555.402, providing:

"(1) A trust receipt transaction within the meaning of this act is any transaction to which an entruster and a trustee are parties, for 1 of the purposes set forth in subsection (3) whereby

(a) The entruster or any third person delivers to the trustee goods, documents or instruments in which the entruster (1) prior to the transaction has, or for new value (2) by the transaction acquires or (3) as the result thereof is to acquire promptly, a security interest. . . ."

Subsection (3) provides:

"A transaction shall not be deemed a trust receipt transaction unless the possession of the trustee thereunder is for . . . 1 of the following:

(a) In the case of goods, documents or instruments, for the purpose of selling or exchanging them, or of procuring their sale or exchange; or

(b) In the case of goods or documents, for the purpose of manufacturing or processing the goods delivered or covered by the documents, with the purpose of ultimate sale, or for the purpose of loading, unloading, storing, shipping, transshipping or otherwise dealing with them in a manner preliminary to or necessary to their sale. . . ."

third party, delivers to the trustee goods in which the entruster, who has already paid for the goods, has a security interest. This is the tripartite arrangement which for the most part¹⁶ is recognized under the UTRA as it was at common law.

The more complicated trade-in transaction is brought within the UTRA by a completely different, but by no means novel, line of reasoning. Section 10 of the UTRA provides that the entruster shall be entitled to the proceeds of the sale "as against all classes of persons as to whom his security interest was valid at the time of disposition by the trustee,"¹⁷ if the entruster makes a demand for accounting within ten days of the sale. This has been interpreted to mean that a failure on the part of the entruster to make such demand within ten days allows a subsequent lien to take precedence.¹⁸ Therefore, if the entruster makes his demand promptly and proceeds to make a new arrangement with regard to the car taken as a trade-in, a new trust receipt for the trade-in would be valid under the UTRA, since a third person delivered to the trustee goods "in which entruster . . . for new value by the transaction acquires . . ." a security interest.¹⁹ The "new value," as described by section 1, would be the release of the security interest in the trade-in which was acquired by prompt demand.²⁰ If such demand is not made and the trustee uses the trade-in as security for a loan from another financier, this would come within the third type of transaction described.

The use of trust receipts in the purchase of used cars from private individuals involves the bipartite type transaction, since the dealer has absolute title at the time he approaches the financier. As already stated, there has been no case deciding whether or not the UTRA applies in this situation. The common law condemnation of the bipartite trust receipt and the specific statement by the draftsmen of the UTRA that it was not intended to change existing chattel mortgage and conditional sales law²¹ must be balanced against the likewise specific statement by the draftsmen that the UTRA was intended to do away with

¹⁶ For a tripartite transaction valid at common law which may be invalidated by the UTRA, see 82 *UNIV. PA. L. REV.* 270 at 272 (1934).

¹⁷ *Mich. Comp. Laws* (1952 Supp.) §555.410.

¹⁸ *Peoples Finance and Thrift Co. of Visalia v. Bowman*, 58 *Cal. App. (2d)* 729, 137 *P. (2d)* 729 (1943); *Universal Credit Co. v. Citizens State Bank of Petersburg*, 224 *Ind. 1*, 64 *N.E. (2d)* 28 (1945).

¹⁹ UTRA §2(1)(a)(i), *Mich. Comp. Laws* (1952 Supp.) §555.402(1)(a)(1).

²⁰ UTRA §1, *Mich. Comp. Laws* (1952 Supp.) §555.401 defines "new value" so as to include ". . . new advances or loans made, or new obligations incurred, or the release or surrender of a valid and existing security interest, or the release of a claim to proceeds under section 10. . . ."

²¹ See note 4 *supra*.

the meaningless technicalities that had hampered the use of trust receipts,²² and also against the wording of the UTRA which would seem to allow bipartite trust receipts when new goods are acquired by the dealer.

That the UTRA as it was originally approved by the commissioners did not apply to the usual chattel mortgage situation seems clear. Section 2 requires a delivery of goods to the trustee as part of the transaction by which the entruster acquires his security interest. Further proof that the UTRA was not intended to effect chattel mortgage law is provided by the fact that several states added a third clause to section 2 which has been referred to as the "disemboweling" clause by Professor Llewellyn.²³ This clause defines a trust receipt transaction as one whereby:

" . . . the entruster gives new value in reliance upon the transfer by the trustee to such entruster of a security interest in goods or document in possession of the trustee and the possession of which is retained by the trustee. . . ."²⁴

The necessity of adding such a clause, which eliminates the requirement of a delivery to the trustee of goods or documents as part of the same transaction whereby the entruster acquires his security interest, is ample proof that the UTRA did not cover situations where the dealer borrowed money on his existing stock in trade. However, it does not follow that any time the security interest must pass from the dealer

²² Commissioners' Prefatory Note, 9a U.L.A. 277 (1951).

²³ HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS OF UNIFORM STATE LAWS AND PROCEEDINGS 105 (1938).

²⁴ Cal. Stat. (1935) p. 1930, Cal. Civ. Code (1937) §3014(1)(c). In the case of *In re Boswell*, (9th Cir. 1938) 96 F. (2d) 239, the constitutionality of the amendment was upheld against the argument that the act contained chattel mortgage provisions under a trust receipt title, the court in effect saying that trust receipts and chattel mortgages were one and the same to businessmen. The amendment was either ignored or misunderstood by the California court in *Metropolitan Finance Corp. of California v. Morf*, 42 Cal. App. (2d) 756, 109 P. (2d) 969 (1941), since the court required a tripartite transaction for trust receipts. In *C.I.T. Corp. v. Commercial Bank of Patterson*, 64 Cal. App. (2d) 722, 149 P. (2d) 439 (1944), involving substantially the same facts as did the *Morf* case, the court cited the *Morf* case and yet stated that a bipartite transaction was valid under §2(1)(a) of the UTRA, again ignoring the so-called chattel mortgage clause. In 1939 this clause was repealed, but in 1940 it was re-enacted with the limitation that it apply only to the automobile industry; in 1946 it was expanded to apply also to the airplane industry. The history, policy, and confusion of this clause is discussed in *VOLD, CASES ON SALES*, 2d ed., 432, n. 59 (1949), and 41 *COL. L. REV.* 1134 (1941). A case arising under the Illinois act, which also contains a chattel mortgage clause, indicates the type of problem that may arise under the confusing chattel mortgage provision. Plaintiff filed a statement of intention of trust receipt financing with A, and afterward defendant filed a similar statement. Defendant made a loan to A and took a trust receipt on A's existing stock in trade, and then plaintiff made a loan to A and took a trust receipt on the same goods. The court decided that the filing gave no interest in the goods and held for defendant. *Donn v. Auto Dealers Co.*, 385 Ill. 211, 52 N.E. (2d) 695 (1944).

to the financier the UTRA precludes trust receipts. To the contrary the UTRA specifically states: "The security interest of the entruster may be derived from the *trustee* or from any other person, and by pledge or by transfer of title or otherwise."²⁵ Therefore, the requirement under the UTRA seems to be the same requirement that originally validated tripartite trust receipts and was later lost sight of in the absolute condemnation of all bipartite trust receipts, namely the acquisition of new goods by the trustee.²⁶

Although there is no case in point, several decisions give strong indication that a situation in which a dealer acquires title to goods and *promptly* transfers a security interest to the entruster who gives *new value*²⁷ is within the UTRA definition of a trust receipt. The case of *In re Chappell*²⁸ held that the instruments involved were not trust receipts, because the dealer had the goods for too long a time when he transferred the security interest to the bank. The court limited the use of trust receipts to the acquisition of new goods. Likewise the court in *In re San Clemente Electric Supply*,²⁹ which was decided on alternative grounds, stated that trust receipts are not to be used for securing loans on existing stocks of goods, distinguishing the case where the security interest is transferred to the entruster promptly after the dealer acquires the goods.³⁰

²⁵ UTRA §2(1), Mich. Comp. Laws (1952 Supp.) §555.402(1)(b)(2). Emphasis added.

²⁶ In support of the proposition that the UTRA validates the transaction described, see Bacon, "A Trust Receipt Transaction: II," 5 *FORDHAM L. REV.* 240 at 257 et seq. (1936); Henley, "Uniform Trust Receipts Act," 23 *MISS. L.J.* 125 at 126 (1952): "Under subsequent developments, the financial institution usually does not acquire title from the producers or manufacturers; it acquires its title or security interest from the trustee in a transaction solely between two parties. This practice is specifically authorized by the Uniform Trust Receipts Act." See also 9 *SR. JOHNS L. REV.* 250 at 261 (1934); 12 *N.Y. UNIV. L.Q. REV.* 468 at 470 (1935); 18 *TEMPLE L.Q.* 406 (1944). The following is from 15 *ORE. L. REV.* 171 at 175 (1936): "In summary the act validates: (a) the tripartite transaction; (b) the bipartite transaction where the entruster's security interest is created by the same transaction in which the delivery of possession is made to the trustee; and (c) the bipartite transaction, involving instruments and documents, where the trustee has acquired title, and for new value exhibits such instruments as documents to the entruster, or his agent, and gives a security interest therein." In 41 *COL. L. REV.* 1134 at 1138, n. 24 (1941), there are listed four types of bipartite transactions made valid by the UTRA and other legislation.

²⁷ See note 20 *supra*.

²⁸ (D.C. Ore. 1948) 77 F. Supp. 573.

²⁹ (D.C. Cal. 1951) 101 F. Supp. 252.

³⁰ Cf. *Automobile Banking Corp. v. Weicht*, 160 Pa. Super. 422 at 428, 51 A. (2d) 409 (1947), where it was stated: "There are two types of trust receipt transaction: (a) the tripartite, where the finance company advances the funds for the purchase of the chattel, purchases it and receives title to it from the manufacturer and delivers possession to the dealer who gives his trust receipt to the finance company; or (b) the bipartite where the dealer has purchased and received title directly from the manufacturer and gives his receipt to the financing company. . . . The former is called the true or orthodox type, and

One further requirement for the validity of the bipartite trust receipt must be met. Section 2(1)(b)(ii) of the UTRA requires that delivery to the trustee "[be] pursuant to a prior or concurrent written and signed agreement of the trustee to give . . ." a writing designating the goods concerned, and reciting that a security interest will pass to the entruster, if trust receipts are not executed immediately.³¹ Therefore, there must be a *pre-existing contract* between the dealer and the financier which provides that the financier will finance the dealer's purchases and the dealer will execute trust receipts to the financier.³² This requirement is in accord with the intention that the UTRA not apply to chattel mortgages which are more likely to be isolated instances of loans to the dealer, rather than a common course of financing the acquisition of new goods.

One writer feels that there is another requirement for the bipartite trust receipt under the UTRA, viz., that the delivery by the third party be induced by a commitment to such third party by the financier at the request of the dealer.³³ This theory is novel and is supported neither by authority in the cases nor by other writers. Nor does the proponent of this theory attempt to offer any authority other than the UTRA itself, which has no such requirement on its face. The purpose of requiring the financier to induce delivery by a third person to the dealer is to ensure that the delivery and the execution of the trust receipt be one transaction, e.g., that trust receipts be used only in the financing of the acquisition of new goods. This is clearly the policy of the UTRA and it would seem that the UTRA can effectuate this policy without the engrafting of new and technical limitations. It should be recalled that one of the purposes of the UTRA was to do away with exactly this type of technicality, which was developed by overly zealous courts at common law.³⁴

our Pennsylvania cases have been largely of that type. [Citing cases.] One of the purposes of the Uniform Trust Receipts Act was to recognize and validate the transaction of the second type."

³¹ Mich. Comp. Laws (1952 Supp.) §555.402(1)(b)(2).

³² *In re Chappell*, (D.C. Ore. 1948) 77 F. Supp. 573 at 575. After this case, Oregon adopted the chattel mortgage clause, Ore. Laws (1951) c. 134, §1, amending Ore. Comp. Laws Ann. (1940) §75-102.

³³ McGOWAN, TRUST RECEIPTS 69, n. 43 (1947).

³⁴ On the UTRA generally, see Hanna, "Trust Receipts," 29 COL. L. REV. 545 (1929); Bogert, "The Effect of the Trust Receipts Act," 3 UNIV. CHI. L. REV. 26 (1935); Bacon, "A Trust Receipt Transaction: II," 5 FORDHAM L. REV. 240 (1936); 20 VA. L. REV. 689 (1934); 82 UNIV. PA. L. REV. 279 (1934); 12 N.Y. UNIV. L.Q. REV. 468 (1935); 15 ORE. L. REV. 171 (1936); McGOWAN, TRUST RECEIPTS (1947); 168 A.L.R. 359 (1947).

IV. *The Status of the Purchaser in Ordinary Course in Michigan Prior to the Uniform Trust Receipts Act*

Until recently it had been assumed that a purchaser in ordinary course of a used car in Michigan would take title free of encumbrances even though the chattel mortgage or other security device was recorded.³⁵ However, late in 1952 the Michigan Supreme Court suddenly provided a means for security holders to enforce their liens against consumers after leaving merchandise in the hands of the dealer-mortgagor. *Bayer v. Jackson City Bank and Trust Co.*³⁶ held that a chattel mortgagee could leave a used car in the possession of a dealer-mortgagor, and by retaining the certificate of title to the car could enforce his lien against a purchaser, if the mortgagor could not or did not pay the debt. The writer has already voiced his exception to this decision,³⁷ and the legislature seems also to have taken issue with the proposition expressed in the *Bayer* case that the purchaser could obtain no interest in the automobile because he failed to acquire an immediate transfer of the certificate of title. The court relied on provisions of the Certificate of Title Act which required the dealer to ". . . execute and acknowledge an assignment and warranty of title upon the certificate of title and deliver the same to the person to whom such transfer is made,"³⁸ and imposed a penalty upon the dealer for failure to do so.³⁹ These provisions were interpreted to mean that without such assignment and delivery the transaction was totally void.⁴⁰ After the transaction involved in the *Bayer* case took place and while the suit was pending, the legislature passed an amendment to the Certificate of Title Act to the effect that such assignment and immediate delivery is required only when the sale is made to a *licensed dealer*, and providing for a completely different procedure when a sale

³⁵ *Daas v. Contract Purchase Corp.*, 318 Mich. 348, 28 N.W. (2d) 226 (1947), noted in 46 MICH. L. REV. 255 (1947).

³⁶ 335 Mich. 99, 55 N.W. (2d) 746 (1952).

³⁷ 51 MICH. L. REV. 919 (1953).

³⁸ Mich. Comp. Laws (1948) §257.235.

³⁹ Mich. Comp. Laws (1948) §257.239.

⁴⁰ A hitherto unmentioned factor which further casts doubt on the proposition that the sale was totally void in the *Bayer* case is that the mortgagee, by retaining possession of the certificate of title, prevented the dealer from complying with Mich. Comp. Laws (1948) §257.235, which required that the dealer ". . . shall retain and have in his immediate possession at all times such assigned certificate of title. . . ." Mich. Comp. Laws (1948) §257.239 makes it ". . . a misdemeanor for *any* person to fail or neglect to properly endorse and deliver a certificate of title to a transferee or owner lawfully entitled thereto." Emphasis added. Whether or not this sanction applied to one who held the certificate of title as a security holder, the court held that one who caused the violation of an express requirement of a statute could claim the benefit of that statute.

or other transfer is made to anyone else.⁴¹ By doing away with the requirement of an immediate delivery of the certificate of title to the consumer, it would appear that the legislature must necessarily mean to do away with the line of decisions holding that a dealer could pass no interest to a consumer without such delivery.⁴²

The amendment to the Certificate of Title Act does not necessarily dispose of the *Bayer* case,⁴³ since it is unclear whether the decision rested on the ground that no interest could pass to the purchaser without the certificate of title, or that the recorded chattel mortgage was notice to all the world of the mortgagee's interest in the car,⁴⁴ or that the retention of the certificate of title by the mortgagee protected his interest.⁴⁵

If the court meant to say that the recorded mortgage gave the purchaser notice, then the decision is against the clear weight of authority and completely ignores the hardships imposed on purchasers which were previously recognized in the *Daas* case.⁴⁶ The court in effect would be requiring *every* purchaser of *every* type of chattel to search the record before he could safely make a purchase, and there is no assurance that a search of the record in his own locality would be sufficient.⁴⁷

If the court also meant to say that the retention of the certificate of title by the security holder gave the purchaser notice, then it has

⁴¹ Mich. Pub. Acts (1951) No. 270, effective Sept. 28, 1951. Mich. Comp. Laws (1952 Supp.) §257.235 now reads: "When the transferee of a vehicle is a dealer who holds the same for resale and operates the same only for purposes incident to resale and displays thereon the registration plates issued for such vehicle or when a transferee does not drive such vehicle or permit it to be driven on the highways, except for demonstration purposes incident to resale, the transferee shall not be required to obtain transfer of registration of such vehicle or forward the certificate of title to the department but such transferee shall retain and have in his immediate possession at all times such assigned certificate of title and upon transferring his title or interest to another person shall execute and acknowledge an assignment and warranty of title upon the certificate of title and deliver the same to the person to whom such transfer is made *if a licensed dealer; otherwise application for a new title shall be made by the transferor as provided in section 217(b).*" (Amending portion in italics.)

⁴² *Bayer v. Jackson City Bank and Trust Co.*, 335 Mich. 99 at 106, 55 N.W. (2d) 746 (1952). Cf. 7 BLASHFIELD, CYCLOPEDIA OF AUTOMOBILE LAW AND PRACTICE, perm. ed., §4255 (1950); 18 A.L.R. (2d) 813 (1951).

⁴³ The *Bayer* case does not apply to the purchase of new automobiles, since there is no certificate of title in existence until the first sale is made, as was decided in *Northwestern Finance Co. v. Crouch*, 258 Mich. 411, 242 N.W. 771 (1932).

⁴⁴ *Bayer v. Jackson City Bank and Trust Co.*, 335 Mich. 99 at 101, 55 N.W. (2d) 746 (1952).

⁴⁵ *Id.* at 103.

⁴⁶ *Daas v. Contract Purchase Corp.*, 318 Mich. 348, 28 N.W. (2d) 226 (1947).

⁴⁷ See citations of authorities noting the insuperable administrative task involved, and the inequalities resulting from enforcing the lien after the security holder has given the dealer ostensible ownership, in 46 MICH. L. REV. 255 (1947); 51 MICH. L. REV. 919 (1953).

ingeniously provided for a new means of perfecting chattel security devices, which could serve as a substitute for the usual recording requirements. By retaining the certificate of title, an otherwise unsecured creditor could demand that his claim to the automobile be satisfied first, because no valid sale of the car could be made without the certificate of title he holds. The Certificate of Title Act would become a law providing for the perfection of chattel security just as recording acts do. In this way the court would make compliance with the recording act unnecessary, since the security holder could perfect his lien merely by retaining possession of the certificate of title. This would put purchasers in ordinary course in the same position that chattel mortgage recording acts normally place only creditors of the mortgagor. A certificate of title might be ideal for recording liens, and much more convenient and practical than a recorder's office. Nevertheless, if the court meant to espouse the theory that the retention of the certificate of title was a means of perfecting a lien, the Michigan Certificate of Title Act received an extremely strained construction.⁴⁸

V. *The Effect of the Uniform Trust Receipts Act on the Rights of a Purchaser in Ordinary Course*

In contrast to the precarious position of the purchaser in ordinary course under Michigan law prior to September, 1952, the UTRA permits such a purchaser⁴⁹ to take free of the entruster's security interest.⁵⁰ It therefore becomes manifest that if the transactions dis-

⁴⁸ *Nelson v. Vieregiver*, 230 Mich. 38, 203 N.W. 164 (1925), decided that the indorsement of a lien on the certificate of title, in compliance with the requirements of Mich. Comp. Laws (1948) §257.222(c), did not satisfy the requirement of filing under the Chattel Mortgage Recording Act, Mich. Comp. Laws (1948) §566.140. However, the instant theory is distinguishable in that the effectiveness of the lien results from the retention of the certificate of title and not from the indorsement of the lien on the certificate as in the Vieregiver case. For a case which holds that a Certificate of Title Act supersedes a Chattel Mortgage Recording Act, see *Motor Investment Co. v. City of Hamlin*, 142 Tex. 486, 179 S.W. (2d) 278 (1944). Cf. 3 Wyo. L.J. 92 (1948).

⁴⁹ UTRA §1, Mich. Comp. Laws (1952 Supp.) §555.401, defines a buyer in the ordinary course of trade as one ". . . to whom goods are sold and delivered for new value and who acts in good faith and without actual knowledge of any limitation on the trustee's liberty of sale, including one who takes by conditional sale or under a pre-existing mercantile contract with the trustee to buy the goods delivered, or like goods, for cash or on credit. 'Buyer in the ordinary course of trade' does not include a pledgee, a mortgagee, a lienor, or a transferee in bulk."

⁵⁰ UTRA §9(2), Mich. Comp. Laws (1952 Supp.) §555.409(2), provides:

"(a) Sales by trustee in the ordinary course of trade.

(1) Where the trustee, under the trust receipt transaction, has liberty of sale and sells to a buyer in the ordinary course of trade, whether before or after the expiration of the 30-day period [for filing] specified in subsection (1) of section 8 of this act, and

cussed in parts II and III of this comment involve valid trust receipts, a purchaser in ordinary course will enjoy the benefits of the UTRA.

There then arises the question of whether the financier can avoid the operation of the UTRA by intentionally denominating the transaction as something other than a trust receipt. The fact that a particular security device is called a chattel mortgage or a conditional sale by the parties will not take the transaction out of the UTRA.⁵¹ Nor will a filing of the instrument under the Chattel Mortgage Recording Act remove the transaction from the operation of the UTRA, since section 16 provides:

"As to any transaction falling within the provision both of this act and of any other act requiring filing or recording, the entruster shall not be required to comply with both, but by complying with the provisions of either at his election may have the protection given by the act complied with; *except that buyers in the ordinary course of trade as described in subsection (2) of Section 9, and lienors as described in Section 11, shall be protected as therein provided, although the compliance of the entruster be with the filing or recording requirements of another act.*"⁵²

And finally, if the retention of the certificate of title is held to be a means of perfecting a security holder's interest, this in effect seems to make the Certificate of Title Act a recording act and section 16 will again bring the transaction within the UTRA. This leaves open the question of whether the parties can engage in a transaction qualifying as a trust receipt under section 2 of the UTRA, and still avoid the protection which section 9 of the UTRA gives to the purchaser in ordinary course by expressing an intention not to have section

whether or not filing has taken place, such buyer takes free of the entruster's security interest in the goods so sold, and no filing shall constitute notice of the entruster's security interest to such a buyer.

(2) No limitation placed by the entruster on the liberty of sale granted to the trustee shall affect a buyer in the ordinary course of trade, unless the limitation is actually known to the latter. . . .

"(c) Liberty of sale.

If the entruster consents to the placing of goods subject to a trust receipt transaction in the trustee's stock in trade or in his sales or exhibition rooms, or allows such goods to be so placed or kept, *such consent or allowance shall have like effect as granting the trustee liberty of sale.*" Emphasis added.

⁵¹ UTRA §2(2), Mich. Comp. Laws (1952 Supp.) §555.402(2), provides for the only formal requirements of a trust receipt: "A writing such as is described in subsection 1, paragraph (b)(1) [". . . designating the goods, documents or instruments concerned, and reciting that a security interest therein remains in or will remain in, or has passed to or will pass to, the entruster . . ."], signed by the trustee, and given in or pursuant to such a transaction, is designated in this act as a 'trust receipt.' *No further formality of execution or authentication shall be necessary to the validity of a trust receipt.*" Emphasis added.

⁵² Mich. Comp. Laws (1952 Supp.) §555.416. Emphasis added.

9 apply and not to have the security device qualify as a trust receipt. The policy of the UTRA to protect the purchaser in ordinary course as expressed in sections 9 and 16 should not be defeated by these very obvious avoidance devices. The courts ought to continue their willingness to look through the form of the transaction, and if the requirements for a trust receipt are met, any additions or substitutions should be immaterial as long as the substance of the transaction remains unchanged.⁵³

The amendment to the Certificate of Title Act and the passage of the UTRA indicate a clear intention on the part of the legislature to protect purchasers of chattels and especially used cars from what are in practical effect secret liens. If there is a delivery of goods to the trustee and the financier promptly acquires his security interest for new value pursuant to a prior written agreement with the trustee, then the UTRA will provide adequate protection to financiers and consumers, and the legislature will have accomplished its purpose.

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⁵³ This is especially true in Michigan where all attempts to avoid the Chattel Mortgage Recording Act were brushed aside and almost every chattel security device was called a chattel mortgage, void unless recorded.