

**ABA Business Law Section**  
**Uniform Commercial Code Committee**  
**Secured Transactions Subcommittee**

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A recent case from Texas reminds us that state certificate of title laws governing perfection of security interests in vehicles is anything but uniform and raises a red flag for motor vehicle securitization programs in general.

According to the decision *In re Clark Contracting Services, Inc. v. Wells Fargo Equipment Finance*, 2008 WL 5459818 (Bankr. W.D. Tex. 2008), Clark Contracting Services, Inc. (the “Debtor”) executed notes in favor of CIT Group/Equipment Financing, Inc. (“CIT”) secured by motor vehicles. CIT’s security interest was perfected by obtaining certificates of title listing CIT’s liens in accordance with the requirements of Section 3.11(a) of the Texas Uniform Commercial Code (“UCC”) and the Texas Transportation Code (the “Certificate of Title Act”). A few months later, Wells Fargo Equipment Finance (“Wells Fargo”) purchased the notes payable to CIT but did not record the assignments to it in accordance with the Certificate of Title Act. Thereafter, the Debtor commenced a Chapter 11 case under the United States Bankruptcy Code.

The Debtor challenged Wells Fargo’s security interests claiming that the “strong-arm” power accorded to a trustee in bankruptcy (and a debtor in possession) under Section 544(a) of the Bankruptcy Code permitted avoidance of Wells Fargo’s security interests by reason of the fact that a hypothetical lien creditor would prevail over the unrecorded interests of Wells Fargo. In response, Wells Fargo argued that recordation of the assignment to it was permitted, but not required, by the Certificate of Title Act and that a contrary rule would conflict with Section 9.310 of the UCC.

The court was not persuaded by Wells Fargo’s arguments, finding, instead, that, because UCC Section 9.311(a) required a security interest in motor vehicles to be perfected in accordance with the Certificate of Title Act, the perfection of and maintenance of a security interest in motor vehicles is subject to a perfection scheme that differs from the UCC. “Rather than relying on a generally searchable database [as does the UCC], the perfection [of the Certificate of Title Act] scheme relies on physical notation of security interests on the very document required to legally transfer a motor vehicle.” *Id.* The court found that “the basic principles that underlay the scheme of perfection (and thereby notice to third parties) in the special context of motor vehicles points strongly to the conclusion that assignments too must be notated on the certificate of title if the lienholder’s claim is to be effective against . . . judgment creditors.” *Id.* In particular, the court concluded that the language of the Texas Certificate of Title Act, unlike certificate of title acts of other states, required that a lienholder could assign a lien only by complying with the procedures set forth in the Texas Certificate of Title Act, which included application by the

assignor, signature by the assignee, and the issuance of a new certificate of title showing the assignee as the lienholder.

While one could argue with the conclusion of the court, this case emphasizes that, when non-uniform state laws such as the Certificate of Title Act affect perfection questions, creditors should beware of assuming that the principles of the Uniform Commercial Code will prevail. This case can be expected to encourage additional levels of legal due diligence particularly in connection with assignments of financings secured by motor vehicles.