

# In the United States Bankruptcy Court

## for the Northern District of Iowa

---

CREGAR'S AUTOWERK, INC.  
Debtor.

Bankruptcy No. L92-00872C  
Chapter 7

---

ROSS AUTO SALES  
Plaintiff

Adversary No. 92-1218LC

vs.

CREGAR'S AUTOWERKS, INC.;  
THOMAS G. McCUSKEY, Trustee;  
CITY NATIONAL BANK; and  
KELLEY'S AUTO  
Defendants.

---

### DECISION AND ORDER

---

#### I.

The matter before the court is the motion for summary judgment filed by the plaintiff, Ross Auto Sales (ROSS). The motion is resisted by Thomas G. McCuskey, the chapter 7 trustee (TRUSTEE) and by Kelley's Auto (KELLEY). The two other defendants have not appeared in the proceeding and default of record has been entered against them.

The granting of a motion for summary judgment is appropriate when there is no genuine issue as to any material fact and the movant is entitled to judgment as a matter of law. Fed.R.Bankr.P. 7056(c).

In support of its motion, Ross has submitted an affidavit and has filed a statement of material facts and a legal brief. The trustee agrees that the facts are not in "particular dispute." Trustee's Brief, Docket 18, page 1. He contends, however, that, as a matter of law, Ross is not entitled to judgment. Neither the trustee nor Kelley has submitted an affidavit in support of its resistance.

Although findings of fact are not necessary in ruling on a motion for summary judgment, they are often helpful to the parties and any reviewing court. Certain relevant facts are not in genuine dispute. They are as follows, taken almost verbatim from the affidavit of Rex Ross.

1. On or about May 4, 1992, Ross Auto Sales sold to Cregar's AutoWerks, Inc., as Debtor-in-Possession, two (2) automobiles, to wit: a 1982 Porsche 911, Serial No. WP0AA0916CS120570, and a 1982 Mercedes-Benz 380SL Sedan, Serial No. WDBCA33A8CB030743. The agreed upon prices were \$15,000.00 for the Porsche and \$13,500.00 for the Mercedes-Benz.
2. Ross Auto Sales received checks from Debtor-in-Possession, Cregar's AutoWerks, Inc. dated May 4, 1992 drawn on Norwest Bank Iowa, N.A., Cedar Rapids, Iowa,

- Account No. 47-14-739. The Porsche was paid for by check number 10109 and the Mercedes-Benz was paid for by check number 10110.
3. Ross Auto Sales deposited the \$15,000 check, number 10109, into its bank account at the La Plata State Bank in La Plata, Missouri. On May 13, 1992, Ross Auto Sales received word from the La Plata State Bank that the \$15,000.00 check issued by Cregar's AutoWerks, Inc., as Debtor-in-Possession, had been dishonored by Norwest Bank, N.A. based upon insufficient funds.
  4. Immediately upon notification by the La Plata State Bank of the dishonorment of the \$15,000.00 check issued by Cregar AutoWerks, Inc. as Debtor-in-Possession, [Rex Ross], on behalf of Ross Auto Sales, contacted an employee of Cregar's AutoWerks, Inc. and was assured that sufficient funds had been deposited into the account to cover the two checks. [Rex Ross] presented both checks from Cregar's AutoWerks, Inc. to the La Plata State Bank. On May 22, 1992 [Rex Ross] was notified by the La Plata State Bank that both checks had been dishonored by Norwest Bank, N.A.
  5. On or about May 23, 1992, . . . Judy Ross, on behalf of Ross Auto Sales contacted Cregar's AutoWerks, Inc. to notify it that [Ross] intended to rescind the sale of the Porsche and Mercedes-Benz automobiles and come to Cedar Rapids to take possession of them. Mr. James Coonley, II, on behalf of Lease Iowa, Inc., indicated that a buyer had been located for the Porsche 911 automobile and that a reissued check for \$15,000.00 would be ready when [Rosses] traveled to Cedar Rapids to take possession of the Mercedes-Benz automobile.
  6. On or about May 26, 1992, [Mr.] and Mrs. Ross traveled to Cedar Rapids, Iowa to either receive payment for the Porsche 911 or to return with it and the Mercedes-Benz 380SL automobile to La Plata, Missouri. An inspection of the Mercedes-Benz revealed that it needed routine servicing prior to making the trip back to La Plata, Missouri. [Rosses] agreed to have Cregar's AutoWerks, Inc. perform the service work rather than take a chance on damaging the mechanical systems of the car.
  7. Cregar's AutoWerks, Inc., voluntarily turned over all the paperwork for the automobiles, including the Iowa title for the Porsche 911, to Ross Auto Sales after the delay in financing/purchase by Lease Iowa, Inc.
  8. Ross Auto Sales, continues to hold the original titles to the two vehicles, the Porsche 911, Serial No. WP0AA0916CS120570, and the 1982 Mercedes-Benz 380SL Sedan, Serial No. WDBCA33A8CB030743, for which a claim of rescission is made.
  9. That it was the intention of [Rex Ross] and Cregar's AutoWerks, Inc. to rescind the sale after it became apparent that Cregar's AutoWerks, Inc. was no longer going to be able to do business as a going concern.

Cregar's Autowerks, Inc. (CREGAR) filed its chapter 11 petition on May 1, 1992. The case was converted to chapter 7 on May 29, 1992. Thomas G. McCuskey was appointed as the chapter 7 trustee.

## II.

Resolution of the dispute between Ross and the trustee depends on whether 11 U.S.C. § 546(c) applies to a post-petition purchase of goods by a debtor-in-possession or whether instead the transaction is governed solely by state law.

Ross contends that it made a valid and timely demand for reclamation of the two autos and that the court should require their turnover by the trustee. It argues that its reclamation right arises under Iowa Code § 554.2507(2) which provides no requirement of a written reclamation demand and no time limit for making the demand.

The trustee contends that upon the purchase of the autos by the debtor-in-possession, the autos became property of the estate subject to a claim for reclamation which cannot be enforced because it did not meet the requirements of 11 U.S.C. § 546(c)(1). Trustee points out first that Ross made no written demand to reclaim and second, that Ross did not demand return of the goods before 10 days after their receipt.

Kelley argues that it has an artisan's lien against the 911 Porsche for work done to it at the request of Cregar. In its motion for summary judgment, Ross argues that upon dishonor of the check used to pay for the Porsche, the sale between Ross and Cregar was rescinded, apparently divesting Cregar of ownership in the vehicle and restoring it to Ross. Ross further contends that because Ross did not assent to Kelley's working on the car, Kelley could not obtain an artisan's lien under Iowa law.

### III.

The trustee concedes that under Iowa Code § 554.2507(2), Ross would have a right of reclamation because of the dishonor of Cregar's checks. However, the trustee argues that 11 U.S.C. § 546(c) limits the state-created reclamation right by mandating a written notice of reclamation given before 10 days after the receipt of the goods even though no such limits exist under Iowa Code § 554.2507(2). The trustee asserts that the vehicles, by virtue of the sale transaction, are property of the estate and cannot be reclaimed by Ross because of Ross' failure to meet the requirements of 11 U.S.C. § 546(c). The trustee says he does not rely on the use of any of his avoidance powers to defeat Ross' claim for reclamation.

Such an argument is inconsistent with the Bankruptcy Code. Section 546(c) is a limitation on the trustee's avoidance powers. It comes into play to prevent the use of avoidance powers to defeat the right of reclamation provided under other statute or common law. If the trustee is not relying on any avoidance power to claim a superior right to the vehicles, the court does not see that § 546(c) is relevant to this dispute. The transaction in question was entered into by the debtor-in-possession after the filing of the chapter 11 case. The debtor was entitled to make cash purchases of inventory in the normal operation of its business. See 11 U.S.C. §§ 1108 and 1107. The trustee, or debtor-in-possession, is required to "manage and operate the property in his possession . . . according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof." 28 U.S.C. § 959(b). In buying inventory from Ross, Cregar's was bound by the Uniform Commercial Code as enacted in Iowa. Iowa Code Chapter 554, Article 2, Uniform Commercial Code (UCC). Although the purchased vehicles became property of the estate under 11 U.S.C. § 541(a)(7), the estate's interest acquired by purchase was subject to being defeated by the right of reclamation drawn from Iowa Code § 554.2507. A precondition for reclamation under the UCC existed when Cregar's checks used for payment were dishonored. There is no requirement that a reclamation demand by an unpaid cash seller be made within 10 days. The original UCC comment to § 2-507(2) stated that "[t]he provision of this Article for a ten day limit within which the seller may reclaim goods delivered on credit to an insolvent buyer is also applicable here." UCC Comment, 3, Iowa Code § 554.2507 (1967). The Permanent Editorial Board (PEB) Commentary No. 1, issued March 10, 1990, changed this view:

3. Subsection (2) deals with the effect of a conditional delivery by the seller and in such a situation makes the buyer's "right as against the seller" conditional upon payment. These words are used as words of limitation to conform with the policy set forth in the bona fide purchase sections of this Article. Should the seller after making such a conditional delivery fail to follow up his rights, the condition is waived. This subsection (2) codifies the cash seller's right of reclamation which is in the nature of a lien. There is no specific time limit for a cash seller to exercise the right of reclamation. However, the right will be defeated by delay causing prejudice to the buyer, waiver, estoppel, or ratification of the buyer's right to retain possession. Common law rules and precedents governing such principles are applicable (Section 1-103). If third parties are involved, Section 2-403(1) protects good faith purchasers.

(Emphasis added.)

Ross made the demand was made within a reasonable time, 19 days after the sale and one day after Ross was notified that the checks would for a second time be dishonored. The trustee has not offered evidence to show that the time of the demand was prejudicial to him. Nor has the trustee relied on waiver, estoppel or ratification. The Court of Appeals for the Eighth Circuit has held that when the rights of a good faith purchaser or bankruptcy trustee are not involved, there is no ten-day deadline by which an unpaid cash seller must seek reclamation. Burk v. Emmick, 637 F.2d 1172, 1175-76 (8th Cir. 1980). But the rights of a trustee, as a good faith purchaser, relate to real estate, not personalty, and are provided to the trustee as of the commencement of the case, not as of the date of conversion. 11 U.S.C. § 544(a)(3). Our case involves a post-petition transaction by the debtor-in-possession; thus neither the good faith purchaser status of the trustee nor the concern of the Eighth Circuit should limit the effectiveness of Ross' right of reclamation to 10 days.

The trustee argues also that Ross failed to meet the requirements of 11 U.S.C. § 546(c) because it failed to make its reclamation demand in writing. Neither Iowa Code § 554.2507(2) nor § 554.2702(2) requires that the demand be in writing. This is significant as "writing" or "written" is a defined term under the Uniform Commercial Code. Iowa Code § 554.1201(46). It is noteworthy that Iowa Code § 554.2702(2) extends the ten-day period for making a reclamation demand when a misrepresentation of solvency has been made to the seller in writing. Had the drafters of the section desired to require the reclamation demand to be written, they knew how to draft the statute to accomplish that result. Inasmuch as the court concludes that 11 U.S.C. § 546(c) does not apply to this post-petition transaction, the written demand required by that section is not necessary for a creditor to make a satisfactory demand where a debtor-in-possession or a trustee has failed to pay for goods purchased post-petition.

Based upon the undisputed facts that have been presented, the court concludes that Ross' reclamation demand was legally sufficient under Iowa Code § 554.2507 and that Ross is entitled to return of the vehicle in the possession of the trustee.

As to the vehicle in the possession of Kelley, the outcome of the dispute between Ross and Kelley may have a bearing on Ross' claim against the trustee for possession of that vehicle. Although not expressly stated, the court presumes from the arguments of the parties that the Porsche is still in Kelley's possession or it could not be claiming an artisan's lien. Unresolved issues as to the Porsche will be discussed at the end of Part IV.

Ross' claim against the trustee cannot be fully adjudicated on the motion. Ross has prayed for various remedies including incidental damages. Ross' motion and accompanying affidavit provide nothing to the court regarding incidental damages.

#### IV.

In its complaint (Count IV), Ross alleges that Kelley claims an artisan's lien against the Porsche 911 automobile to secure payment for body work done to the car. Kelley admits that it claims such a lien. Ross contends that Kelley does not have a valid artisan's lien under Iowa law because Kelley performed body work to the Porsche at the request of Cregar, and not with the knowledge or consent of Ross, the true owner. Kelley counters that Cregar, at the time it requested the work, was represented as the owner of the Porsche and that Kelley had no reason to believe otherwise.

In its prayer, Ross asks the court to determine that Kelley's lien is invalid, to require Kelley to turn over the auto and to require Kelley to pay damages for its "wrongful assertion" of the lien. Ross' affidavit in support of its motion for summary judgment makes no reference to when Kelley obtained possession of the Porsche, when Cregar requested the work, or when Kelley did the work. From the briefs, it appears that the following facts are undisputed: Cregar obtained the Porsche from Ross on or about May 4, 1992, in exchange for a check which was dishonored the first time on or about May 13 and the second time on or about May 22, 1992. Ross demanded the return of the cars on May 23. Cregar gave possession of the Porsche to Kelley for a paint job and other work. Kelley did the work and has not been paid. Kelley thought Cregar was the owner. Kelley did not seek Ross' permission to work on the car.

An artisan's lien is a possessory interest in property created by Iowa Code § 577.1:

Any person who renders any service or furnishes any material in the making, repairing, improving, or enhancing the value of any inanimate personal property, with the assent of the owner, express or implied, shall have a lien thereon for the agreed or reasonable compensation for the service and material while such property is lawfully in the person's possession, which possession the person may retain until such compensation is paid, but such lien shall be subject to all prior liens of record, unless notice is given to all lienholders of record and written consent is obtained from all lienholders of record to the making, repairing, improving, or enhancing the value of any inanimate personal property and in this event the lien created under this section shall be prior to liens of record.

Iowa Code § 577.1(1).

Ross contends that Kelley's purported lien is invalid because when Cregar authorized the work to the Porsche, Ross was not the owner. Ross says the sale of the Porsche was rescinded upon dishonor of the check used by Cregar to pay for it. Ross argues that at that moment, Cregar had only a possessory interest in the vehicle, Ross again was the owner, and it did not authorize the work by Kelley. Absent authorization by the owner, Ross says Kelley cannot obtain lien rights under Iowa Code § 577.1.

So far as the court can find, neither the pleadings, the motion for summary judgment, Ross' affidavit nor the briefs indicate an undisputed time when Kelley did the work to the Porsche. Kelley's resistance to the motion states that when the vehicle was moved to Kelley's, Ross and Cregar had an ongoing sales transaction, one in which the cars and titles had been exchanged, but the checks had not yet been dishonored. This statement is not supported by affidavit or otherwise. Furthermore, Kelley's

resistance states that at the time the work to the Porsche was requested, Cregar was the owner of the Porsche or could reasonably be assumed to be so. Resistance, page 1.

Ross correctly states that for an artisan to obtain a lien under Iowa Code § 577.1, it must accomplish the defined work with the assent of the "owner." But Ross has cited no authority for the proposition that upon the check's dishonor, the sale was rescinded and Ross again became the owner. Even if this were so, to the extent that the work was authorized or perhaps completed before the dishonor, Ross would need to show that somehow the effect of the dishonor was to rescind the sale at a date which related back before the authorization or the work. Ross has not discussed these possible issues in its motion or supporting papers.

The court does not find any authority for the proposition that the sale was, so to speak, automatically rescinded upon the dishonor of the checks. The transaction between the parties was a sale of goods governed by Article 2 of the Uniform Commercial Code as adopted in Iowa. Iowa Code, Chapter 554, Article 2. Although the term "rescission" is used in Article 2 (see, for example, § 554.2209(2) and 554.2721), cancellation of the contract is among the seller's remedies provided by the Code. Iowa Code § 554.2703(f). "'Cancellation' occurs when either party puts an end to the contract for breach by the other and its effect is the same as that of 'termination' except that the canceling party also retains any remedy for breach of the whole contract or any unperformed balance." Iowa Code § 554.2106(4); Nora Springs Co-op Co. v. Brandau, 247 N.W.2d 744, 749 (Iowa 1976).

It has been written that "rescission" has become an ambiguous term, and as a result, "the framers of the Uniform Commercial Code sought to limit rescission to cases where the seller has committed fraud or where there has been a mistake." Robert A. Hillman, *Contract Remedies, Equity and Restitution in Iowa* § 3.3(F) (1979). There is pre-Code support for such limited use of rescission. Kramer v. Messner, 101 Iowa 88, 69 N.W. 1142, 1145 (1897). There it is stated that, "It has never been held, in any well-considered case, that a vendor of personal property can rescind a contract of sale, after having delivered the property into the hands of the vendee, simply because the vendee failed to make payments according to the terms of the contract. In order to justify a rescission, there must, as a general rule, be fraud, misrepresentation, or mistake." *Id.* at 1145. But see, Maytag Co. v. Alward, 253 Iowa 455, 112 N.W.2d 654, 660 (1962) which lists other grounds for rescission.

In this case, the court need not now decide whether "rescission" is an available remedy for Ross or whether Ross has merely intended to take advantage of the remedy of "cancellation" as provided in Iowa Code § 554.2703(f). The court finds no authority for and does not agree with the proposition that at the moment the checks were dishonored, the transaction was automatically rescinded or canceled. For either remedy, there would have needed to be an election of that remedy by Ross.

The requirement of action by the seller to accomplish a rescission or cancellation of the contract, so as to restore ownership in Ross, is supported in the Code. Under the UCC, title to goods generally passes at the time of delivery. Iowa Code § 554.2401(2). The title is "voidable" not void, when "the delivery [of the goods] was in exchange for a check which is later dishonored." Iowa Code § 554.2403(1)(b). Based on Rex Ross' affidavit, the earliest an election to cancel was made was May 23, 1992. Even if under Ross' theory Ross again became the "owner" upon rescission or cancellation, there is no indication of when Kelley's did the work in question for which it asserts the artisan's lien. Thus, even if Ross' theory were correct, the court would not have enough facts to determine that Ross was the true owner when the work was requested by Cregar's or done by Kelley's.

Moreover, the reclamation by Ross would not automatically defeat any artisan's lien which Kelley may have. According to Commentary No. 1, by the UCC's Permanent Editorial Board, a cash seller's

right of reclamation is in the "nature of a lien." Iowa Code § 554.2507, PEB Commentary No. 1, 3, March 10, 1990. To the extent that is so, it would be an unrecorded lien, and, at least until the cash seller obtained possession of the goods, an unperfected interest. Article 9 of the UCC generally does not apply to artisan's liens. Iowa Code § 554.9104(c). That section excludes from the Article's coverage "a lien given by statute or other rule of law for services or materials except as provided in § 554.9310 on priority of such liens. . . ." Section 554.9310 gives priority to an artisan's lien over a perfected security interest in the same goods, unless the statute creating the artisan's lien provides otherwise. In Iowa, it does. Section 577.1 of the Iowa Code makes an artisan's lien subject to all prior liens of record unless the artisan gives notice of the proposed work and obtains the written consent of the prior lienholder. To the extent that Ross, as a reclaiming cash seller under Iowa Code § 554.2507 has rights against the Porsche that are in the nature of an unrecorded lien, Ross' interest would be subject to Kelley's artisan's lien.

Based on the foregoing analysis, the court concludes that Ross has failed to show it is entitled to summary judgment against Kelley.

To the extent that Kelley's artisan lien may defeat Ross' reclamation of the Porsche, such a result may perhaps affect Ross' claim against the trustee. Although Ross' reclamation claim against the trustee might be successful absent the intervention of a third party, the successful assertion of an artisan's lien by Kelley might affect Ross' reclamation claim as to the trustee. Does the successful intervention of Kelley cut off or terminate Ross' reclamation right against the trustee, or does it just subordinate Ross' reclamation right as against the trustee to the payment of Ross' lien? The parties have not dealt with this issue, and the court will not decide it without giving the parties the opportunity to present further argument.

## V.

### ROSS' MOTIONS FOR JUDGMENT BY DEFAULT AGAINST CREGAR'S AUTOWERKS, INC. and CITY NATIONAL BANK

Ross has filed separate motions for Default Judgment against two defendants who have been served with a summons and the complaint but have failed to answer. Judgment of record has entered against the two defendants--Cregar and City National Bank. Ross prays for an award of damages against each of these defendants. In order to enter judgment, the court must determine the amount of damages, if any, that Ross is entitled to from Cregar's and the Bank. Ross' entitlement to incidental damages and their amount will be determined after further hearing.

## ORDER

IT IS ORDERED that Ross Auto Sales' Motion for Summary Judgment against Thomas G. McCuskey and Kelley's Auto is denied.

SO ORDERED ON THIS 12th DAY OF APRIL, 1993.

William L. Edmonds  
Chief Bankruptcy Judge

I certify that on \_\_\_\_\_ I mailed a copy of this order by U. S. mail to: Thomas Fiegen, John Heckel, Jeffrey Taylor, Chris Henderson, and U. S. Trustee.