



Lien Filing Error Renders Creditor's Claim Unsecured

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Many steps creditors take in the process of directly or indirectly originating a vehicle finance agreement are designed to protect the creditor in the event its credit risk assessment was off and the consumer defaults. A handful of those steps also help in what for creditors can be a worst-case scenario – when consumers file for bankruptcy, putting the creditors' recovery at risk.

A key component to originating vehicle-secured credit is the timing of the creditor's perfection of its lien on the collateral. If the creditor timely perfects its security interest, the creditor enjoys better protections as a secured creditor in a consumer's bankruptcy case. On the other hand, if the creditor does not perfect its security interest timely and the consumer files for bankruptcy soon after financing his or her car, the creditor can be deemed unsecured in the bankruptcy and unprotected.

That is what happened to a creditor in a bankruptcy case involving one of its customers, and the technical details of perfection of the security interest under state law were the difference between the creditor's claim being secured and the creditor's claim being unsecured.

Jessica Riddlesprigger bought and financed a car on February 26, 2018. Exeter Finance agreed to finance the purchase and submitted a title application with its lien information to the Alabama Department of Revenue on March 5, 2018. The seller was listed on the title application as Dothan Chrysler Dodge Jeep Ram, but the Certificate of Origin, submitted along with the application, had been issued in the name of Dothan Chrysler Dodge Jeep Ram *Fiat*. Because of the discrepancy in the seller's name, the DOR rejected the title application and returned it to Exeter.

Under Alabama law, to perfect a security interest in a car, the creditor must deliver an application for a certificate of title to the DOR that contains the lienholder's name and address and the date of the security interest, along with the required fee. The security interest relates back and is perfected as of the time of its creation (i.e., the date of the sale, when the consumer grants the security interest to the creditor in the credit agreement) if the creditor takes all required steps within 30 days after the sale.

Exeter submitted a revised application on May 18, 2018, which the DOR received on May 24, 2018. The DOR issued a certificate of title on June 22, 2018, listing Exeter as the lienholder. However, Riddlesprigger had filed a Chapter 13 bankruptcy petition on March 20, 2018, less than 30 days after the financed purchase of her car and well before the state accepted Exeter's lien filing. Exeter filed a proof of claim in the bankruptcy case as a secured creditor, but the Chapter 13 trustee objected to Exeter's proof of claim and secured status on the grounds, among others, that its security interest was not perfected as of the petition filing date.

The U.S. Bankruptcy Court for the Middle District of Alabama agreed with the trustee and allowed Exeter's claim only as an unsecured claim. The court noted the requirements cited above for perfecting a security interest in a car in Alabama and added that if the security interest does not relate back to the date of its creation, then perfection occurs at the time of delivery of the properly completed application and fee to the DOR. In this case, because the properly completed title application with the correct seller's name was submitted to the DOR more than 30 days after Riddlesprigger bought the car and after she filed a bankruptcy petition, the court found that the trustee was entitled to avoid the security interest and found Exeter's claim against the bankruptcy estate to be unsecured.

Cases like these get reported from time to time, and they usually turn on small details – paying the right lien filing fee, using the correct names and addresses, completing the rest of the paperwork accurately, and filing in time. Sometimes the filing errors are the result of clerical mistakes, but sometimes they reflect systemic issues with the lien filing process. For dealers and finance companies, it is critically important to test the process periodically to make sure it works and generates accurate and timely results because the difference between being a secured creditor and an unsecured creditor in a consumer bankruptcy case can significantly affect the creditor's recovery.

In re Riddlesprigger, 2019 Bankr. LEXIS 1843 (Bankr. M.D. Ala. June 14, 2019).