

Initial Decision

94 F.T.C.

IN THE MATTER OF
FORD MOTOR COMPANY, ET AL.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED
VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9073. Complaint, Feb. 10, 1978 — Final Order, Sept. 21, 1979*

This order, among other things, requires Francis Ford, Inc., a Portland, Ore. Ford dealer, to cease failing to dispose of repossessed vehicles in a manner designed to obtain the best possible price; provide information regarding the disposition of such vehicles to defaulting customers; properly calculate surpluses realized from the sale of the vehicles; and repay such surpluses in a timely fashion. The order further requires respondent to identify all surpluses realized back to February 10, 1976, and to notify affected consumers of their existence. Additionally, respondent is required to maintain specified records for at least three years.

Appearances

For the Commission: *Bruce D. Carter, Dean A. Fournier and David R. Pender.*

For the respondents: *Michael J. Esler, Haessler, Stamer, Tilbury & Esler, Portland, Ore.*

INITIAL DECISION BY LEWIS F. PARKER, ADMINISTRATIVE LAW
JUDGE

JAN. 3, 1979

I. PRELIMINARY STATEMENT

A. History of the Case

This case began on February 10, 1976, when the Commission issued a complaint charging Ford Motor Company ("Ford"), Ford Motor Credit Company ("Ford Credit"), and Francis Ford, Inc. ("Francis Ford") with violations of Section 5 of the Federal Trade Commission Act ("FTC Act").

On March 24, 1976, Francis Ford filed its answer, admitting certain allegations of the complaint, denying others and asserting six defenses. Prehearing conferences were held [2] on April 13, 1976 and on February 3 and July 22, 1977. Complaint counsel filed their witness and document lists and trial brief on December 5, 1977. On March 17, 1978, this case was withdrawn from adjudication as to Ford and Ford Credit for purposes of considering a proposed consent agreement executed by these respondents and complaint counsel.

*Complaint published in 93 F.T.C. 402.

This agreement was subsequently placed on the public record for comment.

Hearings with respect to Francis Ford were held from March 21-28, 1978 in Seattle, Washington. On June 26 and 27, 1978, Francis Ford filed a trial brief and list of witnesses, and its exhibit list was filed on July 10, 1978. Francis Ford presented its defense from July 24-28, 1978 in Seattle. The final record consists of 2,166 pages of testimony and argument and almost a thousand exhibits.

The record in this case was closed on September 1, 1978. Complaint counsel and Francis Ford filed their proposed findings on October 13, 1978 and their replies on October 30, 1978. At my request the Commission granted me an extension of time to January 8, 1979 to file this initial decision.

B. Allegations of the Complaint

The complaint alleges that Francis Ford, a Ford dealer, arranges the financing of its retail sales of motor vehicles through Ford Credit or other lenders. When Ford Credit finances a sale, it is alleged, it provides a retail installment contract form which names the customer as buyer and the dealer as seller and which states that the contract is to be assigned to Ford Credit for value, that the buyer is to be indebted to the dealer or its assignee and that the dealer or its assignee is to be a secured party holding a security interest in the vehicle.

The complaint further alleges that if the buyer defaults, Francis Ford has undertaken the obligation, either by express or implied representations in its retail installment contracts, to account to the defaulting buyer for any surplus arising from the resale of repossessed collateral; however, the complaint states, despite the fact that the laws of most states (derived from Article Nine of the Uniform Commercial Code ("UCC")), require a secured party, after default and repossession of the collateral, to account for any surplus [3] of proceeds¹ from the sale of the collateral, Francis Ford has, in a substantial number of instances, deprived defaulting buyers of substantial amounts of money which are rightfully theirs by:

(1) Failing to institute or follow correct procedures for determining the existence or amounts of surpluses realized from the sale of repossessed vehicles,

¹ Defined in the complaint as that sum which is "in excess of the amount needed to satisfy all secured indebtedness, reasonable expenses of retaking, holding, preparing for sale, selling, and the like, and allowable legal costs and fees." (Complaint, Par. Five)

(2) Failing to disclose the existence of these surpluses to defaulting buyers, and

(3) Wrongfully retaining such surpluses in violation of the defaulting buyers' statutory and contractual rights.

Finally, the complaint alleges that repurchase dealers,² one of which is Francis Ford, have failed to inform defaulting buyers of facts necessary to their exercise of the right of redemption granted by state law, and that this failure to disclose material facts has the tendency and capacity to hinder defaulting buyers in exercising this right. This allegation was, however, withdrawn by complaint counsel at the beginning of the hearings.

The following findings of fact, conclusions of law and proposed order are based upon the record in this case and upon the proposed findings and replies of the parties. Any proposed findings not adopted herein in substance or verbatim are rejected either because they are irrelevant or because they are not supported by the record. [4]

II. FINDINGS OF FACT

A. Francis Ford's Business

1. Francis Ford is an Oregon corporation with its office and principal place of business at 509 S.E. Hawthorne Boulevard, Portland, Oregon (Ans. ¶ I).³ It is one of more than 6,000 franchised Ford dealers. It sells new and used cars and trucks and operates parts and service departments. These separate operations are required of franchised dealers by Ford (Tr. 1239-41). Francis Ford's total sales exceeded \$13 million during each of the years 1974 and 1975 (CX's 2321-22). Its pre-tax profits from all of its operations were \$112,406.00, or .0085% of total sales in 1974 (CX 2321) and \$18,934.00, or .0014% of total sales in 1975 (CX 2322).

2. Francis Ford is one of the two highest-volume Ford dealers in the Portland area (Tr. 157). It sells about 2,400 vehicles annually, most of which are sold to retail customers rather than to wholesale

² Dealers who, by contract, agree that Ford Credit and other lending institutions may return repossessed vehicles to them. The lending institutions then receive from these dealers a "payoff" which consists of the unpaid balance of the retail installment contract adjusted by certain charges and credits. The repurchase dealer then resells the vehicle to a third party. (Complaint, Par. Seven)

³ Abbreviations used in this decision are:

CX	- Commission exhibit.
RX	- Respondent's exhibit.
Tr.	- Transcript of testimony.
Ans.	- Francis Ford's answer to the complaint.
Adm.	- Pages 13-14 Francis Ford's response to complaint counsel's second and third requests for admissions dated March 13, 1978.

purchasers or "fleet" operators (CX's 2321-22; Tr. 177). Francis Ford maintains two lots for the retail sale of used vehicles to the public (CX 2358).

3. In calendar year 1975, Francis Ford sold 878 used cars and trucks at retail and 283 used cars and trucks at wholesale (CX 2322). In calendar year 1974, Francis Ford sold 1,093 used cars and trucks at retail and 403 used cars and trucks at wholesale (CX 2321).

4. As of December 31, 1977, 588 retail installment contracts sold or assigned by Francis Ford to Ford Credit were outstanding, and they amounted to a total receivable of approximately \$1,868,000 (Tr. 38-39).

B. Commerce

5. All Ford motor vehicles sold by Francis Ford are manufactured and assembled at plants located outside the [5] State of Oregon. They are shipped to Francis Ford in response to orders placed by Francis Ford with Ford's office in Seattle, Washington (Tr. 472-73).

6. Portland, Oregon is situated adjacent to the Columbia River, the boundary between the States of Oregon and Washington. Portland is the hub of a retail trading zone which includes Clark and Skamania counties in southwestern Washington, and is a Standard Metropolitan Statistical Area which includes Clark County (Stipulation, Tr. 1011-13). Francis Ford advertises its new and used cars and trucks for sale in this market through broadcast (television and radio) and print media (CX's 3601-07, 3622-26, 3631-34C; Tr. 158-62, 175-76). Vancouver is the largest city in Clark County, Washington, and is located immediately across the Columbia River from Portland.

7. The normal dissemination areas of several of the Portland-based television channels and radio stations which carry Francis Ford advertising extend into the State of Washington, including metropolitan Vancouver (Tr. 160-62).

8. In 1975, Francis Ford spent \$221,578 on advertising allocated as follows: \$16,113 to institutional advertising and promotion, \$145,060 to new car advertising, and \$60,405 to used car advertising (CX 2322). In calendar year 1974, Francis Ford spent \$197,622 on advertising, allocated as follows: \$10,835 to institutional advertising and promotion, \$146,343 to new car advertising, and \$40,444 to used car advertising (CX 2321).

9. Francis Ford's advertising volume in the *Portland Oregonian* and *Oregon Journal* newspapers totaled approximately \$134,000 in each of the years 1974 and 1975 (Adms. 10 & 11). The *Oregonian* and *Journal* have substantial interstate circulation: Over 16,000 copies of

the daily edition of the *Oregonian*, 4,800 of the daily edition of the *Journal*, and 33,000 of the *Oregonian* Sunday edition are distributed outside the State of Oregon. Most of this out-of-state circulation is in the State of Washington, about half of it in Clark County (Stipulation, Tr. 1011-13). Francis Ford also advertises occasionally in the Vancouver, Washington *Columbian* (Tr. 158).

10. Francis Ford advertises in the Vancouver, Washington telephone directory yellow pages as well as in the yellow pages for Portland and St. Helens, Oregon (Tr. 164-68). In all of these yellow pages advertisements, Francis Ford's ads appear in conjunction with ads for Washington-located auto dealers (including Ford dealers) who compete with Francis Ford (CX's 3610-13, 3615-16; Tr. 172-73).

[6]

11. Francis Ford arranges for other types of advertising and promotional activity in other areas of the State of Washington (CX's 3604, 3606, 3608, 3622-26, 3631-33; Tr. 162-63, 169-75).

12. Francis Ford makes occasional sales of motor vehicles to residents of states other than Oregon, primarily to persons who reside in the Vancouver, Washington area (Tr. 158, 171).

13. Over half of the retail installment contracts executed by Francis Ford customers are sold or assigned to Ford Motor Credit Company's Portland branch office, which provides financing to Ford dealers and their retail customers in an area of responsibility extending from Oregon northward to Longview, Washington (Tr. 37, 191-93). Ford Credit has other branch offices engaged in like activity throughout the United States (Tr. 34-36). A total of 724 such contracts were sold by Francis Ford to Ford Credit's Portland branch in 1976-77 (Tr. 38).

14. When vehicles sold by Francis Ford are thereafter repossessed and returned to it by the financing institutions it does business with, the repossessions may take place outside the State of Oregon or may involve an out-of-state resident who was either the original customer from whom the vehicle was repossessed or who was the purchaser upon resale after repossession (Tr. 1048-50, 1072-81, 1087-89, 1097-98). Of the 43 repossession transactions discussed below, at least 3 involved out-of-state residents as the original customers (CX's 2771, 3021, 3083-84). Four involved repossession at out-of-state sites (CX's 2416, 2928B, 2963A-B, 3027-30), and in three the resales were to out-of-state residents (CX's 2595, 2934, 3390; Tr. 1049).

15. In connection with its original sales and post-repossession resales of vehicles, Francis Ford has shipped used vehicles to out-of-state purchasers (CX 2595; Tr. 1049-50), and has initiated or

participated in the transmission across state lines of credit reports and various instruments of retail installment credit, title registrations, licensing documents and related correspondence and payments (CX's 2922, 3083-84, 3393), and other business papers related to the extension and enforcement of credit obligations (CX 2938A-B).

16. Approximately three years before issuance of the present complaint, Francis Ford entered into a consent agreement in which it admitted the Commission's jurisdiction, [7] under the "in commerce" standard then applicable, with respect to various alleged practices including representations in newspapers and broadcast advertising, handling of customers' deposits, and preparation of retail installment contracts (82 F.T.C. 1501 (1973)).

17. Francis Ford maintains a substantial course of trade in motor vehicles and motor vehicle credit in commerce, and that trade affects commerce, as "commerce" is defined in the FTC Act.

C. Francis Ford's Retail Installment Contracts

18. About 70 percent of Francis Ford's retail sales of motor vehicles are financed in whole or in part. These consumer credit sales are drawn up on retail installment contracts which are pre-printed forms supplied either by Ford Credit or by the United States National Bank of Oregon ("U.S. Bank"). Francis Ford sells, assigns or transfers over half of these contracts to Ford Credit; the remainder go to U.S. Bank (Tr. 179, 191-93).

19. The Ford Credit installment contract form calls for monthly installment payments by the debtor to the seller (Francis Ford) which are secured by a security interest in the vehicle by Francis Ford or its assignee. The contract provides for its assignment to Ford Credit (CX 2311). The U.S. Bank installment contract form is substantially similar to the Ford Credit form except that it contains a provision for its assignment to U.S. Bank (CX 2314B).

20. The Ford Credit contract form states that: "This contract shall be governed by the laws of the state in which the original Seller [Francis Ford] is located . . .", and identifies the security interest created thereby as "a security interest under the Uniform Commercial Code . . ." (CX 2311). The "default" provision of the contract states that:

Seller shall have all the rights and remedies of a Secured Party under the Uniform Commercial Code, including the right to repossess the Property . . . and to recondition and sell the same at public or private sale. (CX 2311)

[8] The U.S. Bank contract form used in such transactions recites that: "The parties [Francis Ford and its customer] agree that their

relations, rights and duties under this agreement shall be governed by the substantive law of the State of Oregon" (CX 2314B). The "repossession resale" provision of the contract states, *inter alia*, that:

Creditor Dealer will give Customer reasonable notice of the time and place of any public sale or of the time after which any private sale or other intended disposition is to be made. . . . Expenses of retaking, holding, preparing for sale, selling or the like shall include Creditor-Dealer's reasonable attorneys' fees and legal expenses. (CX 2314B)

21. The law referred to above, the UCC, was enacted in Oregon in 1961 and includes a provision that a secured party may, in the event of default, repossess the collateral and sell, lease or otherwise dispose of it and that he "must account to the debtor for any surplus . . ." (ORS ¶ 79.5040(2)).

22. If repossession of a vehicle financed by Ford Credit occurs, Ford Credit sends a form notice to the customer (and to Francis Ford) which states:

The [repossessed vehicle] will be sold by [Ford Credit] or its assignee at a private sale at any time after 10 days from the date shown above unless redeemed by you prior to such sale. The proceeds will be applied first to the payment of the expenses of retaking, holding, preparing for sale and selling said property and reasonable attorney's fees and legal expenses incurred by [Ford Credit], then to the satisfaction of the balance due under the contract covering the financing of said property, and then to the satisfaction of any indebtedness secured by any subordinate security interest in said property. *Any surplus will be paid to you* and, unless prohibited by law, you will remain liable for any deficiency. (emphasis added) (CX's 1240, 2678; Tr. 955)

[9] 23. A similar statement appears in another Ford Credit form which is executed by defaulting customers when they voluntarily surrender their vehicle to Ford Credit:

[T]he undersigned [customer] hereby voluntarily surrenders and returns to you [Ford Credit] the above-described commodity for . . . disposition . . . in conformance with law . . . The undersigned hereby requests and authorizes you to dispose of this property at public or private sale and to apply the net proceeds received therefrom against the amount of the undersigned's present indebtedness to you. If the net proceeds so realized shall be less than the said unpaid balance, after deducting your expenses, the undersigned agrees to remain liable to you for the difference thereof, plus a reasonable fee . . . as attorney fees . . . *If the net proceeds so realized is more than said unpaid balance, you agree to pay the excess to me.* (emphasis added) (CX 2655)

24. The installment contract forms and their incorporation of state law constitute an implied promise by Francis Ford, as a secured party, to account for and pay to the customer any surplus resulting from its resale or other disposition of a vehicle repossessed from the customer, and these forms, along with the notices referred to in

Findings 22 and 23, have the capacity and tendency to lead customers to believe that any surpluses realized after repossession will be paid to them.

D. Repurchase Agreements

25. Since August 15, 1967, Francis Ford has been party to a series of agreements with Ford Credit under which each retail installment contract sold or assigned by Francis Ford to Ford Credit has been governed by the terms of a "Retail Plan" set forth in a Ford Credit dealer manual titled "Automotive Finance Plans for Ford Motor Company Dealers" (CX's 2301, 2303). These agreements provide further that each retail installment contract sold or assigned to Ford Credit is deemed assigned on a "repurchase" basis unless otherwise specified (CX's 2301, 2303). [10]

26. U.S. Bank also has a repurchase agreement with Francis Ford which is similar to Ford Credit's (CX's 2307A-B, 2314B; Tr. 191-92, 1482-83).

27. Under these repurchase agreements Francis Ford is obliged, in the event of a default by the customer, and upon the lender's request and the return of the vehicle, to pay to the lender the outstanding balance on the loan (CX's 1015⁴ and 1016, p. 20; CX 1014, p. 22; CX 2311;⁵ Tr. 1277).

28. Since January 1973, the "repurchase" portion of the Ford Credit retail plan has included the following provision:

EXCESS PROCEEDS ON REALES OF REPOSSESSIONS

If the proceeds (less reasonable selling expenses) received by the dealer from his resale of a repossessed vehicle exceed the repurchase price of the vehicle, he should pay the excess to the customer as required by law (CX's 1015 and 1016, p. 22).

[11] On March 9, 1973 and on July 29, 1974, Francis Ford accepted and agreed to Ford Credit retail plans containing the "excess proceeds" provision (CX 2301).

29. The repurchase agreement between Francis Ford and U.S. Bank also contains an admonition that surpluses realized on resales

⁴ CX 1015, p. 20 states:

The Retail Plan contemplates a sharing of responsibility between the Dealer and Ford Credit with respect to vehicles covered by retail installment contracts on which the customer has defaulted. The standard Retail Plan is a repurchase plan under which Ford Credit assumes responsibility for confiscated vehicles, converted vehicles, certain collision damages to vehicles and for repossessing and returning vehicles to the Dealer after default, and the Dealer assumes the responsibility for repurchasing and merchandising repossessed vehicles.

⁵ The Ford Credit retail installment contract form states:

REPURCHASE: The [dealer] guarantees payment of the full amount remaining unpaid under said [retail installment] contract, and covenants if default be made in payment of any installment thereunder to pay the full amount then unpaid to [Ford Credit] upon demand, except as otherwise provided by the terms of the Ford Motor Credit Company Retail Plan in effect at the time this assignment is accepted.

of repossessed vehicles should be paid to the defaulting customer as required by the UCC (CX 2307A).

30. All retail installment contracts sold or assigned by Francis Ford to Ford Credit and U.S. Bank are subject to repurchase agreements (Tr. 39, 189, 191-92, 1482-83).

E. The Benefits of Repurchase Financing

31. Mr. James Woods, the secretary-treasurer of Francis Ford, testified that it arranges for financing its customer's vehicle purchases because its competition does so, but that because of the costs involved in handling installment contracts, Francis Ford would much rather sell cars for cash (Tr. 1276-77).

32. However, it is apparent that repurchase financing, the only type of financing available to automobile dealers in the Portland area (Tr. 189, 191), does provide certain benefits to Francis Ford. Foremost, of course, is the fact that financing sells automobiles⁶ (Tr. 178-79, 1489, 1514, 2286).

33. There are other tangible monetary benefits which Francis Ford realizes from its repurchase agreements. When it assigns an executed retail installment contract to a financing institution on a repurchase basis, the financing institution credits a share of the total finance charge to Francis Ford. Francis Ford's share of the finance income is the amount by which the finance charge negotiated between Francis Ford and the consumer exceeds the amount of finance income for the financing institution as agreed upon between Francis Ford and that institution. For example, the interest rate which Ford Credit charged on new cars at the time of hearings was 6 percent. If the total finance charge negotiated by Francis Ford were \$1,560 on a hypothetical contract, and as a result of its 6 percent rate, Ford Credit's finance charge was \$1,200, Francis Ford would retain the difference between \$1,560 and \$1,200—\$360 (Tr. 45-46).

34. Francis Ford's sale of cars on retail installment contracts also enables it to sell credit life, accident and [12] health insurance to many customers. It receives a commission of between 35 percent and 37 1/2 percent on its sales of such insurance. Credit life, accident and health insurance meet the customer's obligation under the installment contract if the customer suffers a misfortune covered by the policy. These policies protect the customer against repossession due to sudden loss of income, while protecting Francis Ford against being called upon to perform its obligations under the repurchase agreement with the financing institution (Tr. 180).

⁶ "If everybody sold for cash, all dealers would sell far less cars today than they do by having a contract" (Tr. 1277).

35. "Profit centers" are the revenue generating activities of a merchandising firm which ultimately provide for payment of its indirect or fixed (overhead) expenses (Tr. 546-47). Finance and insurance income may be a major profit center for a dealership (CX 319A-F). Francis Ford realized \$127,827 in finance and insurance income in 1974 and \$124,407 in such income in 1975 (CX's 2321-22).

F. Repossession

1. Calculating the Payoff

36. During calendar year 1974, approximately 91 repossessed vehicles were returned to Francis Ford pursuant to its repurchase agreements with Ford Credit and U.S. Bank (Adm. 9). Approximately 85 repossessed vehicles were returned to Francis Ford by these lending institutions in 1975 (Adm. 8).

37. When Ford Credit and U.S. Bank return a repossessed vehicle to Francis Ford, they calculate a "payoff," that is the amount which the defaulting customer owed them but which, by virtue of the repurchase agreements, Francis Ford now owes them. Francis Ford then looks to the defaulting customer to reimburse it for the payoff plus other legitimate expenses incurred in preparing the repossessed vehicle for sale and in reselling it.

38. The payoff does not equal the amount owed on the installment contract, for it is adjusted by credits for any prepaid but unearned finance charges or insurance premiums, and by charges for such items as collision damage and expenses of repossession by the financial institution (CX's 1016, pp. 20-22; 2307A-B, 2396A, 2564, 2566A-2569, 2571; RX 2565; Tr. 55-59, 62-63). [13]

a. Finance Charges

39. When Francis Ford sells a vehicle under a retail installment contract, the contract customarily provides for the customer to pay a finance charge which is included in the face amount of the contract (e.g., CX 2581A).

40. When Francis Ford assigns a retail installment contract to Ford Credit or U.S. Bank, the financing institution credits Francis Ford's reserve account with the amount by which the gross finance charge negotiated between Francis Ford and the customer exceeds the discount rate agreed to between Francis Ford and the financing institution (CX 1054A-C; Tr. 46-50, 1509-11; Finding 33). The financing institution then sends Francis Ford a check for the unpaid balance owing on the vehicle plus the amount of any premiums for creditor's life, accident, or health insurance financed under the

contract which Francis Ford has arranged through its independent broker (CX 2396A; Tr. 48-49).

41. The Ford Credit and U.S. Bank retail installment contract forms used by Francis Ford provide that if the buyer prepays the obligation in full, the buyer will receive a rebate (credit) of the unearned portion of the finance charge computed under the Rule of 78 (sum of the digits method)⁷ after deducting an acquisition fee of \$15 (CX's 2311 [¶ 14], 2441, 3421, 3461).

42. In the event of an early payoff by a customer purchasing a vehicle under a retail installment contract held by a financing institution pursuant to a repurchase agreement with an automobile dealer, the gross finance charge is prorated by the financing institution under the Rule of 78. The face amount of the contract is then reduced by the amount of the unearned gross finance charge to obtain the payoff. The amount of the finance charge previously credited to Francis Ford, being a part of the gross finance charge, is also prorated under the Rule of 78, and the unearned portion is charged to its reserve account. No charge is made to the customer for the unearned finance charge Francis Ford or the financing institution would have earned had the contract continued for its maximum term (CX's 1954A-C, 2396A, 2431, 3516; Tr. 2267-71).

43. Professor Johnson, one of Francis Ford's expert witnesses, gave an example of proration under the Rule of 78, assuming that the finance institution made a loan on which it assessed a finance charge of \$100 for 12 months. [14] If the debtor paid off the loan prior to the end of its term, after 60 percent of the finance charges were earned by the finance institution, \$40 would be credited to him under the Rule of 78. If an automobile dealer, because of a repurchase agreement, were entitled to 20 percent of the finance charge (\$20) he would, upon early payment, be required to refund his share of the unearned finance charges. In such a case, the finance institution would credit the same amount (\$40) to the debtor and would charge the dealer's reserve account for his share—\$8 (20 percent of \$40)—of the unearned finance charge (Tr. 2267-71).

44. In the event of a repossession under a retail installment contract held by Ford Credit under a repurchase agreement followed by a subsequent redemption of the vehicle by the customer, the customer's payoff and Francis Ford's chargeback are accounted for in the same method as reflected in Finding 42 except that any out-of-pocket expenses incurred in making the repossession are added to the payoff amount to be paid by the redeeming customer (CX 2396A;

⁷ The "Rule of 78" is a method for prorating finance charges and insurance premiums in the event of early payoff, redemption, or repossession under a retail installment contract (CX 3516; Tr. 55-56, 88, 2267-73).

Tr. 62-63); and, in the event of a repossession from a customer purchasing a vehicle under a retail installment contract held by a financing institution pursuant to a repurchase agreement, Francis Ford's payoff and chargebacks are accounted for by the same method as in Finding 42 (CX's 2396A, 2431; Tr. 69-70, 2267-71).

45. The amount of the Francis Ford's chargeback representing its share of the unearned finance charge for the period after early payoff, redemption, or repossession is not charged or collected as an expense from the customer (CX's 2396A, 2431; Tr. 56-58, 62-65, 69-71, 2270).

b. Insurance

46. When Francis Ford sells creditors' life, accident, or health insurance in connection with the sale of a vehicle under a retail installment contract, the gross insurance premium is included in the face amount of the contract (*e.g.*, CX 2581A). Francis Ford obtains such insurance through independent brokers, and receives a share of the insurance premium (Tr. 1178).

47. In the event of an early payoff by a customer purchasing a vehicle under a retail installment contract held by Ford Credit pursuant to a repurchase agreement where the customer has purchased creditor's life insurance from Ford Life Insurance Company, Ford Credit prorates the amount [15] of the gross insurance premium under the Rule of 78. The face amount of the obligation is then reduced by the amount of the unearned gross premium. The portion of the gross premium previously credited to Francis Ford is prorated under the Rule of 78 and the unearned portion is charged back to the dealer (CX 2396A; Tr. 52, 55-56, 85-88, 139).

48. In the event of either an early payoff or repossession on a direct loan on which U.S. Bank has sold creditor life, accident, or health insurance and received a commission, the gross insurance premium is prorated and the balance owing is reduced by the amount of the unearned gross premiums (Tr. 1526-33).

2. Resale of the Repossessed Vehicle

a. Francis Ford's Practice

49. Francis Ford engages in substantial sales of used vehicles to retail customers (Finding 3). When, pursuant to its repurchase obligation, Francis Ford receives a repossessed vehicle from Ford Credit or U.S. Bank, it treats most of them in the same manner as

other used vehicles which it has obtained through other methods and often sells them at retail.⁸

50. There is some evidence in the record that Francis Ford has obtained prices close to retail book value for repossessed vehicles:

a. The Wallace P.⁹ repossession was resold for \$1,425 on 6/21/75 (CX 2501). It was a 1969 Ford Pickup, Model F100 (CX 2561), with 87,855 miles on it at the time of resale (RX 2570A). The retail blue book value for this vehicle was \$1,560 (RX 10, p. 234), less a mileage adjustment of \$135 (RX 10, p. 10), leaving a retail blue book value of \$1,425. [16] The wholesale blue book value for this vehicle was \$1,125 (RX 10, p. 234), less a mileage adjustment of \$100 (RX 10, p. 10), leaving a wholesale blue book value of \$1,025.

b. The Hugh W. repossession was resold for \$5,275 on 8/13/75 (CX 2503). It was a 1975 Ford Elite with 9,220 miles on it at the time of resale (RX 2609A). The retail blue book value for this vehicle was \$5,270 (RX 11, p. 102), plus a mileage adjustment of \$100 (RX 11, p. 8) leaving a retail blue book value of \$5,370. The wholesale blue book value for this vehicle was \$4,150 (RX 11, p. 102), plus a mileage adjustment of \$75 (RX 11, p. 8), leaving a wholesale blue book value of \$4,225.

c. The Gregory D. repossession was resold for \$2,702 on 3/15/75 (CX 2504). It was a 1973 Pinto, two-door, S/W, four-speed manual transmission, with 27,173 miles on it at the time of resale (RX 2637B). The retail blue book value for this vehicle was \$2,605 (RX 9, p. 95), plus a mileage adjustment of \$100 (RX 9, p. 10) and less an accessory adjustment for manual transmission of \$65 (RX 9, p. 11), leaving a retail blue book value of \$2,640. The wholesale blue book value for this vehicle was \$1,950 (RX 9, p. 95), plus a mileage adjustment of \$75 (RX 9, p. 10) and less an accessory adjustment for manual transmission of \$50 (RX 9, p. 11), leaving a wholesale blue book value of \$1,975.

d. The Benjamin T. repossession was resold for \$4,750 on 8/12/75 (CX 2506). It was a 1975 Mustang II Ghia, V-8 (RX 2671), with 3,365 miles on it at the time of resale (RX 2684). The retail blue book value for this vehicle was \$4,675 (RX 11, p. 102), plus a mileage adjustment of \$65 (RX 11, p. 10) and plus an accessory adjustment of \$265 (RX 11, p. 102), leaving a retail blue book value of \$5,005. The wholesale blue book value for this vehicle was \$3,650 (RX 11, p. 102) plus a mileage

⁸ Forty-one of the 43 repossessed vehicles on which Francis Ford realized surpluses were sold at retail by a person to whom Francis Ford paid a salesman's commission (CX's 2501-43; Tr. 932).

⁹ Complaint counsel have requested that the full names of the persons involved in the repossessions analyzed in this decision not be revealed.

adjustment of \$50 (RX 11, p. 10) [17] and plus an accessory adjustment for V-8 engine of \$200 (RX 11, p. 102), leaving a wholesale blue book value of \$3,900.

e. The Ronald A. repossession was resold for \$3,295 on 2/18/75 (CX 2509). It was a 1972 Ford Gran Torino, two-door, sports roof (RX 2761), with 53,669 miles on it at the time of resale (RX 2756A). The retail blue book value for this vehicle was \$2,885 (RX 8, p. 94), less a mileage adjustment of \$200 (RX 8, p. 9), leaving a retail blue book value of \$2,685. The wholesale blue book value for this vehicle was \$2,175 (RX 8, p. 94), less a mileage adjustment of \$150 (RX 8, p. 9), leaving a wholesale blue book value of \$2,025.

51. In practice, Francis Ford has never compared income and expenses on repossessed vehicles at the time they were resold to determine whether surpluses resulted therefrom (Tr. 1086-87, 1175). Instead, Francis Ford has assumed, because of the way it values repossessed vehicles, that their resale always resulted in a deficiency (Tr. 1253, 1373, 1375).

52. The one occasion on which Francis Ford did compare income and expenses on repossessed vehicles resulted from a June 27, 1975 letter from the Commission's Seattle Regional Office. In response to this letter, and upon the advice of its then counsel, Francis Ford prepared and submitted to the Seattle Regional Office in July 1975 a summary tabulation of income and expenses on each of 27 repossessed vehicles returned to it by Ford Credit and U.S. Bank between October 1 and December 31, 1974 (CX 2344; Tr. 210-24, 1119-21, 1135, 1161). This summary tabulation was drawn from various types of records maintained by the dealership, including (a) records showing costs directly attributable to preparation and resale of the vehicles and (b) records showing certain department-wide and overall dealership expenses, indirect in nature (*e.g.*, imputed capital costs, general advertising, lot maintenance and other overhead items such as phone, water, lights and rent), which Francis Ford apportioned to the 27 vehicles on a prorata basis (Tr. 1123-24, 1128-31, 1134).

53. Among the records of direct outlays for these repossessed vehicles which Francis Ford consulted in preparing these tabulations were the internal repair orders it had generated at the time of reconditioning the 27 vehicles in question. For purposes of its response to [18] the Commission's Seattle Office, Francis Ford altered many of the repair orders applicable to these vehicles by crossing out figures which it concluded were too low and entering higher or additional figures (Tr. 1146-51).

54. According to this analysis, and taking the figures supplied by

Francis Ford at face value, 22 of the 27 vehicles had been resold (as of July 16, 1975) and 10 of the 22 had generated surpluses ranging in amount from \$19.15 to \$923.93 and totaling \$3,195.84 (CX 2344).

55. On or about July 23, 1975, upon advice of its then counsel, Francis Ford prepared and sent to each of the persons from whom the above 10 vehicles had been repossessed a check in the amount of the "surplus"—or "amount over and above sales expenses"—thus determined (*e.g.*, CX's 3336, 3339; Tr. 221-24).

56. Except for the 10 checks drawn on or about July 23, 1975 in connection with its response to the Commission's Seattle Office, Francis Ford has never paid or attempted to pay any money to defaulting customers as a refund of surplus and has never advised defaulting customers in any way that money was received by Francis Ford in excess of its expenses and other outlays on the vehicles repossessed from such customers (Adm. 3A; Tr. 222, 483-84).

b. Wholesale Value vs. Resale Price

57. Francis Ford attempts to justify its conduct by arguing that it need not compute surpluses because the value which should be assigned to repossessed vehicles is not the actual selling price (generally a retail price) but an estimated wholesale value.

58. Financial institutions in the Pacific Northwest, including Portland, Oregon, do sell repossessed vehicles,¹⁰ often through auto auctions, at wholesale (Tr. 118-19, 1890-91); and, when they compute surpluses or deficiencies, can legally (and complaint counsel concede this (Tr. 1223)) use the wholesale price as the "fair market value" of the vehicle.¹¹ [19]

59. Because the wholesale price seldom exceeds the payoff when financial institutions are obliged to resell repossessed vehicles, they rarely realize surpluses. A loan officer for the U.S. Bank testified that he had seen no surpluses on the sale of repossessed vehicles in more than 20 years (Tr. 1505). The local office manager of Ford Credit said that he had seen only one surplus on the sale of repossessed vehicles in 16 years (Tr. 406).

60. However, Francis Ford, unlike Ford Credit and U.S. Bank, has used car facilities through which it can, and does, sell repossessed cars and it often obtains a retail price on those resales; nevertheless, Francis Ford claims that it makes no economic sense to require it to credit a defaulting customer with the price at which a

¹⁰ Vehicles which are not returned to dealers under repurchase agreements, and which the financial institutions therefore must dispose of.

¹¹ See *Mount Vernon Dodge, Inc. v. Seattle-First Nat'l Bank*, 18 Wn. App. 569, 570 P.2d 702, 712 (1977).

repossessed vehicle was sold, for that price was realized through Francis Ford's, not the customer's, efforts.

61. This argument finds some support in the testimony of two experts called by Francis Ford. Professor Dale O'Bannon, a teacher of economics at Lewis and Clark College in Portland, Oregon, testified with respect to the economic concept of "opportunity cost"—that is, a cost which has occurred by foregoing some particular kind of activity—and its application to the issue of repossession surpluses (Tr. 1571-72).

62. Professor O'Bannon, after being asked to make certain assumptions,¹² testified that a repurchase dealer loses the opportunity to make a normal sale when he is forced to fulfill his repurchase obligations (Tr. 1583). [20] At the same time, the defaulting purchaser (assuming that there is a surplus calculated on the basis of the actual resale price) would receive the value added by the dealer, a value which is due to the dealer's capital investment (Tr. 1587, 1645).¹³ Thus, according to Dr. O'Bannon, "economic fairness" dictates that a dealer who resells a repossessed vehicle at retail, and who is permitted by law to recover reasonable expenses, should be permitted to retain the difference between its wholesale value and the price at which it was sold. This figure would include commissions, necessary repairs to the vehicle, contributions to overhead, and profit¹⁴—that is, his normal gross margin (Tr. 1594-95).

63. Professor Robert Johnson, director of the credit research center, Purdue University, has a doctorate in finance and was a consultant under contract with the Federal Trade Commission's Office of Policy Planning who was hired to evaluate proposed trade regulation rules on creditors' remedies, one of which deals with repossession practices (Tr. 2149-50). This proposed rule would require that the defaulting customer be credited, when calculating a surplus or deficiency, with the retail value of the repossessed article (Tr. 2154).

64. In testifying on the effects of the relief sought by complaint counsel, Professor Johnson postulated a hypothetical repossession in which the wholesale value of the vehicle was \$2,000, the payoff was

¹² a. That a dealer in used vehicles has limited capital and limitations on his capacity to sell cars;
b. That the dealer has substantial experience in choosing and selling used cars for his account;
c. That the dealer has available to him virtually every current make and model of used vehicle;
d. That the dealer is required to use his capital to buy back, as a forced purchaser, a repossessed car and sell it at retail. (Tr. 1573)

¹³ It is apparent that in some cases, Francis Ford's facilities and professional sales staff have generated a higher resale price on repossessed vehicles than would have been obtained by the defaulting purchaser if he had resold it (Tr. 722, 731, 770, 772, 786, 798, 892), and it can be said that Francis Ford's efforts have added value to the vehicles.

¹⁴ According to Dr. O'Bannon, profits are an expense because they "are nothing more than the cost of keeping a firm in business." (Tr. 1595).

\$2,000 and the gross margin was \$400 (*i.e.*, the vehicle was sold for \$2,400) (Tr. 2174).

65. If complaint counsel prevail, according to the Professor, the defaulting customer, rather than the dealer, would be entitled to the \$400 margin.¹⁵ The "loss" of [21] this \$400—and the probability of similar "losses" on other repossessions—would force the dealer to make adjustments in his business: he might lower the price he pays for trade-ins, raise the prices of cars he sells, or take steps to weed out those customers who are repossession risks and, in the process, deny credit to customers who would have been good risks (Tr. 2176-78). There would also be an industrywide impact on creditors, who would resort to nonrecourse financing (Tr. 2180-81), on credit sales, which would be lower, on new car sales and on new car prices (Tr. 2183-84).

66. Despite what appears to be a logical basis for the theories of Professors O'Bannon and Johnson, I cannot accept them for several reasons. The first—a legal one—will be discussed in my conclusions of law. Second, the theories are based on an assumption—the unlimited availability of every make and model of used car—which is questionable (Tr. 1591, 1607, 1906, 2249). Third, there would be a potential for substantial abuse if the dealer were permitted to retain his "normal" margin on the resale of a repossessed vehicle, for the computation of that margin would depend on a wholesale appraisal by the person who would benefit from application of the theories of Francis Ford's experts (Tr. 2300-01).

67. Professor Johnson conceded that economists prefer that value be established through an arm's length transaction rather than by an appraisal but he argued that abuse could be prevented by setting up an enforcement procedure that would "make it in the self interest of the wholesale manager to accurately establish the wholesale price" (Tr. 2327). However, neither he nor any other witness outlined the procedure which could be used or gave any estimate of the costs which might be involved in policing wholesale appraisals by retail dealers. Furthermore, in addition to the fact that it is required by the UCC and Oregon law, the virtue of complaint counsel's theory is that it makes computation of surpluses or deficiencies relatively simple, for the price to be used is one which has been determined in an arm's length transaction. Finally, I cannot ignore the requirement of the UCC because of possibly adverse economic effects if the proposed order were imposed upon the automobile industry for this

¹⁵ The hypothetical assumes no out-of-pocket costs to prepare the car for sale (Tr. 2175).

is a question of administrative discretion which only the Commission has the authority to deal with. [22]

68. For these reasons, I find that the appropriate price for determining whether Francis Ford realized a surplus or suffered a deficiency on the resale of repossessed vehicles is the actual resale price of those vehicles.

G. Allowable Expenses

1. Overhead

69. The parties agree that under the UCC Francis Ford can deduct from the price at which it sells a repossessed vehicle all costs directly resulting from its repossession, preparation for sale and resale. However, complaint counsel argue that only these costs are deductible and that overhead (indirect) expenses are not.

70. In support of their position, complaint counsel called Dr. Gerald L. Cleveland, a professor of accounting at Seattle University. Dr. Cleveland testified that the following overhead expenses should not be allowed as deductions when a dealer calculates a surplus or deficiency because this would allow the dealer to recover the same expenses twice:

- a. Rental expenses for a used car lot.
- b. Imputed interest on dealer funds invested in a repossessed car.
- c. Interest on funds borrowed by the dealership.
- d. Depreciation on the dealership's buildings.
- e. Administrative accounting expenses.
- f. Salaries of supervisors.
- g. Salaries of lot boys. (Tr. 540, 561-65, 566-67, 654-55, 694-95)

71. Although he claimed that his theory is based upon accepted accounting principles, Dr. Cleveland's conclusion seems to be derived not from widely accepted principles but from his belief that a dealer who resells a repossessed automobile is a fiduciary of the defaulting customer with respect to surpluses (Tr. 557). Dr. Cleveland believes that a dealer-fiduciary [23] should not benefit from his trust (Tr. 560) but he has not, in my opinion, satisfactorily explained what accepted accounting principle prohibits a fiduciary from recovering legitimate overhead expenses.

72. I must conclude, as did respondent's expert witness, Mr. James W. Porter, that a dealer who repossesses a vehicle does incur overhead expenses in preparing it for sale and in reselling it which do not duplicate overhead expenses which were incurred when the car was sold to the defaulting purchaser. Mr. Porter, a CPA who has

performed accounting functions for some 350 automobile dealerships since 1946 (Tr. 1730), testified that while accountants might differ over whether certain costs are fixed or not, accountants agree that overhead costs are considered costs of sale which should be allocated (deducted) from the resale price of a repossessed vehicle (Tr. 1770-71, 1804).

73. While I accept the principle that a dealer does incur overhead expenses when he resells a repossessed vehicle, the problem of determining what that cost is forces me to conclude that, as a practical matter, overhead should not be deductible from the resale price of that vehicle. Mr. Porter's explanation of how overhead would be allocated to the resale of each repossessed vehicle in a dealer's inventory reveals that a cost study of Francis Ford's business would have to be done periodically to determine these expenses (Tr. 1757-63, 1768-72, 1824).

74. I agree with Dr. Cleveland that in setting up a system under which Francis Ford should be required to account for surpluses (or deficiencies) on repossessed vehicles, the paramount consideration should be simplicity and minimal cost of compliance (Tr. 557-58). Allowing the allocation of overhead might impose expenses for a cost accounting system which exceed the overhead expenses which are computed. Furthermore, Commission compliance efforts would be greatly complicated, for the validity of the cost allocations would have to be determined periodically.

75. Disallowing overhead expenses is not, in my opinion, unfair, for other businesses involved in repossessions which have overhead expenses do not deduct them when they compute surpluses or deficiencies. Financial institutions deduct only out-of-pocket expenses (those directly resulting from the repossession) in calculating the amount of a surplus or a deficiency (CX 1225A-E; Tr. 167-68, 694, 1226). In computing surpluses or deficiencies realized on nonrecourse repossessions, Ford Credit deducts from the [24] resale price only the payoff balance and the out-of-pocket expenses paid out to third parties (Tr. 703-04). Overhead is not included as an expense (Tr. 704).

76. In the period from 1972 through 1974, Ford Credit's Central Collections Department attempted to collect deficiencies for Ford dealers with respect to certain repurchase accounts. In determining the collectible expenses of dealers, Ford Credit included only the dealer's out-of-pocket expenses (Tr. 707).

77. Since 1971 or earlier, on the advice of counsel, Damerow Ford Company of Beaverton, Oregon (a competitor of Francis Ford) has computed and paid surpluses realized upon the resale of repossessed

vehicles by deducting the payoff, direct costs of repairs, and sales commission from the resale price. Overhead has not been deducted (Tr. 839-51).

2. Over and Underallowances

78. An overallowance may occur when a vehicle is received by an automobile dealer in trade. An overallowance is the amount by which the agreed trade-in amount exceeds the wholesale value of the vehicle (Tr. 674, 1015-18, 1020-23). An underallowance may occur when a vehicle is received by an automobile dealer in trade. An underallowance is the amount by which the agreed trade-in amount is less than the wholesale value of the vehicle (Tr. 682, 1016-17, 1019, 1032).

79. Francis Ford had underallowances and overallowances on some of the repossession dispositions in evidence in this proceeding (RX's 2663-64, 2702-03, 2763, 2765; Tr. 1995, 2003, 2006, 2014).

80. Overallowances or underallowances affect the determination of resale proceeds for a repossessed vehicle (Tr. 554). An overallowance is a subtraction from the selling price of the repossessed vehicle and an underallowance is an addition to the selling price (RX 2400D; CX 2344).

3. Other Expenses

The out-of-pocket expenses which are allowable when computing a surplus or deficiency include the cost of repairs in preparing the vehicle for resale, towing and storage charges, and commissions paid to salesmen and their supervisors who actually participate in the sale of the repossessed vehicle. Post-resale repairs are also allowable if they are a condition of sale. [25]

82. Contrary to Francis Ford's claim, I find that chargebacks on the unearned portion of finance charges or insurance premiums are not an expense and cannot be deducted from the resale price of a vehicle which it repossesses.

4. Surpluses Realized by Francis Ford on Sales of Repossessed Vehicles

83. Complaint counsel offered in evidence 43 charts which analyze the sale by Francis Ford of repossessed vehicles (CX's 2501-43). Their proposed findings duplicate each of these charts with some corrections (for example, on line 26, commissions paid by Francis Ford to assistant sales managers which complaint counsel now concede are deductible expenses).

84. I find that the charts accurately reflect, as to each transaction, the resale price of the vehicle in question, the net payoff made by Francis Ford to the financial institution, adjustments to the resale price for overallowance or underallowance and all legitimate expenses incurred by Francis Ford in preparing the vehicle for sale and in reselling it.

85. The repossession charts disclose, and I find, that Francis Ford realized the following surpluses, in six of which it made some payment to the defaulting customer. In only one of those six cases did the customer receive the total surplus.

<i>CX #</i>	<i>Customer Name</i>	<i>Amount of Surplus</i>	<i>Payment by Francis Ford to Customer</i>
2501	Wallace P.	\$545.86	None
2502	Bruce S.	\$268.00	None
2503	Hugh W.	\$ 89.74	None
2504	Gregory D.	\$848.35	None
2505	Stanley D.	\$513.65	None
2506	Benjamin T.	\$153.02	None
2507	Odeh D.	\$633.36	None
2508	Richard W.	\$281.14	\$149.92
2509	Ronald A.	\$460.60	None
2510	Lloyd D.	\$220.16	None
2511	Raymond H.	\$327.17	None
2512	L. C. Y.	\$806.48	None
2513	Art F.	\$221.85	None
2514	Richard L.	\$173.14	None
2515	Birdie T.	\$336.96	None
2516	John C. H.	\$169.31	None
2517	William K.	\$161.02	None [26]
2518	Dale W.	\$110.98	None
2519	Charles R.	\$506.87	None
2520	Gary R.	\$411.01	\$80.12
2521	Robert S.	\$ 71.50	None
2522	Harold L.	\$611.02	\$230.72
2523	Steve C.	\$544.93	None
2524	Rex B.	\$386.56	None
2525	Matt M.	\$385.61	None
2526	Thomas B.	\$1,064.43	None
2527	Daniel D.	\$348.03	None
2528	Robert C.	\$605.67	None
2529	Harry E.	\$184.26	None
2530	Keldon A.	\$ 96.37	None
2531	Jack D.	\$ 76.01	None
2532	William M.	\$1,164.29	None
2533	Brian K.	\$133.44	None
2534	Thomas H.	\$351.22	None
2535	Paul M.	\$377.35	\$85.17
2536	Lee B.	\$547.79	\$738.63
2537	John R. H.	\$1,045.73	None

2538	Patricia C.	\$518.26	\$201.19
2539	Robert T.	\$152.50	None
2540	Paul S.	\$368.66	None
2541	Clifford B.	\$232.20	None
2542	John B.	\$299.44	None
2543	Charles M.	\$333.91	None

These repossession transactions produced over \$17,000 in surpluses initially withheld by Francis Ford. Francis Ford continues to retain some \$15,000 from the surpluses in 42 of the transactions.

H. The Typical Defaulting Customer

86. As would be expected, and as has been found in some studies, many of the customers from whom vehicles are repossessed have financial problems, are ill, or unemployed (Johnson, Tr. 2226). Included among the Francis Ford customers whose vehicles were sold at a surplus were a customer who could not read (Tr. 896), a person whose spouse was suffering a mental breakdown at the time of the repossession (Tr. 828), and a person who had lost his \$425 per month job and was no longer able to make his \$171 monthly payments on the financing Francis Ford had arranged (\$64 per month for the borrowed down payment and an additional \$107.10 payments on the retail installment contract held by Ford Motor Credit) (Tr. 748, 754, 755). Other specified reasons for default which are listed in legible documents in the record include reduced income (CX's 2779, 2925, 2964A, 3025A, 3343A), unemployment (CX's 2855, 3104B), and bankruptcy (CX 3145A). [27]

III. CONCLUSIONS OF LAW

A. The FTC Act and the Definition of "Unfair"

The theory of the complaint is that the retention of surpluses on the resale of repossessed vehicles is an "unfair" practice within the meaning of Section 5 of the FTC Act. This vague standard has, fortunately, been fleshed out considerably in the past several years by the Commission, most clearly in the following definition which was quoted by the Supreme Court in *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 244 n. 5 (1972):

The Commission has described the factors it considers in determining whether a practice that is neither in violation of the antitrust laws nor deceptive is nonetheless unfair: "(1) whether the practice, without necessarily having been previously considered unlawful, offends public policy as it has been established by statutes, the common law, or otherwise — whether, in other words, it is within at least the penumbra of some common-law, statutory, or other established concept of fairness; (2) whether it is immoral, unethical, oppressive or unscrupulous; (3) whether it causes

substantial injury to consumers (or competitors or other businessmen)" "Statement of Basis And Purpose of Trade Regulation Rule 408 . . ." 29 Fed. Reg. 8324, 8355 (1964)

Complaint counsel argue that Francis Ford's retention of surpluses meets all three of the "unfairness" definitions announced by the Commission; the practice is, they claim, a violation of state law; it is immoral, unethical, oppressive and unscrupulous; and, it injures those consumers who they call "repossession victims."

B. The UCC and Oregon Law

Oregon law regarding the obligation to pay surpluses realized on the resale of repossessed vehicles is, according to complaint counsel, derived from Article 9 of [28] the UCC (Oregon Revised Statutes (ORS) §§ 79.1010-79.5070). Francis Ford, on the other hand, argues that a dealer's rights with respect to repossessed vehicles are controlled not by Article 9, but by Article 2. If applicable in this case, Article 2 would permit Francis Ford to recover consequential damages, including overhead costs and lost profits when a customer defaults, for UCC § 2-708(2) provides:

If the measure of damages provided in subsection (1) is inadequate to put the seller in as good a position as performance would have done the measure of damages is the profit (including reasonable overhead) which the seller would have made from full performance by the buyer. . . .

Francis Ford relies on the draftsmen's comments to § 9-113 for its claim that it is entitled to lost profits and overhead under Article 2: "[A] seller who reserves a security interest by agreement does not lose his rights under the Sales Article (Article 2) . . ." (§ 9-113, Comment 5). This comment is taken out of context. The language of § 9-113 and other comments on that section make it very clear that the rights of a secured party on default by the debtor are governed by Article 2 *only* if the security interest arises *under* Article 2, *e.g.*, liens arising by operation of law where the buyer does not have possession of the goods. In this case, however, Francis Ford's security interest arises from a specific provision of Article 9 (see UCC § 9-102(1)) and, since Article 9 creates that interest, Article 9, not Article 2, defines the rights and obligations of the secured party and the debtor.

Francis Ford's argument is also erroneous because UCC § 2-708 provides for seller's damages only if there has been nonacceptance or repudiation by the buyer. Such breaches occur under Article 2 when a party by overt communication or action informs the other party that he does not intend to render any performance under the contract or when a party hinders the other party from any performance. (See UCC § 2-610 and *J. White and R. Summers*,

Handbook of the Law Under the Uniform Commercial Code, 1972, pp. 168-175). Since repossessions by dealers occur only after a vehicle has been sold by delivery and acceptance (performance by both buyer and seller) § 2-708 is inapplicable, and Francis Ford's citation of cases allowing recovery of lost profits is misplaced because they concern either nonacceptance or repudiation of a contract and do not deal with Article 9 security interests. [29]

Finally, the drafters of the UCC intended Article 9 to be "a comprehensive scheme for the regulation of security interests in personal property . . ." UCC § 9-101, Official Comment. Its aim is to provide a unified structure for the regulation of sales made on credit where the goods serve as a security for the extension of credit, whereas Article 2 deals with the formation of unsecured sales contracts and the rights of the parties to those contracts. It was not intended to govern secured transactions¹⁶ and I do not accept the argument that its provisions are controlling here.

UCC § 9-102(1) states that Article 9 applies to any transaction which is intended to create a security interest in personal property and to any sale of accounts or chattel paper. Security interests¹⁷ created by pledge, assignment, conditional sale and other devices are expressly included under the coverage of Article 9. UCC § 9-102(2).

Pursuant to the retail installment contract it enters into with its customers and UCC § 1-201(37), Francis Ford is a secured party. When Francis Ford sells or assigns its security interest in the financed vehicle either to Ford Credit or U.S. Bank, those institutions become the secured parties:

"Secured party" means a lender, seller or other person in whose favor there is a security interest, including a person to whom accounts or chattel papers have been sold. UCC § 9-105(1)(m), and Comment 2.

When either Ford Credit or the U.S. Bank repossesses a vehicle and returns it to Francis Ford pursuant to a repurchase [30] agreement, Francis Ford once again becomes the party holding a security interest in the vehicle:

A person who is liable to a secured party under a guaranty, indorsement, repurchase agreement or the like and who receives a transfer of collateral from the secured party or is subrogated to his rights has thereafter the rights and duties of the secured party.

¹⁶ See UCC § 2-102.

Unless the context otherwise requires, this Article applies to transactions in goods; it does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate only as a security transaction. . . .

The comment to this section states that the words, "security transactions" are "used in the same sense as in the Article on Secured Transactions (Article 9)."

¹⁷ Defined in UCC § 1-201(37) as "an interest in personal property or fixtures which secures payment or performance of an obligation."

Such a transfer of collateral is not a sale or disposition of the collateral under this Article. UCC § 9-504(5).

After Francis Ford fulfills its repurchase obligation and resells the repossessed vehicle, it, as the secured party, is required to pay any surplus due, and may pursue any deficiency owed by, the defaulting customer:

If the security interest secures an indebtedness, the secured party must account to the debtor for any surplus, and, unless otherwise agreed, the debtor is liable for any deficiency. . . . UCC § 9-504(2).

In its retail installment contracts with customers, Francis Ford recognizes and acknowledges its duty under state law to pay any surpluses realized upon resale of a repossessed vehicle (Findings 20, 21).

C. Francis Ford Has Realized, and Has Not Paid, UCC Surpluses

1. Introduction

There is no serious dispute that Francis Ford is required by state law to pay surpluses to defaulting customers; rather, the dispute is over the price which may be used, and the deductions which may be made from that price, in calculating a surplus or deficiency. The language of the UCC and court interpretations of that language reveal that complaint counsel's claims are correct, *i.e.*, (1) that the price which must be used under the UCC to calculate surpluses or deficiencies is, for dealers such as Francis Ford, the actual price (in many cases the retail price) at which the repossessed vehicle was sold and (2) that overhead is not a deductible expense which may be charged against the resale price. [31]

2. Actual Sale vs. Wholesale Appraisal

Francis Ford argues that the amounts which should be credited to the repossessions analyzed by complaint counsel are the wholesale values of the vehicles, not the prices at which they were sold. This position is contrary to the repurchase agreements Francis Ford has with U.S. Bank and Ford Credit. The Ford Credit agreement refers to "excess proceeds on resale," and the U.S. Bank version speaks of ". . . an excess of net proceeds upon the sale. . . ." (Finding 28 and CX 2307A). Furthermore, the notices sent to defaulting customers by Ford Credit and to Francis Ford contemplate that the repossessed vehicles will be sold (Finding 22).

Section 9-504 of the UCC also supports complaint counsel's argument:

A secured party after default may sell, lease or otherwise dispose of any or all of the collateral . . . the proceeds of disposition shall be applied . . . to . . . the reasonable expenses of retaking, holding, preparing for sale or lease, selling, leasing and the like. . . . UCC § 9-504(1).

Disposition of the collateral may be by public or private proceedings. . . . Sale or other disposition. . . . UCC § 9-504(3). See also Comments 1, 5 and 6.

The words “sell,” “lease” or “otherwise dispose” clearly refer to a situation in which the dealer parts with possession of the vehicle,¹⁸ and indeed, Francis Ford did so in the repossessions analyzed above. Nowhere—in the UCC, the comments, or court interpretations—is there any suggestion that a dealer who sells a repossessed vehicle at retail can assign a wholesale value to it for purposes of meeting his obligations under § 9-504. Such an interpretation would defeat its purpose: [32]

The purpose of § 9-504(5), UCC, is to insure that the value of repossessed collateral is measured by a bona fide sale in the marketplace, and not by an artificial value [such as] the balance due on the debtor’s contract. *Reeves v. Associates Financial Services Co., Inc.*, 197 Neb. 107, 247 N.W.2d 434, 439 (Neb. App. 1976).

See also *Carter v. Ryburn Ford Sales, Inc.*, 451 S.W.2d 199 (Ark. Sup. Ct. 1970), an action by a Ford dealer to recover a Ford truck. In computing the deficiency, the dealer’s calculation was based on his having credited the debtor with an estimated value of the vehicle. This “purchase” by the dealer was held to be not in conformity with the Uniform Commercial Code. To the same effect see *Vic Hansen & Sons, Inc. v. Crowley*, 57 Wis.2d 106, 203 N.W.2d 728, 733 (1973), where the court said such “a practice has no place in a private sale of a debtor’s collateral . . .” Also, California’s motor vehicle law contains a provision paralleling UCC § 9-504 which makes it clear that the surplus is to be determined from the proceeds of resale. The statute provides for a written accounting itemizing the following data on each repossessed vehicle: (1) the gross proceeds of the disposition, (2) reasonable and necessary expenses incurred in retaking, holding, preparing for and conducting the sale, and certain attorneys’ fees and legal expenses, and (3) satisfaction of the indebtedness. Cal. Civ. Code § 2983.2(b). It goes on to recite that:

In all sales which result in a surplus, the seller or holder shall furnish [such] an accounting [to the debtor/buyer]. Such surplus shall be returned to the buyer within 45 days after the sale is conducted. [Cal. Civ. Code § 2983.2(c)].

I also reject Francis Ford’s argument that § 83.830(1)(b) of

¹⁸ UCC § 9-505 does permit retention of collateral in discharge of an obligation under certain circumstances but the fact that this section was included in the UCC indicates that § 9-504 contemplates the secured party’s relinquishment of the collateral.

Oregon's Consumer Credit Act permits it to value repossessed vehicles at wholesale and that the Act therefore repeals the UCC's requirement that the resale price of the vehicle be credited to the defaulting customer. First, many vehicles are sold within 90 days of repossession and, if they are sold at retail, that price would be the "fair market value" under the Act. Second, if a particular vehicle were not sold at the time a deficiency suit were brought, I believe that the Oregon courts would require a retail dealer such as Francis Ford to value the vehicle at an estimated retail price for purposes of computing any deficiency. [33]

3. Retail vs. Wholesale Disposition and the "Best Possible Price"

While I accept the proposition that Francis Ford must value repossessed vehicles at their actual selling prices, and not at estimated wholesale values, this conclusion produces a rather interesting result, for what the defaulting customers are owed under UCC § 9-504 is not the result of some intrinsic residual values in the repossessed vehicles (after the payoff and repossession expenses are satisfied) but is dependent upon the status of the reseller. For example, if Ford Credit repossesses a vehicle from a defaulting customer and, because it has no repurchase agreement with a dealer, disposes of it at wholesale (since it has no retail facilities), the wholesale price would, complaint counsel concede (Finding 58), be the "proceeds" which, under § 9-504, Ford Credit would use to calculate a surplus or deficiency. If that wholesale price were equal to the payoff plus legitimate expenses, the defaulting purchaser would not receive any payment of surplus. On the other hand, if Francis Ford, by virtue of its repurchase agreement, took possession of the same vehicle and resold it at retail, it would, under the UCC, be obliged to credit the same defaulting customer with the retail price. If that retail price exceeded the payoff plus legitimate expenses, a surplus would be owed the defaulting customer.

Francis Ford asks why it cannot assign a wholesale value to vehicles which it repossesses which is equal to the wholesale price which Ford Credit can lawfully assign to vehicles which it repossesses. The answer which complaint counsel give—that Ford Credit has no retail facilities while Francis Ford does—is not convincing for it tends to support Professor O'Bannon's argument that surpluses are realized because of Francis Ford's retail facilities and expertise (Finding 62).

The answer is much simpler: Despite the apparent soundness of Professor O'Bannon's economic argument, the UCC requires a retail dealer like Francis Ford to compute surpluses or deficiencies using

the price at which the repossessed vehicle was sold, and that price would generally be the retail price, for disposition at retail rather than at wholesale would usually realize the best possible return on the collateral. The view that the secured party should obtain the best possible price for the collateral which he holds is based on the theory that he is a fiduciary with respect to the collateral:

[I]f the creditor decides to liquidate the collateral, he must act as the debtor's fiduciary in disposing of the assets. *United States v. Terrey*, 554 F.2d 685, 693 (1977).

In *Vic Hansen & Sons, Inc. v. Crowley*, 57 Wis.2d 106, 203 N.W. 2d 728, 731 (1973), the Wisconsin Supreme Court held: [34]

Prior to the enactment of the Uniform Commercial Code in Wisconsin, this court held that the secured party owed a duty to the debtor to use all fair and reasonable means in obtaining the best price for the property on sale. [citations omitted] This duty was not abandoned upon the enactment of the Code. The purpose of the Uniform Commercial Code is the protection of both the creditor and the debtor. Each party to the transaction has certain duties. The duty of the secured party in this instance was to obtain the best possible price it could obtain for the collateral for the benefit of the debtor.

Similarly, in *Elster's Sales v. El Bodrero Hotel, Inc.*, 250 Cal. App.2d 258, 58 Cal. Rptr. 492, 493 (1967), a California court concluded that:

[The] policy of the law . . . requires a repossessing seller to resell at the best obtainable price on commercially reasonable terms. [citations omitted] This policy tends to protect a defaulting buyer from any greater loss by way of deficiency judgment than the market reasonably justifies . . .

The secured party's obligation was described as follows in *Foster v. Knutson*, 84 Wn.2d 538, 549, 527 P.2d 1108, 1115 (1974):

He is required to use his best efforts to sell the collateral for the highest price and to have a reasonable regard for the debtor's interests.

See also, *Credit Bureau Metro, Inc. v. Mims*, 119 Cal. Rptr. 622, 623 (1975) (" . . . failure to use 'best efforts' to obtain the highest possible price for the collateral is a breach of the secured party's obligation to act in good faith and in a commercially reasonable manner."); *Luxurest Furniture Manufacturing Co. v. Furniture Warehouse Sales, Inc.*, 132 Ga. App. 661, 209 S.E.2d 63, 65 (1974) (the seller must exercise "due diligence in attempting to get the best price obtainable"); *Dynalectron Corp. v. Jack Richards Aircraft Co.*, 337 F.Supp. [35] 659, 663 (W.D. Okla. 1972) (secured party must use "due diligence" to get the best price); *GMAC v. Elwell*, 7 UCC Rep. Serv. 1074 (N.Y. Civ. Ct. 1970) ("pledgee owes to the debtor the duty of obtaining the best price upon a sale of the pledged chattel," a duty

violated by GMAC's sale of the vehicle to itself with no effort to obtain a fair price from any purchasers).

4. Overhead Is Not an Allowable Expense

Section 9-504(1)(a) permits the secured party to charge the defaulting purchaser with:

the reasonable expenses of retaking, holding, preparing for sale or lease, selling, leasing and the like and, to the extent provided for in the agreement and not prohibited by law, the reasonable attorneys' fees and legal expenses incurred by the secured party. . . .

The UCC does not define the term "reasonable expenses" but complaint counsel argue that common law precedents, incorporated into the UCC by reference, call for the conclusion that the only "reasonable expenses" are out-of-pocket costs and that overhead is not an allowable expense.

Sections 9-207 and 9-504 establish the rights and duties of a secured party with respect to collateral in his possession. Section 9-207, which applies to collateral held before a default, requires the secured party to use reasonable care in the custody and preservation of such collateral, and provides that reasonable expenses incurred by the secured party in caring for and preserving the collateral are chargeable to the debtor and are secured by the collateral unless there is agreement to the contrary.

The draftsman's comments to these two sections indicate that they follow common law precedents. UCC § 9-207, Comment 2; § 9-504, Comment 2. Under the pre-Code pledge law to which these two sections refer, a pledgee was entitled to charge to the debtor only out-of-pocket expenses actually incurred in maintaining and preserving the collateral. The pledgee was not entitled to charge for expenses that would have been incurred regardless of the debtor's default, and it has been held that under the UCC, only reasonable out-of-pocket expenses [36] can be allowed. Professor Grant Gilmore, the original reporter on Article 9, states with respect to the out-of-pocket principle:

The rule seems to be well-established that only "direct" expenses — the out-of-pocket costs of repossession, storage and the like incurred in connection with the particular goods — can be claimed by the secured party. The courts have regularly turned down attempts to include indirect expenses — such as the secured party's general cost of doing business — or to avoid the necessity of proving actual expenses by using the 15 percent formula which is also used in the attorneys' fees clause. 2 Gilmore, *Security Interests in Personal Property*, § 43.5 (1963).

This position is supported by the case law prior to enactment of

