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Automobiles - Recordation of Chattel Mortgage Not Constructive Notice to Good Faith Purchaser from Dealer-Estoppel

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AUTOMOBILES—RECORDATION OF CHATTEL MORTGAGE NOT CONSTRUCTIVE NOTICE TO GOOD FAITH PURCHASER FROM DEALER—ESTOPPEL

For a number of years plaintiff, General Credit, Inc., has assisted defendant Winchester, Inc., an automobile dealer, in financing the purchase of new cars by advancing the purchase price to the manufacturer and taking liens on such cars to secure the sums advanced. After the cars had come into Winchester's possession that concern would apply to and receive from the Division of Motor Vehicles a dealer's certificate of title for each car, under Section 46-106 of the Virginia Code of 1950, issued in the name of Winchester showing thereon a lien in favor of General Credit for the amount of the purchase price. The certificate of title was held by General Credit until its lien was paid. With the permission of General Credit, Winchester placed such cars on display in its showrooms. General Credit relied upon Winchester on the sale of such car to collect the purchase price. Upon the discharge of the liens, certificates of title would be transferred to the respective purchasers. Defendants Baker and Bermudez purchased a car from Winchester which had been financed in the regular manner. They received a receipted invoice showing the details of the sale transaction and were advised that in a few days they would receive from the Division of Motor Vehicles a certificate of title for the car and that in the meantime the receipted invoice would serve as evidence of their title. The purchasers were not informed that the title of the car was held in the name of Winchester subject to the lien thereon in favor of General Credit. Winchester failed to pay General Credit and thus discharge the recorded lien. Upon learning that the car had been sold to Baker and Bermudez, General Credit took possession of the car and brought this action to determine the rights of the parties. The trial court held that General Credit was estopped to assert its duly recorded lien against bona fide purchasers. On appeal, *held*, affirmed. *General Credit, Inc.* v. *Winchester, Inc.*, 198 Va. 711, 85 S.E.2d 201 (1955) (Miller, Buchanan and Smith, JJ., dissenting).

It is a fundamental principle of both the civil law and the common law that with certain exceptions no one can transfer a

better title to personal property than he has. One of the exceptions is the passage of title by estoppel.[1] Further, though a dangerous and misleading appearance may be created by every bailment, the mere possession of chattels by an agent with permission of his principal will not enable the agent to give good title against the latter, even though the buyer is a bona fide purchaser.[2] Hence the general rule of agency that a principal is not bound by the unauthorized sale of his agent unless he has in some way clothed the agent with authority to sell, in which case he may be estopped to assert his ownership as against a bona fide purchaser who buys from the agent.[3]

In the *General Credit* case, Winchester had apparent authority to sell. In fact, from the course of dealing between General Credit and Winchester it would appear that General Credit had expressly permitted such sales. In either event the doctrine of estoppel would prevent an assertion of the lien by General Credit upon the principle of agency presented.

An estoppel is that which prevents the showing of the actual truth, and when there is an estoppel it shuts out the evidence of the truth.[4] Estoppels are tolerated in only a few cases and only from absolute necessity since they prevent the actual truth.[5] The elements of estoppel are: (1) there must have been a representation or concealment of the facts; (2) such representation or concealment must have been made with knowledge of the facts, unless the party making it was bound to know the facts, or his ignorance of them was due to gross negligence; (3) the party to whom it was made must have been ignorant of the truth of the matter as to which the representation was made; (4) it must have been made with the intention that the party should act on it; (5) it was the inducement to the action of the other party; and (6) the party claiming the estoppel must have been misled to his injury.[6] These elements of estoppel were all present in the transactions leading to the litigation of the *General Credit* case. General Credit, with knowledge of the facts (it held a

[1] 24 R.C.L. 373 (1929).
[2] 19 Am.Jur., Estoppel §68 (1939); 24 R.C.L. 391 (1929).
[3] Am.Jur., Agency §§114 seq. (1936); 24 R.C.L. 378, 392 (1929).
[4] 7 Michie's Jurisprudence, Estoppel §2 (1949).
[5] *Ibid.*
[6] 7 Michie's Jurisprudence, Estoppel §16 (1949).

lien on an automobile to be sold by Winchester) represented that Winchester had a good title (it was not customary to inform the purchasers of the state of the title) with the intention that people should purchase automobiles from Winchester. Baker and Bermudez did not know the true facts (they were not informed of the lien), they were induced to act unaware of the true facts (they logically believed that Winchester had a clear title to the automobile), and they were misled to their injury (they made a down payment on the automobile). Thus Winchester had apparent authority to sell, and consequently General Credit was estopped to assert its lien. The Court applied the maxim "where one of two equally innocent persons must suffer, he should bear the burden whose conduct has induced the loss."[7]

Upon applying the above mentioned principles of agency and estoppel, we have the basis for the decision of the *General Credit* case and a clear and simple formula which may be applied to all cases in point with the principal case. The decision, however, was one in which three Justices dissented and to them the formula did not seem so clear and simple. The dissension occurred because of Section 46-71 of the Virginia Code of 1950. It provides in part:

> Such certificates of title, when issued by the Division showing a lien of encumbrance, shall be deemed adequate notice to the Commonwealth, creditors and purchasers that a lien against the motor vehicle exists and the recording of such reservation of title, lien or encumbrance in the county or city wherein the purchaser or debtor resides or elsewhere is not necessary and shall not be required. . . .

When Winchester applied for a certificate of title as permitted by Section 46-106, it had recorded thereon the lien which General Credit held. Section 46-71 provides that such recordation shall be notice to the Commonwealth, creditors and purchasers. Herein lies the real issue of the case under comment: Notwithstanding the principles of agency and estoppel, does the recordation of a chattel mortgage or a conditional sales contract constitute constructive notice of the lien of the mortgagee or title

[7] 196 Va. 711, 85 S.E.2d 201, 203 (1955).

of the conditional vendor when the chattel has been left in the hands of a dealer engaged in the sale of such chattels? It would seem that the cases are equally divided on this question.[8]

The leading case cited by jurisdictions holding that such recordation does not constitute notice is *Boice* v. *Finance & Guarantee Corp.*[9] The Supreme Court of Appeals of Virginia said in that case: "The constructive notice furnished by a recorded mortgage or deed of trust in such cases is not sufficient. The act of knowingly permitting the goods to be handled and used by the seller in the ordinary and usual conduct of his business is just as destructive of the rights of the creditors as if such permission had been expressly granted in the mortgage or deed of trust."[10] The mortgagee financier in the *Boice* case had the mortgage recorded under the provisions of Section 5189 of the Code of Virginia of 1919, which provided for the recordation of all reservations of title or liens on goods or chattels sold. The Court reasoned:

> It is a matter of common knowledge, and will therefore be judicially noticed, that in the large cities there are department stores in which a customer can buy most anything from a nutcracker to a threshing machine, from a doll carriage to an automobile. It would never occur to a customer that he must be on his guard to see whether the article was bulky, of large value and easily susceptible of identification, and if so examine the registry for liens thereon.[11]

Although the *General Credit* and *Boice* cases were decided on the theory of estoppel, some courts have reached the same result on the theory that the mortgagee waives his rights against a purchaser from a dealer in goods or chattels when he permits the dealer to display and sell such goods or chattels. In *Howell* v. *Board*[12] the court said:

> . . . the mortgage is wholly ineffective as to the excepted class, that is, purchasers, because of the express or implied understanding between the parties which constitutes a

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[8] See cases cited in Annot., 136 A.L.R. 821 (1942).
[9] 127 Va. 563, 102 S.E. 591 (1920).
[10] *Id.* at 570, 102 S.E. 591, 593.
[11] *Ibid.*
[12] 185 Okla. 513, 94 P.2d 831 (1939).
[13] 185 Okla. 513, ..., 94 P2d 830, 832.

> waiver. The recording of a chattel mortgage does not add to its actual force and effect. It merely imparts constructive knowledge of the mortgage to subsequent purchasers and makes their subsequently acquired rights subject to the rights of the mortgagee. When as in this case, by reason of agreement express or implied, the mortgagee has no rights against subsequent purchasers of the class here involved, the fact that the mortgage was filed of record does not confer such rights.[13]

The recordation of the mortgage was constructive notice, but the mortgagee waived his right to rely on that fact.

Those courts holding to the opposite view that recordation does constitute such constructive notice as to prevent a vendee from being a good faith purchaser have been just as convincing. They reason that where liens and mortgages are found on public records, any person of ordinary prudence would, by the exercise of reasonable care, learn of their existence.[14] Further, the rule "where one of two equally innocent parties must suffer, he whose conduct caused the loss must bear the burden" cannot be applied, because a purchaser who under a statute has constructive notice is not an innocent party.[15] To hold that such recordation is not constructive notice would be to hold that property on sale by a dealer in such property could not be mortgaged.[16] The purchase of an automobile is not such an ordinary occurrence as to make it particularly burdensome for a purchaser to examine the records.[17] When a statute provides that recordation of a lien or mortgage is notice to any purchaser, it is within the province of the legislature to change the law and not the courts.[18]

The General Assembly of Virginia in 1926 enacted as Chapter 149 legislation concerning registration of titles to automobiles. It provided for the issuance of titles, the recordation of any liens thereon, and declared the effect of such issuance and recordation. This enactment, as subsequently amended,[19] is now carried in the Code of 1950 under "Title 46. Motor Vehicles." Sales of automobiles are no longer subject to the sections of the Code governing sales of goods or chattels generally.

[14] Finance & Guarantee Co. v. Defiance Motor Truck Co., 145 Md. 94, 125 A. 585 (1924).
[15] Hardin v. State Bank, 119 Wash. 169, 205 P. 382 (1922).
[16] Palmisano v. Louisiana Motors Co., 166 La. 416, 117 So. 446 (1928).
[17] *Ibid.*
[18] Finance & Guarantee Co. v. Defiance Motor Truck Co., 145 Md. 94, 125 A. 585 (1924).
[19] Va. Acts 1932, p. 613; Va. Acts 1934, p. 380.

A majority of the Court in the *General Credit* case decided that these acts were designed to supersede the former provisions that a sale of an automobile or a mortgage thereon should be recorded in the local clerk's office. Code Sections 46-42 and 46-106 provided a more expedient method of recordation and a simpler method for determining any liens on automobiles by requiring that recordation be made at a central place, the Division of Motor Vehicles. The pertinent sections of the enactment were designed for no other purpose and did not change the law as laid down in the *Boice* case.

The dissenting Justices believed that the purpose of the enactment did not stop with expediency and simplicity. Their reasons were somewhat more profound. The language of Section 46-71 was clear and simple: "Such certificates of title, when issued by the Division showing a lien or encumbrance shall be deemed adequate notice to the Commonwealth, creditors, and purchasers that a lien against the motor vehicle exists . . ." The wording does not exclude purchasers who buy from dealers. The legislature was aware that a car will probably be offered for sale in the usual course of business by a dealer who applies for a certificate of title, whether it be with or without a recorded lien.

We have good arguments for both sides of the question as to whether or not the Virginia General Assembly intended that recordation be constructive notice. It would appear, however, that on this question the arguments advanced by the dissenting opinion are perhaps more convincing than those presented by the majority of the Court. If the chattel is an automobile, it should be pointed out that a purchaser no longer has to determine whether it is bulky and conseqently subject to recordation, as was necessary under Section 5189 of the Code of 1919. If the legislature did not intend to change the law as it existed under the *Boice* doctrine, why did it provide by Section 46-106 that certificates of title would be issued to dealers in automobiles and by Section 46-71 that liens on automobiles recorded thereon would be notice to purchasers? Today sales of automobiles are made almost exclusively by and through dealers in new and used cars; the purchase of an automobile from an individual not in the business of selling cars is the exception rather than the rule. Can it be said that the General Assembly was unaware of this,

or that being aware of it intended that all references to purchases in Title 46 of the Code apply only to that small percentage of purchases from private individuals. It seems strange that the legislature was referring to and providing for the exception rather than the rule without so stating.

The *Boice* case was decided thirty-five years ago, and the relevant enactments were made six years later. From the passage of Title 46 of the Code to the *General Credit* decision there had been no case decided which was directly in point with the *Boice* case. Whether the legislature intended that recordation should constitute constructive notice or not, it is unfortunate that there has been little or no indication since the passage of the pertinent acts that the *Boice* doctrine was still law in Virginia; in fact the indications have been otherwise.

In a suit to determine priority of liens, where appellant had financed the sale of a truck at the request of a purchaser and certificate of title had been issued without notice of appellant's lien thereon, it was held that although the Division of Motor Vehicles had been notified of the lien, a subsequent creditor of the purchaser had better rights to the truck than appellant.[20] The Virginia Court said in that case:

> The statute, in our opinion, is plain and unambiguous. The key sentence in the section is this: "Said certificates of title, when issued by the division showing a lien or encumbrance, shall be deemed adequate notice to the Commonwealth, creditors and purchasers." It follows therefore, that when a certificate of title is issued which fails to show a lien or encumbrance, it is notice to the world that the property is free from any lien or encumbrance, and if transferred to a bona fide purchaser, the latter would obtain a good title. There being no lien or record as required by statute, an execution creditor stands in the same situation as a bona fide purchaser without notice.[21]

Would the fact that the lien was recorded have made any difference in the Court's opinion? It appears from the holding and decision of this case that if the lien had been recorded on the

[20] Maryland Credit Finance Co. v. Franklin Credit Finance Co., 164 Va. 579, 180 S.E. 408 (1935).
[21] *Id.* at 582, 180 S.E. 408, 409.

title, a subsequent creditor or bona fide purchaser could not have won over the lienholder. Yet the purchaser was clothed with apparent ownership. The Court was not concerned with the doctrine of estoppel since there was a specific statutory provision covering the situation.

In *Universal Credit Co.* v. *Botetourt Motor Co.*[22] the Court said:

> When applications are made within such time (ten days from acquisition of lien or sale) notice to all persons, including the Commonwealth, dates from the day on which the liens were acquired.[23]

The Court was referring to the application for certificate of title, and it is not to be implied that purchasers from persons having apparent title are exempt from the provisions of the Code. The Court says *all* persons will be on notice. Again in *Staunton Industrial Loan Corp.* v. *Wilson*[24] it was said by the Court of Appeals for the Fourth Circuit:

> In Virginia today, a man would not buy an automobile on the strength of possession, for the sole evidence of ownership of a motor vehicle is the registered title. . . . So, too, a creditor must not be misled by possession, but must look to the title certificate, and when a lien is registered thereon notice is given, be the mortgage oral or written.[25]

It would certainly not seem that such broad language refers only to the small number of purchasers who buy from private individuals not dealing in automobiles.

Despite all inferences from the cases in Virginia from 1926 to 1955, the Supreme Court of Appeals in the case under comment has held in effect that possession is title in the overwhelming majority of transactions marking the sale of automobiles. It is submitted that whether or not recordation of a lien or encumbrance should be constructive notice to purchasers is a matter to be determined by the legislature. It seems that the common

[22] 180 Va. 159, 21 S.E.2d 800 (1942).
[23] *Id.* at 174, 21 S.E.2d 800, 805.
[24] 190 F.2d 706 (4th Cir. 1951).
[25] *Id.* at 709.

notice statutes are insufficient in many jurisdictions, including Virginia, to provide that such recordation shall be constructive notice. In cases involving purchasers of automobiles from dealers such statutes do no more than provide a wide field for speculation by the courts as to the intent of the legislature. If the General Assembly intends that such recordation shall constitute notice to purchasers from dealers it must go further and state its intentions in express terms.

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