

IN THE COURT OF APPEALS OF TENNESSEE
AT NASHVILLE

FILED

October 26, 1999

Cecil Crowson, Jr.
Appellate Court Clerk

MAHMOUD ALDURIDI, HOLLY J.)
ENOCH, WILLIAM J. FALCONE,)
TONYA D. FEURY, CARMEL)
JOHNSON, MELISSA JOHNSON,)
SANNYU OBARD, NATHAN K. SMITH,)
TONYA M. SMITH, and RUTH)
WILLEY,)

Plaintiffs,)

Davidson Chancery No. 98-611-II

Appeal No. 01A01-9901-CH-00063

CARMEL JOHNSON, MELISSA)
JOHNSON, SANNYU OBARD and)
RUTH WILLEY,)

Plaintiffs/Appellants,)

vs.)

COMMUNITY TRUST BANK, N.A.,)
FIFTH THIRD BANK, HYUNDAI)
MOTOR FINANCE COMPANY, INC.,)
and NATIONSBANK OF TEXAS, N.A.,)

Defendants,)

HYUNDAI MOTOR FINANCE)
COMPANY, INC. and NATIONSBANK)
OF TEXAS, N.A.,)

Defendants/Appellees.)

APPEAL FROM THE CHANCERY COURT OF DAVIDSON COUNTY
AT NASHVILLE, TENNESSEE

THE HONORABLE CAROL McCOY, CHANCELLOR

For the Plaintiffs/Appellants: _____

For the Defendants/Appellees: _____

Kenneth J. Mitteldorf
Nashville, Tennessee

Julie C. Murphy
Nashville, Tennessee

**AFFIRMED IN PART, REVERSED
IN PART AND REMANDED**

HOLLY KIRBY LILLARD, J.

CONCURS:

W. FRANK CRAWFORD, P.J., W.S.

ALAN E. HIGHERS, J.

OPINION

This case involves consumer installment sales contracts assigned by the seller to a creditor. The plaintiff consumers filed suit against the creditor assignee who financed their consumer contracts to purchase vehicles, seeking rescission or modification of the contracts based on the wrongful conduct of the seller. The trial court allowed the plaintiffs to recover from the creditor for the seller's misconduct, based on the Federal Trade Commission's Holder Rule, but limited the plaintiffs' recovery to the amount each plaintiff had paid to the creditor. We affirm in part, reverse in part, and remand.

Most of the original plaintiffs in this lawsuit have settled their claims. The remaining plaintiffs, Sannyu Obard ("Obard") and Ruth Willey ("Willey"), have not settled their claims. In outlining the facts, we will first give an overview of facts common to all of the plaintiffs, and then detail the facts as to Plaintiffs Obard and Willey.

The Plaintiff/Appellants each bought a car from Hillman Hyundai ("Hillman"). Their consumer installment sales contracts were assigned to the Defendant/Appellee, NationsBank of Texas, N.A. ("NationsBank"). Hillman failed to perform its duties under the contracts by failing to satisfy existing liens on the cars the Plaintiffs traded in. Hillman subsequently filed bankruptcy. The Plaintiffs then filed suit, seeking to rescind or modify their contracts with Hillman's assignee, NationsBank, and recover amounts paid under the contracts.

Each consumer installment sales contract included the Federal Trade Commission's Rule Concerning Preservation of Consumers' Claims and Defenses ("the FTC Holder Rule" or "the Holder Rule"), which provides that:

Any holder of this consumer credit contract is subject to all claims and defenses which debtor could assert against the seller of goods or services obtained pursuant hereto or with the proceeds hereof. Recovery hereunder by the debtor shall not exceed amounts paid by the debtor hereunder.

16 C.F.R. § 433 (1997). The parties stipulated that the pivotal issue is the interpretation of the FTC Holder Rule under the facts presented.

The parties stipulated that Plaintiff Obard purchased a 1996 Ford Escort from Hillman on July 5, 1997. Hillman assigned the Obard consumer installment sales contract to NationsBank. As part of the transaction, Obard executed a purchase money security agreement ("the Obard contract"), traded in a 1993 Geo Metro to Hillman worth \$7700, and put down \$500 in cash. The trade-in vehicle was subject to a lien in the amount of \$4800 held by Lockheed Federal Credit Union

("Lockheed"). Obard received a credit for the Geo Metro which was traded in; this was calculated by subtracting the lien from the total value. As part of the sales contract for the Escort, Hillman was to pay off the Lockheed lien on the trade-in, the Metro. Hillman failed to pay off the lien, and Lockheed repossessed the Metro. Lockheed then sold the Metro and assessed a deficiency judgment against Obard for \$5046.54. Obard is not seeking rescission of her contract, and thus does not seek recovery of the installment payments she made to NationsBank.

The parties also stipulated to the facts of Plaintiff Willey's transaction. Willey purchased a 1996 Chevrolet Camaro from Hillman Hyundai on August 14, 1997. As part of the transaction, Willey executed a purchase money security agreement ("the Willey contract"). In the transaction, Willey traded in a 1995 Hyundai to Hillman and put down a \$500 cash down payment. The parties stipulated that the Hyundai was worth \$8500 at the time of trade in. The Hyundai was subject to a lien in favor of Bank One for \$7700. Hillman agreed to satisfy the Bank One lien, but failed to do so.

Hillman assigned the Willey contract to NationsBank. Willey paid NationsBank \$551.78 after the contract was assigned. Willey subsequently discovered that GMAC held a prior properly perfected security interest in the Camaro, created by the persons who sold the vehicle to Hillman. Hillman failed to satisfy its contractual obligation to satisfy the prior lien on the Camaro. Consequently, Willey had to surrender the Camaro to GMAC. After Hillman filed bankruptcy, Willey recovered possession of the Hyundai previously traded in to Hillman. The vehicle was damaged, however, and was worth less than \$8500. The parties did not stipulate as to the value of the damaged trade-in vehicle.

The Plaintiffs filed suit against NationsBank on March 2, 1998. Plaintiff Obard asserted that, under the FTC Holder Rule, NationsBank was liable for Hillman's breach of contract and Hillman's violations of the Tennessee Consumer Protection Act. Obard sought the amount of her unpaid lien to Lockheed in the amount of \$5046.54, the \$500 cash down payment, interest, charges and fees accrued since the deficiency judgment, and compensation for negative credit reports generated by Lockheed. Obard originally sought to rescind the contract assigned to NationsBank, but later chose not to rescind the contract.

Plaintiff Willey also contended that NationsBank was liable under the Holder Rule for Hillman's breach of contract and Hillman's violations of the Tennessee Consumer Protection Act.

Willey originally sought rescission of the contract, recovery for the monthly installments of \$551.78 paid to NationsBank, the \$8500 value of the vehicle she traded in, and the \$500 cash down payment. After Willey recovered the trade-in vehicle, she sought only the diminution in value of that vehicle. Both Plaintiffs sought reasonable attorney's fees and costs pursuant to the Tennessee Consumer Protection Act, Tenn. Code Ann. § 47-18-109.

NationsBank's answer admitted that Hillman assigned the Obard and Willey contracts to it, but denied that it was liable "for all claims and defenses which [Plaintiffs] could assert against Hillman." NationsBank raised the affirmative defense that the Plaintiffs sought relief not contemplated by the Holder Rule.

The parties then filed cross motions for summary judgment, based on the stipulated facts. The Plaintiffs asserted in their motion for summary judgment that the FTC Holder Rule entitled them to recover all consideration paid on the contracts, whether in cash or in trade, even if that amount was in excess of the amount actually received by NationsBank. NationsBank argued that its liability was limited to the amount it actually received from the Plaintiffs.

Following the hearing on the cross motions for summary judgment, the trial court found that the Plaintiffs were entitled to rescind the contracts made with Hillman and assigned to NationsBank. The trial court limited the Plaintiffs' recovery to the amount they paid to NationsBank and did not permit them to recover for payments to Hillman. Accordingly, the trial court dismissed Obard's complaint since Obard sought to recover for the \$5046.54 deficiency judgment, but did not seek rescission of the contract or recovery for amounts paid to NationsBank. The trial court concluded that the recovery sought by Willey also exceeded the recovery permitted by the Holder Rule since she sought the diminution in value of the 1995 Hyundai traded in to Hillman. The trial court limited Willey's recovery to \$551.78, the amount paid to NationsBank. The trial court denied the Plaintiffs' request for attorney's fees, reasoning that attorney's fees constituted amounts in excess of the amounts paid by the Plaintiffs to NationsBank.

Our review of this case is governed by rule 13(d) of the Tennessee Rules of Appellate Procedure, which provides that review of findings of fact by the trial court shall be *de novo* upon the

record of the trial court, accompanied by a presumption of correctness of the findings of fact, unless the evidence preponderates otherwise. *See* Tenn. R. App. P. 13(d); *Union Carbide Corp. v. Huddleston*, 854 S.W.2d 87, 91 (Tenn. 1993). The trial court's conclusions of law, however, are afforded no such presumption. *See Campbell v. Florida Steel*, 919 S.W.2d 26, 35 (Tenn. 1996).

On appeal, the Plaintiffs argue that the trial court erred in holding that the FTC Holder Rule limits recovery to the amount the Plaintiffs paid to NationsBank, resulting in the trial court's dismissal of Obard's complaint and award of only \$551.78 to Willey. The Plaintiffs also contend that the trial court erred in denying their claim for attorney's fees.

The pivotal issue in this case centers on the limits of the Federal Trade Commission's Holder Rule. This rule cuts off a creditor's rights as a holder in due course. *See Ford Motor Credit Co. v. Morgan*, 536 N.E.2d 587, 540-41 (Mass. 1989). Without the Holder Rule, a creditor to whom the consumer's contract had been assigned could assert its right to be paid, even where the seller who assigned the contract committed fraud, or breach of warranty or contract. *Id.* at 541. The Holder Rule requires that parties to certain transactions include the following notice provision in the contract:

Notice: Any holder of this consumer credit contract is subject to all claims and defenses which debtor could assert against the seller of goods or services obtained pursuant hereto or with the proceeds hereof. Recovery hereunder by the debtor shall not exceed amounts paid by the debtor hereunder.

This language becomes a part of the contract. 41 Fed. Reg. 20022, 20023 (1976). The FTC has released guidelines explaining the purpose of the Rule:

In adopting this Rule the Commission determined that it constitutes an unfair and deceptive practice . . . for a seller . . . to employ procedures which make the consumer's duty to pay independent of the seller's duty to fulfill his obligations.

* * * *

The Commission's Rule is . . . designed to prevent the widespread use of credit terms which compel consumers to pay a creditor even if the seller's conduct would not entitle the seller to be paid. It is designed to preserve the consumer's legally sufficient claims and defenses so that they may be asserted to defeat or diminish the right of a creditor to be paid, where a seller who arranges financing for a buyer fails to keep his side of the bargain.

Id. Recovery under the Holder Rule is twofold:

[A] consumer can (1) defend a creditor suit for payment of an obligation by raising a valid claim against a seller as a set-off, and (2) maintain an affirmative action against a creditor who has received payments for a return of monies paid on account. The latter alternative will only be available where a seller's breach is so substantial that a court is persuaded that rescission and restitution are justified.

40 Fed. Reg. 53506, 53524 (1975) (emphasis added).

The Guidelines explain that the debtor can recover only “a refund of monies paid under the contract,” and that the consumer “will not be entitled to receive from the creditor an affirmative recovery which exceeds the amounts of money the consumer has paid in.” 41 Fed. Reg. at 20023. In discussing the limitation on recovery, the FTC guidelines contemplate recovery where rescission is not warranted:

[I]f a seller’s conduct gives rise to damages in an amount exceeding the amounts paid under the contract, the consumer may (1) sue to liquidate the unpaid balance owed to the creditor and to recover the amounts paid under the contract and/or (2) defend in a creditor action to collect the unpaid balance. The consumer may not assert [against] the creditor any rights he might have against the seller for additional consequential damages and the like. The same situation would exist where a seller’s conduct would, as a matter of law, entitle a buyer to rescission and restitution. The consumer . . . could initiate proceedings to invalidate the credit contract and receive a return of monies paid on account. If a down payment were made under the credit contract, the consumer could recover the down payment as well as other payments.

Id. Indeed, the Guidelines discuss that “[t]he vast majority of cases, in the staff’s opinion, will involve a limited right of set-off against the unpaid balance. Most sellers do not do business in a way that creates a right to rescission . . .” *Id.* at 20024.

In this case, the trial court found that the Plaintiffs were entitled to rescind their contracts. Thus, under the Holder Rule, they can maintain an affirmative action against the creditor assignee NationsBank. However, the trial court held that recovery is limited to the amounts actually paid by the Plaintiffs to NationsBank pursuant to the contracts. Plaintiff Obard’s decision not to seek rescission does not limit her from obtaining a recovery for amounts paid under the contract.

This case turns on whether the Plaintiffs can recover for monies paid under the contracts to the seller rather than to the creditor assignee NationsBank. The Holder Rule is ambiguous on this issue. Although the Holder Rule limits recovery to “amounts paid by the debtor hereunder,” it does not expressly limit recovery to amounts paid to the creditor assignee. The trial court held that, under Tennessee law, “the Holder Rule limits the Plaintiffs’ affirmative recovery against the Creditors to the amounts paid by the Plaintiffs *to the Creditors.*” The reasoning for this holding was not included in the final order.

On appeal, NationsBank argues that, for each Plaintiff, Hillman entered into two distinct and separate transactions: (1) the agreement to pay off the lien on the trade in vehicle, and (2) the finance agreement, subsequently assigned to NationsBank. NationsBank asserts that the Plaintiffs’

claims arise from Hillman's breach of the agreements to pay off the liens rather than the purchase contract assigned to NationsBank. Consequently, NationsBank reasons that the Plaintiffs' claims against Hillman for failure to pay off the liens cannot be asserted against NationsBank. In support of this argument, NationsBank cites a portion of the FTC guidelines stating that

[i]t is possible for a consumer to have a claim or defense against a seller because of a separate transaction. The provision required by the Rule would not allow him [the consumer] to assert such a claim or defense against the holder. The holder's obligations are limited to those arising from the transaction which he finances.

41 Fed. Reg. at 20024. Thus, NationsBank argues that its obligations are limited to the purchase contract that it furnished and do not extend to Hillman's separate obligation to pay off the liens on the vehicles traded in by the Plaintiffs.

In support of its argument, NationsBank cites *LaBarre v. Credit Acceptance Corp.*, 11 F. Supp. 2d 1071 (D. Minn. 1998), *aff'd in part for proposition cited by NationsBank; rev'd in part on other grounds*, 175 F.3d 640 (8th Cir. 1999). In *LaBarre* the court held that a creditor assignee was not liable for the seller's failure to satisfy its obligation to obtain insurance on the vehicle it sold. The *LaBarre* court reasoned that, under Minnesota law, the assignment of a consumer credit contract does not impose obligations on the assignee unless the assignee specifically assumes those obligations. *See id.* at 1076. The court also relied on Minnesota law which provides that claims against assignees can be used only to extinguish or diminish an assignee's claim, and cannot be used to impose liability on the assignee unless the assignee assumes the assignor's duty. *See id.*

In response to NationsBank's argument that the Plaintiffs' purchases of the vehicles from Hillman consisted of two separate transactions, the Plaintiffs cite the FTC guidelines quoted above, which explain that the Holder Rule was adopted to prevent sellers from arranging credit terms that separate the consumer's duty to pay from the seller's duty to keep its promises. Viewing the purchase as two separate transactions, the Plaintiffs assert, would revert back to the very situation the Holder Rule was designed to remedy.

In this case, both of the Plaintiffs traded in vehicles in their purchase transactions with Hillman. In return for their trade-ins, the Plaintiffs received credits in the form of a down payment for the net value of the vehicles traded in, which was calculated by subtracting the outstanding liens from the total value of the vehicles. Hillman agreed to pay off the liens on the trade-in vehicles, after which it could dispose of the vehicles as it saw fit. It is fair to assume that the Plaintiffs would not

have given up possession of their vehicles without Hillman's promise to pay off the liens. Otherwise, the Plaintiffs would not have received full credit for the trade-in vehicles. When Hillman failed to pay the lien, the Plaintiffs had already given up their assets and were nevertheless obligated to pay the liens, but received credit from Hillman only for the net value of the trade-in vehicles. Hillman benefitted from its wrongdoing by receiving the full value of the trade-in vehicles, while crediting the Plaintiffs for only a portion of their value. Because Hillman's payment or non-payment of the liens affected the amount of down payment credit the Plaintiffs received, it was an integral part of the overall transaction. We must conclude that separating Hillman's obligation to pay off the liens from the purchase of the new vehicles would be contrary to the spirit of the Holder Rule and the reason for its adoption. For this reason, NationsBank cannot avoid liability on the purchase transaction by arguing that the Plaintiffs' claims arise from a separate transaction.

Since the Plaintiffs' contracts with Hillman did not involve two separate transactions, NationsBank stands in the shoes of Hillman, and the Plaintiffs may raise any claims or defenses against NationsBank that they could assert against Hillman. As noted above, the Plaintiffs' recoverable damages are limited to "amounts paid by the debtor" under the consumer credit contract. The parties dispute the meaning of this phrase.

The parties disagree about the holdings of two Tennessee cases titled *Patton v. McHone*, referred to as *Patton I*, 822 S.W.2d 608 (Tenn. App. 1991) and *Patton II*, No. 01A01-9207-CH-00286, 1993 WL 82405 (Tenn. App., Mar. 24, 1993). *Patton I* involved the purchase of a used car by the plaintiffs. The contract included the Holder Rule. *Patton I*, 822 S.W.2d at 618. After the sale, the plaintiffs discovered that the car had been damaged prior to purchase. The plaintiffs sued the seller. The plaintiffs also sued the creditor who financed the transaction and to whom the contract was assigned. *Id.* at 613. The trial court dismissed the plaintiffs' claims against the seller and the creditor, and awarded the creditor a deficiency judgment against the plaintiff buyers. *Id.* at 611. The plaintiff buyers appealed. The appellate court held that the seller had breached its implied warranty of merchantability. *Id.* at 617. The Court of Appeals noted that the plaintiffs could assert the same claims and defenses against the creditor's claim for payment as they could have asserted against the seller. *Id.* at 618. However, while the creditor had all of the seller's rights and liabilities, the Court noted that the plaintiffs did not have "an open-ended right to obtain affirmative relief"

against the creditor. *Id.* The Court in *Patton I* allowed the plaintiffs to recover payments made to the creditor. *Id.* at 619.

In its analysis, the Court in *Patton I* alluded to the Holder Rule, noting that inclusion of the Holder Rule in the retail installment sales contract made a particular provision of the Uniform Commercial Code (U.C.C.) inapplicable and rendered the contract non-negotiable. *Id.* at 618. However, while the Court mentioned the Holder Rule, its analysis focused on a U.C.C. provision:

Tenn. Code Ann. § 47-9-318(1) is intended only to permit an account debtor to assert against an assignee the same defensive claims it could assert against the assignor. It does not empower an account debtor to recover from the assignee because of the assignor's non-performance.

Id. (citations omitted). *Patton I* did not discuss either the impact of the Holder Rule on this analysis, or whether a consumer could recover for payments made to the seller, rather than the creditor, under the retail installment sales contract. *Patton I* merely permitted recovery for amounts paid on the contract to the creditor. *Id.* at 619. The cause was remanded to the trial court to determine the amount of the plaintiff consumers' judgment against the seller and the creditor. *Id.*

The second appeal, *Patton II*, involved the appellate court's review of the trial court's decision on remand. *Patton II*, 1993 WL 82405. On remand, the trial court granted the plaintiff consumers an award of attorney's fees against both the seller and the creditor. In *Patton II*, the appellate court reversed the award of attorney's fees against the creditor, stating:

The trial court's decision [to award attorney's fees] in the instant case places an affirmative weapon in the hands of the consumer against the assignee, when the only "weapon" contemplated by the Act, the regulations, the FTC Rules, and the UCC are non-payment through rescission and refund of the amount paid.

We think the Chancellor improperly held that [the creditor] was responsible for the wrongs of [the seller]. UCC 9-318(1) is intended solely as a shield limiting the account debtor's potential liability in a suit brought by the assignee; it cannot be used as a sword to permit an account debtor to obtain affirmative recovery from the assignee based on assignor's non-performance.

Id., at *5. Thus, while the *Patton* cases limit the consumers' rights to recovery to payments made by them under the contract, neither *Patton I* nor *Patton II* discusses recovery for payments or value given to the seller as opposed to the creditor. We must look outside Tennessee for the interpretation of the Holder Rule on this point.

On this issue, the Plaintiffs cite *Maberry v. Said*, 911 F. Supp. 1393 (D. Kan. 1995). In *Maberry*, the plaintiff consumer purchased a vehicle after the seller told him that the vehicle had low mileage. As a part of the transaction, the consumer signed a security agreement which included a

promissory note. *See id.* at 1397. The consumer traded in a vehicle as a down payment on the sale. The seller then assigned the note to the creditor. *See id.* at 1398. The consumer later discovered that the seller had misrepresented the mileage of the vehicle. The plaintiff consumer filed suit, seeking, among other remedies, a recovery from the creditor assignee of the net value of the car he traded to the seller. The creditor assignee argued that it was not liable for the value of the trade-in since it was received by the seller rather than the creditor. The *Maberry* court held that the plaintiff consumer

does not lose rights by virtue of the assignment of the note If [the seller] held the loan, the trade in would be considered payment 'hereunder.' [The plaintiff consumer] can assert any claim or defense against [the creditor assignee] that he could against [the seller]. Therefore, the FTC holder rule authorizes [the plaintiff consumer] to recover the trade in value from [the creditor assignee], which, in turn could consider what its rights might be against [the seller].

Id. at 1403. Accordingly, the court in *Maberry* allowed the plaintiff consumer to recover from the creditor assignee the value of the trade-in received by the seller.

The Plaintiffs also cite *Resolution Trust Corp. v. Cook*, 840 S.W.2d 42, 49 (Tex. App. 1992). In *Resolution Trust*, the plaintiffs obtained financing for some home improvements. The finance contract, which included the Holder Rule, was transferred from the original note holder and eventually ended up in the possession of the Resolution Trust Company, a receiver. *See id.* at 45. The plaintiffs later sued the contractor and the creditor, alleging that the home improvement work was not completed. *See id.* at 44. A money judgment was granted against Resolution Trust. On appeal, Resolution Trust argued that it did not receive any funds from the consumers and thus was not liable for a refund of payments made to previous holders of the finance contract. *See id.* at 49. The appellate court found that, under the Holder Rule,

it is of no moment that the entities held liable for the amounts paid by the [plaintiffs] never received any payments from them, for the clear and unambiguous language of the contractual provision notifies all potential holders that if they accept an assignment of the contract, they will become subject to any claims or defenses the debtor can assert against the seller.

Id. at 49. Thus, the court in *Resolution Trust* held that the assignee of the finance contract could be held liable for payments he did not receive -- those made to previous holders of the finance contract.

NationsBank argues that the Holder Rule should be interpreted to limit the liability of the creditor assignee to payments it received, not payments the consumer made to the seller assignee. In its brief, it cites several cases. *See Eachen v. Scott Housing Sys., Inc.*, 630 F. Supp. 162 (M.D.

Ala. 1986); *Home Sav. Assoc. v. Guerra*, 733 S.W.2d 134 (Tex. 1987); *Oxford Fin. Cos., Inc. v. Velez*, 807 S.W.2d 460 (Tex. App. 1991); *Briercroft Serv. Corp. v. De Los Santos*, 776 S.W.2d 198 (Tex. App. 1988). While all of the cases cited by NationsBank hold that a consumer cannot recover more than the amounts paid under the contract, none involves a factual situation in which the plaintiff consumer seeks to recover from the creditor assignee payments made to the seller of the goods. Thus, these cases do not address the key issue in this appeal.

In the event of seller misconduct in which full recovery cannot be had from the seller, the risk of loss must fall to one of two innocent parties, the consumer or the creditor assignee. The Holder Rule addresses the allocation of this risk of loss. *See* 40 Fed. Reg. at 53522 (stating that “[o]ur primary concern . . . has been the distribution or allocation of costs occasioned by seller misconduct in credit sales transactions”). The FTC Guidelines indicate an intent that the creditor, rather than the consumer, bear the risk of seller misconduct: “Sellers and creditors will be responsible for seller misconduct.” *Id.* at 53524. *See also Simpson v. Anthony Auto Sales, Inc.*, 32 F. Supp. 2d 405, 409 (W.D. La. 1998) (concluding that “[t]he FTC Holder Rule was . . . designed to reallocate the cost of seller misconduct to the creditor, who is in a better position to absorb the loss or recover the cost from the guilty party--the seller”); *Maberry*, 911 F. Supp. at 1402 (determining that “[t]he FTC holder rule reallocates the cost of seller misconduct from the consumer to the creditor”); *Guerra*, 733 S.W.2d at 135 (finding that the “FTC rule was therefore designed to reallocate the cost of seller misconduct to the creditor”).

The risk of this loss is allocated to the creditor rather than the consumer because the creditor is usually in a better position to bear the risk:

[B]ased on [a] simple public policy determination: as between an innocent consumer and a third party financier, the latter is generally in a vastly superior position (1) to return the cost to the seller, where it properly belongs, (2) to exert an influence over the behavior of the seller in the first place, and (3) to the extent the . . . [financier] cannot return the cost (as in the case of fly-by-night dealers), to

‘internalize’ the cost by spreading it among all consumers as an increase in the price of credit.

Hardeman v. Wheels, Inc., 565 N.E.2d 849, 852 (Ohio App. 1988) (quoting 2 Fonseca, Handling Consumer Credit Cases (3 Ed. 1987) 703, Section 24:1). Knowing that it bears the cost of seller misconduct, the creditor “will simply not accept the risks generated by the truly unscrupulous merchant. The market will be policed in this fashion and all parties will benefit accordingly.” Michael M. Greenfield & Nina L. Ross, *Limits on a Consumer’s Ability to Assert Claims and Defenses Under the FTC’s Holder in Due Course Rule*, 46 Bus. Law. 1135, 1137 n.11 (1991).

The Holder Rule states only that “[r]ecovery hereunder by the debtor shall not exceed amounts paid by the debtor hereunder.” This language does not limit the amounts recoverable to the amount paid by the debtor *to the creditor assignee*. The FTC Guidelines do not indicate such an intent; indeed, the Guidelines underscore that the creditor rather than the consumer should bear the risk of seller misconduct. Moreover, the Holder Rule is a remedial measure adopted for the protection of consumers, 41 Fed. Reg. at 20023, and thus should be interpreted broadly to effectuate this intent. Caselaw and commentators addressing the Holder Rule emphasize that creditors are in a better position than consumers to protect themselves against unscrupulous sellers and to bear the cost of seller misconduct.

For these reasons, we conclude that the Holder Rule does not limit the consumer’s recovery to amounts paid to the creditor assignee. The consumer may recover from the creditor assignee for payments made under the contract, regardless of whether the payments were made to the seller or to the creditor assignee. The decision of the trial court is reversed on this issue. However, the language of the Holder Rule clearly limits recovery under the provision to “amounts paid by the debtor hereunder.” Therefore, the consumer may not recover from the creditor assignee under the Holder Rule for damages in excess of amounts the consumer paid under the contract.

In this case, Plaintiff Obard seeks recovery for the deficiency judgment assessed against her because of Hillman’s failure to pay off the lien, claiming the amount as a payment made under the contract. The effect of Hillman’s failure to pay off the lien was that Obard gave Hillman a vehicle worth \$7700 and received a credit as a down payment for \$2900. Therefore, Obard was out \$4800, the amount of the lien. This was value given to Hillman pursuant to the contract for which Obard received nothing in return. Obard may recover this amount from NationsBank under the Holder

Rule. Obard seeks another \$246.54 in costs assessed against her in the deficiency judgment. Obard did not pay these costs under a provision of the contract, but instead was assessed the costs because of Hillman's failure to pay off the lien. Obard cannot recover this amount since it was not a payment made under the contract. "A rule of unlimited liability would place the creditor in the position of an absolute insurer or guarantor of the seller's performance. We do not construe this to be the purpose of the FTC rule." *Guerra*, 733 S.W.2d at 136. In addition, Obard paid \$500 in cash as part of the down payment on the vehicle she purchased. Ordinarily, Obard would be entitled to recover this amount from NationsBank as an amount paid under the contract. However, because Obard chose not to rescind the contract, she cannot recover the \$500 cash downpayment on the contract. Obard further seeks compensation for damage to her credit report because of the deficiency judgment. These damages, however, are not payments made under the contract, and Obard, therefore, cannot recover them under the Holder Rule. In sum, Plaintiff Obard's recovery is limited to \$4800, the amount of the lien.

Willey seeks recovery for the diminution in value of the vehicle which was traded in to Hillman and later recovered in a damaged condition. At trade-in, the vehicle was worth \$8500, and was subject to a lien in the amount of \$7700. Although the value of the damaged trade-in vehicle was not stipulated, the parties do not dispute that it was worth less than \$8500 after Willey recovered it. The trial court did not determine the dollar amount of the vehicle's diminished value.

The effect of Hillman's failure to pay off the lien, and Willey's subsequent retrieval of the vehicle in a damaged condition, was that Willey did not recover the full value of her payments under the contract. Willey gave Hillman a vehicle worth \$8500 and received a down payment credit of \$800. Hillman failed to pay off the lien on the trade-in vehicle, as it had agreed. Although Willey was later able to retrieve the car from Hillman's bankruptcy estate, it was in a damaged condition, and worth less than it was at the time she traded it in. The value of the trade-in was value given to Hillman, and constitutes amounts paid under the contract. Under the Holder Rule, Willey may recover from NationsBank the diminution in value of the trade-in vehicle. Willey also paid \$500 in cash to Hillman as a down payment. Willey is entitled to recover this amount from NationsBank as an amount paid under the contract. Willey also seeks recovery for payments of \$551.78 to NationsBank. Willey's right to recover the payments made to NationsBank was not disputed. Thus, Willey can recover \$551.78 from NationsBank for payments made directly to NationsBank. In sum,

under the Holder Rule, Willey may recover from NationsBank the \$500 down payment made to Hillman, payments to NationsBank in the amount of \$551.78, and the diminution in value of the trade-in vehicle. Accordingly, we remand this case back to the trial court to determine the diminution in value of the trade-in vehicle and to calculate the total recovery.

The Plaintiffs also assert that the trial court erred in denying their request for attorney's fees. The Plaintiffs maintain that Hillman violated the Tennessee Consumer Protection Act, under which reasonable attorney's fees and costs may be awarded. The Plaintiffs argue that they should be permitted to assert against NationsBank any claims that they could assert against Hillman, and thus that they are entitled to recover from NationsBank for their attorney's fees. The Plaintiffs also argue that the limitation in the Holder Rule to recovery for "amounts paid by the debtor hereunder" does not apply to bar recovery for attorney's fees, despite the fact that the attorney's fees exceed the amount the Plaintiffs paid under the contract. *See Guerra*, 733 S.W.2d at 137 (allowing consumers to recover attorney's fees in excess of the amount they paid under the contract). In support of their argument, the Plaintiffs cite a consumer law commentator:

The creditor's liability for the consumer's attorney fees should not be capped by the creditor's maximum liability for seller-related claims. The purpose of attorney fees are to encourage settlement, make it economically feasible for consumers to bring small claims, and to discourage sellers and creditors from using their superior legal resources to wear down the consumer. All of these purposes would be thwarted if attorney's fees were lumped in with the recovery on the merits and capped at the amount of the creditor's maximum liability.

In addition, the attorney fees are not being awarded because of the seller's conduct, but because of the creditor's conduct. It is the creditor who is refusing to settle the claim and who insists on litigating the issues.

National Consumer Law Center, *Unfair and Deceptive Acts and Practices*, § 6.6.3.4 (4th ed. 1997).

NationsBank argues that the FTC Holder Rule limits recovery of attorney's fees to amounts paid under the contract. The FTC Holder Rule limits a plaintiff's recovery to the amounts paid under the contract, but does not limit a plaintiff's recovery against a creditor based on independent state law grounds. "The words 'recovery hereunder' which appear in the text of the Notice refer specifically to a recovery under the Notice. If a larger affirmative recovery is available against a creditor as a matter of state law, the consumer would retain this right." 41 Fed. Reg. at 20023; *see also Guerra*, 733 S.W.2d at 136. Thus, a plaintiff's statutory or common law claim against the creditor for attorney's fees is not subject to the limitation of the FTC Holder Rule. Recovery under the Holder Rule, however, is limited to amounts paid by the consumer under the contract. Recovery

for amounts in excess of this, such as a claim for attorney's fees not paid under the contract, must be based on an independent statutory or common law ground. Therefore, where the plaintiff's claim for attorney's fees is based on the seller's misconduct, recovery under the Holder Rule is limited to the amounts paid under the contract. *See Riggs v. Anthony Auto Sales, Inc.*, 32 F. Supp. 2d 411, 417 (W.D. La. 1998); *Simpson*, 32 F. Supp. 2d at 410 (both cases holding that "a creditor's derivative liability for seller misconduct under the FTC rule is limited to the amount paid by the consumer under the credit contract").

In this case, both Plaintiffs premise their claim against NationsBank for attorney's fees on NationsBank's status as a holder of the credit contracts and Hillman's alleged violations of the Tennessee Consumer Protection Act. Thus, the claim for attorney's fees against NationsBank is based in part on the Holder Rule, and not entirely on an independent statutory or common law ground. Accordingly, Plaintiffs Obard and Willey cannot recover attorney's fees from NationsBank. The trial court's denial of attorney's fees to the Plaintiffs is affirmed.

In sum, under the FTC Holder Rule, the Plaintiffs may recover the full amount paid under their contracts, regardless of whether the value was given to the seller, Hillman, or to the creditor assignee, NationsBank. Their recovery cannot exceed the amounts paid under the contract. Plaintiff Obard's recovery is limited to the amount of the unpaid lien, or \$4800, which was value given to Hillman under the contract. Obard is not entitled to recover the \$246.54 in costs assessed against her in the deficiency judgment because of Hillman's failure to pay off the lien, as this money was not paid under the contract. Plaintiff Willey's recovery is limited to the \$500 cash down payment, the \$551.78 in installment payments to NationsBank, and the diminution in value of the vehicle she traded in. The cause is remanded to the trial court to determine the diminution in value of the trade-in vehicle and Willey's total recovery. The Plaintiffs' claim for attorney's fees against NationsBank is based in part on the Holder Rule. In this case, the attorney's fees are not an amount "paid by the debtor hereunder" and thus are not recoverable under the Holder Rule. The trial court's denial of the Plaintiffs' claim for attorney's fees is affirmed.

The decision of the trial court is affirmed in part, reversed in part, and remanded for further proceedings consistent with this Opinion. Costs are assessed equally against the Appellee and the Appellants, for which execution may issue if necessary.

HOLLY KIRBY LILLARD, J.

CONCUR:

W. FRANK CRAWFORD, P. J., W.S.

ALAN E. HIGHERS, J.