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An Uneasy Relationship Between the Bankruptcy Reform Act and the Uniform Commercial Code: Delayed and Continued Perfection of Security Interests

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AN UNEASY RELATIONSHIP BETWEEN THE BANKRUPTCY REFORM ACT AND THE UNIFORM COMMERCIAL CODE: DELAYED AND CONTINUED PERFECTION OF SECURITY INTERESTS

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I. INTRODUCTION

The widespread adoption of article 9 of the Uniform Commercial Code¹ in the 1950s and 1960s resulted in an “uncertain correlation”² between state personal property security law and the Bankruptcy Act of 1898.³ Although the Bankruptcy Act of 1898 frequently relied upon existing state law to determine the validity of a secured creditor’s interest in the personal property of a bankrupt debtor, its provisions were more compatible with pre-Code personal property security law.⁴ As a result, courts often struggled to reconcile the meanings of the two statutes.⁵

The enactment of the Bankruptcy Reform Act of 1978⁶ held out the promise of greater correspondence between the concepts of bank-

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1. Uniform Comm. Code §§ 1-101 to 11-108 [hereinafter cited as U.C.C.]. All references are to the 1972 Official Text of the U.C.C. unless otherwise noted.

2. 2 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY 1283 (1965).

3. Act of July 1, 1898, ch. 541, 30 Stat. 544, *repealed by* Act of Nov. 6, 1978, Pub. L. No. 95-598, § 401(a), 92 Stat. 2549 [hereinafter cited as Bankruptcy Act].

4. See Professor Gilmore’s exploration of the relationship between the delayed perfection of transfers permitted by § 60a(7) of the Bankruptcy Act and the concept of notice filing adopted by the drafters of article 9. 2 G. GILMORE, *supra* note 2, at 1325-35.

5. See, e.g., *DuBay v. Williams*, 417 F.2d 1277 (9th Cir. 1969).

6. Act of Nov. 6, 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. § 101-151326 (1982), *as amended by* Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333).

ruptcy law and those of article 9. The Commission on the Bankruptcy Laws of the United States, established in 1970 to study the Bankruptcy Act of 1898,⁷ relied heavily on the work of practitioners and scholars familiar with article 9.⁸ The statutory revision proposed by the Commission in 1973 embodied many recommendations made by these practitioners and scholars,⁹ and served as an important foundation for the Bankruptcy Reform Act.¹⁰

Although the Bankruptcy Reform Act employs concepts drawn from article 9,¹¹ some incongruities between the two statutes remain. For example, under the provisions of article 9, a secured party may, in certain circumstances, delay perfection of a security interest without sacrificing priority to other parties whose claims to the secured collateral arise before the security interest is perfected. If perfection is about to expire or lapse, article 9 requires the secured party to continue the perfection of the security interest in order to retain priority over others who may claim an interest in the collateral. The Bankruptcy Reform Act of 1978 also makes delayed perfection of security interests in personal property effective against the trustee in bankruptcy, but the Reform Act authorizes delayed perfection in cases in which article 9 does not. In addition, the Reform Act does not expressly sanction continuation of perfection after bankruptcy proceedings have been instituted.

This article explores some of the uncertainties in the relationship between the Bankruptcy Reform Act and article 9. It first describes and evaluates the article 9 provisions dealing with delayed and continued perfection. Against this background, the article examines the relationship of delayed and continued perfection, under both the Reform Act and article 9, to the bankruptcy trustee's avoiding powers. Finally, some suggestions for legislative changes in the Reform Act are offered.

II. DELAYED AND CONTINUED PERFECTION UNDER ARTICLE 9

Article 9 of the Uniform Commercial Code establishes three methods of perfecting security interests: by filing a financing state-

7. Act of July 24, 1970, Pub. L. No. 91-354, 84 Stat. 468.

8. REPORT OF THE COMM'N ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 137, 93d Cong., 1st Sess. pt. I, at 1-301; pt. II, at 1-300 (1973).

9. *Id.* pt. II.

10. A detailed legislative history of the Bankruptcy Reform Act of 1978 appears in Klee, *Legislative History of the New Bankruptcy Code*, 54 AM. BANKR. L.J. 275 (1980). The legislative documents are reproduced in A. RESNICK & E. WYPYSKI, *BANKRUPTCY REFORM ACT OF 1978: A LEGISLATIVE HISTORY* (1979).

11. See, for example, the definitions of inventory in 11 U.S.C. § 547(a)(1) (1982) and U.C.C. § 9-109(4).

ment,¹² by taking possession of the collateral,¹³ and through automatic perfection (without either filing or possession).¹⁴ Of these, filing is the most commonly employed means of perfection. It also presents the greatest number of delayed and continued perfection issues.

A. Delayed Perfection

Many pre-article 9 statutes regulating security interests in personal property required the creditor to file the actual security agreement between the parties, or a copy thereof, in order to protect his interest from others who might claim the debtor's property.¹⁵ Because these "transaction filing" statutes mandated filing the agreement creating the security interest, the creditor could not protect his interest until the security transaction had been completed. Consequently, the statutes often contained a grace period, running from the time at which the parties entered into the agreement, during which the creditor could file and obtain protection against third parties whose claims to the collateral arose while the security agreement was "off record."¹⁶

In contrast to pre-Code transaction filing statutes, article 9 utilizes a "notice filing" system.¹⁷ It permits filing a simple notice of a security interest, the financing statement,¹⁸ and does not require that the security agreement¹⁹ be placed on the public record.²⁰ Thus, the parties to a secured transaction may complete a financing statement and file it "before a security agreement is made or a security interest otherwise attaches."²¹ For this reason, article 9, unlike transaction

12. U.C.C. § 9-302(1). The mechanics of filing are governed by U.C.C. §§ 9-401 to -408.

13. *Id.* § 9-305.

14. *E.g.*, *id.* § 9-302(1)(d).

15. *E.g.*, UNIF. COND. SALES ACT §§ 5, 10, 2 U.L.A. (act superseded by U.C.C.). For an expansive discussion of the filing systems employed by pre-article 9 statutes regulating personal property security interests, see 1 G. GILMORE, *supra* note 2, at 463-98, 579-631.

16. *E.g.*, UNIF. COND. SALES ACT § 5, U.L.A. (act superseded by U.C.C.) (contract must be "filed within ten days after the making of the conditional sale").

17. U.C.C. § 9-402, comment 2. The notice filing system of article 9 is derived from the filing system of the Uniform Trust Receipts Act. UNIF. TRUST RECEIPTS ACT § 13, 9C U.L.A. 220 (1957) (act superseded by U.C.C.).

18. U.C.C. § 9-402(1). An example of a financing statement is set out in U.C.C. § 9-402(3).

19. *Id.* §§ 9-105(1)(l), -203(1)(a).

20. A copy of the security agreement may be filed, however, if it contains the information required for a financing statement. *Id.* § 9-402(1).

21. *Id.* Article 9 also expressly provides that a financing statement filed before the parties to a security transaction enter into a security agreement will perfect the security interest when the agreement is completed and the security interest otherwise attaches. *Id.* § 9-303(1). A security agreement "attaches" when the parties have entered into an enforceable security agreement, value has been given by the secured party, and the debtor has rights in the secured collateral. *Id.* § 9-203(1).

filing statutes, does not generally provide for filing grace periods.²² Despite this lack of necessity for grace periods, however, article 9 does permit delayed filing to be effective against intervening third party claims to collateral in some instances.

The most important delayed filing provision in article 9 is section 9-301(2) which states:

If the secured party files with respect to a purchase money security interest before or within ten days after the debtor receives possession of the collateral, he takes priority over the rights of a transferee in bulk or of a lien creditor which arise between the time the security interest attaches and the time of filing.

The scope of the section is quite limited. Only a secured party who has a purchase money security interest can take advantage of the ten day grace period for filing.²³ Section 9-107 defines a purchase money security interest as a security interest:

(a) [T]aken or retained by the seller of the collateral to secure all or part of its price; or (b) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.

Filing within ten days after the debtor receives possession of the collateral gives the secured party priority only over an intervening transferee in bulk or lien creditor.²⁴ If another secured creditor perfects his security interest before the purchase money secured party files, his claim may take priority over the purchase money security interest.²⁵

It is important to note that the secured party's protection against transferees in bulk and lien creditors may last for more than ten days in some cases. Section 9-301(2) requires that the purchase money se-

22. 1 G. GILMORE, *supra* note 2, at 496-98.

23. The section allows a grace period only in cases in which perfection of the security interest is accomplished by filing. *See also* U.C.C. § 9-305: "A security interest is perfected by possession from the time possession is taken without relation back and continues only so long as possession is retained."

24. A "lien creditor" means a creditor who has acquired a lien on the property involved by attachment, levy or the like and includes an assignee for benefit of creditors from the time of assignment, and a trustee in bankruptcy from the date of the filing of the petition or a receiver in equity from the time of appointment.

Id. § 9-301(3).

25. *Id.* § 9-312(5)(a). *But see infra* notes 32-37 and accompanying text.

cured party file before or within ten days after the debtor takes *possession* of the collateral. After filing, however, the secured party takes priority over transferees in bulk and lien creditors whose claims to the collateral arise between the time that the security interest *attaches* and the time of filing. A security interest can attach when the debtor has rights in the secured collateral,²⁶ even if the debtor has not received possession of the collateral.²⁷ In cases in which the debtor has rights in the collateral before receiving possession of it, the secured party will be protected against the intervening claims of bulk transferees and lien creditors for more than ten days after attachment, so long as he files within ten days after the debtor takes possession.

Although section 9-301(2) is limited in scope, it is not clear that the provision is warranted. The drafters of article 9 believed that advance filing of financing statements would be difficult, if not impossible, in typical purchase money security transactions.²⁸ The typical situation where a buyer "walks in off the street" and enters into a security transaction, however, involves the seller or perhaps a lender retaining a purchase money security interest in consumer goods. There is no need for a filing grace period in this situation because a purchase money security interest in consumer goods is automatically perfected without filing or possession.²⁹ If more substantial collateral is involved, the parties are likely to negotiate the details of their financing arrangement and, during these discussions, complete and file a financing statement.³⁰ Thus, a filing grace period is unnecessary because the secured party easily could file before extending credit or

26. U.C.C. § 9-203(1)(c).

27. If the debtor is buying goods that are to be the secured collateral, the debtor obtains a special property in them when they are identified to the contract for sale, even though the goods have not been delivered to the debtor. *Id.* § 2-501(1). *See also* J. WHITE & R. SUMMERS, UNIFORM COMMERCIAL CODE 917 (2d ed. 1980).

28. 1 G. GILMORE, *supra* note 2, at 498.

29. U.C.C. § 9-302(1)(d).

30. In occasional cases in which perfection of a security interest is governed by a statute other than article 9, it may be necessary to complete a security transaction before the security interest can be perfected. *E.g.*, FLA. STAT. § 319.27(2) (Supp. 1982) (to be noted on a motor vehicle certificate of title, the notice of a lien must show, among other things, the date of the lien and the make, type, and vehicle identification number of the motor vehicle).

It also is possible that practical problems, other than that of being unable to negotiate a security transaction in advance, may make early filing of a financing statement difficult for secured parties. For example, it may not be possible to describe the secured collateral adequately until negotiations are complete. *See* U.C.C. § 9-110, -402(1). Moreover, there may be delays associated with the delivery of the financing statement to the filing officer, particularly in jurisdictions that have established a central, statewide filing system. *Id.* § 9-401(1) (first alternative subsection (1)). Neither of these difficulties is unique to purchase money security interests, however, and the solution to both is clear: do not advance funds to the debtor until the financing statement is completed and filed.

making a loan to the debtor. Nevertheless, the drafters concluded that, in the event of a priority conflict with an intervening lien creditor or a bulk transferee, all purchase money secured parties should receive the benefit of a filing grace period.³¹

A second delayed filing provision, section 9-312(4), establishes a ten day grace period for purchase money security interests in collateral other than inventory.³² As in section 9-301(2), the grace period is available only to holders of purchase money security interests³³ and runs from the time that the debtor receives possession of the collateral.³⁴ Section 9-312(4) provides only that the security interest must be "perfected," rather than "filed,"³⁵ but the interest usually will be perfected by filing.³⁶ Unlike section 9-301(2), section 9-312(4) gives the purchase money secured party priority only over other secured parties who claim an interest in the same collateral. When the sections are read together, however, it is clear that one with a purchase money security interest in collateral other than inventory can obtain priority over the competing claims of lien creditors, transferees in bulk, and other secured parties by filing within ten days after the debtor receives possession of the collateral. While those with purchase money security interests in inventory cannot take advantage of the filing grace period of section 9-312(4) to defeat conflicting security interests in the same collateral, they can take priority over

31. It may be worth noting that purchase money security interests received favorable priority treatment under some pre-article 9 statutes and cases dealing with personal property security interests. 2 G. GILMORE, *supra* note 2, at 743-58; J. WHITE & R. SUMMERS, *supra* note 27, at 1043.

32. Section 9-312(4) provides: "A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral or its proceeds if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter."

A third filing grace period appears in U.C.C. § 9-313(4)(a). Under that provision, a secured party who has a purchase money security interest in goods that become fixtures and files before the goods become fixtures or within ten days thereafter, takes priority over the interest of an encumbrancer or owner of the real estate whose interest arises before the goods become fixtures.

33. *Id.* § 9-107.

34. A security interest may attach before the debtor receives possession of the collateral. *See supra* notes 26-27 and accompanying text.

35. *See* U.C.C. § 9-301(2) (filing requirement for priority). *See also infra* note 37 and accompanying text.

36. Perfection by possession is effective only from the time that the secured party takes possession of the collateral and it does not relate back to an earlier time. *Id.* § 9-305. Security interests that are automatically perfected when they attach, *e.g.*, *id.* § 9-302(1)(d) (purchase money security interests in consumer goods), fall within the scope of section 9-312(4). The favorable priority treatment that the section gives to purchase money secured parties normally is not important when these interests are involved, however. *See* 2 G. GILMORE, *supra* note 2, at 798-800.

lien creditors and transferees in bulk under section 9-301(2).³⁷

Criticism of the filing grace period of section 9-312(4) in the context of a notice filing system is much the same as that of the grace period established by section 9-301(2).³⁸ Delayed filing is unnecessary when the purchase money security interest is automatically perfected upon attachment.³⁹ In addition, no filing grace period is needed by a secured party who negotiates a financing arrangement with the debtor, because the parties can complete and file a financing statement before the secured party extends credit. The drafters of article 9 believed, however, that the business practice of filing a financing statement after delivery of secured collateral (other than inventory) to the debtor supported the inclusion of a filing grace period in section 9-312(4).⁴⁰

B. Continued Perfection

Continued perfection issues arise in cases in which the perfection of a security interest must be extended beyond the time when the original act of perfection ceases to be effective. A secured party may find it necessary to continue perfection of his security interest in a number of situations: a filed financing statement may lapse;⁴¹ a period of temporary perfection may expire;⁴² the debtor or the collateral may move to another jurisdiction;⁴³ the debtor may change its

37. U.C.C. § 9-301(2). The priority of a purchase money security interest in inventory over conflicting security interests in the same collateral is governed by U.C.C. § 9-312(3), which does not contain a filing grace period. The drafters of article 9 believed that the methods of financing inventory were sufficiently different from those employed for other types of collateral to warrant the imposition of different perfection and notification requirements in cases involving purchase money security interests in inventory. *Id.* § 9-312(3), comment 3.

38. See *supra* notes 28-31 and accompanying text.

39. *E.g.*, U.C.C. § 9-302(1)(d).

40. 2 G. GILMORE, *supra* note 2, at 799-800.

41. "[A] filed financing statement is effective for a period of five years from the date of filing. The effectiveness of a filed financing statement lapses on the expiration of the five year period unless a continuation statement is filed prior to the lapse." U.C.C. § 9-403(2).

42. To the extent that a security interest in instruments or negotiable documents arises for new value under a written security agreement, it is perfected automatically for a period of 21 days from the time it attaches. *Id.* § 9-304(4). A security interest in instruments, negotiable documents, or goods in the possession of a bailee other than one who has issued a negotiable document remains perfected for a period of 21 days when a secured party with a perfected security interest makes the instruments, documents, or goods available to the debtor for certain, specified purposes. *Id.* § 9-304(5). In either event, however, the secured party must take additional steps before the expiration of the 21 day period to continue the perfection of the security interest. *Id.* § 9-304(6).

A security interest in noncash proceeds not covered by a filed financing statement meeting the requirements of U.C.C. § 9-306(3)(a) becomes unperfected 10 days after the debtor receives the proceeds unless "the security interest in the proceeds is perfected before the expiration of the ten day period." *Id.* § 9-306(3)(c).

43. Perfected security interests in documents, instruments, ordinary goods, and posses-

name, identity, or corporate structure;⁴⁴ or the secured party may decide to release to the debtor collateral in which a security interest has been perfected by possession.⁴⁵

If the secured party meets the requirements for continuing the perfection of a security interest before the original period of perfection expires, the security interest is deemed to be perfected continuously.⁴⁶ Moreover, the secured party's priority over other interests in the same collateral dates from the time of the original perfection.⁴⁷ If continuation is not accomplished before the original perfection ceases to be effective, however, questions may arise concerning the priority of the security interest over other claims to the collateral that arose prior to the lapse in perfection.

Several article 9 provisions specify the consequences of failure to reperfect a security interest before the original act of perfection ceases to be effective. Under section 9-403, a filed financing statement lapses five years after the original filing, and the security interest becomes unperfected unless a continuation statement is filed within six months prior to the expiration of the five year period. A security interest that becomes unperfected upon lapse "is deemed to have been unperfected as against a person who became a purchaser or lien creditor before lapse."⁴⁸ Although a security interest may have been senior to the claim of another secured creditor⁴⁹ or a lien credi-

sory interests in chattel paper become unperfected four months after the collateral is moved to another jurisdiction unless the secured party perfects the security interest in the new jurisdiction within the four month period. *Id.* § 9-103(1)(d), (4). Perfected security interests in accounts, general intangibles, mobile goods, and nonpossessory interests in chattel paper become unperfected four months after the debtor moves to another jurisdiction unless the secured party perfects the security interest in the new jurisdiction within the four month period. *Id.* § 9-103(3)(e), (4). Analogous, albeit more complex, requirements govern the reperfecting of security interests in goods covered by a certificate of title when the goods are moved to another jurisdiction. *Id.* § 9-103(2).

44. Where a debtor so changes its name, identity, or corporate structure that a filed statement "becomes seriously misleading, the filing is not effective to perfect a security interest in collateral acquired by the debtor more than four months after the change, unless a new appropriate financing statement is filed before the expiration of that time." *Id.* § 9-402(7).

45. A security interest that is perfected by the secured party's taking possession of the collateral "may be otherwise perfected . . . before or after the period of possession by the secured party." *Id.* 9-305.

46. U.C.C. § 9-303(2) reads in full:

(2) If a security interest is originally perfected in any way permitted under this Article and is subsequently perfected in some other way under this Article, without an intermediate period when it was unperfected, the security interest shall be deemed to be perfected continuously for the purposes of this Article.

47. *Id.* § 9-201, -301(1)(b) (priority conflicts with lien creditors); *id.* § 9-312(5) (priority conflicts with other secured creditors).

48. *Id.* § 9-403(2).

49. A "purchaser" is a person who takes by purchase. U.C.C. § 1-201(33). "A 'purchase'

tor⁵⁰ whose interest arose during the time the original filed financing statement was effective, it becomes junior to the other interest if the secured party fails to file a continuation statement within the required period.⁵¹ Furthermore, even if the secured party files a financing statement after the original financing statement lapses, his interest will be junior to the claims of the other parties whose interests arose in the interim, between the lapse and the filing.⁵²

Section 9-103 contains analogous rules. When collateral is subject to a perfected security interest in one jurisdiction and the collateral or the debtor moves to another jurisdiction, the secured party normally must reperfect the security interest in the new jurisdiction within four months.⁵³ If the secured party fails to reperfect within the four month period, "the security interest becomes unperfected at the end of that period and is thereafter deemed to have been unperfected as against a person who became a purchaser after removal."⁵⁴ As in section 9-403(2), a security interest that may have been senior to the interest of a purchaser of the collateral while it was originally perfected is subordinated to the purchaser's interest if the secured party fails to reperfect before the original act of perfection ceases to be effective in the new jurisdiction. Unlike section 9-403(2), however, section 9-103 allows only a purchaser, and not a lien creditor to take priority over the security interest.⁵⁵

Other article 9 sections make it clear that the secured party must continue the perfection of his security interest before its original perfection expires,⁵⁶ but they do not specify the effect of a failure to

includes taking by sale, discount, negotiation, mortgage, pledge, lien, issue or reissue, gift or any other voluntary transaction creating an interest in property." *Id.* § 1-201(32).

50. A 'lien creditor' means a creditor who has acquired a lien on the property involved by attachment, levy or the like and includes an assignee for benefit of creditors from the time of assignment, and a trustee in bankruptcy from the date of the filing of the petition or a receiver in equity from the time of appointment.

Id. § 4-302(3).

51. *Id.* § 9-403, comment 3. See also *In re Super Treads*, 7 Bankr. 532 (Bankr. M.D. Ga. 1980); *Eastern Indus. Prod. Credit Ass'n v. Farmers State Bank*, 31 Ohio App. 2d 252, 287 N.E.2d 824 (1972); *Stearns Mfg. Co. v. National Bank & Trust Co.*, 86 York Legal Record 89 (Pa. C. 1972); *Morse Electro Prod. Corp. v. Beneficial Indus. Loan Co.*, 90 Wash. 2d 195, 579 P.2d 1341 (1978).

Professor Gilmore is critical of U.C.C. § 9-403(2), noting that the subordination of a security interest upon lapse to a junior interest is inconsistent with the general trend of pre-article 9 secured transactions law. 1 G. GILMORE, *supra* note 2, at 588-92.

52. U.C.C. § 9-301(1)(b), 9-312(5); see also 1 G. GILMORE, *supra* note 2, at 592-94.

53. U.C.C. § 9-103(1)(d), (3).

54. *Id.* § 9-103(1)(d)(i). See also *id.* § 9-103(3)(e).

55. See Review Comm. for art. 9 of the U.C.C., Perm. Ed. Bd. for the U.C.C., Final Report at 245 (1971).

56. U.C.C. § 9-304(6), -305, -306(3)(c).

do so. For example, if a secured party has a perfected security interest in collateral,⁵⁷ the security interest normally continues in identifiable proceeds received by the debtor upon disposition of the collateral,⁵⁸ and the security interest in the proceeds is continuously perfected.⁵⁹ This continuous perfection expires ten days after the debtor receives the proceeds unless the financing statement covering the original collateral satisfies the requirements of section 9-306(3)(a)⁶⁰ or the proceeds are identifiable cash proceeds.⁶¹ To extend the perfection beyond ten days, the secured party must perfect his security interest directly in the proceeds.⁶²

Section 9-306 leaves unanswered the question of whether the claim of a lien creditor or another secured party that arose while the security interest was perfected takes priority if the security interest is not reperfected within the ten day period. There are, of course, two potential answers to this question. First, the secured party, whose interest was senior to that of the competing claimant while the security interest was perfected, becomes junior to the competing claimant when the period of temporary perfection expires. Alternatively, the security interest retains its priority, established while it was perfected, over the competing interest.

The first solution provides a result similar to the rule in section 9-403(2) governing the priority of lapsed financing statements,⁶³ and would establish general uniformity in the article 9 rules dealing with lapse of perfection.⁶⁴ Moreover, if the competing claimant is another secured party with a perfected security interest, the priority rules of article 9 provide indirect support for this solution. Section 9-

57. Although the discussion in the text focuses on the continuation of a perfected security interest in proceeds, the analysis and solutions suggested also are applicable to the continuation of nonfiled perfected security interests governed by U.C.C. §§ 9-304(6) and 9-305.

58. *Id.* § 9-306(2).

59. *Id.* § 9-306(3).

60. Specifically, the filed financing statement must cover:

[T]he original collateral and the proceeds are collateral in which a security interest may be perfected by filing in the office or offices where the financing statement has been filed and, if the proceeds are acquired with cash proceeds, the description of collateral in the financing statement indicates the types of property constituting the proceeds.

Id. § 9-306(3)(a).

61. *Id.* § 9-306(3)(b).

62. *Id.* § 9-306(3)(c).

63. *Supra* notes 48-52 and accompanying text. Because U.C.C. § 9-403(2) deals with the lapse of filed financing statements, it is not applicable to cases in which a security interest is perfected by some means other than filing.

64. Adoption of this solution would not establish complete uniformity because U.C.C. § 9-103(1)(b) and (3)(e) provide that only the conflicting interest of a purchaser, and not that of a lien creditor, takes priority over a security interest whose perfection lapses after the collateral or the debtor moves to another jurisdiction. *See supra* note 55 and accompanying text.

312(5)(a) states that conflicting security interests in the same collateral "rank according to priority in time of filing or perfection." The section further provides that priority dates from the time of filing or perfection "provided that there is no period thereafter when there is neither filing nor perfection." By negative implication, when a secured party allows his perfection to lapse or expire, priority dates only from the time of any later reperfecting. A conflicting security interest perfected prior to the lapse or expiration of an earlier interest would continue to date its perfection from the time of its original filing or perfection and would take priority even if the earlier interest were later reperfected.⁶⁵

The second solution corresponds to the position taken by pre-article 9 personal property security law.⁶⁶ It would lend support to the article 9 policy of subordinating the interests of competing claimants to that of a secured party who has previously perfected his security interest.⁶⁷ This policy is based on the notion that a claimant who takes an interest in collateral with notice of a previously perfected security interest, or without having checked to determine whether such an interest exists, assumes the risk of subordination. Because a system of perfection is intended to give notice to those who might deal with a debtor's collateral, as well as encourage them to seek out the information, adverse parties who obtain, or could have obtained, notice should be bound by it. While the failure to continue the perfection of a security interest before it expires may result in denial of priority for that interest over a claim that arises after lapse, it does not diminish the notice given to others before the period of perfection lapsed.⁶⁸

The holdings of the few courts that have faced this issue are divided,⁶⁹ and provide no clear judicial rule concerning whether a se-

65. It is important to note, however, that there is no parallel rule governing priority conflicts between secured parties and lien creditors containing this same implication. Thus, the language of article 9 does not fully support the first solution.

66. 1 G. GILMORE, *supra* note 2, at 581-84, 589.

67. U.C.C. §§ 9-201, 9-301(1)(b) (subordination of a lien creditor to a perfected security interest); *id.* § 9-312(5) (earlier perfected security interest takes priority over later perfected interest).

68. 1 G. GILMORE, *supra* note 2, at 588-94.

69. *Security Sav. Bank v. United States*, 440 F. Supp. 444 (S.D. Iowa 1977) (perfection lapsed when secured party failed to perfect its interest in proceeds within 10 days after their receipt by debtor, and lien creditor who levied during 10 day period took priority over secured party); *Barnett Bank v. Applegate*, 379 So. 2d 1284 (Fla. 1st D.C.A. 1978) (perfection of security interest lapsed upon failure of secured party to perfect its interest in proceeds within 10 days of their receipt by debtor, and previously junior security interest in collateral became senior to secured party); *Blair Milling & Elevator Co. v. Wehrkamp*, 217 Kan. 122, 535 P.2d 457 (1975) (secured party who failed to perfect its security interest in proceeds within 10 days after their receipt by debtor took priority over lien creditor who levied on proceeds during 10 day

curity interest is subordinated to previously junior claimants when the perfection of the security interest lapses and the interest is not reperfected within the ten day period. This lack of certainty in both article 9 and case law may raise troublesome problems for secured parties whose debtors become bankrupts.

III. DELAYED AND CONTINUED PERFECTION UNDER THE BANKRUPTCY REFORM ACT OF 1978

As in article 9, a number of the provisions of the Bankruptcy Reform Act of 1978 permit delayed perfection of personal property security interests. Moreover, it may be particularly important for a secured party to continue the perfection of his security interest, even after the debtor goes bankrupt. The remainder of this article evaluates the sections of the Bankruptcy Reform Act that deal with delayed and continued perfection of security interests, and analyzes their relationship with article 9.

A. Sections 544 and 546(b)

Section 544 of the Bankruptcy Reform Act provides, in part:

(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—

(1) a creditor that extends to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists.

Like its predecessor, section 70c of the Bankruptcy Act of 1898,⁷⁰ section 544(a)(1) arms the trustee with extensive powers. The trustee has the rights of one who extends credit, and obtains a judicial lien on all property on which such a creditor could have obtained a judicial lien, as of the commencement of the bankruptcy case.⁷¹ The trus-

period; decided under 1962 version of article 9).

70. Act of June 22, 1938, ch. 575, § 1, 52 Stat. 879, *repealed by* Act of Nov. 6, 1978, Pub. L. No. 95-598, § 401(a), 92 Stat. 2549.

71. "A voluntary case under a chapter of this title is commenced by the filing with the bankruptcy court of a petition under such chapter by an entity that may be a debtor under such chapter." 11 U.S.C. § 301 (1982). Sections 302 and 303 specify the time of the commencement of the case when joint or involuntary petitions are filed.

tee need not subrogate to an actual creditor; his powers under this section arise "whether or not such a creditor exists." Any information that the trustee or an actual creditor may have about transfers of the debtor's property is irrelevant because the trustee's rights under section 544(a)(1) exist "without regard to any knowledge of the trustee or of any creditor."⁷²

Although the Bankruptcy Reform Act empowers the trustee with the rights of a creditor holding a judicial lien, it does not specify the substantive content of those rights. Instead the trustee's rights under section 544(a)(1) are determined by the substantive law of the jurisdiction governing the property in question,⁷³ typically state law. Consequently, when a conflict arises under section 544(a)(1) between the trustee and a creditor with a security interest in personal property,⁷⁴ the trustee's power to avoid the security interest is governed by article 9.

Under section 9-301(1)(b), an unperfected security interest is generally subordinated to the rights of a party who becomes a lien creditor before the interest is perfected. A lien creditor is defined in section 9-301(3) to include both a creditor who acquires a lien on property by attachment, levy or the like, and a trustee in bankruptcy. Because the trustee obtains the rights of a judicial lien creditor at the commencement of the bankruptcy case, a security interest that is unperfected at that time is subordinate to the rights of the trustee and can be avoided by the trustee.⁷⁵

Although the trustee's avoidance powers as a hypothetical lien creditor under section 544(a)(1) enable him to avoid most security interests that are unperfected as of the commencement of the case, his powers are limited by section 546(b) of the Bankruptcy Reform Act: "(b) The rights and powers of a trustee under section 544, 545, and 549 of this title are subject to any generally applicable law that permits perfection of an interest in property to be effective against an entity that acquires rights in such property before the date of

72. For a general discussion of the differences between § 544(a)(1) of the Bankruptcy Reform Act and § 70c of the Bankruptcy Act of 1898, see 4 COLLIER ON BANKRUPTCY § 544.02 (15th ed. 1979); Levin, *An Introduction to the Trustee's Avoiding Powers*, 53 AM. BANKR. L.J. 173, 174-76 (1979).

73. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 544.02, at 544-8 to-10.

74. Section 544(a) of the Bankruptcy Reform Act states that the trustee may avoid any "transfer" of property. "Transfer" means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property, including retention of title as a security interest and foreclosure of the debtor's equity of redemption." 11 U.S.C. § 101(46) (1982), *as amended* by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 368.

75. *E.g.*, *In re Turley*, 17 Bankr. 99 (Bankr. D.S.D. 1981).

such perfection."⁷⁶

For a secured party to take advantage of the protection from avoidance offered by section 546(b), the generally applicable law must grant him priority over the holder of a judicial lien whose interest in the collateral arose before the secured party perfected his security interest. The only section of article 9 that so provides is section 9-301(2):⁷⁷ a purchase money secured party who files a financing statement before or within ten days after the debtor receives possession of secured collateral takes priority over a lien creditor whose rights arise between the time the security interest attaches and the time of filing. Consequently, a purchase money secured party whose ten day grace period for filing has not expired as of the commencement of the case may still obtain protection from avoidance. Section 546(b), in effect, incorporates the delayed perfection rule of section 9-301(2) into the Bankruptcy Reform Act.⁷⁸ Because there are no article 9 grace periods for nonpurchase money security interests, the holder of such an interest who has not perfected it as of the commencement of a bankruptcy case cannot take advantage of the protection from avoidance afforded by section 546(b).

When it enacted section 546(b), Congress did not make an independent policy decision concerning the necessity of permitting secured parties to delay perfection of their security interests. Instead, the section was designed to protect parties who might rely on delayed filing provisions under state law from the surprise intervention of a bankruptcy petition.⁷⁹ At least with regard to security interests in personal property, Congress merely deferred to the determination made by the drafters of article 9.⁸⁰

76. 11 U.S.C. § 546(b) (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377. Section 545 of the Bankruptcy Reform Act establishes and defines the trustee's power to avoid the fixing of statutory liens on the debtor's property. 11 U.S.C. § 545 (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377. Section 549 permits the trustee to avoid certain postpetition transfers of property of the estate. 11 U.S.C. § 549 (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 379.

77. See *supra* notes 23-27 and accompanying text. U.C.C. § 9-312(4) is of no utility to the secured party under § 546(b) of the Bankruptcy Reform Act. Under § 9-312(4), a secured party who perfects his security interest after another party asserts a claim to the collateral gains priority only over an earlier perfected security interest, and not over the rights of an intervening lien creditor. See *supra* notes 32-37 and accompanying text.

78. When it enacted § 546(b) of the Bankruptcy Reform Act, Congress was aware of the specific protection against the trustee's avoidance powers that U.C.C. § 9-301(2) would give to a purchase money secured party. H.R. REP. NO. 95-595, 95th Cong., 1st Sess. 371 (1977).

79. *Id.* Section 546(b) is the statutory successor to § 67c(1)(B) of the Bankruptcy Act of 1898. Act of July 5, 1966, Pub. L. No. 89-495, §§ 3, 4, 80 Stat. 168, repealed by Act of Nov. 6, 1978, Pub. L. No. 95-598, § 401(a), 92 Stat. 2549. Unlike § 67c(1)(B), however, § 546(b) authorizes delayed perfection of consensual transfers as well as of statutory liens. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 546.03, at 546-47.

80. See *supra* notes 28-31 and accompanying text.

In order for a purchase money secured party to obtain protection under section 546(b), he must actually file a financing statement within ten days after the debtor receives possession of the secured collateral, even if the bankruptcy case has already commenced.⁸¹ In most cases, the filing of the bankruptcy petition operates as a stay of any act to "create, perfect, or enforce" any lien against property of the bankruptcy estate,⁸² or against property of the debtor to the extent that the lien secures a claim that arose before the commencement of the case.⁸³ The bankruptcy filing, however, does not automatically stay acts taken to perfect an interest in property when the trustee's rights and powers are limited by section 546(b).⁸⁴ Thus, a purchase money secured party whose ten day grace period for perfection has not expired at the commencement of a bankruptcy case can take advantage of the delayed filing provision of section 9-301(2) without fear of violating the Bankruptcy Reform Act's automatic stay.⁸⁵

Because a perfected security interest in personal property takes priority over the rights of a lien creditor whose claim to the collateral arises after perfection,⁸⁶ the trustee, as a hypothetical lien creditor under section 544(a)(1), cannot avoid a security interest that is perfected before the commencement of the case.⁸⁷ If the perfection of a security interest would otherwise lapse during the bankruptcy proceedings, however, it is less clear whether the secured party must continue the perfection in order to retain priority over the trustee and, if so, how continuation of perfection is to be accomplished.

When a filed financing statement lapses before continuation, the security interest becomes unperfected and is deemed to have been unperfected against a person who became a lien creditor or a purchaser before the lapse.⁸⁸ The previously senior secured party becomes, upon lapse, junior to intervening claimants.⁸⁹ A similar "reversal of priority" rule also may apply when a security interest is perfected by a means other than filing, and the period of perfection

81. Cf. *In re Fiorillo & Co.*, 19 Bankr. 21 (Bankr. S.D.N.Y. 1982) (mechanic's lien filed after commencement of the case but within 4 month grace period established by state mechanics' lien law).

82. 11 U.S.C. § 362(a)(4) (1982).

83. *Id.* § 362(a)(5).

84. *Id.* § 362(b)(3), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 371.

85. Cf. *In re Fiorillo & Co.*, 19 Bankr. 21 (Bankr. S.D.N.Y. 1982).

86. U.C.C. § 9-201, 9-301(1)(b).

87. *E.g.*, *In re E.G. Hoover Co.*, 16 Bankr. 435 (Bankr. M.D. Pa. 1982).

88. U.C.C. § 9-403(2); see also *supra* note 48 and accompanying text.

89. See *supra* notes 49-51 and accompanying text.

expires before perfection is continued.⁹⁰ In either case, if the perfection expires during bankruptcy proceedings and is not continued, the secured party may become junior to the trustee or others who assert an interest in the secured collateral.⁹¹

A potential, although partial, solution to this problem appears in section 9-403(2). Under that section, if a security interest has been perfected by filing when the insolvency proceedings are commenced, it will remain perfected until the end of sixty days after the termination of the proceedings.⁹² The section eliminates the need to file a continuation statement during bankruptcy proceedings by providing that a financing statement does not lapse during the proceedings. Thus, the secured party would maintain the priority established by his financing statement over claimants whose interests might otherwise become senior to the security interest upon lapse. Although the section establishes a rule applicable only in insolvency, it governs conflicts between a secured party whose interest is perfected by filing and all other types of claimants to the secured collateral. Consequently, the provision also would appear to permit a secured party to retain priority over the trustee if the trustee's interest in the collateral was subordinate to that of a security interest perfected by filing as of the commencement of bankruptcy proceedings. Because section 9-403(2) deals only with security interests perfected by filing, it provides no protection in cases in which a security interest is perfected other than by filing and the perfection expires after the commencement of the bankruptcy case.⁹³

Section 546(b) of the Reform Act appears to be of little help to a secured party who seeks to continue the perfection of his security

90. See *supra* notes 56-69 and accompanying text.

91. The need to continue the perfection of a security interest after the commencement of the case might arise in a number of situations. For example, if a security interest in property acquired by a debtor before bankruptcy covers proceeds of that property, the interest in the proceeds is generally effective against the trustee even though the estate may acquire proceeds after the commencement of the case. 11 U.S.C. § 552(b) (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 380. A security interest in noncash proceeds not covered by a filed financing statement meeting the requirements of U.C.C. § 9-306(3)(a) becomes unperfected 10 days after receipt of the proceeds, however, unless "the security interest in the proceeds is perfected before the expiration of the ten day period." *Id.* § 9-306(3)(c). Thus, a secured party with an interest in proceeds acquired by the estate after the commencement of the case might find it necessary to perfect his security interest in the proceeds before the ten day period of automatic perfection expires. See *supra* notes 56-62 and accompanying text.

92. Section 9-403(2) provides: "If a security interest perfected by filing exists at the time insolvency proceedings are commenced by or against the debtor, the security interest remains perfected until termination of the insolvency proceedings and thereafter for a period of sixty days."

93. See Review Comm. for Art. 9 of the U.C.C., Perm. Ed. Bd. for the U.C.C., Final Report at 245 (1971).

interest after the commencement of the case, especially if the security interest has been perfected by a means other than filing. As previously noted, section 546(b) subjects the trustee's avoidance powers under section 544(a)(1) to any generally applicable law that permits perfection to be effective against one who acquires rights in the secured property before the date of perfection.⁹⁴ The trustee's avoiding powers arise as of the commencement of the case. Thus, if a security interest is perfected at that time, the trustee does not acquire his rights "before" the date of perfection. Although section 546(b) "incorporates" into the Bankruptcy Reform Act the delayed filing provisions of article 9, it does not incorporate the statute's continuation of perfection sections.⁹⁵ Consequently, section 546(b) does not protect a secured party who must continue the perfection of his security interest from the avoiding powers of the trustee.⁹⁶

Moreover, if a secured party must continue the perfection of his security interest after the commencement of bankruptcy proceedings, and attempts to do so, he will most likely violate the automatic stay.⁹⁷ Section 362(b)(3) of the Reform Act does provide relief from the automatic stay for an act to perfect an interest in property "to the extent that the trustee's rights and powers are subject to such perfection under section 546(b)." Because acts to continue the perfection of a security interest do not appear to fall within the scope of section 546(b), however, the relief from the automatic stay provided by section 362(b)(3) is unavailable.⁹⁸ Thus, the secured party must either risk violating the stay in order to continue the perfection of his security interest,⁹⁹ or request the bankruptcy court to lift the

94. See *supra* note 76 and accompanying text.

95. See *supra* note 78 and accompanying text.

96. If applicable state law requires seizure of property or commencement of an action to accomplish perfection of an interest in the property against an entity that acquires rights before perfection, "and such property has not been seized or such action has not been commenced before the date of the filing of the petition," § 546(b) provides that "such interest in such property shall be perfected by notice [to the trustee] within the time fixed by such law for such seizure or commencement." 11 U.S.C. § 546(b) (1982), *as amended by* Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377. Article 9 does not require either seizure of property or commencement of an action to perfect a security interest, and a secured party cannot take advantage of this notice provision of § 546(b) to perfect, or continue the perfection of, his security interest after the commencement of the case. *Cf. In re Utah Agricorp, Inc.*, 12 Bankr. 573 (Bankr. D. Utah 1981) (filing of a reclamation suit against the trustee was "neither the statutory nor functional equivalent of a filing within this state" and did not eliminate the need to continue the perfection of a security interest in collateral brought into the state after the security interest in it was perfected in another jurisdiction; decided under the Bankruptcy Act of 1898).

97. 11 U.S.C. § 362(a)(4), (5) (1982).

98. See *supra* notes 82-85 and accompanying text.

99. An individual injured by a willful violation of the automatic stay may recover actual damages, costs, attorney's fees, and, in appropriate cases, punitive damages. 11 U.S.C. § 362(h),

stay so that continuation can be accomplished.¹⁰⁰

The most effective protection for the secured party whose perfection expires after the commencement of the case lies not in the statutory language of the Bankruptcy Reform Act or article 9, but in case law developed under the Bankruptcy Act of 1898. Under these holdings, the rights of the trustee and the secured party to property transferred by the debtor prior to bankruptcy are fixed, or frozen, at the initiation of the bankruptcy proceedings.¹⁰¹ If a security interest is perfected as of the commencement of the case, the trustee, whose rights as a judicial lien creditor arise at that time, is junior to the secured party. Should the perfection of the security interest thereafter cease to be effective, the secured party need not file a continuation statement or otherwise seek to continue the perfection. Rather, the secured party retains his priority established at the commencement of the case, even if he does nothing after that time to continue the perfection of his security interest.

Not all cases decided under the Bankruptcy Act of 1898 held that the relative priority of a secured party and the trustee is frozen at the time bankruptcy proceedings begin.¹⁰² Moreover, when perfection by a means other than filing ceases to be effective during bankruptcy proceedings, the secured party cannot be certain that he will retain priority against parties other than the trustee who claim an interest in the secured collateral.¹⁰³ For these reasons as well as the absence of clear statutory language in either the Reform Act or the Uniform Commercial Code, it remains uncertain whether a secured party must attempt to continue the perfection of his security interest after commencement of a bankruptcy case. In light of this uncertainty, if the

Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 352. Cf. *In re Miller*, 22 Bankr. 479 (D. Md. 1982) (repossession of automobile by secured party who was without notice that debtor had filed a bankruptcy petition and subsequent refusal to return automobile to debtor violated automatic stay; damages resulting from loss of use of automobile awarded to debtor pursuant to court's power to punish civil contempt); *In re Munsey Corp.*, 10 Bankr. 864 (Bankr. E.D. Pa. 1981) (secured party whose interest was unperfected as of the commencement of the case must remove from filing system a financing statement filed in violation of the automatic stay after the date of the petition).

100. 11 U.S.C. § 362(d) (1982).

101. *Lockhart v. Garden City Bank & Trust Co.*, 116 F.2d 658 (2d Cir. 1940); *In re South County Motel Corp.*, 19 U.C.C. Rep. Serv. (Callaghan) 1254 (D.R.I. 1976). See also 1 G. GILMORE, *supra* note 2, at 584-85.

102. *In re Utah Agricorp, Inc.*, 12 Bankr. 573 (Bankr. D. Utah 1981). It should be noted that the strength of this case as precedent is open to question because of the court's obvious confusion of a "lien creditor" with a "purchaser" under the Uniform Commercial Code.

103. See *supra* notes 93-94 and accompanying text. Cf. *Eastern Ind. Prod. Credit Ass'n v. Farmers State Bank*, 31 Ohio App. 2d 252, 287 N.E.2d 824 (1972) (where trustee did not assert an interest in secured collateral and secured party failed to file a continuation statement before the filed financing statement lapsed during bankruptcy proceedings, previously junior secured party obtained priority over first secured party).

perfection of a security interest would otherwise expire after the commencement of a bankruptcy case, the secured party should request the bankruptcy court to lift the automatic stay so that continuation can be accomplished.¹⁰⁴

B. Section 547(e)

Under section 547(b) of the Bankruptcy Reform Act of 1978,¹⁰⁵ the trustee may avoid, as preferential, any transfer¹⁰⁶ of an interest of the debtor in property that is made:

(1) to or for the benefit of a creditor; (2) for or on account of an antecedent debt owed by the debtor before such transfer was made; (3) made while the debtor was insolvent; (4) made—

(A) on or within 90 days before the date of the filing of the petition; or (B) between 90 days and one year before the date of the filing of the petition, if such creditor, at the time of such transfer was an insider;

(5) that enables such creditor to receive more than such creditor would receive if—

(A) the case were a case under chapter 7 of this title; (B) the transfer had not been made; and (C) such creditor received payment of such debt to the extent provided by

104. 11 U.S.C. § 362(d) (1982).

105. 11 U.S.C. § 547(b), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78. The preference provisions of § 547 of the Bankruptcy Reform Act are, in many respects, quite different from those of § 60 of the Bankruptcy Act of 1898, but the central concept of a preference as a transfer of property of the debtor to a creditor for or on account of an antecedent debt remains much the same. Bankruptcy Act, § 60, 30 Stat. at 562.

Some of the more significant changes effected by § 547 of the Bankruptcy Reform Act that are not discussed in this article include: the reduction of the period in which preferential transfers may occur from four months to 90 days prior to bankruptcy; the creation of a presumption that the bankrupt was insolvent during the preference period; the elimination of the requirement that a trustee prove that the transferee had reasonable cause to believe that the debtor was insolvent when the transfer was made; and the creation of a statutory formula limiting a secured party's ability to protect from the trustee's avoiding powers after-acquired property that is subject to a perfected security interest. 11 U.S.C. § 547(b)(4)(A), (c)(5), (f) (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78. These and other changes have spawned a substantial literature. *E.g.*, 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547; J. WHITE & R. SUMMERS, *supra* note 27, at 999-1017; Clark, *Preferences Under the Old and New Bankruptcy Acts*, 12 U.C.C. L.J. 154 (1979); Kaye, *Preferences Under the New Bankruptcy Code*, 54 AM. BANKR. L.J. 197 (1980); Kronman, *The Treatment of Security Interests in After-Acquired Property Under the Proposed Bankruptcy Act*, 124 U. PA. L. REV. 110 (1975); Note, *Avoidance of Preferential Transfers Under the Bankruptcy Reform Act of 1978*, 65 IOWA L. REV. 209 (1979).

106. A transfer of the debtor's property includes the creation of a security interest in it. 11 U.S.C. § 101(48) (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 368.

the provisions of this title.

If a debtor transfers property to a creditor because of a previous obligation of the debtor, the trustee can avoid the transfer as a preference, assuming he can demonstrate that the other elements of a preference exist. Section 547(e)¹⁰⁷ is crucial to the preference scheme of the Reform Act because it defines the time at which a transfer, for purposes of section 547, occurs and, thus, effectively controls the determination of whether a transfer was made for or on account of an antecedent debt.¹⁰⁸

In general, a transfer for purposes of section 547 occurs when the interest of the transferee in the transferred property is perfected.¹⁰⁹ Section 547 does not mandate the method of perfecting an interest in property, but it does specify the effect that perfection must have. Section 547(e)(1)(B), for example, provides that a transfer of personal property is perfected when "a creditor on a simple contract cannot acquire a judicial lien that is superior to the interest of the transferee." Like section 544(a)(1),¹¹⁰ section 547(e) permits state substantive law to determine when a judicial lien creditor can acquire an interest in the transferred property superior to that of the transferee.¹¹¹ Thus, when the challenged transfer is the creation of a security interest in personal property, the relevant provision is section 9-301(1)(b), which provides that an unperfected security interest is subordinate to the claim of one who becomes a lien creditor before the security interest is perfected. Essentially, the tests of the Reform Act and article 9 converge. Under section 547(e), a transfer is perfected, and thus occurs, at the time at which a lien creditor cannot acquire rights superior to those of the transferee. Under section 9-301(1)(b) a lien creditor can subordinate the transferee only when he levies on the collateral before the transferee perfects his security interest.¹¹²

Although section 547(e) of the Reform Act generally allows state law to define the circumstances in which a judicial lien creditor can acquire rights in transferred property that are superior to those of a transferee, the Reform Act also overrides article 9 and permits

107. 11 U.S.C. § 547(e) (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78.

108. The Bankruptcy Reform Act contains no definition of the term "antecedent." Section 547(b)(2) simply states that an antecedent debt must be "owed by the debtor before such transfer was made."

109. *E.g., id.* § 547(e)(2)(B).

110. *See supra* notes 73-74 and accompanying text.

111. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.46, at 547-136.

112. U.C.C. § 9-301(1)(b), (2).

delayed perfection in cases in which article 9 does not authorize it. Under section 547(e)(2)(A),¹¹³ for example, if a security interest is perfected at the time that the interest is created or within ten days thereafter, the transfer of the property, for purposes of section 547, is deemed to occur when the interest was created, not when it was perfected. This result occurs under the Reform Act even though the act of perfection may have been undertaken after the creation of the security interest and, under state law, a lien creditor could have acquired rights superior to those of the secured party before perfection.

To illustrate this point, assume that a secured party makes a loan to a debtor on May 1 and the parties enter into an enforceable non-purchase money security interest on that date. The secured party files to perfect the security interest on May 8. For purposes of section 547, the transfer is deemed to have occurred on May 1, rather than on the actual date of perfection, May 8. Because the loan was made on May 1 and the debt arose at that time, the transfer was not made for or on account of an antecedent debt and it cannot be avoided by the trustee as a preference. If the same transaction had occurred outside of bankruptcy, however, a lien creditor who levied on the property between May 1 and May 8, would take priority over the secured party. In contrast to section 547(e)(2)(A), section 9-301(2) provides a ten day filing grace period only to purchase money secured parties, not to secured creditors with nonpurchase money security interests.¹¹⁴ In preference cases, then, the Reform Act clearly allows more secured parties to delay perfection than does article 9 in nonbankruptcy cases.¹¹⁵

113. Section 547(e)(2), 11 U.S.C. § 547(e)(2), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78, states, in full:

(2) For the purposes of this section, except as provided in paragraph (3) of this subsection, a transfer is made—

(A) at the time such transfer takes effect between the transferor and the transferee, if such transfer is perfected at, or within 10 days after, such time; (B) at the time such transfer is perfected, if such transfer is perfected after such 10 days; or (C) immediately before the date of the filing of the petition, if such transfer is not perfected at the later of—

(i) the commencement of the case; or (ii) 10 days after such transfer takes effect between the transferor and the transferee.

114. See *supra* note 23 and accompanying text.

115. The intersection of two statutory systems with differing perfection requirements may result in circular priority problems. See 2 G. GILMORE, *supra* note 2, at 1022-23. For example, assume that a nonpurchase money secured party takes a security interest in collateral and makes a loan to the debtor on May 1, but does not perfect his security interest until May 8. On May 6, a lien creditor levies on the secured collateral and, on June 1, the debtor files a bankruptcy petition. Under § 9-301(1)(b), the lien creditor is entitled to priority over the secured party because he levied before the security interest was perfected. Assuming the other elements

Section 547(e)(2)(A) also permits delayed perfection of security interests by means other than filing in cases in which article 9 does not. The section states that a transfer must be perfected, but does not specify any particular method of perfection. Under section 9-305 a secured party may perfect a security interest by taking possession of the collateral. Because a secured party takes priority over a lien creditor if he takes possession of the collateral before the lien creditor levies on it,¹¹⁶ perfection by possession satisfies the section 547(e)(1)(B) test for perfection of a transfer.¹¹⁷ Consequently, under section 547(e)(2)(A), if a secured party takes possession of the collateral within ten days after making a loan and creating an enforceable security interest, perfection is deemed to have occurred at the time of the loan and creation of the security interest, and the trustee cannot avoid the transfer as a preference. In nonbankruptcy cases, however, article 9 establishes no grace periods for secured parties who perfect a security interest by taking possession of the collateral.¹¹⁸ As a result, a lien creditor who levies on the collateral before the secured party takes, or attempts to take, possession is not subordinated to the claim of the secured party.¹¹⁹

For a number of reasons, Congress chose to give broad effect in preference cases to the delayed perfection of security interests. First, delayed perfection was permitted by section 60a(7) of the Bankruptcy Act of 1898,¹²⁰ and the provisions of section 547(e)(2) simply extend and clarify that policy.¹²¹ Under section 60a(7), perfection could be delayed up to twenty-one days, depending upon the length of any grace period established by state law. If state law did not specify a grace period, section 60a(7) I.(B) provided that, where perfec-

of a preference are present, however, the trustee can avoid the lien as a preference because it is a transfer of the debtor's property made to a creditor for or on account of an antecedent debt. Finally, because the security interest was perfected within 10 days after the secured party made a loan to the debtor, the transfer of the debtor's property represented by the security interest is not a preference and the trustee cannot avoid it. Thus, the lien creditor is prior to the secured party, the trustee can avoid the lien, and the secured party defeats the trustee. Fortunately, such a circular priority problem cannot arise under the Reform Act. Section 551 of the Reform Act provides that any transfer avoided by the trustee under § 547 "is preserved for the benefit of the estate." 11 U.S.C. § 551 (1982). The trustee takes over the rights of the lien creditor, whose lien he has avoided, and can defeat the secured party's claim by asserting the lien creditor's priority over the secured party. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 551.01, at 551-52.

116. U.C.C. § 9-201, 9-301(1)(b).

117. See *supra* note 109 and accompanying text.

118. See *supra* note 23.

119. U.C.C. § 9-301(1)(b).

120. Act of Mar. 18, 1950, ch. 70, § 1, 64 Stat. 24, repealed by Act of Nov. 6, 1978, Pub. L. No. 95-598, § 401(a), 92 Stat. 2549.

121. See Clark, *supra* note 105, at 164-65.

tion occurred "within twenty-one days after the transfer, the transfer shall be deemed to be made or suffered at the time of the transfer." Although pre-article 9 "transaction filing" statutes often contained filing grace periods of varying lengths,¹²² the drafters of article 9 adopted a "notice filing" system that, in their view, made grace periods unnecessary except in cases involving purchase money security interests.¹²³ Because article 9 established no delayed filing grace periods for nonpurchase money security interests, it was unclear whether nonpurchase money secured parties could take advantage of the twenty-one day period of section 60a(7) I.(B). It also was unclear whether a purchase money secured party could delay perfection for twenty-one days or was limited to the ten day period specified in article 9.¹²⁴ Commentators generally agreed that both purchase money and nonpurchase money secured parties should be able to delay perfection for twenty-one days under section 60a(7) I.(B).¹²⁵ Congress put the issue to rest by matching the grace period in section 547(e)(2)(A) with the ten day grace period given to purchase money secured parties under article 9.¹²⁶

Congress did not defer to the judgment of the drafters of article 9, however, and limit the protection of the delayed filing provision of section 547(e)(2)(A) to secured parties holding purchase money security interests. There appear to be two reasons for this decision. As a practical matter, there may often be a delay between the creation of a security interest and its perfection.¹²⁷ Congress apparently recognized this fact and made a policy decision that all secured parties should have ten days in which to accomplish perfection without being subjected to the risk that delay will result in a transfer being avoided as preferential. More importantly, section 547 applies to preferential transfers of realty, as well as personalty.¹²⁸ Thus, the delayed perfection rules of section 547(e) must take into account the differences between the perfection of interests in realty and the perfection of security interests in personal property.¹²⁹ Interests in real property normally cannot be perfected before the transaction creating the interest is completed because real property recording statutes require

122. See *supra* notes 15-16 and accompanying text.

123. See *supra* notes 17-25 and accompanying text.

124. 2 G. GILMORE, *supra* note 2, at 1325-35.

125. See Clark, *supra* note 105, at 158-59.

126. U.C.C. § 9-301(2); Clark, *supra* note 105, at 164.

127. See Clark, *supra* note 105, at 158.

128. 11 U.S.C. § 547(b) (1982), as amended by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78, provides that "the trustee may avoid any transfer of an interest of the debtor in property."

129. *E.g., id.* § 547(e)(1)(A); 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.48.

that the deed or mortgage, or a copy thereof, be recorded.¹³⁰ If a mortgage on real property cannot be perfected by recording until after the loan is made and the transaction is completed, the transfer, of necessity, would be made for or on account of an antecedent debt. The grace period of section 547(e)(2)(A) protects a real estate mortgagee from the risk that his mortgage will be avoided as a preference if the mortgagee records the mortgage within ten days after making the loan.

Section 547(e)(2)(C)(ii) of the Reform Act appears to extend the ten day grace period for delayed perfection of security interests to situations in which a bankruptcy case commences before the ten day period expires.¹³¹ Assume, for example, that a secured party makes a loan to a debtor on May 1 and that the parties create an enforceable security interest in the debtor's property on that date. On May 6 the debtor files a bankruptcy petition and, on May 8, the secured party files to perfect its security interest. Section 547(e)(2)(C)(ii) implies that a transfer perfected within ten days after it takes effect is not deemed to have been made at the commencement of the case; thus, it must be deemed to have been made at the time the transfer takes effect. Consequently, in the example above, the transfer of the security interest in the debtor's property would not have been made for or on account of an antecedent debt and could not be avoided as a preference.

Under the provisions of the Reform Act, as originally enacted, an attempt to perfect a security interest pursuant to section 547(e)(2)(C)(ii) after the commencement of a case violated the automatic stay.¹³² The original version of section 362(b)(3) of the Reform Act rendered the stay inoperative only when the trustee's rights were subject to delayed perfection under section 546(b).¹³³ Under section 546(b), however, the trustee's rights and powers under "sections 544, 545, and 549" are subject to delayed perfection under generally applicable law. Because section 546(b) does not apply to delayed perfec-

130. *E.g.*, FLA. STAT. § 695.01(1) (Supp. 1983).

131. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.45, at 547-135.

132. 11 U.S.C. § 362(a)(4), (5) (1982). Not all commentators agreed with this position. The author of COLLIER ON BANKRUPTCY stated:

If the ten-day period for perfection has not yet expired when the petition is filed, it can still be utilized to relate back to the actual time of transfer. In other words, if the petition is filed a week after a transfer was made, three days are still left to perfect it and the automatic stay should not apply to depart from the intent of the statute in this regard.

The author cited no authority for this proposition, however. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.45, at 547-135.

133. *See supra* notes 81-85 and accompanying text.

tion under section 547,¹³⁴ the automatic stay prevented a secured party from relying on section 547(e)(2)(C)(ii) to perfect his security interest after bankruptcy began. The secured party, of course, could request that the bankruptcy court lift the automatic stay so that he could perfect his security interest after the commencement of the case.¹³⁵ If the date of perfection was to relate back to the time of transfer under section 547(e)(2)(C)(ii), however, the secured party would be required to act quickly enough to have the stay lifted and perfect his interest before the ten day grace period for delayed perfection expired.

Congress has amended section 362(b)(3) to eliminate the possibility that a secured party who perfects his security interest under section 547(e)(2)(C)(ii) after the commencement of a case will violate the automatic stay. Section 362(b)(3) now provides that the filing of a bankruptcy petition does not operate as a stay of "any act to perfect an interest in property . . . to the extent that such act is accomplished within the period provided under section 547(e)(2)(A) of this title."¹³⁶ If a secured party is permitted to perfect a security interest within the ten day grace period of section 547(e)(2)(A) without violating the automatic stay, even though a bankruptcy petition has been filed, the transfer of the security interest will be deemed to have occurred when it was made, and not at the time of perfection. In cases in which the debt arose at the time of the original transfer, the transfer would not be made for or on account of an antecedent debt and the trustee could not avoid it as a preference.

This amendment to section 362(b)(3) does not resolve all of the problems associated with the perfection of security interests after the commencement of the case under section 547(e)(2)(C)(ii). If a non-purchase money secured party perfects his security interest after the commencement of the case under section 547(e)(2)(C)(ii), the trustee can, in every case, avoid the security interest under section 544(a)(1).¹³⁷ Section 544(a)(1) arms the trustee with the rights of a lien creditor as of the commencement of a bankruptcy case, and enables him to avoid a security interest in personal property that is unperfected on that date.¹³⁸ When generally applicable state law permits perfection of a security interest to be effective against one who acquires rights in the property before perfection, the trustee cannot

134. *In re Ken Gardner Ford Sales, Inc.*, 10 Bankr. 632 (Bankr. E.D. Tenn. 1981).

135. 11 U.S.C. § 362(d) (1982).

136. 11 U.S.C. § 362(b)(3), *as amended by* Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 371.

137. *See* Kaye, *supra* note 105, at 218; *cf.* 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.51, at 547-160.1.

138. *See supra* notes 73-75 and accompanying text.

avoid a security interest that is unperfected at the time of bankruptcy, provided the secured party perfects his interest within the applicable grace period.¹³⁹ Section 9-301(2) of the Uniform Commercial Code establishes a grace period for the delayed perfection of purchase money security interests,¹⁴⁰ but no such period exists for nonpurchase money interests. Thus, the broad authorization in section 547(e)(2)(C)(ii) for delayed perfection after the commencement of the case is essentially meaningless to the nonpurchase money secured party whose interest will always fall to the trustee under section 544(a)(1).

If the purpose of section 547(e)(2)(C)(ii) of the Reform Act is to shield both purchase money and nonpurchase money security interests from attack as preferences by permitting perfection after commencement of the case, Congress has been unsuccessful in accomplishing its objective. Although Congress has amended the Reform Act to make it clear that the automatic stay does not bar the perfection of a security interest after the commencement of the case, where perfection is undertaken pursuant to section 546(e)(2)(C)(ii), a nonpurchase money security interest always can be avoided under section 544(a)(1). Congress might remedy this problem by extending to nonpurchase money security interests the protection given to purchase money interests under section 546(b). The reason for authorizing delayed perfection in section 546(b) is to incorporate into the Reform Act state law policies dealing with delayed perfection, however, and an amendment giving protection to nonpurchase money security interests would establish a federal rule inconsistent with the policies of article 9. Thus, the best solution to this problem may be to eliminate delayed perfection after commencement of the case under

139. 11 U.S.C. § 546(b) (1982), *as amended* by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377. *See supra* notes 76-78 and accompanying text.

140. A purchase money security interest is protected from the trustee's avoiding powers under § 544(a)(1) of the Bankruptcy Reform Act, 11 U.S.C. § 544(a)(1) (1982), *as amended* by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377, when it is perfected after the commencement of the case, but within the ten day grace period for delayed filing established by U.C.C. § 9-301(2). *See supra* notes 77-78 and accompanying text. It also normally would be protected from the trustee's power to avoid preferences, even if the secured party could not perfect the security interest after the commencement of the case under § 547(e)(2)(C)(ii). 11 U.S.C. § 547(e)(2)(C)(ii) (1982). Section 547(c)(3) of the Reform Act provides that the trustee may not avoid, as a preference, a purchase money security interest that is perfected before 10 days after the debtor takes possession of the secured collateral. Because § 362(b)(3) makes the automatic stay inoperative in cases in which delayed perfection is effective against the trustee under § 546(b), the purchase money secured party is permitted to perfect his security interest after the commencement of the case. If he does so, the delayed perfection should be effective against the trustee for purposes of § 47(c)(3), as well as § 544(a)(1). *Id.* § 362(b)(3), 544 (a)(1), 546(b), 547(c)(3), *as amended* by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333. Section 547(c) of the Reform Act is discussed more fully at *infra* notes 141-67 and accompanying text.

section 547, unless applicable nonbankruptcy law establishes a grace period for perfection of the transfer challenged by the trustee.

C. Sections 547(c)(1) and (c)(3)

Section 547(c)¹⁴¹ of the Bankruptcy Reform Act lists types of transfers that cannot be avoided as preferences, even if all of the elements of a preference were present when the transfer occurred. Two of these types of transfers may involve delayed perfection under article 9:

- (c) The trustee may not avoid under this section a transfer—
 - (1) to the extent that such transfer was—
 - (A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and (B) in fact a substantially contemporaneous exchange; . . .
 - (3) that creates a security interest in property acquired by the debtor—
 - (A) to the extent such security interest secures new value that was—
 - (i) given at or after the signing of a security agreement that contains a description of such property as collateral; (ii) given by or on behalf of the secured party under such agreement; (iii) given to enable the debtor to acquire such property; and (iv) in fact used by the debtor to acquire such property; and
 - (B) that is perfected on or before 10 days after the debtor receives possession of such property.

The language of section 547(c)(3) differs somewhat from the definition of a purchase money security interest in section 9-107 of the Uniform Commercial Code,¹⁴² but both sections apply only to a security interest taken by a creditor who makes a loan or extends

141. 11 U.S.C. § 547(c) (1982), *as amended* by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 355 and 377-78. For the most part, the exceptions to the trustee's power to avoid preferential transfers that appear in § 547(c) had no statutory counterparts in the Bankruptcy Act of 1898. Many are codifications of prior judicial decisions, however. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.03, at 547-19 to -23.

142. U.C.C. § 9-107 states:

A security interest is a "purchase money security interest" to the extent that it is

- (a) taken or retained by the seller of the collateral to secure all or part of its price; or
- (b) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.

credit¹⁴³ that enables the debtor to acquire the secured collateral. Both sections also require that the loan or credit must have been used by the debtor to obtain the collateral.¹⁴⁴ In addition, the "enabling loan"¹⁴⁵ provision of section 547(c)(3) parallels generally the elements of section 9-301(2) of the Uniform Commercial Code, which protects purchase money secured parties against intervening claims by lien creditors.¹⁴⁶ Despite these general similarities, there are differences between section 547(c)(3) and section 9-301(2). Section 547(c)(3) specifies that new value must be given to the debtor "at or after the signing of a security agreement that contains a description of such property as collateral." Neither section 9-107 nor section 9-301(2) expressly requires that a purchase money security interest be accompanied by a written security agreement, but such a requirement is implicit in section 9-301(2). That section establishes a ten day grace period, beginning when the debtor receives possession of secured collateral, during which a purchase money secured party may file a financing statement and obtain priority over a lien creditor who levies on the collateral between the time the security interest attaches and the time of filing.¹⁴⁷ If a debtor is in possession of secured collateral, however, article 9, like section 547(c)(3) of the Reform Act,¹⁴⁸ requires the parties to the secured transaction to enter into a

143. Section 547(c)(3) of the Reform Act states that the creditor must have given "new value" to the debtor. "New value" is:

[M]oney or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation.

11 U.S.C. § 547(a)(2) (1982), *as amended* by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78. This definition is essentially the same as the requirement in U.C.C. § 9-107 that a purchase money secured party must sell the collateral wholly or partially on credit, or must make an advance or incur an obligation so that the debtor can obtain the collateral.

144. The secured party may be required to trace the proceeds of a loan in order to demonstrate that it was in fact used by the debtor to obtain the secured collateral. 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.39, at 547-122; Kaye, *supra* note 105, at 205.

145. H.R. REP. No. 595, 95th Cong., 1st Sess. 373 (1977).

146. *See supra* notes 23-27 and accompanying text.

147. *See supra* notes 23-24 and accompanying text.

148. Section 547(c)(3)(B) of the Reform Act states that a security interest must be "perfected" within ten days after it attaches, but does not specify a particular method of perfection. 11 U.S.C. § 547(c)(3)(B) (1982), *as amended* by Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78. Theoretically, a secured party could perfect a purchase money security interest by taking possession of the collateral and, if he did so within 10 days after the security interest attached, the interest might qualify for protection against avoidance under § 547(c)(3). Because § 9-301(2) of the Uniform Commercial Code applies only to purchase money security interests that are perfected by filing, under this interpretation § 547(c)(3) would cover a greater number of secured transactions than does § 9-301(2). It is doubtful that § 547(c)(3) protects security interests that are perfected by possession, however. The section also requires that new

written security agreement containing a description of the collateral.¹⁴⁹

In addition, the ten day grace period¹⁵⁰ of section 547(c)(3) may be used to protect a purchase money security interest from avoidance as a preference when the delayed perfection period of section 547(e)(2)(A) is not available. Under section 547(e)(2)(A), when a security interest is perfected within ten days after it takes effect, the transfer of the debtor's property is deemed to have occurred at the time that the transfer took effect, and not at the time of perfection.¹⁵¹ Although a security interest takes effect when it attaches and becomes enforceable,¹⁵² a secured party, including a purchase money secured party, may make a loan or extend credit to the debtor before the security interest becomes enforceable. In such cases, the delayed perfection period of section 547(e)(2)(A) will not protect the security interest from avoidance as a preference. That section relates the time of transfer back only to the time that the security interest became enforceable, and not to the time of the loan or the extension of credit. Consequently, the transfer would still be treated as having been made for or on account of an antecedent debt, even though perfection of the security interest may have occurred within ten days after its attachment. Under section 547(c)(3), however, the trustee may not avoid a purchase money security interest that is perfected within ten days after the debtor receives possession of the secured collateral, no matter when the enabling loan was made. Thus, a purchase money secured party who advances funds to the debtor before a security interest becomes enforceable is protected from the

value be given to, and used by, the debtor to "acquire" the secured property. If the secured party possesses the secured collateral, the debtor has not acquired it (property in the possession of the secured party normally is not of great utility to the debtor) and § 547(c)(3) should not be applicable to the transaction.

149. U.C.C. § 9-203(1)(a).

150. Both § 547(c)(3) of the Reform Act and § 9-301 of the Uniform Commercial Code create ten day grace periods during which a secured party can delay perfection of his security interest. As originally enacted, the Reform Act required that the security interest be perfected within ten days after it attached. In contrast, article 9 requires a financing statement to be filed within ten days after the debtor receives possession of the secured collateral. The difference could create a trap for the unwary secured creditor, because a security interest can attach before the debtor receives possession of secured collateral. *See supra* notes 26-27 and accompanying text. If the security interest did attach before the debtor obtained possession, a secured party who relied on article 9 and dated his filing grace period from the time of possession could find that the delayed filing period of § 547(c)(3), as originally enacted, had expired. *See Kaye, supra* note 105, at 105-06. Congress removed this potential pitfall for secured creditors by amending § 547(c)(3)(B) to provide that the grace period runs from the time the debtor receives possession of secured collateral. 11 U.S.C. § 547(c)(3) (1982), *as amended by* Act of July 10, 1984, Pub. L. No. 98-353, 98 Stat. 333, 377-78.

151. 11 U.S.C. § 547(e)(2)(A) (1982).

152. U.C.C. § 9-203(2).

trustee's claim that the transfer was preferential, so long as he perfects the security interest within ten days after the debtor obtains possession of the collateral.¹⁵³

Section 547(c)(1) of the Reform Act states that the trustee may not avoid, as a preference, a transfer that was intended by the parties to be a contemporaneous exchange for new value, if the transfer was in fact a substantially contemporaneous exchange. For purposes of section 547, a transfer can occur when a security interest is perfected.¹⁵⁴ Because the Reform Act does not define the term "contemporaneous," it is arguable that section 547(c)(1) permits delayed perfection of new value security interests that do not meet the requirements of either section 547(e)(2) or section 547(c)(3), so long as the parties intended the secured transaction to be a contemporaneous exchange and the delayed perfection was, in fact, substantially contemporaneous with the creation of the security interest.¹⁵⁵

The legislative history indicates that Congress did not have delayed perfection of security interests in mind when it enacted section 547(c)(1). Rather, the section was designed to protect short term "credit" transactions involving the use of checks from avoidance as preferences.¹⁵⁶ When goods are purchased with a check, the transaction is technically a credit transaction¹⁵⁷ because there is a delay between the time of sale and payment of the check. The actual transfer of the buyer's funds to the seller at the time of payment is thus a transfer for or on account of the antecedent debt that arose at the time of sale. Such a transfer could be avoided by the trustee under section 547(b) if the other elements of a preference were present at the time of payment of the check. Congress intended to insulate this type of transaction from attack as a preference.¹⁵⁸ Many commentators¹⁵⁹ quickly pointed out, however, that section 547(c)(1) also appeared to codify prior bankruptcy decisions¹⁶⁰ holding that a slight delay in the creation or perfection of a security interest was not preferential if the parties, from the outset, intended¹⁶¹ the transaction to

153. J. WHITE & R. SUMMERS, *supra* note 27, at 1006-07.

154. 11 U.S.C. § 547(e)(2)(B) (1982).

155. See J. WHITE & R. SUMMERS, *supra* note 27, at 1006; Hagedorn, *The Survival and Enforcement of the Secured Claim Under the Bankruptcy Reform Act of 1978*, 54 AM. BANKR. L.J. 1 (1980); Kaye, *supra* note 105, at 198-99.

156. H.R. REP. No. 595, 95th Cong., 1st Sess. 373 (1977).

157. U.C.C. § 2-511.

158. See Levin, *supra* note 72, at 186.

159. See, e.g., 4 COLLIER ON BANKRUPTCY, *supra* note 72, § 547.37, at 547-118; Countryman, *Bankruptcy Preferences—Current Law and Proposed Changes*, 11 U.C.C. L.J. 95, 105 (1978); Kaye, *supra* note 105, at 198-99.

160. *Dean v. Davis*, 242 U.S. 438 (1917).

161. Where the creditor and the debtor did not intend a loan to be secured at the time it

be secured.

Predictably, a number of secured creditors who failed to perfect their security interests within the ten day grace periods of sections 547(e)(2) and 547(c)(3) have sought protection against avoidance by invoking section 547(c)(1). Almost as predictably, the responses of the courts to the arguments of the secured parties have differed. A number of courts have held that section 547(c)(1) does not apply to credit transactions.¹⁶² Thus, a secured party who makes an enabling loan by giving new value to a debtor, but does not perfect his security interest within ten days after the debtor receives possession of the collateral, cannot take advantage of section 547(c)(1) to escape the trustee's claim that the transfer that occurred at the time of perfection was a preference.¹⁶³ Although some support for this interpretation may be found in the legislative history, the language of section 547(c)(1) does not expressly prohibit its application to credit or security transactions. These courts, then, appear to have read section 547(c)(1) too restrictively.

Other courts have decided that a secured party may use section 547(c)(1) to obtain protection from the trustee's power to avoid preferences.¹⁶⁴ If a secured party makes an enabling loan to a debtor, but does not perfect his security interest within ten days after the debtor obtains possession of the collateral, the security interest may nevertheless be protected if the parties intended the security transaction to be contemporaneous with the extension of credit and the court finds it was substantially contemporaneous. While the language of section 547(c)(1) is broad enough to support these holdings, this interpretation of the statute reduces the ten day grace period of section 547(c)(3) to a mere evidentiary presumption.¹⁶⁵ As a result, in any case in which a purchase money secured party fails to perfect within the grace period of section 547(c)(3), the trustee could be forced to litigate whether the transfer was intended to be, and was, contempo-

was made, but later entered into a security transaction, the security interest in the debtor's property was a preferential transfer. *National City Bank v. Hotchkiss*, 231 U.S. 50 (1913).

162. See, e.g., *Gower v. Ford Motor Credit Co. (In re Davis)*, 22 Bankr. 644 (Bankr. M.D. Ga. 1982); *Valley Bank v. Vance (In re Vance)*, 22 Bankr. 26 (Bankr. D. Idaho 1982); *Knave v. Enlow (In re Enlow)*, 20 Bankr. 480 (Bankr. S.D. Ind. 1982); *Exchange Bank of Polk County v. Christian (In re Christian)*, 8 Bankr. 816 (Bankr. M.D. Fla. 1981).

163. E.g., *Waldschmidt v. Ford Motor Credit Co. (In re Murray)*, 27 Bankr. 445 (Bankr. M.D. Tenn. 1983).

164. E.g., *Ray v. Security Mutual Finance Corp. (In re Arnett)*, 17 Bankr. 912 (E.D. Tenn. 1982); *General Motors Acceptance Corp. v. Martella (In re Martella)*, 22 Bankr. 649 (Bankr. D. Colo. 1982); *Jahn v. First Tennessee Bank of Chattanooga (In re Burnette)*, 14 Bankr. 795 (Bankr. E.D. Tenn. 1981).

165. See *Waldschmidt v. Ford Motor Credit Co. (In re Murray)*, 27 Bankr. 445, 452 (Bankr. M.D. Tenn. 1983).

aneous.¹⁶⁶ There is no reason to believe that Congress intended to create such a possibility when it enacted section 547(c)(1). To the contrary, the ten day grace period in section 547(c)(3) suggests that Congress expected a relatively simple resolution of questions regarding the delayed perfection of purchase money security interests.

Because the words "substantially" and "contemporaneous" are imprecise by nature and are not defined in the Reform Act, it appears that Congress used them in section 547(c)(1) to give courts some flexibility in preference cases. Nevertheless, courts should restrict the applicability of section 547(c)(1) to cases that do not involve mere delayed perfection of security interests. If the issue in a preference case is one of delayed perfection, sections 547(c)(3) and 547(e)(2) should be applied exclusively to determine the validity of a security interest. Section 547(c)(1) can then be applied when issues other than delayed perfection arise, such as when a secured party and a debtor delay the creation of a security interest for a limited time,¹⁶⁷ or when a buyer pays for property with a check.

IV. CONCLUSION

Without question, the Bankruptcy Reform Act of 1978 brought bankruptcy law closer to the legal concepts of article 9 of the Uniform Commercial Code. It is also clear, however, that the provisions of the two statutes often differ substantially in cases in which delayed or continued perfection of security interests is involved. In adopting the Reform Act, Congress did not incorporate wholesale the policy choices made by the drafters of article 9. Instead, the Reform Act contains numerous examples of independent policy decisions made by Congress. Thus, under section 547 of the Reform Act, all secured parties, not just purchase money secured parties, have a grace period in which to perfect their security interests and the grace period of section 547 appears to be applicable to security interests perfected by possession as well as by filing.

Some provisions of the Reform Act also contain flaws that should be remedied by Congress or the courts. The uncertainty that surrounds the secured party's right to continue the perfection of his security interest after commencement of bankruptcy proceedings should be addressed by Congress. Section 547(e)(2)(C)(ii) should be rewritten to make it clear that a secured party may perfect his security interest after commencement of the case only in cases in which

166. See *Weill v. Tennessee Central Credit Union (In re Kelley)*, 3 Bankr. 641 (Bankr. E.D. Tenn. 1980).

167. See *Dean v. Davis*, 242 U.S. 438 (1917).

state law expressly permits delayed perfection of a security interest. Finally, the courts, and perhaps Congress, should limit the application of section 547(c)(1) so that section cannot be employed to sanction delayed perfection of security interests in cases in which the Reform Act does not expressly authorize it.