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THE SELLER'S RIGHT TO RECLAIM: ANOTHER CONFLICT BETWEEN THE UNIFORM COMMERCIAL CODE AND THE BANKRUPTCY ACT?

John A. Sebert, Jr.*

I. Introduction

For years, unsecured sellers who sold goods to insolvent buyers have had the right to reclaim those goods if the buyer committed some variety of fraud when acquiring the goods.¹ If the requisite fraud was established, reclamation was valid against the insolvent buyer's trustee in bankruptcy on the theory that the original transaction was voidable by the seller because of the fraud, and because the trustee acceded to no greater title to the goods than the buyer had.² This right of reclamation existed even though it resulted, at least in some cases, in preferential treatment of the unpaid seller over other unsecured creditors of the bankrupt. Moreover, while the fraud leading to the invocation of the right to reclaim prior to the Uniform Commercial Code was often relatively clear and active, such active fraud was not always required; courts permitted sellers to establish the requisite fraud by engaging in presumptions, rebuttable in theory but not often rebutted in fact, that a buyer who makes a purchase while he is insolvent would normally know of his financial condition and thus commits "fraud" by making a purchase for which he knows or should know he cannot pay.³ Such decisions, by finding a tacit representation of solvency whenever a buyer makes a purchase on credit and then permitting the use of

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1 See generally 4A W. COLLIER, BANKRUPTCY ¶ 70.41 (14th ed. J. Moore 1974) [hereinafter cited as COLLIER]; 3A R. DUESENBERG & L. KING, SALES AND BULK TRANSFERS UNDER THE UNIFORM COMMERCIAL CODE § 13.03 (4) (a) (1974) [hereinafter cited as DUESENBERG & KING].

2 See Bankruptcy Act § 70(a), 11 U.S.C. § 110(a) (1970); 4A COLLIER ¶ 70.41.

The fundamental policy underlying the right of reclamation has been explained as follows:

Where goods are obtained by fraud of the bankrupt, the seller may rescind the contract of sale and reclaim them if he can identify them in the hands of the trustee. This is on the theory that fraud renders all contracts voidable, and that neither in law nor in morals would the trustee be justified in holding goods obtained by the fraud of the bankrupt for the benefit of other creditors. Such creditors have no right to profit by the fraud of the bankrupt to the wrong and injury of the party who has been deceived and defrauded. This does not result in a preference in favor of the seller who thus retakes goods obtained from him by fraud, because in such case the seller retakes his own property. . . .

Manly v. Ohio Shoe Co., 25 F.2d 384, 385 (4th Cir. 1928) (citations omitted).

3 Cases involving active fraud include *In re* A. C. Kelly & Co., 6 F. Supp. 221 (S.D.N.Y. 1933) (active concealment); *Bateman v. Patterson*, 212 Ga. 284, 92 S.E.2d 8 (1956) (active concealment); *In re Monson*, 127 F. Supp. 625 (W.D. Ky. 1955) (bad faith misrepresentation); *In re Koretz*, 6 F.2d 225 (7th Cir. 1925) (intent not to pay). See generally 4A COLLIER ¶ 70.41.

Cases presuming fraud when a buyer makes a purchase while insolvent include *In re Meiselman*, 105 F.2d 995, 998 (2d Cir. 1939); *California Conserving Co. v. D'Avanzo*, 62 F.2d 528 (2d Cir. 1933); *Manly v. Ohio Shoe Co.*, 25 F.2d 384 (4th Cir. 1928); *In re Penn Table Co.*, 26 F. Supp. 387 (S.D. W.Va. 1939); *In re Paper City Mill Supply Co.*, 28 F.2d 115 (D. Mass. 1928); *In re Gurvitz*, 276 F. 931 (D. Mass. 1921).

presumptions to establish the fraud required for reclamation, went a long way toward creating a right of reclamation that is not much different from that presently found in the U.C.C.

The Uniform Commercial Code sets forth the seller's right to reclaim in § 2-702.⁴ In some respects the U.C.C. makes it easier for a seller to exercise his right of reclamation. If he acts quickly, making a demand within 10 days of the buyer's receipt of the goods, the requirement of affirmatively establishing some form of fraud by the buyer is eliminated. The theory, as explained in the comment, is that "any receipt of goods on credit by an insolvent buyer amounts to a tacit business misrepresentation of solvency and therefore is fraudulent. . . ."⁵ Even if the seller does not make a timely demand within the 10-day period, he may still reclaim later⁶ if the buyer made a written misrepresentation of solvency within three months prior to delivery.⁷ Again, no affirmative proof of fraud is necessary; reclamation is available even if the misrepresentation was innocent.⁸

In other respects, however, the seller's right to reclaim under U.C.C. § 2-702 is less broad than under prior law. Unless the seller acts promptly—within 10 days of the buyer's receipt of the goods—he may reclaim only if there has been a written misrepresentation of solvency within three months prior to receipt of the goods. Thus the right to reclaim for oral misrepresentations, or for the "tacit misrepresentation" that some courts had previously recognized when an insolvent buyer purchased on credit,⁹ is limited to a very short period. Moreover, under the U.C.C. the seller's right to reclaim, if exercised, is an exclusive remedy with respect to the goods reclaimed.¹⁰ Thus a reclaiming seller is deprived of the right to claim a deficiency with respect to reclaimed goods and cannot, with respect to any such deficiency, share in the distribution of assets to the general creditors of the bankrupt.

Despite the relatively well-settled right of the seller under prior law to re-

4 U.C.C. § 2-702 (1962 version) provides in pertinent part:

(2) Where the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days after the receipt, but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply. Except as provided in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.

(3) The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser or lien creditor under this Article (Section 2-403). Successful reclamation of goods excludes all other remedies with respect to them.

The 1972 version deletes "or lien creditors." See notes 29, 30 *infra* and accompanying text.

5 U.C.C. § 2-702, Comment 2 (1962 version). Some argue that the U.C.C. merely made irrebuttable the previous rebuttable presumption of fraud. See King, *Reclamation Petition Granted: In Defense of the Defrauded Seller*, 44 REF. J. 81, 82 (1970). Others claim the U.C.C. abandons any requirement of fraud. See Countryman, *Buyers and Sellers of Goods in Bankruptcy*, 1 N. MEX. L. REV. 435, 455 (1971). Further debate about such semantics hardly seems useful.

6 Presumably the seller still would have to act with due diligence.

7 The seller probably must show that he relied on the misrepresentation. See J. WHITE & R. SUMMERS, UNIFORM COMMERCIAL CODE § 7-15 (1972).

8 Some pre-Code cases also permitted a seller to reclaim if he relied on a false financial statement even if the misrepresentation was unintentional. See *Sternberg v. American Snuff Co.*, 69 F.2d 307 (8th Cir. 1934).

9 See note 3 *supra* and accompanying text.

10 See U.C.C. § 2-702(3) (1962 version).

claim goods from an insolvent buyer in many circumstances, sellers attempting to reclaim under U.C.C. § 2-702 have been faced with numerous challenges, some of them successful, by trustees in bankruptcy. It has been urged that the seller's right to reclaim is voidable under the trustee's powers as a hypothetical lien creditor.¹¹ It has been argued that the right to reclaim is invalid as a statutory lien under § 67(c)(1)(A) of the Bankruptcy Act,¹² or as a state-created priority prohibited by § 64 of the Bankruptcy Act.¹³ It might also be asserted that the right to reclaim amounts to a voidable preference.¹⁴ It is these arguments that this article will address.

II. The Trustee As Lien Creditor

Under § 70(c) of the Bankruptcy Act the trustee is a hypothetical lien creditor and is vested with all the powers of a creditor of the bankrupt who had obtained a lien upon the bankrupt's property at the date of bankruptcy.¹⁵ The 1962 version of U.C.C. § 2-702(3) provides:

The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser *or lien creditor* under this Article (Section 2-403)¹⁶

The italicized language has led to the question whether the trustee, because of his position as a hypothetical lien creditor, therefore has priority over the rights of the reclaiming seller. An extended analysis of this particular problem, which has been discussed by other commentators,¹⁷ would serve little purpose at this time. Some consideration is necessary, however, in order to present a full picture of the reclaiming seller's rights against the trustee in bankruptcy.

The principal difficulty in resolving the lien creditor question is that, while U.C.C. § 2-703(3) clearly provides that the rights of the reclaiming seller are subject to the rights of a lien creditor, that section does not indicate what the rights of a lien creditor are or where those rights are to be found. To date, most

11 See, e.g., *In re Kravitz*, 278 F.2d 820 (3rd Cir. 1960).

12 11 U.S.C. § 107(c)(1)(A) (1970). See, e.g., *In re Federal's, Inc.*, 12 U.C.C. REP. SERV. 1142 (E.D. Mich. 1973) (in bankruptcy), *aff'd*, 402 F. Supp. 1357 (E.D. Mich. 1975); *In re Good Deal Supermarkets Inc.*, 384 F. Supp. 887 (D.N.J. 1974).

13 11 U.S.C. § 104 (1970). See *In re Federal's, Inc.*, 12 U.C.C. REP. SERV. 1142 (E.D. Mich. 1973) (in bankruptcy), *aff'd*, 402 F. Supp. 1357 (E.D. Mich. 1975). See also Countryman, *supra* note 5, at 452.

14 See Bankruptcy Act § 60, 11 U.S.C. § 96(b) (1970).

15 The section provides in relevant part:

The trustee shall have as of the date of bankruptcy the rights and powers of . . . a creditor who upon the date of bankruptcy obtained a lien by legal or equitable proceedings upon all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt upon a simple contract could have obtained such a lien, whether or not such a creditor exists. . . .

Bankruptcy Act § 70(c), 11 U.S.C. § 110(c) (1970).

16 U.C.C. § 2-702(3) (1962 version) (emphasis added). The 1972 version deletes "lien creditor."

17 See, e.g., Braucher, *Reclamation of Goods From a Fraudulent Buyer*, 65 MICH. L. REV. 1281 (1967); Hawkland, *The Relative Rights of Lien Creditors and Defrauded Sellers—Amending the Uniform Commercial Code to Conform to the Kravitz Case*, 67 COM. L.J. 86 (1962); Kennedy, *The Trustee in Bankruptcy Under the Uniform Commercial Code*, 14 RUTG. U. L. REV. 518, 549-53 (1960); Shanker, *A Reply to the Proposed Amendment of UCC Section 2-702(3)*, 14 WES. RES. L. REV. 93 (1962).

courts have agreed with the Third Circuit, in *In re Kravitz*,¹⁸ that the rights of a lien creditor are not to be found in U.C.C. § 2-702, or elsewhere in Article 2, or, for that matter, anywhere in the U.C.C. Those courts have instead resorted to non-U.C.C. state law to determine the relative priority of the reclaiming seller and the trustee in bankruptcy in his role as hypothetical lien creditor.¹⁹ The result has generally been favorable for the seller; although the court in *Kravitz* concluded that a lien creditor prevailed over the reclaiming seller under Pennsylvania law,²⁰ courts interpreting the law of other states have, for the most part, concluded that the reclaiming seller prevailed.²¹

These decisions result in a regrettable, but probably acceptable, lack of uniformity in a statute that was intended to create a uniform law of sales. A more serious threat, at least to reclaiming sellers, is the possibility that a court might adopt one of the interpretations of U.C.C. § 2-702 proffered by Professor Shanker. He argued, partly from the desire to maintain uniformity, that U.C.C. § 2-702 is itself a priority provision subordinating the rights of reclaiming sellers to those of lien creditors.²² This interpretation is subject to question, however, because it fails adequately to explain the cross-reference in U.C.C. § 2-702(3). The right to reclaim is subject to "the rights of a buyer in the ordinary course or other good faith purchaser or lien creditor *under this Article (Section 2-403)*. . . ."²³ This language indicates that U.C.C. § 2-702 is not itself a priority provision and that the rights of purchasers and lien creditors are to be found elsewhere.²⁴ Shanker's interpretation—that U.C.C. § 2-702(3) itself declares the rights of lien creditors to be superior to those of reclaiming sellers—would make the seller's right to reclaim against an insolvent buyer almost totally useless because that right would be ineffective against the trustee in bankruptcy.

Alternatively, Shanker argued that the right to reclaim is analogous to a security interest and that, under U.C.C. § 9-301(1)(b),²⁵ the trustee in bankruptcy, as lien creditor, would prevail over any reclaiming seller who had not perfected his security interest as of the date of bankruptcy either by appropriate filing or by taking possession of the goods.²⁶ An initial difficulty with this propo-

18 278 F.2d 820 (3rd Cir. 1960).

19 See, e.g., *In re Mel Golde Shoes*, 403 F.2d 658 (6th Cir. 1968); *In re Royalty Homes, Inc.*, 8 U.C.C. REP. SERV. 61 (Ref. E.D. Tenn. 1970).

20 278 F.2d at 820 (3d Cir. 1960).

21 See note 19 *supra*.

22 Shanker, *supra* note 17, at 97-98.

23 U.C.C. § 2-702(3) (1962 version) (emphasis added). The 1972 version deletes "lien creditor."

24 Professor Shanker argues that the cross-reference in § 2-702 was only for the purpose of defining the terms, such as lien creditor and buyer in the ordinary course, used therein. Shanker, *supra* note 17, at 97-98. The difficulty with this position is that the only section referred to in U.C.C. § 2-702 is U.C.C. § 2-403. While that section does contain an explanation of the rights of buyers in ordinary course, buyer in the ordinary course is *defined* elsewhere (in § 1-201(9)) and lien creditor is not mentioned in U.C.C. § 2-403. If the Code drafters had been intending only to cross-reference definitions, they most likely would have cited U.C.C. §§ 1-201(9) and 9-301(3) (1962 version). The latter section does contain a definition of lien creditor.

25 U.C.C. § 9-301(1) (1962 version) provides in pertinent part:

(1) Except as otherwise provided in subsection (2), an unperfected security interest is subordinate to the rights of . . .

(b) a person who becomes a lien creditor without knowledge of the security interest and before it is perfected; . . .

26 Shanker, *supra* note 17, at 102-06. See *In re Richardson Homes Corp.*, 18 U.C.C. REP. SERV. 384 (N.D. Ind. 1975) (in bankruptcy).

sition is that the seller's right to reclaim is created by statute, not by agreement of the parties, and thus does not appear to be the type of interest covered by Article 9, which applies to "security interests created by contract."²⁷ When compared with prior law, both interpretations substantially restrict the seller's right to reclaim. Since the official comments indicate an intention to extend the rights of a reclaiming seller,²⁸ it is extremely doubtful that the drafters ever intended such a result.

In 1966 the Permanent Editorial Board for the Uniform Commercial Code, apparently reacting in part to the risk of nonuniformity created by the *Kravitz* line of decisions and in part to the more serious threat posed by the Shanker arguments, recommended the deletion of the offending "or lien creditor" language from U.C.C. § 2-702(3).²⁹ In states that have adopted that recommendation,³⁰ sellers reclaiming under U.C.C. § 2-702 will clearly prevail over the trustee in bankruptcy's rights as a lien creditor under § 70(c) of the Bankruptcy Act, since the trustee's rights as a lien creditor are measured by state law.³¹ Even in states that have not deleted the "lien creditor" language from U.C.C. § 2-702, reclaiming sellers normally have prevailed over the trustee because the courts have referred to non-U.C.C. state law, which has generally been favorable to the reclaiming sellers, to determine the rights of lien creditors.³²

III. The Right to Reclaim: A Statutory Lien?

A. *The Problem*

By far the most serious threat to the seller's right to reclaim from an insolvent buyer is the possibility that the right to reclaim will be considered a statutory lien that first becomes effective upon a debtor's insolvency. Such liens are invalid against the debtor's trustee in bankruptcy under § 67(c)(1)(A) of the Bankruptcy Act.³³ In a significant recent decision, *In re Federal's, Inc.*,³⁴

27 U.C.C. § 9-102(2) (1962 version); see Braucher, *supra* note 17, at 1290.

28 See U.C.C. § 2-702, Statement of Changes (1962 version).

29 PERMANENT EDITORIAL BOARD, UNIFORM COMMERCIAL CODE, Report No. 3, at 3 (1966).

30 For a recent listing of 15 states that have deleted the "lien creditor" language, see Henson, *Reclamation Rights of Sellers Under Section 2-702*, 21 N.Y.L.F. 41, 41-42 n.2 (1975).

31 See 4A COLLIER ¶ 70.49.

32 See notes 18-21 *supra* and accompanying text.

33 This section provides:

The following liens shall be invalid against the trustee:

(A) every statutory lien which first becomes effective upon the insolvency of the debtor, or upon distribution or liquidation of his property, or upon execution against his property levied at the instance of one other than the lienor; . . .

(B) every statutory lien which is not perfected or enforceable at the date of bankruptcy against one acquiring the rights of a bona fide purchaser from the debtor on that date, whether or not such purchaser exists . . . ;

(C) every statutory lien for rent and every lien of distress for rent, whether statutory or not. . . .

11 U.S.C. § 107(c)(1)(A)-(C) (1970).

34 12 U.C.C. REP. SERV. 1142 (E.D. Mich. 1973) (in bankruptcy), *aff'd*, 402 F. Supp. 1357 (E.D. Mich. 1975). On appeal, the district court held that the rights of the reclaiming seller were subordinate to the rights of lien creditors under relevant Michigan law and that therefore the trustee in bankruptcy, as hypothetical lien creditor under § 70(c) of the Bankruptcy Act, prevailed over the seller. *Id.* at 1359-63. The district court also considered and agreed with the bankruptcy judge's conclusions that the right to reclaim set forth in U.C.C. § 2-702 was invalid against the trustee as a statutory lien and as a state-created priority. *Id.* at 1363-68.

a bankruptcy judge concluded that a seller's right to reclaim was invalid as a statutory lien. Panasonic had delivered electronic entertainment equipment to Federal's Department Stores on credit on August 10, 1972. Shortly thereafter Federal's filed a Chapter XI petition for an arrangement and Panasonic immediately sent written demands for reclamation of the equipment. Those demands were received by Federal's and by its Chapter XI receiver on August 19, 1972,³⁵ clearly within the 10-day demand period of U.C.C. § 2-702(2). In denying Panasonic's reclamation petition, the bankruptcy judge stated that the Code

confers upon a specified class of creditors "preferential treatment as against the buyer's other creditors" As such it conflicts with the express purpose of the Bankruptcy Act.³⁶

He then went on to hold that the seller's right to reclaim under U.C.C. § 2-702 amounted to a statutory lien and therefore was invalid against the trustee.³⁷ Since the decision in *Federal's* a number of other courts have considered the issue, some concluding that the U.C.C. § 2-702 right to reclaim is invalid as a statutory lien³⁸ and others rejecting the statutory lien argument asserted by trustees in bankruptcy.³⁹

Without doubt, the key to whether the seller's right to reclaim is valid against the trustee in bankruptcy is the determination of whether that right is a "statutory lien." If it is, it clearly runs afoul of § 67(c)(1)(A) of the Bankruptcy Act because, under that Act, a seller may reclaim only if the buyer receives goods while insolvent; thus the right to reclaim "first becomes effective upon the insolvency of the debtor."⁴⁰ In making the crucial determination of whether the right to reclaim is a statutory lien, one might logically look first to the Bankruptcy Act's definition of statutory lien:

35 12 U.C.C. REP. SERV. at 1143.

36 *Id.* at 1151-52.

37 *Id.* at 1153. The bankruptcy judge relied upon *In re Trahan*, 283 F. Supp. 620 (W.D. La.), *aff'd per curiam*, 402 F.2d 796 (5th Cir. 1968), *cert. denied sub nom.* Bernard v. Beneficial Finance Co., 394 U.S. 930 (1969) and upon *In re J. R. Nieves & Co.*, 446 F.2d 188 (1st Cir. 1971). The vendor's lien statutes in those two cases, from Louisiana and Puerto Rico respectively, were similar to each other but different from U.C.C. § 2-702 in that they gave the vendor a preference for the value of personal property sold to the debtor for which the debtor had not paid. The court in *Trahan* held that the Louisiana vendor's lien was a statutory lien but that it was valid against the trustee because it was effective regardless of the insolvency of the debtor and because it met the additional test of § 67(c)(1)(B) of the Bankruptcy Act—it was valid against bona fide purchasers. *In re Trahan*, 283 F. Supp. at 625-27. The court in *Nieves*, assuming but not deciding that the Puerto Rico vendor's lien was a statutory lien, agreed that it did not violate § 67(c)(1)(A) of the Bankruptcy Act because it was effective whether or not the debtor was insolvent, but held that the Puerto Rico vendor's lien was invalid against the trustee under § 67(c)(1)(B) of the Bankruptcy Act because the lien was not effective against bona fide purchasers. *In re J. R. Nieves*, 446 F.2d at 190-94. *Nieves* is curious, to say the least, in that the court purports to "assume without deciding" a point essential to its holding. If the Puerto Rico vendor's lien statute were not a statutory lien it could not be invalid against the trustee under § 67(c)(1)(B) of the Bankruptcy Act.

38 See *In re Perskey & Wolf, Inc.*, — F. Supp. —, 19 UCC REP. SERV. 812 (N.D. Ohio 1976); *In re Giltex, Inc.*, — F. Supp. —, 17 U.C.C. REP. SERV. 887 (S.D.N.Y. 1975); *In re Good Deal Supermarkets, Inc.*, 384 F. Supp. 887 (D.N.J. 1974); *In re Wetson's Corp.*, 17 U.C.C. REP. SERV. 423 (S.D.N.Y. 1975) (in bankruptcy).

39 See *In re Telemart Enterprises, Inc.*, 524 F.2d 761 (9th Cir. 1975), *cert. denied sub nom.* Holzman v. Alfred M. Lewis, Inc., 96 S. Ct. 1466 (1976); *In re National Bellas Hess, Inc.*, 17 U.C.C. REP. SERV. 430 (S.D.N.Y. 1975) (in bankruptcy).

40 11 U.S.C. § 107(c)(1)(A) (1970). Professor Henson appears to argue that, even if the U.C.C. § 2-702 right to reclaim is a statutory lien, it would not be invalid. He states that the

"Statutory lien" shall mean a lien arising solely by force of statute upon specified circumstances or conditions, but shall not include any lien provided by or dependent upon an agreement to give security, whether or not such lien is also provided by or is also dependent upon statute and whether or not the agreement or lien is made fully effective by statute.⁴¹

This definition is an example of a cardinal error of draftsmanship—using the term that is to be defined (lien) in the definition. The definition does make it clear that consensual security interests, such as those provided for in Article 9 of the U.C.C., are not encompassed within the term "statutory lien," but beyond that it is of little help.⁴²

B. *The Legislative History of § 67(c) of the Bankruptcy Act*

The legislative history of § 67(c), although far from conclusive, is at least more useful. The present version of § 67(c) was added to the Bankruptcy Act in 1966.⁴³ The committee report contained the following explanation of the provision in § 67(c)(1)(A) invalidating statutory liens that first become effective on insolvency:

The first of these provisions strikes at liens which merely determine the order of distribution upon insolvency or liquidation. This kind of lien is not a specific property right which may be asserted independently of a general distribution and regardless of the transfer of the property. This is clearly a disguised priority.⁴⁴

seller's right becomes effective immediately upon the buyer's receipt of goods on credit while insolvent and that it therefore does not "become effective only at the date the bankruptcy petition is filed." Henson, *supra* note 30, at 52. The difficulty with this argument is that the Bankruptcy Act invalidates statutory liens that first become effective upon insolvency rather than upon the filing of a bankruptcy petition. One is insolvent under the Bankruptcy Act when his debts exceed the fair value of his property, and this normally occurs some time prior to the filing of a petition in bankruptcy. See Bankruptcy Act § 1(19), 11 U.S.C. § 1(19) (1970).

Professor Henson also seems to suggest that the reclamation right under the U.C.C. might be saved because its definition of insolvency is broader than that of the Bankruptcy Act, including not only the Bankruptcy Act test but also inability to pay debts as they come due and failure to pay debts in the ordinary course of business. See U.C.C. § 1-201(23) (1962 version). Thus he appears to urge that the right to reclaim under the U.C.C., even if a statutory lien, is not one which becomes effective only upon insolvency as defined in the *Bankruptcy Act*. Henson, *supra* note 30, at 52. It is doubtful that a court, once it concluded that a lien was a statutory lien within the policy of § 67(c), would permit that policy to be avoided by the simple expedient of having a slightly different definition of insolvency than that found in the Bankruptcy Act. Moreover, Professor Henson ignores § 67(c)(1)(B) of the Bankruptcy Act, which invalidates all statutory liens that are not perfected at the date of bankruptcy against bona fide purchasers. 11 U.S.C. § 107(c)(1)(B) (1970). The seller's right to reclaim under U.C.C. § 2-702 is expressly made subject to the rights of bona fide purchasers. See *English v. Ralph Williams Ford*, 17 Cal. App.3d 1038, 1047-48, 95 Cal. Rptr. 501, 506 (1971). Thus as long as the U.C.C. § 2-702 right is considered a statutory lien it would be invalid against the trustee even if one accepted the tenuous argument that it is not a lien that first becomes effective upon insolvency.

41 Bankruptcy Act § 1(29a), 11 U.S.C. § 1(29a) (1970).

42 It has been said that the definition is primarily a definition of "statutory" rather than of "lien." See King, *Statutory Liens Under New § 67(c) of the Bankruptcy Act*, 42 *REV. J.* 11, 12 (1968).

43 Act of July 5, 1966, Pub. L. No. 89-495, § 4, 80 Stat. 268 (1966). For a general discussion of the treatment of statutory liens prior to 1966 and of the 1966 amendments, see Seligson, *Treatment of Statutory Liens in Bankruptcy—The 1966 Amendments of Section 67(b) and (c)*, 27 *FED. B. J.* 111 (1967).

44 S. REP. No. 1159, 89th Cong., 2d Sess. (1966), reprinted in, [1966] U.S. CODE CONG. & ADMIN. NEWS 2456, 2461.

This language has been relied upon by some to demonstrate that the U.C.C. § 2-702 right to reclaim should be considered a statutory lien.⁴⁵ It is obvious that labels ought not be conclusive; the mere fact that the drafters of the U.C.C. did not denominate the U.C.C. § 2-702 right a "lien" ought not to save it from the application of § 67(c).⁴⁶ On the other hand, the quoted language from the committee report does not inevitably lead to the conclusion that the seller's right of reclamation is a statutory lien. Instead, the passage seems to suggest a distinction between "specific property rights" and priorities in the distribution of assets upon insolvency. There is other language in the report that further supports a distinction between priority provisions and property interests, evidencing a desire to invalidate the former but to preserve the latter. In discussing the inadequacies of the then-existing version of § 67(c), which postponed statutory liens on personal property that were not accompanied by possession, the committee stated:

It will be recalled that one of the major objectives of the Chandler Act was to overcome the distortion of the Federal order of distribution by the creation of spurious statutory liens. . . . However, a recent reexamination of State lien statutes has shown that neither the standard of possession nor the distinction between real and personal property is an entirely satisfactory criterion. *Some liens which are genuine property rights are affected and others which were essentially State-created priorities escape.*⁴⁷

It is submitted that the seller's right to reclaim under U.C.C. § 2-702 is much more akin to the "property right" which the committee desired to preserve than to the state-created priority in the distribution of the bankrupt's assets which the committee wished to invalidate. It appears that the "liens" about which the committee was concerned were liens, such as landlords' liens, wage liens, and tax liens, that attach to all or large portions of a bankrupt's property and that therefore present grave risks of seriously depleting the bankrupt's estate at the expense of the unsecured creditors. The seller's right to reclaim is

45 Countryman, *supra* note 5, at 444. Professor Countryman uses the cited excerpt while arguing that the buyer's right, under U.C.C. § 2-502, to replevy from an insolvent seller goods for which he has paid all or part of the price amounts to a statutory lien. He later says, however, that he believes the same arguments apply to the seller's right to reclaim under U.C.C. § 2-702. *Id.* at 452.

A full discussion of the buyer's right under U.C.C. § 2-502 is beyond the scope of this article. It can be pointed out, however, that the buyer's U.C.C. § 2-502 rights at least are somewhat different from the seller's right to reclaim. The seller is able to remove from the bankrupt estate only the asset that he contributed to the estate whereas the buyer is given priority not to the asset he contributed (presumably money) but to the goods that he bought, which may have been created in part from the money that he contributed but to which many other unsecured creditors of the debtor, such as employees and suppliers, also may have contributed. Moreover, even if the buyer's rights under U.C.C. § 2-502 are invalid as a statutory lien, little is lost. The buyer's U.C.C. § 2-502 rights are almost entirely illusory under the provisions of the U.C.C. itself because he has a right to replevy the goods for which he has paid only if the seller "becomes insolvent within ten days after receipt of the first installment on their price." U.C.C. § 2-502(1) (1962 version). It will be a rare instance where a buyer can show that the seller actually became insolvent during the short 10-day period after receipt of the first payment from the buyer.

46 In at least this respect I agree with Professor Countryman. *See* Countryman, *supra* note 5, at 444.

47 S. REP. No. 1159, 89th Cong., 2d Sess. (1966), reprinted in [1966] U.S. CODE CONG. & ADMIN. NEWS 2456, 2460-61 (emphasis added).

not such a lien. It attaches *only* to the particular assets that the seller has contributed to the bankrupt's estate and for which the bankrupt has not paid. The unpaid seller is given no priority in the distribution of any other assets. Moreover, the right of reclamation, if exercised, is the seller's *exclusive* remedy with respect to the goods reclaimed.⁴⁸ By reclaiming, the seller gives up any right to claim a deficiency against the bankrupt's estate (such as damages for the excess of contract price over resale price⁴⁹ or for lost profits⁵⁰) and therefore gives up the right to receive any further distribution on account of that claim.⁵¹ Thus a seller reclaiming goods under U.C.C. § 2-702 will not be able to deplete the assets of the bankrupt estate beyond the specific assets that he contributed to that estate. The reclaiming seller, therefore, does not present the same risk of depleting all of the assets of the estate that is presented by the holders of liens that attach to broad ranges of the bankrupt's property.

There is further support in the legislative history of § 67(c) for the thesis that the right to reclaim is not the type of "lien" encompassed by the statute. In 1952 Congress enacted the present definition of statutory lien and a version of § 67(c) that postponed statutory liens on personal property that were not accompanied by possession.⁵² In explaining those changes, the House Report stated:

Liens on personal property unaccompanied by possession, however, are of the nature of "floating liens," which attach to all a debtor's personalty, although the property he owns is commonly changing from day to day. If any provisions for priority were labeled a "lien," such a lien would be indistinguishable from floating liens on personal property.

There is accordingly reason to restrict such liens to the same extent that priorities are restricted.⁵³

Thus, at least in 1952, when the definition of statutory lien was inserted in the Bankruptcy Act, it was thought that the principal problem with statutory liens was that they attached to all of the debtor's property and were, essentially, floating liens.⁵⁴ Although the substance of § 67(c) was changed in 1966, the definition of statutory lien has not been altered. In addition, while the committee reports in 1966 do not explicitly repeat the 1952 description of a statutory lien as one attaching to all of the debtor's property, all of the cases cited in the reports of the Senate and House judiciary committees involved the types of liens that normally do attach to all, or broad ranges of, the debtor's property, such as landlord liens

48 U.C.C. § 2-702(3) (1962 version).

49 This measure of damages is normally available under U.C.C. § 2-706 (1962 version).

50 Lost profits are recoverable under U.C.C. § 2-708(2) (1962 version) in appropriate circumstances, such as if the seller was a lost volume seller.

51 Others have noted this difference between U.C.C. § 2-702 and ordinary liens. See Note, *U.C.C. § 2-702: Conflict With § 67c(1)(A) of the Federal Bankruptcy Act*, 53 N.C. L. Rev. 169, 175-76 (1974).

52 Act of July 7, 1952, Pub. L. No. 82-456, § 21(d), 66 Stat. 420, 427 (1952).

53 H. REP. NO. 2320, 82d Cong., 1st Sess. (1952), reprinted in [1952] U.S. CODE CONG. & ADMIN. NEWS 1960, 1973.

54 It is also significant that the Congress' initial attempt to deal with statutory liens, by postponing some statutory liens under § 67(c) of the Act of 1938, was prompted in part by studies showing that tax and rent liens often took up large portions of the bankrupt estates. See 4 COLLIER ¶ 67.20(3).

and wage and tax liens.⁵⁵ Finally, there is no mention in the 1966 committee reports of the seller's right to reclaim, and certainly no indication that the right to reclaim under U.C.C. § 2-702 was thought to be a statutory lien. If Congress had intended to call into question the seller's right to reclaim, which had been recognized in many circumstances under prior law,⁵⁶ one would expect to find some mention of that intention in the committee reports.

While the legislative history of the Bankruptcy Act's treatment of statutory liens is far from conclusive, it is significant that there is in the committee reports no indication that the seller's right to reclaim would be affected by the provisions relating to statutory liens. In addition, the reports contain relatively strong evidence that, in the statutory lien provisions, Congress was concerned with types of creditor remedies that are significantly different from the seller's right to reclaim, that is, with liens such as tax and landlord liens that attach to broad classes of the bankrupt's property and that present a substantial risk of seriously depleting the assets of the bankrupt estate. Thus the legislative history at least appears to provide some support for the position that the seller's right to reclaim is not a statutory lien under § 67(c)(1)(A) of the Bankruptcy Act.

C. Policy Considerations

Numerous important considerations of history and policy also support this conclusion. If the U.C.C. § 2-702 right to reclaim is a statutory lien, the expansion under the U.C.C. of the right to reclaim, by eliminating the need to prove fraud, would be affected. Also, the right to reclaim would be called into question in situations where that right had been firmly established prior to the U.C.C., such as when an insolvent buyer purchases goods on credit intending never to pay for them.⁵⁷ The seller's right to reclaim in this clearly fraudulent situation is also covered by U.C.C. § 2-702, and the U.C.C. does not distinguish between such situations and ones, such as in *Federal's*, in which a buyer, though insolvent, purchases without any affirmative misrepresentation of his financial situation and with full intention to pay.⁵⁸ If the right to reclaim set forth in U.C.C. § 2-702 is invalid as a statutory lien in the latter situation, would it not

55 The report of the Senate Judiciary Committee essentially quoted the earlier report of the House Judiciary Committee. See H. REP. No. 136, 89th Cong., 1st Sess. (1965). All of the cases cited in the Senate Judiciary Committee report were in the quotation from the House Report. See S. REP. No. 1159, 89th Cong., 2d Sess. (1966), reprinted in [1966] U.S. CODE CONG. & ADMIN. NEWS 2456. The cases cited were: *In re Einhorn Bros., Inc.*, 272 F.2d 434 (3d Cir. 1959) (distraint for rent); *Rochell v. City of Dallas*, 264 F.2d 166 (5th Cir. 1959) (state tax lien); *In re Quaker City Uniform Co.*, 238 F.2d 155 (3d Cir. 1956) (lien for rent); *California State Dept. of Employ. v. United States*, 210 F.2d 242 (9th Cir. 1954) (state tax lien); *City of New Orleans v. Harrell*, 134 F.2d 399 (5th Cir. 1943) (city tax lien); *In re Eakin Lumber Co.*, 39 F. Supp. 787 (N.D. W.Va. 1941), *aff'd sub nom.* *Reconstruction Finance Corp. v. Sun Lumber Co.*, 126 F.2d 731 (4th Cir. 1942) (wage lien).

56 For a discussion of the seller's right to reclaim under pre-U.C.C. law, and of the success in asserting that right against the trustee in bankruptcy, see notes 1-3 *supra* and accompanying text.

57 See, e.g., *In re Koretz*, 6 F.2d 225 (7th Cir. 1925).

58 See *In re Federal's, Inc.*, 12 U.C.C. REP. SERV. 1142 (E.D. Mich. 1973) (in bankruptcy), *aff'd*, 402 F. Supp. 1357 (E.D. Mich. 1975).

also be invalid in the former?⁵⁹ Before reaching a result that thus raises such serious questions about a right to reclaim that has been firmly established for years, more careful attention to the policies of the Bankruptcy Act and the U.C.C. is required than has been given by the courts which have concluded that the seller's right to reclaim is invalid as a statutory lien.

In analyzing the underlying policy considerations, it is first important to re-emphasize the limited nature of the seller's right to reclaim under the U.C.C. Section 2-702 permits the seller to recover only the asset that he has contributed to the estate. This crucial point, which constitutes the most significant difference between the right of reclamation and the liens with which Congress was primarily concerned, has largely been ignored in the cases.⁶⁰ The advantage to the reclaiming seller is further limited, as previously indicated, by the fact that reclamation, if elected, is the seller's exclusive remedy with respect to the reclaimed goods; he may not also file a claim for a deficiency as an unsecured creditor.⁶¹

In addition, the right to reclaim is short-lived. Unless there has been a written misrepresentation of solvency made within three months prior to delivery, reclamation must be demanded within 10 days after buyer's receipt of the goods.⁶² The short 10-day period reduces significantly one potential source of prejudice to other creditors of the buyer—the possibility that a creditor will have lent money or otherwise acted in reliance on buyer's possession of the goods that seller is attempting to reclaim. The likelihood of such reliance by a creditor within the 10-day period may be minimal, and in any event a careful creditor could partially protect himself from reclamation by waiting to rely on such goods until buyer had had them for more than 10 days. Admittedly, some risk would remain even after the end of the 10-day period: the goods could still be reclaimed if a written misrepresentation of solvency had been made to the seller within three months prior to delivery.⁶³ But an intervening creditor probably ran the risk of reclamation in the case of such misrepresentation even before the U.C.C.⁶⁴

Finally, the seller's right to reclaim is expressly subject to the rights of good faith purchasers,⁶⁵ which has been correctly held to include not only buyers but

59 U.C.C. § 2-702(2) (1962 version) purports to state the only basis for reclamation from an insolvent buyer:

Except as provided in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay. *Id.* Thus it might be argued that a seller could not fall back upon any common law rights to reclaim from a fraudulent buyer. Some courts, however, have attempted to preserve the common law reclamation rights by interpreting U.C.C. § 2-702(2) as the sole basis of reclamation only if that section is not invalidated by the trustee in bankruptcy. *See In re Giltex, Inc.*, — F. Supp. —, 17 U.C.C. REP. SERV. 887, 896 (S.D.N.Y. 1975); *In re Wetson's Corp.*, 17 U.C.C. REP. SERV. 423, 429 (S.D.N.Y. 1975) (in bankruptcy).

60 One court did recognize the possibility that Congress might have intended only to invalidate statutory liens that attach to broad categories of a debtor's assets but ultimately concluded that Congress intended to invalidate both such broad liens and any lien that became effective on insolvency. *See In re Giltex*, — F. Supp. —, 17 U.C.C. REP. SERV. 887 (S.D.N.Y. 1975). The court failed to place sufficient emphasis on the fact that the right of reclamation attaches not just to a specific asset but to the very asset contributed to the estate by the seller.

61 *See* notes 48-51 *supra* and accompanying text.

62 U.C.C. § 2-702(2) (1962 version).

63 *Id.*

64 *See, e.g., Sternberg v. American Snuff Co.*, 69 F.2d 307 (8th Cir. 1934); *In re Monson*, 127 F. Supp. 625 (W.D. Ky. 1955); *In re Tate-Jones & Co.*, 85 F. Supp. 971 (W.D. Pa. 1949).

65 U.C.C. § 2-702(3) (1962 version).

also holders of security interests in the goods being reclaimed.⁶⁶ Thus any creditor who relies on goods recently acquired by a buyer could protect himself from reclamation by obtaining a security interest in those goods under Article 9.⁶⁷

The persons most likely to be affected by reclamation are the vast bulk of unsecured creditors who have not relied in any meaningful way on the buyer's possession of the goods being reclaimed but who, it is argued, are prejudiced because reclamation reduces the assets of the bankrupt estate and thus reduces the amount available for distribution to the general creditors. It is said that reclamation gives the seller preferential treatment over other creditors who are similarly situated and that the other creditors are unfairly prejudiced.⁶⁸ While reclamation undoubtedly gives the seller preferential treatment, it is submitted that that preference is, on balance, justified. If the seller is not permitted to reclaim, the goods that he sold the bankrupt will be retained in the estate for the benefit of all of the unsecured and non-relying creditors. It might be more appropriate in those circumstances to ask what policies justify permitting the unsecured creditors to benefit, at the expense of the seller, from goods that the seller sold to the bankrupt while he was insolvent and that otherwise would not have been in the bankrupt estate. As long as there are provisions, as there are in the U.C.C., to reduce the risk of prejudice to creditors who might have actually relied on the buyer's possession of the goods, it seems that the equities are with the seller.

Professor Countryman responds to this argument by suggesting that, if the seller of goods has a right to reclaim, it is difficult to justify the different treatment of those who lend money or render services on credit to an insolvent but do not have a similar right to reclaim.⁶⁹ The distinction that Professor Countryman ignores is that it would be much more difficult, if not impossible, to structure a right to "reclamation" for a lender or one who renders services that did not involve substantially more serious prejudice to the rights of other creditors. Reclamation of goods results in the return to the seller of goods sold. Return in specie would be impossible for services rendered to the bankrupt. If one who rendered services were to be given some sort of reclamation right, it would have to be either a right to the value of the services or to the product that his services helped create. The latter solution would create potentially serious problems of

66 See, e.g., *In re Daley, Inc.*, 17 U.C.C. Rep. Serv. 433 (D. Mass. 1975) (in bankruptcy); *First-Citizens Bank & Trust Co. v. Academic Archives, Inc.*, 179 S.E.2d 850 (N.C. App. 1971). The definition of purchase under the U.C.C., which includes the taking by "mortgage, pledge, lien . . . or any other voluntary transaction creating an interest in property," is clearly broad enough to include a security interest, and a purchaser is defined as one who takes by purchase. See U.C.C. §§ 1-201(32), (33) (1962 version).

67 It probably is not even necessary that the security interest be perfected in order to prevail over a reclaiming seller. U.C.C. § 9-201 (1962 version) provides that security agreements are effective according to their terms unless otherwise provided in the U.C.C., and reclaiming sellers are not listed in U.C.C. § 9-301 (1962 version) as a type of party who prevails over the holder of an unperfected security interest. In an analogous situation, one court has held that the holder of an unperfected security interest in an automobile had priority over a seller attempting to reclaim under U.C.C. §§ 2-507 and 2-511, which give a seller the right to reclaim goods in a "cash sale" if they are delivered in return for payment by check and the check is dishonored. *Guy Martin Buick, Inc. v. Colorado Springs Nat'l Bank*, 511 P.2d 912 (Colo. App. 1973).

68 See, e.g., Bjornstad, *Reclamation of Goods by Unsecured Sellers in Bankruptcy Proceedings*, 24 *DRAKE L. REV.* 357, 363 (1975).

69 Countryman, *supra* note 5, at 455. Some courts have also questioned why sellers should be singled out for favorable treatment. See *In re Wetson's Corp.*, 17 U.C.C. REP. SERV. 423, 427 (S.D.N.Y. 1975) (in bankruptcy).

prejudice to others whose services or goods might also have contributed to the final product. On the other hand, since an attempt to place a value on services is always a somewhat speculative undertaking, permitting one to "reclaim" the value of services rendered to an insolvent would always involve a risk that the services would be overvalued, thus prejudicing other creditors by reducing the bankrupt estate by more than the value of the services rendered.⁷⁰ As for the loan analogy, it might be easier to return money lent to an insolvent, if the money can be identified through some form of tracing, but money received by an insolvent is much more likely than goods to be relied upon by other creditors who would then be prejudiced if the lender were given a right of reclamation. This is not to say that there necessarily are no circumstances in which it would be appropriate to give a lender or one who rendered services a right of reclamation. But it does suggest that additional difficulties are created that provide a rational basis for a legislature to conclude that sellers should have a right to reclaim while lenders and persons who render services should not.

Finally, critics of the U.C.C. § 2-702 right of reclamation often point out that a seller can always assure himself of the right to recover goods from an insolvent buyer by taking and perfecting a purchase-money security interest in the goods sold.⁷¹ The seller's right of reclamation is thus depicted as providing protection primarily for the careless and indolent. In many circumstances this characterization would be both inaccurate and unfair. Many sales between merchants are made on short-term credit of 30 or 60 days or less, and sellers frequently make such short-term credit sales without taking a security interest. Taking a security interest would involve various costs, including payment of filing fees, effort to prepare security agreements and financing statements, and delay in consummating sales. These costs, although possibly minor in any single transaction, could well be significant in the aggregate and in many situations would not be justified in light of the minimal risk of nonpayment normally incurred. Thus the extension of short-term unsecured credit is a reasonable and important mercantile practice. U.C.C. § 2-702 is an attempt to provide some minimal protection for unsecured sellers in the unusual situation where they are unpaid because their buyer was insolvent when the goods were received.⁷²

70 In addition to the general vagaries of measuring the value of services, by what standard would that value be measured? One typical measure would be the cost of obtaining similar services at the time they were rendered. But that cost might be significantly different from, and often more than, the increase in the value of the bankrupt estate attributable to those services. For example, a contractor might do home improvement work "worth" (in the sense of cost of obtaining similar services) \$1,000, but that work might increase the market value of the home by only \$800. If the contractor were given a "right of reclamation" based on the \$1,000 value of his services, other creditors would be prejudiced because the estate would be depleted by more than the \$800 increased market value attributable to the work. A solution might be to measure the reclamation right by the increase in the value of the estate attributable to the work rendered (\$800 in the example), but value in that sense is even more difficult to estimate accurately than is the cost of obtaining similar services.

71 Countryman, *supra* note 5, at 451.

72 The Commission on the Bankruptcy Laws of the United States apparently agrees, although its report was substantially completed prior to the decision in *In re Federal's*. Section 4-606 of the Commission's proposed new Bankruptcy Act, which invalidates certain statutory and common-law liens, contains an express exception preserving any lien

(1) which secures a debt incurred for the repair, preservation, shipment, storage, manufacture, or improvement of . . . property of the estate.

REPORT OF THE COMM'N ON BANKRUPTCY LAWS OF THE UNITED STATES, H. R. DOC. NO. 93-137, 93d Cong., 1st Sess., pt. II, at 164-66 (1973). The Commission's note cited *In re J. R.*

IV. The Right to Reclaim: A State-Created Priority?

Another way to attack the seller's right to reclaim, closely connected with the argument that reclamation is invalid as a statutory lien, is to assert that the right to reclaim is a state-created priority in violation of § 64(a) of the Bankruptcy Act,⁷³ which establishes priorities for the distribution of the bankrupt estate and which invalidates all priorities created by state law except certain priorities for landlords.⁷⁴ Most of the arguments presented in relation to statutory liens are also applicable to the claim that the right to reclaim amounts to a state-created priority. Bankruptcy courts have long recognized the seller's right to reclaim from an insolvent buyer who committed various types of "fraud" and have not considered that right to be an invalid state-created priority.⁷⁵ The expansion of the right to reclaim under the U.C.C., primarily by permitting reclamation without an affirmative showing of fraud, is not so significant as to justify a different result. Moreover, § 64 governs priorities in the distribution of the assets of the bankrupt estate, and the right to reclaim is not such a priority. It is more accurately considered a specific property interest in goods sold to the insolvent buyer, a type of property interest that the Congress intended to preserve.⁷⁶ In fact, the right to reclaim is essentially a right to rescind the contract with the buyer and retake the goods. As one court recently pointed out in rejecting the argument that U.C.C. § 2-702 is invalid as a state-created priority, nothing in the Bankruptcy Act prevents a state from expanding the grounds for rescission of a contract beyond those provided at common law.⁷⁷

Nieves & Co., 446 F.2d 188 (1st Cir. 1971), which invalidated the Puerto Rico vendor's lien, and appears intended to preserve both the Puerto Rico vendor's lien and the seller's right to reclaim from attack as a statutory lien. It would have been preferable, however, if a term broader than "manufacture" had been used in the proposed statute. For a discussion of *Nieves*, see note 37 *supra*.

The tentative draft of the proposed Bankruptcy Act presently being considered by the House Judiciary Committee would clearly validate the U.C.C.'s 10-day right of reclamation, although it appears to leave open to question the right to reclaim beyond 10 days when there is a misrepresentation of solvency. Section 546(b) of the proposed Act provides:

The rights and powers of the trustee under sections 544, 545, and 547 of this title are subject to any statutory or common-law right of a seller, in the ordinary course of such seller's business, of goods to the debtor to reclaim such goods if the debtor has received such goods on credit while insolvent, but such a seller may not reclaim any such goods unless such seller demands reclamation of such goods within ten days after receipt of such goods by the debtor.

H.R. 6, 95th Cong., 1st Sess. § 546(b) (1977).

⁷³ 11 U.S.C. § 104 (1970).

⁷⁴ Both the bankruptcy judge and the district court concluded in *Federal's* that U.C.C. § 2-702 was also invalid as a state-created priority. See *In re Federal's, Inc.*, 12 U.C.C. REP. SERV. 1142 (E.D. Mich. 1973) (in bankruptcy), *aff'd*, 402 F. Supp. 1357 (E.D. Mich. 1975). See also Bjornstad, *supra* note 68, at 367-68; Countryman, *supra* note 5, at 444, 452. There have been other decisions invalidating various state liens as state-created priorities, but the liens in question were broad ones attaching to large portions of the bankrupts' assets. See *Elliott v. Bumb*, 356 F.2d 749 (9th Cir.), *cert. denied sub nom. Schutzbank v. Elliott*, 385 U.S. 829 (1966); *N.W. Day Supply Co. v. Valenti*, 343 F.2d 756 (1st Cir. 1965).

⁷⁵ See notes 1-3 *supra* and accompanying text.

⁷⁶ See notes 43-56 *supra* and accompanying text for a discussion of the legislative history of the statutory lien provisions, which reflects a congressional purpose to preserve property rights and to invalidate only true priorities. Professor Braucher also concluded that the seller's right to reclaim is an interest in property and not a priority violative of § 64(a). See Braucher, *supra* note 17, at 1295-96.

⁷⁷ See *In re Telemart Enterprises, Inc.*, 524 F.2d 761, 766 (9th Cir. 1975), *cert. denied sub nom. Holzman v. Alfred M. Lewis, Inc.*, 96 S. Ct. 1466 (1976).

V. The Right to Reclaim: A Voidable Preference?

It is easy to see how one might argue that the seller's right to reclaim would, in appropriate circumstances, amount to a voidable preference under § 60 of the Bankruptcy Act.⁷⁸ A voidable preference is a transfer of nonexempt property made or suffered by the bankrupt for or on account of an antecedent debt within four months of bankruptcy to or for the benefit of a creditor and while the debtor was insolvent, if the effect of the transfer was to enable the transferee to obtain a greater percentage of his debt than other creditors of the same class and if the transferee, at the time of the transfer, had reasonable cause to believe that the debtor was insolvent.⁷⁹ Although it would appear possible to fit the right to reclamation within this definition, the major commentators are in almost unanimous agreement that the seller's right to reclaim normally is not a voidable preference.⁸⁰

The justification for this result traditionally proffered in the cases is that when the seller reclaims there is no transfer from a debtor to a creditor. The buyer never had title since the goods were not his until he paid for them.⁸¹ One writer has recently suggested that this argument is no longer valid because, under U.C.C. § 2-401(2), title passes to the buyer on delivery, absent an explicit contrary agreement.⁸² This change in the rules relating to passage of title, however, should not lead to the conclusion that the right to reclaim is now a voidable preference. The title retention argument made in the cases was always somewhat fictional since, even under pre-U.C.C. law, a buyer on open credit had effective title for most purposes, although that title was voidable in some circumstances by a reclaiming seller. Essentially the same situation presently exists under the U.C.C., although the term "voidable title" is not used expressly.⁸³ Moreover, the fundamental basis of the general agreement that reclamation is not a voidable preference is the realization that other creditors normally are not unfairly prejudiced when a seller reclaims goods for which he has not been paid; on the contrary, permitting other creditors to benefit from goods delivered but not paid for would in fact be unfair to the seller.⁸⁴ These facts are not affected by any

78 11 U.S.C. § 96 (1970).

79 *Id.* See J. WHITE & R. SUMMERS, *supra* note 7, § 24-4.

80 See, e.g., 3 COLLIER, *supra* note 1, ¶ 60.18 at 843-44; 3A DUSENBERG & KING, *supra* note 1, § 13.03(4)(d)(iv), at 13-43-44; MACLACHLAN, BANKRUPTCY 307 (1956).

81 See, e.g., Ullman v. N. Sobel, Inc., 47 F.2d 612, 614 (S.D.N.Y. 1931); Fisher v. Shreve, Crump & Low Co., 7 F.2d 159 (D. Mass. 1925).

82 Bjornstad, *supra* note 68, at 364.

83 See *In re Telemart Enterprises, Inc.*, 524 F.2d 761, 765 (9th Cir. 1975), *cert. denied sub nom. Holzman v. Alfred M. Lewis, Inc.*, 96 S. Ct. 1466 (1976). In this case the court held that, because the buyer's title was in effect voidable, there would be no transfer on account of an antecedent debt and therefore the seller's right to reclaim could not be a voidable preference. 524 F.2d at 764.

84 Professor King has stated the argument this way:

The delivery of the goods is usually in contemplation of immediate or nearly immediate payment without knowledge of the buyer's inability to pay. Had the buyer performed, there would have been no diminution of his estate because of that which was obtained by it; to create a voidable preference because of the inability to pay would be to give the general creditors an unnecessary windfall marked by the proceeds obtained from the sale of the delivered goods.

King, *Voidable Preferences and the Uniform Commercial Code*, 52 CORNELL L. Q. 925, 939 n. 53 (1967).

Obviously the situation is reversed, and other creditors might be seriously prejudiced, if the

modifications of the technical rules concerning passage of title.

VI. Conclusion

Although bankruptcy courts have long recognized the right of a seller in many circumstances to reclaim goods sold to an insolvent buyer, the current version of the seller's right to reclaim, embodied in U.C.C. § 2-702, has been subject to attack on many fronts. The most recent and serious challenges have been in the form of assertions, accepted by some courts⁸⁵ and rejected by others,⁸⁶ that the U.C.C. § 2-702 right of reclamation is invalid against the trustee in bankruptcy as a statutory lien or a state-created priority. Challenges to the seller's right to reclaim are certainly understandable, for reclamation does, to some extent, give a seller preferential treatment over other unsecured creditors of the bankrupt. This article, however, has attempted to demonstrate that, when viewed in light of the legislative history and the policies of the Bankruptcy Act, the seller's right to reclaim is not a statutory lien within the prohibitions of § 67 and does not contravene other provisions of the Bankruptcy Act. On the contrary, the reclamation right found in U.C.C. § 2-702 is a reasonable one. It does not unfairly prejudice other creditors of the bankrupt buyer and affords only minimal protection for sellers who sell on short-term unsecured credit—a common and important commercial practice—and who are unpaid because their buyer was insolvent when the goods were delivered.

seller fails to reclaim within the 10-day period of U.C.C. § 2-702 or to reclaim quickly after discovery of a written misrepresentation of solvency that eliminates the 10-day limitation on reclamation. If a seller fails to act promptly, a later attempt at reclamation may well be held a voidable preference. See *In re Colacci's of America, Inc.*, 490 F.2d 1118 (10th Cir. 1974) (reclamation amounts to voidable preference when seller permitted buyer to retain goods for four months after learning of buyer's inability to pay).

85 See *In re Perskey & Wolf, Inc.*, — F. Supp. —, 19 U.C.C. REP. SERV. 812 (N.D. Ohio 1976); *In re Giltex, Inc.*, — F. Supp. —, 17 U.C.C. REP. SERV. 887 (S.D.N.Y. 1975); *In re Good Deal Supermarkets, Inc.*, 384 F. Supp. 887 (D.N.J. 1974); *In re Wetson's Corp.*, 17 U.C.C. REP. SERV. 423 (S.D.N.Y. 1975) (in bankruptcy); *In re Federal's, Inc.*, 12 U.C.C. REP. SERV. 1142 (E.D. Mich. 1973) (in bankruptcy), *aff'd*, 402 F. Supp. 1357 (E.D. Mich. 1975).

86 See *In re Telemart Enterprises, Inc.*, 524 F.2d 761 (9th Cir. 1975), *cert. denied sub nom.* *Holzman v. Alfred M. Lewis, Inc.*, 96 S. Ct. 1466 (1976). *In re National Bellas Hess, Inc.*, 17 U.C.C. REP. SERV. 430 (S.D.N.Y. 1975) (in bankruptcy).