

University of Illinois College of Law
Law and Economics Working Papers

Year 2005

Paper 46

The Brave New World of Bankruptcy
Preferences

Charles J. Tabb*

*University of Illinois College of Law, ctabb@law.uiuc.edu

This working paper is hosted by The Berkeley Electronic Press (bepress) and may not be commercially reproduced without the permission of the copyright holder.

<http://law.bepress.com/uiuclwps/art46>

Copyright ©2005 by the author.

The Brave New World of Bankruptcy Preferences

Charles J. Tabb

Abstract

This article examines in detail the amendments made to the bankruptcy preference laws by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. The author was Reporter for a nationwide survey of the preference laws conducted in the late 1990s by the American Bankruptcy Institute, and which recommended several amendments that eventually did become law in the 2005 Act. The article first examines the genesis of the 2005 amendments in that earlier study, and in the Report of the National Bankruptcy Review Commission, which relied heavily on the ABI Report. Then the article analyzes in depth the specific amendments to the preference law, namely: (1) the creation of a safe harbor for small preferences; (2) changes to the venue rules for preference actions; (3) modification of the defense for “ordinary course of business” transfers; (4) changes to the enabling loan safe harbor; (5) amendments to the timing rules regarding liens; (6) the exclusion of payments pursuant to alternative repayment plans; and (7) an attempt by Congress, again, to fix problems relating to recovery from non-insider parties, as against whom the transfer was not avoidable, as first made notorious in the *Deprizio* case

Abstract:

The Brave New World of Bankruptcy Preferences

by Charles J. Tabb, Alice Curtis Campbell Professor of Law and the Associate Dean for Academic Affairs at the University of Illinois College of Law

Forthcoming in AMERICAN BANKRUPTCY INSTITUTE LAW REVIEW

This article examines in detail the amendments made to the bankruptcy preference laws by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. The author was Reporter for a nationwide survey of the preference laws conducted in the late 1990s by the American Bankruptcy Institute, and which recommended several amendments that eventually did become law in the 2005 Act. The article first examines the genesis of the 2005 amendments in that earlier study, and in the Report of the National Bankruptcy Review Commission, which relied heavily on the ABI Report. Then the article analyzes in depth the specific amendments to the preference law, namely: (1) the creation of a safe harbor for small preferences; (2) changes to the venue rules for preference actions; (3) modification of the defense for “ordinary course of business” transfers; (4) changes to the enabling loan safe harbor; (5) amendments to the timing rules regarding liens; (6) the exclusion of payments pursuant to alternative repayment plans; and (7) an attempt by Congress, again, to fix problems relating to recovery from non-insider parties, as against whom the transfer was not avoidable, as first made notorious in the *Deprizio* case.

The Brave New World of Bankruptcy Preferences

Copyright © 2005 by

Charles J. Tabb

Alice Curtis Campbell Professor of Law and Associate Dean for Academic Affairs
University of Illinois College of Law

Introduction

On April 20, 2005, President Bush signed into law S. 256, the “Bankruptcy Abuse Prevention and Consumer Protection Act of 2005” (hereafter “BAPCPA” or “2005 Act”).¹ While the consumer amendments garnered the lions’ share of public attention, significant changes were made to almost every area of bankruptcy law. This paper addresses the changes effected to bankruptcy preference law and practice.

Origins of Key Amendments: The American Bankruptcy Institute Preference Study

The most important changes to preference law in BAPCPA had their genesis in a study sponsored by the American Bankruptcy Institute, the Report of which was published in May 1997.² That study was the final product of a Task Force on Preferences formed in May 1995 by the Unsecured Trade Creditor Committee of the American Bankruptcy Institute, chaired by Joseph S.U. Bodoff of Boston. Two surveys were mailed; one (the “credit providers survey”) to 1200 members of the National Association of Credit Managers and 386 members of the Commercial Finance Association, and the second (the “practitioners’ survey”) to one thousand members of the American Bankruptcy Institute. Response was good: 467 (29.4%) of the credit providers returned a completed survey and 356 (35.6%) of the practitioners did so.

The study was motivated by the following concerns, as explained in the Chair’s Introduction to the Report:

While many supported the concept of recovering certain transfers made shortly before a bankruptcy filing, increasingly, complaints were voiced that the preference law was unfair and should be modified drastically or eliminated completely. Even the most ardent supporters of the preference law expressed the view that some change was mandated. The concerns ranged from claims that the law was not providing for a meaningful redistribution of property, to abuses in the manner in which preference claims were pursued, to claims that the law, through uncertain concepts like “ordinary course of business,” fostered unnecessary and expensive litigation. These concerns, in varying degrees, were expressed by trade creditors, lenders, and bankruptcy practitioners alike.³

¹ S. 256, 109 P.L. 8, 119 Stat. 23 (109th Cong., 1st Sess. 2005).

² American Bankruptcy Institute Task Force on Preferences, Prof. Charles Jordan Tabb, Reporter, PREFERENCE SURVEY REPORT (ABI Bankruptcy Reform Study Project) (May 1997) (hereafter “Preference Survey report” or “ABI Report”).

³ *Id.*, Introduction by Joseph S.U. Bodoff, Chair.

The “Preference Survey Report,” for which I served as Reporter, made four “Recommendations”⁴ for changes to the preference law and put forward nine “Other Ideas for Consideration.”⁵ Several of these Recommendations and Other Ideas soon were adopted as Recommendations in the October 1997 Report of the National Bankruptcy Review Commission.⁶ Those Recommendations then were incorporated almost verbatim in each version of the many bankruptcy reform bills that were considered by Congress from 1997 to 2005, and were enacted as part of BAPCPA.

Specifically, the following three suggestions of the ABI Report were adopted by the NBRC Report and now have been made law by BAPCPA. They are the most important of the 2005 amendments regarding bankruptcy preference litigation.

First, ABI Report Recommendation One: *Limit preference actions to cases involving a minimum dollar amount.*⁷ The suggested floor dollar amount was \$5,000. The NBRC Report adopted this as its own Recommendation 3.2.1, *Minimum Amount to Commence a Preference Action under 11 U.S.C. § 547*: “11 U.S.C. § 547 should provide that \$5,000 is the minimum aggregate transfer to a noninsider creditor that must be sought in a nonconsumer debt preference avoidance action.”⁸

Second, ABI Report “Idea for Consideration” Thirteen: *Amend the venue rules to protect defendants from having to defend in a distant forum, at least when the amount in controversy is below a stated amount.*⁹ The Report noted that, though the venue amendment addressed a similar problem as the minimum floor amount, namely giving preference defendants more protection from nuisance suits, it might well be worth doing both, with the venue amount in controversy being set at a higher amount than the floor minimum.¹⁰ The NBRC Report did precisely this, in its Recommendation 3.2.2, *Venue of Preference Actions under 28 U.S.C. § 1409*: “28 U.S.C. § 1409 should be amended to require that a preference recovery action against a noninsider seeking less than \$10,000 must be brought in the district where the creditor has its principal place of business. This Recommendation applies to nonconsumer debts only.”¹¹

⁴ *Id.* at 25-27.

⁵ *Id.* at 27-31.

⁶ National Bankruptcy Review Commission Final Report, Prof. Elizabeth Warren, Reporter, *BANKRUPTCY: THE NEXT TWENTY YEARS* (October 20, 1997) (hereafter “NBRC Report”).

⁷ ABI Report, *supra* note 2, at 25.

⁸ NBRC Report, *supra* note 6, at 794.

⁹ ABI Report, *supra* note 2, at 30.

¹⁰ *Id.* at 31.

¹¹ NBRC Report, *supra* note 6, at 794.

Third, ABI Report Recommendation Four: *Clarify the ordinary course of business defense*.¹² The road to clarity, the Report suggested, was through more objectification. The NBRC Report followed that road in its Recommendation 3.2.3, *Ordinary Course of Business Exception under 11 U.S.C. § 547(c)(2)(B)*: “11 U.S.C. § 547(c)(2)(B) should be amended to provide a disjunctive test for whether a payment is made in the ordinary course of the debtor’s business if it is made according to ordinary business terms.”¹³

Almost eight years after the ABI Report was published, these recommendations were enacted into law.

The Amendments

In the 2005 Bankruptcy Act, several significant amendments were made to the bankruptcy and jurisdictional laws affecting preferences, including the three described above, as well as four others. The three noted above are described first.

1. *Small Preference Safe Harbor*

A new exception, section 547(c)(9), precludes the trustee from avoiding as a preference a transfer “if, in a case filed by a debtor whose debts are not primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than \$5,000.”¹⁴ In short, section 547(c)(9) ends preference liability in business cases for “small” preferences, defined as those below \$5,000. For creditors in consumer cases, the new small preference safe harbor offers no succor; creditors in those cases can look only to the much smaller \$600 safe harbor.¹⁵ Note that the safe harbor applies to all “property.”

2. *Venue Protections*

The venue rules for “proceedings” – which include preference avoidance actions – in 28 U.S.C. section 1409 were amended in 2005 to give substantially greater protection to creditor defendants. The default rule for the venue of proceedings is that the bankruptcy trustee can sue in “the district court in which such case is pending,”¹⁶ meaning the home bankruptcy court, irrespective of where the creditor defendant is located. Prior to the 2005 Act, under an exception to this default rule, a creditor was entitled to be sued where the *creditor* resided if the amount sued for was less than \$1,000, or for a consumer debt of less than \$5,000.¹⁷ The 2005 Act greatly expands the protective reach of section 1409(b), raising the threshold amount for

¹² ABI Report, *supra* note 2, at 27.

¹³ NBRC Report, *supra* note 6, at 794.

¹⁴ 109 P.L. 8, § 409(3), *codified at* 11 U.S.C. § 547(c)(9).

¹⁵ 11 U.S.C. § 547(c)(8).

¹⁶ 28 U.S.C. § 1409(a).

¹⁷ 28 U.S.C. § 1409(b).

consumer debts from \$5,000 to \$15,000, and creating a new rule entitling non-insider defendants on non-consumer debts to be sued where they reside if the debt is less than \$10,000.¹⁸

3. *Ordinary Course Defense*

In section 547(c)(2), the defense for transfers made in the ordinary course of business has been changed dramatically, by the simple expedient of changing an “and” to an “or.”¹⁹ Prior to the 2005 Act, a preference defendant invoking the ordinary course defense had to show *both* that the transfer was “made in the ordinary course of business or financial affairs of the debtor and the creditor” “*and*” “made according to ordinary business terms.” Courts understood the former provision to require proof of the ordinariness of the transfer subjectively, in light of the established practices between *this* creditor and the debtor, and the latter to require proof that the transfer comports with the objective practices in the industry at large.²⁰ The trick, though, was that both had to be established. Now, with the switch from the conjunctive “and” to the disjunctive “or,” *either* proof of subjective *or* objective ordinariness will suffice.

4. *Enabling Loan Safe Harbor*

Commercial law historically has been solicitous of “purchase money” liens, where the creditor takes as security the very collateral for which the creditor loaned the money that enabled the debtor to purchase that property (thus the colloquialism “enabling loan”). One way in which such purchase money liens or enabling loans have been advantaged is to give the secured creditor a grace period to perfect and still maintain priority as against third parties whose own rights arise in the interim between the creation of the lien and its subsequent perfection. The bankruptcy preference law includes this grace period for perfecting enabling loans.²¹ Before the 2005 amendments, the safe harbor for enabling loans, section 547(c)(3), required that the creditor’s security interest be perfected on or before 20 days after the debtor received possession of the collateral. The 2005 Act changed the grace period to perfect in section 547(c)(3)(B) from 20 days to 30 days.²²

5. *Timing Changes*

In preference litigation, it is critical to ascertain when a transfer is “made,” since a creditor is potentially vulnerable to avoidance only for a limited discrete time period after the

¹⁸ *Id.* § 410, *codified at* 28 U.S.C. § 1409(b).

¹⁹ *Id.* § 409(1), *codified at* 11 U.S.C. § 547(c)(2).

²⁰ *See* Charles Jordan Tabb, *THE LAW OF BANKRUPTCY*, § 6.18, at 386-88 (Foundation Press 1997). *See, e.g., In re Tolona Pizza Products Corp.*, 3 F.3d 1029 (7th Cir. 1993).

²¹ *See id.* § 6.19, at 389-91.

²² 109 P.L. 8, § 1222, *codified at* 11 U.S.C. § 547(c)(3)(B).

making of the transfer (90 days generally,²³ one year for insiders²⁴). Also, only transfers on account of *antecedent* debts are vulnerable,²⁵ and thus if a transfer is “made” at the time the debt arises, there is no preference.²⁶ For certain types of transfers (especially liens), there may be a potential difference between the time the transfer is effective as between the transferor and transferee, and the time the transfer is perfected so as to be effective against third parties.²⁷

Section 547(e)(2) contains timing rules for such instances. Prior to the 2005 Act, under section 547(e)(2)(A), if a transfer was perfected within 10 days of when it became effective as between the transferor and transferee, it was deemed made for preference purposes at that earlier time, rather than at the time of perfection. If perfected after the 10-day grace period, then under subsection (e)(2)(B) it was deemed made at the later time of perfection. The 2005 Act extended the 10-day grace period of section 547(e)(2) to 30 days.²⁸ This change partially coordinates with the extension of the enabling loan grace period noted above.

6. *Alternative Repayment Plan Payments Excluded*

The 2005 Act created an entirely new preference safe harbor for transfers “made as a part of an alternative repayment schedule between the debtor and any creditor of the debtor created by an approved nonprofit budgeting and credit counseling agency.”²⁹ Curiously, this safe harbor was inserted in a new subsection (h) in section 547, rather than being grouped with the other safe harbors in subsection (c).

7. *Deprizio Fixed (Again)*

One court decision can create a lot of work for Congress; consider *Levit v. Ingersoll Rand Fin. Corp.*,³⁰ known generally as the “Deprizio” case (the debtor’s name). The Seventh Circuit held in that case that the trustee could *recover* under 11 U.S.C. section 550(a) from a non-insider initial transferee even though the preference was not avoidable as to that non-insider, but was only avoidable as to an insider. In 1994, the recovery section, section 550, was amended by

²³ 11 U.S.C. § 547(b)(4)(A).

²⁴ 11 U.S.C. § 547(b)(4)(B).

²⁵ 11 U.S.C. § 547(b)(2).

²⁶ *See* Tabb, *supra* note 20, § 6.13, at 369-70.

²⁷ *See id.* § 6.9, at 354-55.

²⁸ 109 P.L. 8, § 403, *codified at* 11 U.S.C. § 547(e)(2).

²⁹ *Id.* § 201(b), *codified at* 11 U.S.C. § 547(h).

³⁰ 874 F.2d 1186 (7th Cir. 1989).

adding section 550(c) to preclude recovery from such a non-insider.³¹ However, that “fix” was incomplete, as it did not help the non-insider when no “recovery” was required, as in the case where a lien is simply voided.³² So, in the 2005 Act Congress tried again, adding new section 547(i): “If the trustee avoids under subsection (b) a transfer made between 90 days and 1 year before the date of the filing of the petition, by the debtor to an entity that is not an insider for the benefit of a creditor that is an insider, such transfer shall be considered to be avoided under this section only with respect to the creditor that is an insider.”³³

Assessment and Analysis of the Amendments

1. Small Preference Safe Harbor

Consider the following Hypothetical A. Creditor, a trade supplier located in Maine, regularly ships goods on credit to Debtor, located in Hawaii. The invoices require payment within 20 days; however, for a period of several years Debtor routinely pays Creditor between 30 and 35 days. In the 90 days before Debtor files bankruptcy, Debtor makes three payments aggregating \$5,100 on account to Creditor: \$1,800 on Day 80 (33 days after shipment); \$1,600 on Day 50 (30 days after shipment); and \$1,700 on Day 15 (35 days after shipment). After Debtor files chapter 7 bankruptcy in the District of Hawaii, the bankruptcy trustee commences suit in the District of Hawaii against Creditor. Creditor believes it has an obviously valid “ordinary course” defense under section 547(c)(2) and so answers. The trustee offers to settle for \$3,000. For Creditor, the cost of defending the suit for such a relatively small amount, at such a great distance, is hardly worth it; in short, Creditor feels pressured or coerced into accepting the settlement of what it also believes is an ill-founded claim.

Such cases are the focus of the first two (and in some respects all three) major amendments to the preference laws. As will become evident, these amendments are closely related. Concerning the sort of case just described, the ABI Report notes:

A ... significant and pervasive problem identified is that creditors often feel pressured into making nuisance settlements, even if the action is of dubious validity. ... One of the common problems identified in the survey responses was that of coercive preference litigation. ... When suits are brought for very small amounts, the pressure on the preference defendant to settle is enormous.³⁴

An easy, clean solution is simply to set a floor dollar amount below which the creditor defendant has an absolute defense to a successful preference action. The ABI Report suggested

³¹ Bankruptcy Reform Act of 1994, § 202, P.L. 103-394, 108 Stat. 4106 (103rd Cong., 2d Sess. 1994).

³² See H.R. Rep. No. 109-31, at – (109th Cong., 1st Sess. 2005) (discussing § 1213 of BAPCPA). See also Tabb, *supra* note 20, §6.13, at 368-69.

³³ 109 P.L. 8, § 1213(2), codified at 11 U.S.C. § 547(i).

³⁴ ABI Report, *supra* note 2, at 25.

\$5,000 as the minimum amount; the 2005 Act so provides in new section 547(c)(9).

Establishing such a floor minimum amount is hardly a new idea. The first Bankruptcy Review Commission in 1973 suggested a \$1,000 floor for transfers to non-insiders, in consumer and non-consumer cases alike.³⁵ In an earlier article in which I questioned the wisdom of the ordinary course exception and recommended its repeal, I suggested as a possible second-best alternative adopting a comprehensive small preference exception, echoing the Commission in recommending that the safe harbor be available in both consumer and non-consumer cases.³⁶ I suggested an amount much smaller than the \$5,000 that just became law, something more in line with the \$1,000 suggested by the first Review Commission.

However, Congress ignored the Review Commission's suggestion for a floor amount in the 1978 Code, preferring instead to defer to the discretion of trustees in making the cost-benefit assessment, and indulging in the hope that trustees would not bring cost-ineffective actions. The problem with that thinking, though, is that the cost calculus is not symmetrical between preference plaintiff and defendant, especially given the home court venue advantage; the trustee-plaintiff can bring greater economic pressure to bear on the creditor-defendant to settle than the trustee would suffer if the creditor calls the trustee's bluff and contests. Consider the hypothetical above; surely the economic bias runs strongly in the trustee's favor.

In 1984 Congress did take a small first step along the small-preference-safe-harbor path, adding the \$600 safe harbor applicable only in consumer cases, now codified at 11 U.S.C. section 547(c)(8). The push for that amendment came from the consumer credit industry, which was worried that the then-existing 45-day rule that was originally part of the ordinary course exception unfairly exposed consumer credit providers with a great-than-45-day credit cycle to preference liability.³⁷ Of course, since the 45-day limit in section 547(c)(2) itself also was repealed in 1984, the proffered logic for the new small consumer preference exception was stillborn.

The 1984 exception did not apply to non-consumer cases, notwithstanding the first Review Commission's recommendation for a small preference exception applicable to all types of cases. When the driving motivation for the exception is viewed as anti-nuisance suit protection, as the ABI Report and NBRC Report contemplate, then little reason exists to differentiate between the types of cases in principle – certainly not if viewed from the perspective of the creditor-defendant. One might still draw the dollar amount line differently for business and consumer cases, if the perception is that the interests of other creditors as well as the case dynamics are sufficiently different. Thus we now have a system with a \$600 floor in

³⁵ REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 197, 93rd Cong., 1st Sess. Pt. II, § 4-607(b)(1), at 166.

³⁶ Charles Jordan Tabb, *Rethinking Preferences*, 43 S.C.L. Rev. 981,1033 (1992).

³⁷ See Vern Countryman, *The Concept of a Voidable Preference in Bankruptcy*, 38 Vand. L. Rev. 713, 814 (1985). The original ordinary course exception required the transfer to be made within 45 days of when the debt was incurred.

consumer cases and a \$5,000 floor in non-consumer cases. This differentiation might be defensible in that prospective preference recoveries between \$600 and \$5,000 may be significant assets of the estate in consumer cases, but much less important in most business cases. Thus, we might care a bit less about alleviating settlement pressure on a defendant in a consumer case when the prospective recovery is of what would be a major asset of the estate.

What impact will the new \$5,000 safe harbor have? Is it consistent with a sound preference policy? As the NBRC Report explained, “[t]he tension, therefore, is to develop efficient procedures to restrain abusive litigation techniques by the trustee without interfering with the policy goals of the preference power itself.”³⁸ Those goals “can be summed up as equality of treatment of creditors and deterring the ‘race to the courthouse’ by creditors attempting to improve their position vis-à-vis the debtor on the eve of bankruptcy.”³⁹ The ABI Report urged that “allowing creditors to retain small transfers would not seriously affect the redistribution and deterrence rationales underlying the preference laws, because so little is at stake.”⁴⁰ The NBRC Report likewise argues that “[r]aising the minimum aggregate transfer sought to \$5,000 is consistent with current preference policies. Aggregate transfers of less than that amount are unlikely to create a substantial deviation from equality of treatment for creditors and it is doubtful that such a small transfer would pose a significant threat of premature scavenging of the estate’s assets.”⁴¹

But is this so? Even though I served as Reporter for the ABI Report, in that role I was indeed *reporting* the sentiments of those surveyed. And even then, almost half of the survey respondents favored a threshold of some amount *less* than \$5,000.⁴² Personally I confess to being a skeptic regarding the wisdom of what seems a fairly high threshold amount (\$5,000). Perhaps my suggestion in 1992 for a \$1,000 floor would be a bit low in today’s dollars (indeed that was the same amount suggested back in 1973 by the first Commission), but I would be more comfortable with at most a \$2,000 amount.

That \$2,000 figure also corresponds to what the ABI survey respondents identified as the lowest plausible cost-effective point for *bringing* a preference action.⁴³ That suggests that many believe it is *not* a coercive nuisance suit if in the \$2,000 and up amount, but rather a *real* and valuable economically rational action by the trustee. If so, then the “strike suit” complaint rings hollow. Perhaps not, though. First, as explained above, the economic impact on the trustee plaintiff and creditor defendant is not symmetrical – an action might be economically rational

³⁸ NBRC Report, *supra* note 6, at 796.

³⁹ *Id.*, citing Tabb, *supra* note 36, at 986.

⁴⁰ ABI Report, *supra* note 2, at 25.

⁴¹ NBRC Report, *supra* note 6, at 798.

⁴² ABI Report, *supra* note 2, at 10.

⁴³ *Id.* at 10-11.

for a trustee to pursue but not for a creditor to defend – especially if the suit can be brought in the trustee’s home court venue. Second, litigation costs can quickly get past the \$2,000 amount, and it may be that drawing the line a bit more generously (to preference defendants) is a prudent, fair, and judicially efficient “rough justice” line.

We still might worry, though. As the NBRC Report itself recognizes in discussing “competing considerations,” the concern is that given the small size of most business cases, there rarely are many transfers as high as \$5,000, and thus preference litigation would largely be eliminated in the bulk of business cases.⁴⁴ This would substantially undermine the equality goal – indeed, it is disingenuous to suggest otherwise – and might well encourage aggressive pre-petition debt collection efforts for amounts of a few thousand dollars, but slightly below \$5,000; at the least the “deterrence” rationale is weakened. In many cases the possible preference recoveries are one of the only meaningful potential assets of the bankruptcy estate.

At bottom, this is essentially an empirical question. The work of Professors Lawless and Warren suggests that small business cases are much more prevalent than believed,⁴⁵ which suggests that the negative impact of the \$5,000 floor might be higher than anticipated. We will have to wait and see whether Congress has found just the right heat for the porridge to balance the need for trade creditors to be freed from coercive nuisance litigation without undermining preference goals of equality and deterrence in smaller business cases.

One response the NBRC made to the sort of concerns just noted was that the \$5,000 floor requires an *aggregation* of transfers made during the preference period.⁴⁶ Apparently, the NBRC contemplated that in a case like Hypothetical A described earlier in this section, where the preference defendant received three transfers totaling \$5,100, that defendant would *not* be protected by the new safe harbor. Is that assumption accurate? The same statutory language appears in both the prior small preference exception of \$600 for consumer cases and the new safe harbor, so judicial precedent under the prior safe harbor would be relevant. The relevant language favoring aggregation is that the statute says “*aggregate value* of all property,” but opposing is a reference to “*such transfer*,” as well as the predicate in subsection (c) that a trustee may not avoid “*a transfer*.” Read literally, the latter references seem to point to a singular limitation to *one* transfer, thus precluding aggregation in a case such as the hypothetical in this section. The “aggregation” language could be explained as consistent with this singular “transfer” language where the debtor makes multiple but coordinated transfers as an intended single act of payment on a debt. For example, in Hypothetical A, assume that on Day 80, instead of giving Creditor a check for \$1,800, Debtor returned goods worth \$800 and sent a check for \$1000 to repay the single outstanding debt of \$1,800. One might say that the operative “aggregate” “transfer” was \$1,800. That, however, is a much different matter than saying that

⁴⁴ *Id.*

⁴⁵ See Robert M. Lawless and Elizabeth Warren, *The Myth of the Disappearing Business Bankruptcy*, 93 Cal. L. Rev. (forthcoming 2005).

⁴⁶ NBRC Report, *supra* note 6, at 798.

the distinct transfers on Days 80, 50 and 15 were “such transfer” or “a transfer.” Such an interpretation of the statute is hard to square with the statutory language. Perhaps one might try to assuage this concern by invoking the rule of construction that “the singular includes the plural,”⁴⁷ although it is questionable whether that rule of construction can do that much work. However, the generous (for trustees) “aggregation” reading is responsive to and consistent with the policy concern of alleviating coercive preference litigation pressure, as gauged by the amount in controversy. On that score, the preference defendant who received three transfers totaling \$5,100 and is sued for avoidance and recovery of all three is no different from a defendant who receives a single \$5,100 transfer. We are sure that the latter creditor is not protected by section 547(c)(9); is there any meaningful reason to treat the former, who receives three transfers, differently?

Whatever the nuance of the statute, the cases have split; with some allowing aggregation, and others not.⁴⁸ The trend appears to favor aggregation, and my suspicion is that courts anxious to avoid undue evisceration of preference policy might so hold, especially as emboldened by the NBRC commentary.

Note, though, that if aggregation is allowed as just contemplated, a creditor such as the one envisaged in Hypothetical A would suffer a severe penalty from the receipt of the final transfer in a series of transfers that pushes the creditor’s aggregate total over the \$5,000 mark. Our Creditor who has received two transfers of \$3,400 would, at that point, be immune from preference liability because of section 547(c)(9). Upon receipt of the final \$1,700 transfer, though, Creditor loses its section 547(c)(9) defense entirely. Note that invocation of the \$5,000 safe harbor is an all-or-nothing situation; it is not a *credit* against preference liability. Thus our Creditor who had received \$5,100 in transfers would be potentially liable for \$5,100 in preferences, not just the \$100 extra over the \$5,000 safe harbor. Prior to any bankruptcy, ultra-cautious creditors of a financially distressed debtor might need to keep their own running total of potentially preferential payments received within the past 90 days and either refuse or remit back to the debtor offered transfers that would push them over \$5,000. Thus in Hypothetical A a our Creditor would still be protected (assuming the aggregation view is followed) if it only received a third transfer of \$1599 (for a total of \$4,999), rather than \$1,700 (for a total of \$5,100).

Another interesting and related question is the extent to which the \$5,000 safe harbor will be applied in conjunction with other preference defenses, especially the subsequent advance for new value defense of 11 U.S.C. section 547(c)(4). Consider Hypothetical B: Creditor is a trade supplier of Debtor. On May 1, Debtor’s balance owing on account to Creditor is \$10,000. On May 1, Debtor pays Creditor \$8,000 on the \$10,000 outstanding balance (assume that this payment does not qualify for “ordinary course” protection). On May 15, Creditor ships \$3,500 in goods to Debtor on credit; assume that this \$3,500 transfer would otherwise qualify for the “new value” defense of subsection (c)(4). On July 1, Debtor files bankruptcy. How much, if any, is Creditor’s preference liability? \$4,500? Zero?

⁴⁷ 11 U.S.C. § 102(7).

⁴⁸ See discussion in Tabb, *supra* note 20, § 6.24, at 403-04.

Before 2005, the analysis was straightforward: the initial transfer of \$8,000 was a preference (assuming no other valid defense such as ordinary course); then the Creditor gets a credit under section 547(c)(4) of \$3,500 for the value of goods shipped, reducing the net preference to \$4,500. After the 2005 Act, can Creditor now add on the \$5,000 small preference defense of subsection (c)(9) to eliminate liability for this remaining \$4,500 amount? Reading the statute literally, the answer seems to be “no,” since section 547(c)(9) refers to “such transfer” as being less than \$5,000 as the trigger for the safe harbor, and in context, “such transfer” plainly means the total \$8,000 payment, *not* the net liability after the application of the new value defense. Any doubt on that score should be erased by noting that the identical language “such transfer” is used in the new value exception itself, in section 547(c)(4), and therein clearly refers to the original total amount transferred (here, the \$8,000), before any crediting for new value given by the creditor. One wonders, though, whether courts will give this literal reading to the Code, when the effect would be to treat differently two creditors who otherwise have an identical preference “liability” of < \$5,000, one of whose “liability” is entirely forgiven under section 547(c)(9) because that is the entire amount of the transfer, and the other of whom is held liable since the “liability” of < \$5,000 arose only after netting out new value given. If such piggy-backing of defenses is allowed, then a creditor whose net preference liability is above the \$5,000 mark can escape all preference liability by making a qualifying “new value” transfer to the debtor on the eve of bankruptcy in a sufficient amount to drop the net liability to less than \$5,000 – and thus to zero! That prospect of gaming may incline courts to give the statute its literal reading and not allow piggy-backing.

Another issue that will arise concerns characterization. The differentiation in safe harbors between individual consumer cases (\$600)⁴⁹ and non-consumer cases (\$5,000)⁵⁰ makes it a matter of considerable import to decide whether the case is in the consumer or non-consumer category in cases involving an individual debtor who is engaged to some degree in business. The issue is whether the debtor’s debts are “primarily” consumer debts or not, with “consumer” meaning, as it usually does in commercial law generally, “for personal, family, or household purposes.” There are two issues in play here: first, the debt characterization issue, and second, given those categorizations, calculating whether the “primarily” level has been surmounted. The “primarily consumer debts” concept and limitation is a familiar one in the Bankruptcy Code, and one assumes that courts will draw on past precedent in such cases (particularly in the “substantial abuse” provision in section 707(b) for cases from 1984 to 2005). Given the results of the Lawless and Warren study, courts should be careful to do more than just see which box the debtor checked in his petition, because the true nature of the bulk of his debts may be different. Certainly it seems unfair to a putative preference defendant to saddle that party with the debtor’s own characterization, about which the debtor may have cared little.

2. *Venue Protections*

The concern that preference defendants would be pressured to settle coercive suits is

⁴⁹ 11 U.S.C. § 547(c)(8).

⁵⁰ 11 U.S.C. § 547(c)(9).

particularly great when not only is the amount in controversy relatively modest, but the creditor defendant would have to travel a considerable distance to defend as well. Recall Hypothetical A, with Creditor located in Maine and the bankruptcy case commenced in Hawaii. The venue of the preference suit will make all the difference. If Creditor has to go to Hawaii to defend a suit seeking recovery of \$5,100, it would be more economical to settle, even if Creditor believes (as it does in that Hypothetical) that it has valid defenses. Pyrrhic victories are rarely very satisfying. It is precisely such cases that motivated the amendment in the 2005 Act to the provision in the Judicial Code governing the venue of “proceedings,” 28 U.S.C. section 1409.

The default rule in section 1409, in subsection (a), is that the bankruptcy trustee may commence proceedings in the same district where the main case is pending – in Hypothetical A, Hawaii. This home court venue rule is a great benefit to the trustee, allowing him to save costs by hiring a single local counsel to prosecute virtually all avoidance actions and other related proceedings in the case.⁵¹ Furthermore, trustees value having such related proceedings heard by the home bankruptcy judge, who is most familiar with (and perhaps sympathetic to?) the main case. Balanced against these interests of the estate, though, is the harm to distant creditors who must travel to the debtor’s home court to litigate fairly small claims.

Prior to 2005, the balance tipped in the defendant’s favor and subsection (b) of section 1409 required the trustee to sue where the defendant resided if the action was for a consumer debt of less than \$5,000 or a non-consumer debt of less than \$1,000. The ABI Report⁵² and the NBRC Report⁵³ concluded that the \$1,000 amount was way too low in business cases, and both urged raising the non-consumer venue protective rule to an amount higher than the \$5,000 small preference exception. The NBRC Report suggested a \$10,000 venue trigger amount for non-consumer cases.⁵⁴ However, the NBRC Report also urged keeping the consumer debt amount at \$5,000, arguing that “[t]ransfers on consumer debts are generally smaller and any increase in the amount under the venue provisions may make any preference or property recovery in these cases unlikely.”⁵⁵ Furthermore, the imperative for such a change in consumer cases was lacking, the NBRC Report noted, pointing out that it was only in “business cases where there are perceived abuses of the preference power.”⁵⁶

In the 2005 Act, Congress did adopt the NBRC and ABI recommendation to raise the venue protective floor in 28 U.S.C. section 1409(b) for business debts to \$10,000. This change will be most welcome for creditor defendants. Thus, in Hypothetical A, our Maine Creditor who

⁵¹ See NBRC Report, *supra* note 6, a§ 3.2.2, at 800.

⁵² ABI Report, *supra* note 2, at 30-31.

⁵³ NBRC Report, *supra* note 6, § 3.2.2, at 799-800.

⁵⁴ *Id.*

⁵⁵ *Id.* at 800.

⁵⁶ *Id.*

is potentially liable for \$5,100 now has a right to be sued where it resides, in Maine, where before it could have been sued in Hawaii. The upshot will be, first, that bankruptcy trustees will be more selective about which cases they choose to bring in distant venues, gauged both by the dollar amount at issue and the likelihood of plausible defenses being raised. In a case such as Hypothetical A, where Creditor has a colorable ordinary course defense (especially as *that* defense was amended, see below!), the trustee very well may decide that the game is just not worth the candle. Second, when the trustee does decide to sally forth, it will cost the estate more. The third likely upshot of the change is that creditor defendants will be much less likely to accept settlement offers, since their costs of defending have now gone down and the trustee's costs of prosecuting have gone up.

Simply put, the burden of non-economic actions has been shifted by the 2005 Act from creditor defendants to bankruptcy trustees. Interestingly, of course, the ultimate burden of any foregone preference recoveries is not borne by the trustee, who is simply the representative of the estate, but by the *other* unsecured creditors in the case, who typically are the residual claimants. A trade creditor who might have been disadvantaged by a "coercive" preference suit in one case may have been advantaged in other cases, when other unfortunate trade creditors were the coercive targets. Viewed on a macro level, one might expect unsecured creditors *as a group* to favor whichever legal regime maximizes returns to their entire group. Generous (for trustees) venue rules that keep prosecution costs low would seemingly fit that bill, and one could argue that the 2005 changes accordingly would run counter to the best interests of unsecured creditors as a whole, notwithstanding possible angst (and anger) in the occasional case wherein one's own ox is being gored. But unless one's ox got gored more than average, economic rationality might argue for accepting a pro-trustee venue system. That economic argument, though, is utterly unpersuasive to trade creditors – a truth to which I personally can attest as Reporter for the ABI Preference Study, where I tried in vain to make that argument to the trade creditor representatives. They preferred to take their chances overall if they could get more protection whenever *they* got sued. Congress granted that wish in BAPCPA.

The puzzle in the 2005 venue amendments is why Congress chose to ignore the NBRC recommendation that the venue floor in *consumer* cases *not* be raised. The NBRC Report argued, as noted above, that the amount of transfers in consumer cases is generally smaller than in business cases, that raising the venue amount in consumer cases might dry up preference recoveries altogether, and that, regardless, there was no problem in need of solving in consumer cases, where abuse was not generally reported.⁵⁷ With little or no explanation, though, Congress raised the venue rule privileging defendants to be sued where they reside for recovery of consumer debts from \$5,000 to \$15,000. This is a change that no one was asking for. There are not that many consumer debts that exceed \$15,000. As a practical matter, this little-noticed venue amendment may spell the end of much of the preference litigation – and also of course of preference *recoveries* – in consumer cases. That consequence may make it more difficult to process many consumer cases administratively, where the recoveries obtained in avoidance actions helped pay the costs of administering the estate.

⁵⁷ *Id.*

3. *Ordinary Course Defense*

By far the most important preference defense has been the “ordinary course of business” exception, in § 547(c)(2).⁵⁸ The ABI Survey demonstrates that the ordinary course defense is raised much more often than any other preference defense.⁵⁹ That exception attempts to capture the long-standing notion that not all payments that prefer one creditor over another should be avoided; instead, only those payments that are improperly motivated, by a creditor or debtor knowingly seeking to alter the bankruptcy distributional regime, are considered “bad” preferences and subject to avoidance.⁶⁰ Under the Bankruptcy Act of 1898, a similar function was served by the requirement in § 60b that the trustee prove that the transferee had reasonable cause to believe that the debtor was insolvent when it received the transfer.⁶¹ The 1978 Code abandoned that subjective test but in enacting section 547(c)(2) retained the view that “ordinary” business behavior should not be upset.⁶² As the House Report explained, the exception’s purpose was “to leave undisturbed normal financial relations.”⁶³ This view held even though the effect would be to prefer one creditor over others similarly situated, thus doing extreme violence to the “equality” goal of the preference law.⁶⁴

One can debate the wisdom of such a system.⁶⁵ Even if the basic notion is thought to be a wise one, though, the problem remains: how do you gauge what is “ordinary”?⁶⁶ The Code’s test prior to 2005 required proof that the debt was incurred in the ordinary course, that the transfer was made in the ordinary course of the business or financial affairs of the debtor and the transferee, *and* that the transfer was made according to ordinary business terms. The courts interpreted the second test to require proof of conformity to what was ordinary *subjectively*, as between the debtor and this particular transferee, and then the third test was interpreted to require proof of conformity to ordinariness *objectively*, in the industry at large, and not just as

⁵⁸ Tabb, *supra* note 20, § 6.18, at 382.

⁵⁹ ABI Report, *supra* note 2, at 8, 17.

⁶⁰ See Tabb, *supra* note 36, at 981-82.

⁶¹ Bankruptcy Act of 1898, ch. 541, § 60b, 30 Stat. 544, 562 (repealed 1978).

⁶² Tabb, *supra* note 20, § 6.18, at 383.

⁶³ H.R. Rep. No. 595, 95th Cong., 1st Sess. 373 (1977).

⁶⁴ Tabb, *supra* note 36, at 994.

⁶⁵ Harsh critiques are presented in Tabb, *supra* note 36, at 984 (advocating repeal of section 547(c)(2)), and Countryman, *supra* note 37, at 775-76 (same)(“In view of the feeble inspiration for this exception, and because the exception is completely at war with the concept of a preference and has no rational confining limits, the best future for present section 547(c)(2) is repeal”).

⁶⁶ See ABI Report, *supra* note 2, at 27.

between the debtor and the transferee.⁶⁷ Until 2005, a preference defendant had to prevail on *both* the subjective and objective tests in order to escape preference liability. That is, the elements of subsection (c)(2) were stated in the conjunctive.⁶⁸

In application, though, the ABI Report revealed that participants in the bankruptcy system strongly believed that the exception “was not working well in practice.”⁶⁹ How so? According to the ABI Report, “[t]he biggest problems are that no one knows what it means, and not surprisingly in light of that perception, the application of the defense is inconsistent. Furthermore, many respondents do not believe that the defense affords sufficiently broad protection.”⁷⁰ The principal aspiration expressed was “for greater clarity in this area.”⁷¹

The NBRC Report heeded this plea from the ABI Report and recommended that the road to such clarification be paved by replacing the conjunctive test with a *disjunctive* test, in which the preference defendant could prevail by showing either conformity to prior conduct between the parties or conformity to industry standards.⁷² The intent of the NBRC Report was that “the conduct between the parties should prevail to the extent that there was sufficient prepetition conduct to establish a course of dealing,” and that only “[i]n the event there is not sufficient prepetition conduct to establish a course of dealing, then industry standards should supply the ordinary course benchmark.”⁷³ According to that Report, this approach is salutary because it would eliminate the need for a preference defendant to prove elusive industry standards, and it is “more accurate to rely on the relationship between the parties.”⁷⁴

In the 2005 Act, Congress adopted the proposed NBRC Recommendation verbatim. Thus, by the simple expedient of changing “and” to “or,” Congress effected a notable change in the ordinary course exception and altered the balance of power in preference litigation, in favor of defendant creditors. Assuming that the debt was incurred in the ordinary course (as before), now a creditor can prevail by proving *either* that the transfer was subjectively ordinary, as between the debtor and that transferee, section 547(b)(2)(A), *or* that the transfer was objectively ordinary, measured against the industry, section 547(b)(2)(B).

In practice, the most likely consequence is that the principal focus of preference litigation

⁶⁷ Tabb, *supra* note 20, § 6.18, at 386-88.

⁶⁸ NBRC Report, *supra* note 6, § 3.2.3, at 801.

⁶⁹ ABI Report, *supra* note 2, at 20.

⁷⁰ *Id.*

⁷¹ *Id.* at 25.

⁷² NBRC Report, *supra* note 6, § 3.2.3, at 802.

⁷³ *Id.*

⁷⁴ *Id.*

in this area will be on the issue of conformity with the subjective prior course of dealing between the parties. The hard-to-prove objective industry test is likely to be raised only in rare cases, usually where there was insufficient pre-petition conduct between the parties to establish a course of dealing. That certainly was the intent of the NBRC Recommendation, as mentioned above.

Note, though, that the statutory language does not by its terms limit use of the objective industry test to situations where the parties lack a subjective course of dealing. It would appear to be equally available even if the parties *do* have a course of dealing, yet the transfer at issue does not conform to that course of dealing, but nevertheless still might conform to the industry standard. That is, if the parties' course of dealing was more demanding than the industry standard, and the challenged transfer failed to conform to that stricter standard, might it still be possible for the defendant to prevail under subsection (c)(2) by showing conformity to the laxer industry standard? Consider Hypothetical C, a variant of Hypothetical A. In A, recall that the invoices require payments in 20 days, but Creditor and Debtor have a well-established course of dealing allowing payment between 30 and 35 days. For Hypothetical C, add these facts: first, the norm in the industry is to allow payment in 50-60 days (whereas Creditor and Debtor have a stricter 30-35 day practice), and second, during the preference period, the three challenged transfers from debtor to Creditor each are made 55 days after invoicing. Thus, Creditor and Debtor *have* departed from their own pre-petition course of dealing, in a manner that raises red flags about the possibility that there is disfavored preferential behavior occurring. But the parties are easily covered by the looser industry standard.

In such a case, can Creditor escape preference liability by showing conformity with that laxer industry standard? While the apparent intent of the amendment would suggest not, the statutory language fairly plainly seems to permit such a fall-back defense for the Creditor. The intent is revealed by the above-described commentary in the NBRC Report, whose recommendation Congress adopted *en toto*, which urged gauging "ordinary course" conformity by reference to the parties' course of conduct if that was available, looking to industry standards only in the absence of such conduct. If that test were applied, Creditor would lose in Hypothetical C. But that is not what the statute says. I am no fan of the "plain meaning" rule of statutory interpretation, but it is hard to escape the fact that the statutory word "*or*" used in section 547(c)(2) is not ambiguous. "*Or*" signifies equally available alternative options, *not* a priority ordering favoring one option over the second. My suspicion is that courts will if at all possible fudge in finding "ordinariness" in cases such as Hypothetical C and that usually Creditor will still lose those cases. I am not opposed to such a result as a matter of policy, but it does a bit of violence to the statutory language.

The other sort of case that is likely to arise and that is worrisome under the new ordinary course exception is the exact opposite of the one just posited. That is, even if a transfer is "extraordinary" as judged against ascertainable industry standards, under the new law the creditor appears to be protected if the transfer did not depart from the prior practices of the parties. Indeed, this is likely to be the more common scenario. Consider Hypothetical D, another variant of Hypothetical A. Recall that the invoices require payment in 20 days, and Creditor and Debtor have a practice of 30-35 days for payment. But in Hypothetical D, add the fact that the industry standard (which we will assume is easily established) does strictly require

compliance with the 20-day invoice terms. Creditor gets paid at days 33, 30, and 35 during the preference period. What result?

Here the answer under the new law surely is that Creditor wins. The clear purpose of the NBRC Recommendation that led directly to the 2005 amendment was, as quoted earlier but which bears repeating, “that the conduct between the parties should prevail to the extent that there was sufficient prepetition conduct to establish a course of dealing.”⁷⁵ In Hypothetical D, we have such a course of conduct, and Creditor conformed to it. Now the statutory disjunctive language *and* the statutory purpose are in harmony and point inexorably to an outcome in which Creditor wins. Our intuition in this Hypothetical is that such is not really a bad result; if the idea behind the ordinary course exception is in fact “to leave undisturbed normal financial relations,” then that idea finds fulfillment in a case such as Hypothetical D.

Note, though, that this intuition also rests on the unstated premise that Creditor and Debtor probably were *not* trying to “manipulate their course of conduct prepetition”⁷⁶ with an eye to a possible future bankruptcy proceeding in such a way as to give Creditor an advantage over other competing creditors. Instead we assume that Creditor simply was not as rigorous as its peers in holding the line against Debtor. But what if Creditor’s motivation was not so benign? In the leading case of *In re Tolona Pizza Products Corp.*,⁷⁷ Judge Posner recognized a justification for the objective industry test “to allay the concern of creditors that one or more of their number may have worked out a special deal with the debtor, before the preference period, designed to put that creditor ahead of the others in the event of bankruptcy.”⁷⁸ What if *that* is what was going on – will the new disjunctive test be any safeguard?

This concern is nicely illustrated by “Hypothetical” E, based on the case of *Gulf City Seafoods Inc. v. Ludwig Shrimp Co. (In re Gulf City Seafoods, Inc.)*.⁷⁹ Creditor and Debtor had an unusual, but consistent and longstanding payment practice. When Debtor placed an order for goods with Creditor, Debtor would immediately send a check in payment of the delivery with the order. Normally, Creditor would hold the check for several weeks after delivering the ordered goods to Debtor before presenting the check to Debtor’s bank for payment. By having checks in hand, though, Creditor gained an advantage vis-à-vis other creditors by being able to seek payment earlier than normal if the prospects for payment worsened. Within the preference period, \$72,000 in checks to Creditor cleared Debtor’s bank account. Each of these checks was paid by Debtor’s bank within 40 to 45 days after the delivery of goods for which they paid – fully consistent with the parties’ longstanding, established days-to-payment history and well within the industry norm for days to payment. Are those payments to Creditor avoidable?

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ 3 F.3d 1029 (7th Cir. 1993)

⁷⁸ *Id.* at 1032.

⁷⁹ 296 F.3d 363 (5th Cir. 2002).

Before 2005, Creditor faced a serious risk of losing the ordinary course defense in Hypothetical E, because the Creditor's deal (getting checks in hand in advance of the normal time for payment, as a form of payment security) was not ordinary for the industry – even if, as it happened, Creditor did not actually present the “security” checks early. As a matter of policy, why should this Creditor be allowed to put in place such a special deal that gave it the option to get a jump on other creditors if the debtor's financial affairs turned ugly?

But under BAPCPA, since Creditor put in place its special deal well before the actual onset of bankruptcy, and the parties then adhered to that special deal so as to create a course of dealing, then Creditor might be able to prevail by proving conformity to subjective ordinary course, under section 547(c)(2)(A). The fact of non-conformity to industry standard supposedly would be irrelevant. Taking the statutory language at face value, Hypotheticals D and E should come out the same way, in Creditor's favor. But is that a good result? While we are not bothered in D because we doubt that Creditor has engaged in intentional behavior to give it an advantage over other creditors, such is not the case in E. If Creditor wins under E, as the statutory language suggests, the violence to the preference policies of equality *and* deterrence seems manifest. The question will be how courts can wiggle off the hook in such a situation. I am not sanguine. Escaping the force of the statutory language would be especially difficult here since the NBRC Report clearly contemplated as a “competing consideration” to its Recommendation for adoption of a disjunctive test the possibility that parties would engage in pre-petition manipulative behavior in framing their own course of conduct,⁸⁰ but nevertheless went forward with the Recommendation.

4. *Enabling Loan Safe Harbor and*

5. *Timing Changes*

The next two sets of amendments to section 547 will be discussed together, because they deal with similar problems – fixing the time when a transfer of a security interest is deemed “made” for purposes of applying the preference law, when perfection of the security interest follows its creation, and then determining which of those delayed perfection security interest transfers should be protected from avoidance. In a nutshell, the changes made in 2005 give the creditor/secured party a 30-day grace period to perfect a security interest. This change was made both in the general timing provision of section 547(e)(2) (where the grace period was extended to 30 days from 10 days) and in the enabling loan exception of section 547(c)(3)(B) (where the period was extended from 20 days to 30 days). These changes were made with little explanation or consideration for their impact. The apparent trigger for the changes was the Supreme Court's 1997 decision in *Fidelity Financial Services, Inc. v. Fink*,⁸¹ explained below. First, though, let me lay down some necessary background.

In determining when the transfer of a security interest is “made,” two possible times might be used: when the security interest first becomes effective between the debtor and the

⁸⁰ NBRC Report, *supra* note 6, at 802.

⁸¹ 522 U.S. 211 (1997).

secured party creditor, or when it is perfected as against third parties. Usually perfection requires some sort of public notice of the existence of the security interest, usually by filing a statement of the security interest in a public office under the debtor's name. Such a filing enables interested third parties who are considering doing business with the debtor to check in the public office for filings, in order to learn whether the debtor's assets are encumbered. Absent such a public filing, those third parties typically may treat the debtor's assets as effectively unencumbered because of the debtor's ostensible free-and-clear title, whatever the actual state of affairs. Stated otherwise, "secret" liens (i.e., those not publicly noticed) may be ignored by third parties – especially in the event of the debtor's bankruptcy. This policy against secret liens is enforced in bankruptcy both by the strong-arm clause, section 544(a),⁸² which avoids liens that are unperfected at the time of the bankruptcy filing,⁸³ and by the timing rules of the preference statute, section 547(e), which extends the delayed perfection avoidance power back into the immediate pre-bankruptcy time period.⁸⁴ For bankruptcy purposes, timing rules and avoiding powers depend ultimately on perfection, rather than just when the transfer became effective between the debtor and secured party.

But this invocation of the time of perfection is not an absolute. Secured creditors are given a bit of leeway to effect their perfection, without being subject to avoidance in bankruptcy. For preference purposes, prior to the 2005 Act, 10 days grace was extended to perfect. Under section 547(e)(2), a transfer was deemed "made" when it became effective between the debtor and secured party if perfected within 10 days of that time, section 547(e)(2)(A), but if it was not perfected within 10 days, then the transfer of the security interest was deemed made only when it was perfected, under section 547(e)(2)(B).⁸⁵ The deferral of the time of making meant that the transfer of the security interest was deemed to be on account of an antecedent debt for purposes of section 547(b)(2) and thus potentially preferential, even if the debt was created at the same time the security interest became effective as between the debtor and secured party. Furthermore, the secured party risked being drawn into the preference reach-back period by a delayed perfection that did not occur until after the onset of the preference period. The timing rule in subsection (e)(2) applied (as it still does) to all security interests, whether "purchase money" liens or not.

The timing rule of section 547(e)(2), though, standing alone would provide imperfect protection for purchase money security interests (or "PMSI"), also known as "enabling" loans. Under non-bankruptcy law, purchase-money security interests are given a grace period to perfect and yet still be valid against third parties whose interests arise in the interim between the time the lien was created and the time it was perfected. Thus, under these special rules, the PMSI

⁸² For example, for Article 9 security interests in personal property, this rule is found in U.C.C. § 9-310(a).

⁸³ See Tabb, *supra* note 20, § 6.3, at 336-37.

⁸⁴ See *id.*, § 6.9, at 354-55.

⁸⁵ See *id.* at 355.

effectively “relates back” for priority purposes to the earlier time of creation. For example, under § 9-317(e) in Article 9 of the UCC, a PMSI is valid against intervening interests if perfected within 20 days after the debtor receives delivery of the collateral. The problem, though, for bankruptcy preference purposes is that the 20-day UCC grace period runs from the time the debtor receives possession of the collateral, which could be *later* than when the security interest became effective (“attached”) between the debtor and secured party under UCC § 9-203(b). The timing rule of section 547(e)(2) uses the potentially earlier time when the security interest first became effective. Thus, without more, under section 547(e)(2) alone, a PMSI perfected within 20 days after the debtor received possession of the collateral but more than 10 days after the security interest attached would be vulnerable to preference attack.⁸⁶ No plausible bankruptcy policy supports avoiding a PMSI that would be invulnerable against third parties under non-bankruptcy law.

The solution in the Code as originally enacted was found in the “enabling loan” exception of section 547(c)(3), which protected a PMSI if perfected within 10 days after the debtor received possession of the collateral. Ten days was chosen because that corresponded with the then-prevailing grace period for a PMSI in UCC Article 9. However, the problem developed that the UCC grace period was extended to 20 days and thus the 10-day rule in subsection (c)(3) was inefficacious for a PMSI perfected between 11 and 20 days. Congress responded to this problem in the 1994 Bankruptcy Act by amending subsection (c)(3) to provide for a 20-day grace period,⁸⁷ again intending to mirror the UCC time period.⁸⁸ Notably, though, Congress did not amend the law by simply incorporating grace periods effective under non-bankruptcy law, as it did elsewhere in the Code in section 546(b)(1)(A), but again specified an independent federal time period for perfection. As I predicted,⁸⁹ this 1994 Congressional amendment left open exactly the same problem as before if the applicable state law grace period was *longer* than 20 days, because then the secured party would not find succor in either section 547(e)(2)’s 10-day rule or section 547(c)(3)’s 20-day rule.

That prediction came true in *Fidelity Financial Services, Inc. v. Fink*, decided by the Supreme Court in 1997.⁹⁰ Missouri law gave a secured party *thirty* days to perfect a security interest in a motor vehicle. The secured party mailed in the necessary perfection papers on day 21, and argued that it should be protected from preference avoidance because it complied with the Missouri law. Predictably, the Supreme Court rejected this plea, emphasizing that the time periods in section 547(e)(2) on time-of-transfer and section 547(c)(3) for enabling loans are

⁸⁶ See *id.* § 6.19, at 389-90.

⁸⁷ P.L. No. 103-394, § 203, 108 Stat. 4121 (1994).

⁸⁸ 140 Cong. Rec. H10,767 (daily ed. Oct. 4, 1994) (cited in Tabb, *supra* note 20, § 6.19, at 391 & n.3).

⁸⁹ Tabb, *supra* note 20, § 6.19, at 391.

⁹⁰ 522 U.S. 211 (1997).

federal time periods and do not depend on or incorporate the underlying state law. With that said, the Court had little trouble finding that 21 was more than 20 and that the creditor was not protected by the enabling loan exception.

Showing little in the way of a learning curve, Congress has gone and done it again. In BAPCPA, Congress amended section 547(b)(3)(B) again, this time putting in a *thirty*-day grace period for enabling loans in place of the prior 20-day period.⁹¹ It did not, however, incorporate non-bankruptcy law grace periods (which it does know how to do, as demonstrated by section 546(b)(1)(A)). The new 30-day federal bankruptcy rule is good and well for secured creditors in states (like Missouri) with a 30-day state law perfection rule. So, on the exact facts of *Fink*, the outcome will be different now. But if state law provides a grace period to perfect longer than 30 days, it will be *deja vu* all over again. Secured creditors will *not* have the full state law period to perfect and be impervious to preference attack; they will have only the 30-day period of new section 547(c)(3)(B). As stated above, it is difficult to conceive of a coherent bankruptcy policy reason why secured creditors who comply fully with governing non-bankruptcy laws and who would prevail in a priority battle with intervening lien creditors and purchasers under that non-bankruptcy law should lose in the happenstance that the debtor files bankruptcy. Doing so gives a windfall to the debtor's other creditors, a windfall those creditors could not possibly have obtained outside of bankruptcy.

So, the amendment to the enabling loan exception of section 547(c)(3) gives secured creditors less protection than they deserve. The 2005 amendments to section 547(e)(2) do the opposite, providing secured creditors with *more* protection than seems warranted. Under the amendments to subsection (e)(2), a transfer is deemed made at the time it took effect between the debtor and the creditor if perfected within 30 days of that time.⁹² No explanation for this change is given; one might surmise that it too stems from a “fix-*Fink*” mindset. But why give such extravagant protection to *non*-PMSI secured creditors, and open up such an opportunity for adroit use of secret liens?

Consider Hypothetical F. On May 1, Debtor borrows money from Creditor. As security, Debtor grants Creditor a security interest in a house boat which Debtor owns free and clear. Under state law, a PMSI is deemed to have been perfected from the time the security interest was originally created if public notice is filed within 20 days of when the debtor takes possession of the collateral, but a non-PMSI has no similar “relation-back” rule. Creditor, who learns of Debtor's impending bankruptcy filing, files the necessary public notice on May 30. On June 1, Debtor files bankruptcy. Is Creditor's security interest in the house boat avoidable as a preference?

Under the 2005 Act, the answer is no – Creditor's security interest is not avoidable. This result obtains even though Creditor does not have a PMSI and thus under the applicable state law would not have had priority over intervening lien creditors as of the date of perfection, May 30, since there is no relation-back rule for a non-PMSI. Under new section 547(e)(2), though, that

⁹¹ 109 P.L. 8, § 1222, *codified at* 11 U.S.C. § 547(c)(3)(B).

⁹² *Id.* § 403, *codified at* 11 U.S.C. § 547(e)(2).

omission is irrelevant: the only law that matters is the Bankruptcy Code, and since Creditor perfected within 30 days of when the security interest attached, under § 547(e)(2)(A) the transfer is deemed to have been made at the time the transfer took effect between the transferor and transferee (May 1), and thus there is no antecedent debt and no preference. The fact that Creditor would not qualify for the enabling loan exception is immaterial, because there is no preference in the first place.

This expanded timing rule of § 547(e)(2)(A) empowers creditors holding unperfected security interests in cases like Hypothetical F to engage in avowedly “preferential” behavior, with an eye towards improving their status in the bankruptcy distribution, by taking action to perfect within the preference period, as long as they do so within 30 days after the security interest attached. There is no sort of “intent” limitation or restriction on these timing rules. In Hypothetical F, Creditor has free reign to perfect for any reason. It is hard to discern any justification for this new rule, given that it empowers unperfected secured creditors to get more than they could have under state law and allows them to make pre-bankruptcy grabs. While such was also the case under prior section 547(e)(2), the grace period was a very short 10 days, leaving little opportunity for such avowedly preferential behavior. And even that original 10-day grace period was defensible at most as giving a diligent secured creditor enough time to perfect after a lien was created, in situations where prior or contemporaneous (with creation) perfection was not feasible or possible. Indeed, such was the basis of the original preference-perfection-grace period, in the 1950 Amendments.⁹³ Today, for Article 9 security interests at least, such a rule is anachronistic, since prior or contemporaneous perfection is allowed. Even for those sorts of liens that cannot be pre-perfected, 30 days seems excessively generous.

6. *Alternative Repayment Plan Payments Excluded*

One of the themes of BAPCPA was to encourage (and coerce?) debtors to get credit counseling prior to bankruptcy and, as part of that process, hopefully to enter into consensual repayment plans to their creditors. Congress clearly hoped that individual debtors would be persuaded to make voluntary payments and if possible eschew bankruptcy relief entirely. Several amendments seek to implement these goals. The most direct such “encouragement” was section 109(h)’s bar to an individual debtor filing bankruptcy altogether unless she had received such credit counseling from an approved nonprofit budgeting and credit counseling agency (or was excused therefrom) in the 180 days prior to bankruptcy. The bankruptcy clerk is required by section 111(a)(1) to maintain a publicly available list of agencies that provide the services described in section 109(h). Under section 342(b), prior to the commencement of a case the bankruptcy clerk is required to give an individual consumer debtor a notice that describes “the types of services available from credit counseling agencies.” Under section 362(i), if a debtor’s case is dismissed “due to the creation of a debt repayment plan,” then the good faith filing requirement for the applicability of the stay in a serial case under section 362(c)(3) presumptively is satisfied.

A carrot for debtors to propose alternative repayment schedules prior to bankruptcy is

⁹³ See Countryman, *supra* note 37, at 754 n. 222.

that a creditor who unreasonably refuses to negotiate a reasonable repayment plan on an unsecured consumer debt that meets certain stringent criteria may have its claim reduced by not more than 20 percent, under section 502(k). Finally, pertinent to the present article, a safe harbor was added to the preference law in section 547(h) for transfers made as part of an alternative repayment schedule that was created by an approved nonprofit budgeting and credit counseling agency. This provision offers a juicy carrot to *creditors* to agree to such repayment plans, since they thereby would gain immunity from preference attack in the event of a subsequent bankruptcy. Note that these last two amendments, regarding the claim reduction and the preference safe harbor, were enacted as part of the same section in BAPCPA, entitled “Promotion of Alternative Dispute Resolution.”⁹⁴

There are a few technical points to consider concerning the new preference safe harbor for payments pursuant to alternative repayment plan. First, the statutory protection only applies on its face to repayment schedules “created by an approved nonprofit budgeting and credit counseling agency.” Apparently, then, it will not avail the creditor any (at least under section 547(h)) to agree to a repayment plan that does not have the imprimatur of an approved agency. Why this restriction is included (other than as a full-employment-for-credit-counseling agencies measure) is puzzling, if the intent of Congress is, as the title to the enacting BAPCPA section says, “promotion of alternative dispute resolution.” Why would it not serve the congressional purpose just as well if the debtor and creditor on their own agreed to a repayment plan? Requiring blessing of an agency increases transaction costs. Note, of course, that even if the repayment plan does not qualify for protection under subsection (h), it still may pass muster as an “ordinary course” payment under subsection (c)(2).⁹⁵

Perhaps Congress intended the requirement that the repayment schedule be created by an approved credit counseling agency to be a means to prevent debtors and favored creditors from cooking up special deals, whereby only the favored creditors would get paid. The agency may serve as a check on such blatantly preferential deals, and might insist that the debtor propose repayment ratably to all unsecured creditors. If that is the hidden agenda, though, it would have been easy for Congress simply to impose such a ratable treatment substantive requirement on qualifying repayment schedules.

Second, the statute is unclear as to the extent (if any) of the intended linkage between section 502(k)’s claim reduction provision regarding a creditor’s refusal to agree to a proposed alternative repayment plan and section 547(h)’s preference safe harbor for transfers pursuant to alternative repayment plans. Section 547(h) purports to cover, without limitation, “a transfer ... made as part of an alternative repayment schedule.” The only restriction is the one just noted, that the plan must be created by an approved agency. Nowhere is “alternative repayment schedule” defined in the Code. The only detailed description of such a schedule is found in

⁹⁴ 109 P.L. 8, § 201, *codified at* 11 U.S.C. §§ 502(k), 547(h).

⁹⁵ *See, e.g.,* Arrow Electronics, Inc. v. Justus (*In re Kaypro*), 218 F.3d 1070 (9th Cir. 2000) (payments made pursuant to restructuring agreement are not *per se* excluded from ordinary course protection).

section 502(k), which, as mentioned above, was enacted as part of the same section of BAPCPA as section 547(h). Nothing in section 547(h) purports to limit its coverage to “alternative repayment schedules” that have the following characteristics, which *are* found in section 502(k): only *consumer* debts; debtor proposed plan more than 60 days before bankruptcy; debtor proposed payment of at least 60 percent of the debt over the original repayment period or a reasonable extension thereof; and no part of the debt is nondischargeable. Nor is section 547(h) limited to transfers by *individual* debtors, as does the eligibility bar of section 109(h). Under a plain meaning view, then, none of those limiting characteristics would limit the scope of coverage of section 547(h). But is it possible that Congress intended for those other sections that speak to the role of credit counseling agencies and the creation of alternative repayment schedules to be read *in pari materia* with section 547(h)? Is it necessarily inherent in the very concept of “credit counseling” (or at least as contemplated in the 2005 amendments to the Bankruptcy Code) that it be regarding consumer debts, and for individual debtors?

On a policy level, one can only marvel at the continuing emasculation of the supposed *equality* goal of the preference law. It is getting more and more difficult to say with a straight face that the bankruptcy preference law even *has* a paradigm of equality. Section 547(h) cuts at the very heart of equality. The simple effect of section 547(h) is that creditors who get paid under an alternative repayment schedule get to keep their money, even if other unsecured creditors go unpaid, at a time when the debtor is insolvent. There is no requirement in the statute that alternative repayment plans must propose ratable treatment for all unsecured creditors in order to qualify for protection under section 547(h), although perhaps that would be enforced indirectly through the credit counseling agency approval requirement, as suggested above. Even if the approved alternative repayment schedule itself provides for ratable payment of all unsecured creditors, there is nothing in the statutory safe harbor that requires the debtor to *perform* on such a basis. That is, assume Hypothetical G, under which an alternative repayment plan calls for payment of 60% of unsecured debts to Creditors A, B, and C, but Debtor only pays Creditor A; Creditors B and C get nothing. May Creditor A invoke the safe harbor of section 547(h)? It would appear so.

Nor is section 547(h) necessarily consonant with the other purported principal goal of the preference law, that of *detering* the proverbial “race to the courthouse.” Why not? Demanding creditors may exert coercive pressure on a financially troubled debtor (i) to create an alternative repayment schedule in the first place, and (ii) to pay them in preference to other creditors pursuant to a created schedule, without forfeiting the protection of section 547(h). Revisit Hypothetical G. Assume further that Debtor had not made any payments to any of Creditors A, B, or C pursuant to the created alternative repayment schedule; that Creditor A learned that Debtor was going to file bankruptcy imminently; that Creditor A thereupon insisted that Debtor pay A everything Debtor owed A under the repayment schedule, “or else”; and Debtor did then pay A, but not B or C. Is Creditor A protected by section 547(h)? The answer appears to be “yes” – nothing in that section requires payments to be made “in the ordinary course” or in any other way keeps the creditor from engaging in avowedly preferential behavior.

7. *Deprizio Fixed (Again)*

If a preferential transfer is “avoided” under section 547, the trustee usually then must

“recover” that transfer under section 550. Normally the trustee would “recover” from the party as against whom “avoidance” was effected, and even more tellingly, one might surmise that if the trustee was *not* able to *avoid* as against a party, then neither would the trustee be able to *recover* from that party. As explained below, that seemingly logical surmise could prove wrong. Just such a possibility could present itself in a preference case if a transfer is made directly *to* a party and that transfer is also “for the benefit of” another party. This is called an “indirect” preference. For example, if payment is made on a guaranteed debt, that transfer is beneficial not only to the party who receives the payment, of course, but also to the guarantor, whose own contingent liability has thus been discharged. What happens if the transfer is avoidable *only* as to the guarantor? This could happen, for example, if the payment was made more than 90 days but less than one year before bankruptcy, and the guarantor was an insider but the direct transferee was not an insider. In that situation, under section 547(b)(4), the non-insider would not be subject to preference avoidance. But may recovery still be had from the direct transferee?

In the infamous 1989 case of *Levit v. Ingersoll Rand Fin. Corp.*,⁹⁶ known generally as the “Deprizio” case (which was the debtor’s name), the Seventh Circuit held that the trustee *could* recover under section 550(a) from the non-insider initial transferee in such a situation, even though the preference was not avoidable as to that non-insider, but was only avoidable as to an insider. The *Deprizio* court applied the plain meaning of section 550(a)(1), which says that the trustee may recover from the “initial transferee” (here, the non-insider) *or* “the entity for whose benefit such transfer was made” (here, the insider guarantor”). The court took the disjunctive “or” at face value.

There was considerable wailing and gnashing of teeth in the wake of *Deprizio*. Lenders argued that it was unfair to make them worse off because they had obtained a guaranty. Congress, agreeing that the *Deprizio* outcome was both unfortunate and unintended, amended the recovery section in 1994 in an attempt to reverse *Deprizio*. It did so by adding section 550(c), which precludes recovery from a non-insider transferee on the precise facts of that case, namely, when avoidance occurs under section 547(b) as to a transfer made between 90 days and one year before bankruptcy and which was for the benefit of an insider.⁹⁷

However, the 1994 “fix” was incomplete, for two reasons. First, section 550(c) does not help the non-insider when no “recovery” is required under section 550. Second, that section does not apply to transfers made on indirect preferences within the 90-day period.

Consider the “no recovery” problem first. This would be the case where a *lien* is avoided.⁹⁸ In that situation, no “recovery” is had. The lien is simply set aside. Thus, consider

⁹⁶ 874 F.2d 1186 (7th Cir. 1989).

⁹⁷ Bankruptcy Reform Act of 1994, § 202, P.L. 103-394, 108 Stat. 4106 (103rd Cong., 2d Sess. 1994).

⁹⁸ See H.R. Rep. No. 109-31, at – (109th Cong., 1st Sess. 2005) (discussing § 1213 of BAPCPA). See also Tabb, *supra* note 20, § 6.1, at 331, and §6.13, at 368-69.

Hypothetical H. Creditor, a non-insider, is owed \$25,000 on an unsecured debt by Debtor. Guarantor, an insider, has guaranteed Debtor's debt to Creditor. Six months before bankruptcy, Debtor grants Creditor a lien on collateral worth \$25,000. That transfer of the lien benefited Creditor, of course, but is not avoidable as a preference as against Creditor, since Creditor is not an insider and the transfer was made more than 90 days before bankruptcy. However, that lien transfer *also* benefits Guarantor, by reducing the likelihood that Guarantor will be called upon to honor its secondary obligation to Creditor. The transfer of the lien thus is "for the benefit of" Guarantor even though directly "to" Creditor. Since Guarantor is an insider, subject to the longer one-year preference period, the lien can be avoided. Note that section 550(c) does not help Creditor, because nothing is being "recovered." The lien is just avoided.

In the 2005 Act, Congress tried again to fix this problem, adding new section 547(i) for cases such as Hypothetical H. The new provision, which is located in the *avoidance* section (547) rather than the *recovery* section (550), would protect Creditor on these facts. The new safe harbor provides: "If the trustee avoids under subsection (b) a transfer made between 90 days and 1 year before the date of the filing of the petition, by the debtor to an entity that is not an insider for the benefit of a creditor that is an insider, such transfer shall be considered to be avoided under this section only with respect to the creditor that is an insider."⁹⁹ Thus, avoidance is effective only with respect to Guarantor, not as to the non-insider Creditor, and thus the intent is that Creditor can keep its lien. By placing the safe harbor at the point of avoidance (as per the non-insider) rather than the point of recovery, complete protection is afforded in such a case. As a practical matter, the amendment means that in such a lien avoidance case, the lien itself (held by the protected non-insider) will remain valid, and the vulnerable insider will have to pay the trustee the value of the lien. Note that this amendment in BAPCPA was made applicable to cases filed after the enactment date of April 20, 2005, rather than as of October 17, 2005, which was the effective date for most BAPCPA amendments.

All that is good and well. But even the 2005 "fix" itself might be incomplete. The problem is that, even though it moves the safe harbor point back from recovery to avoidance, it does so *only* for indirect preferences that occur beyond the 90-day preference period. If a party were the direct transferee of an indirect preference *within* the 90-day period that was not avoidable as to them but which was avoidable as to someone else, neither section 550(c) nor section 547(i) would protect them, since both of those sections by their terms apply only to transfers made between 90 days and one year before bankruptcy. Consider, for example, Hypothetical I.

In Hypothetical I, Creditor A loans Debtor \$20,000 and takes a first mortgage on Greenacre. Creditor B subsequently loans Debtor \$10,000, and takes a second mortgage on Greenacre. Real estate values decline, with the value of Greenacre dropping to \$25,000. Within the 90 days before Debtor files bankruptcy, with Greenacre worth \$25,000 at all times, Debtor makes regularly scheduled debt payments of \$5,000 to Creditor A. What result?¹⁰⁰

⁹⁹ 109 P.L. 8, § 1213(2), codified at 11 U.S.C. § 547(i).

¹⁰⁰ This problem, and its analysis, is taken from Tabb, *supra* note 20, § 6.12, at 368-69.

The transfer of \$5,000 is not preferential as to Creditor A, because at all times A was fully secured, and thus there is no preferential effect under section 547(b)(5). However, the payment to A indirectly benefits Creditor B by paying down the debt owed to the first lienholder and accordingly freeing up collateral to secure the junior lienholder. Thus, before the payments, Creditor B's claim of \$10,000 was only partially secured, for \$5,000, with the \$5,000 balance unsecured. However, after the payment to A, Creditor B has become fully secured, because now A is only owed \$15,000, and the collateral is still worth \$25,000. Thus, the transfer "to" Creditor A is "for the benefit" of Creditor B and is preferential as to B. Applying the reasoning of the *Deprizio* case, the trustee in bankruptcy would be able to "avoid" the transfer as to Creditor B and then "recover" the \$5,000 payments from Creditor A, as the "initial transferee" under section 550(a)(1). Neither section 550(c) nor section 547(i) helps Creditor A, since both only apply to transfers made more than 90 days before bankruptcy. So we have the absurd result that a fully secured creditor could be forced to disgorge payments made on its debt. Note too that this case does not even have the possible taint (or justification?) that the creditor against whom the transfer was not avoidable nevertheless may have gotten some subtle benefit, as was argued in *Deprizio* due to the fact of the insider guaranty (*viz.*, that the insider may have influenced the making of the payment on the debt he had guaranteed). Here, Creditor A is not even indirectly benefitted and indeed has no control over or role in the fact that Debtor granted a second mortgage. So, Congress still may have some work to do.

Conclusion

In BAPCPA, lost among the flurry of publicity over the controversial consumer bankruptcy changes, Congress made seven significant amendments to preference law and practice. With these changes, the normative underpinnings of preference law are again weakened. The lame legs that principles of equality and deterrence had to run on were crippled even further. Trade creditors have much to cheer about in the new preference regime, and a sop or two were thrown secured creditors' way as well. There seems little doubt that preference litigation and recoveries thereunder will decline in the "brave new world" of bankruptcy preferences in which we now live.