

# *Minimizing a Manufacturer's Exposure to Bankruptcy Preference Claims by Asserting Purchase Money Security Interests and Special Tools Liens*

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By Daniel M. Morley and Kristen A. Campbell

## **The Preference Problem**

To say that many of Michigan's manufacturers are currently suffering a rash of losses as a result of bankruptcy filings is a monumental understatement. The automotive industry has been particularly hard hit.<sup>1</sup> To add insult to injury, it is not uncommon for manufacturers that have already suffered a loss as a result of a customer's bankruptcy to later receive a notice from the bankruptcy trustee or the debtor in possession<sup>2</sup> that demands that the manufacturer must pay back the monies received from their bankrupt customer within the ninety-day period<sup>3</sup> preceding the "petition date." This ninety-day period is known as the "preference period." The United States Bankruptcy Code<sup>4</sup> (the "Code") presumes that a debtor is insolvent during this ninety-day period.<sup>5</sup> All payments and transfers made to creditors by the debtor during this period are considered suspect and are referred to as "preference payments."

While it may not *seem* fair, the rationale for the disgorgement and return of preference payments under the Code is based on the concept of ensuring the fair and equal treatment of all unsecured creditors. The recovery of preference payments is intended to redistribute the bankruptcy estate's assets equitably among all of the bankrupt's unsecured creditors. Under the Code, the trustee (or the debtor in possession in a Chapter 11 proceeding) may set aside transfers of the debtor's interest in property: 1) to or for the benefit of a creditor; 2) for or on account of an antecedent debt owed by the debtor before such transfer was made; 3) made while the debtor was insolvent; 4) made on or within ninety days before the date the petition was filed (or if the creditor was an insider, on or within one year before the date the petition was filed); and 5) that enabled the creditor to

receive more than the creditor would have received if the case were a Chapter 7 liquidation proceeding.<sup>6</sup> It is important to note that this section does not require proof of intent to receive a preference, notice of the debtor's insolvency, fraud, or any other subjective element.

In many cases, preference claims are the largest asset of the bankruptcy estate. The recovery of preference claims has frequently been referred to as the "bread and butter" for bankruptcy trustees and their attorneys. Often preference claims are the only source of cash with which to pay the fees and expenses of a Chapter 7 trustee, their legal counsel, and other priority expenses.

While a number of defenses to a preference claim are available to a creditor,<sup>7</sup> defending a preference action can be very costly. Preventing a preference claim altogether is preferable (pun intended) to defending such a claim. By altering a manufacturer's status from an unsecured creditor to a perfected secured creditor, a manufacturer may be able to effectively avoid a preference action in its entirety.

## **The Purchase Money Security Interest Solution**

How can a manufacturer avoid a preference claim? In most instances, manufacturers deliver goods to their customers on a credit or on an open account basis. Credit terms may vary from "Net 30," to "Net 60," to "Net 90," or even longer in some instances. And as is often the case, and perhaps even more prevalent in the current economic climate, payments tend to be delinquent a month or more beyond what the contract terms permit. This means that not only is the manufacturer providing the goods on credit, the manufacturer is effectively providing its customers

with short-term financing for those goods. Often these open accounts can grow into the six-figure range or higher. Having to disgorge a six-figure preference payment after the customer files bankruptcy can be devastating to the manufacturer and may even result in the manufacturer's own bankruptcy filing.

As noted, a solution to this preference predicament can be achieved by altering the manufacturer's position from a "general unsecured creditor" to that of a "secured creditor." A payment made to a fully secured creditor during the ninety-day preference period is not preferential. In return for the payment to the secured creditor, the debtor receives a release of the lien in the collateral; and thus, there is technically no depletion of the debtor's estate,<sup>8</sup> so the creditor does not receive more than it would in a Chapter 7 bankruptcy proceeding.<sup>9</sup>

In short, an unsecured manufacturer needs to become a secured creditor. One solution lies in the manufacturer's acquisition of a purchase money security interest in the goods supplied to the debtor/customer on credit. The concept is this: by providing the customer with the goods on credit and allowing the customer to take title to the goods on delivery, the manufacturer is providing the debtor with the financing to purchase the manufactured goods.

A purchase money security interest<sup>10</sup> ("PMSI") is best described as a security interest held by a creditor that has financed the purchase of collateral to secure repayment of all or part of that purchase price. The typical instance of a PMSI occurs when a bank or other financial institution provides financing to a party to purchase a new piece of equipment (or other goods). In return for providing its financing, the bank takes a security interest in the equipment. In the event the borrower defaults on the loan, the bank then repossesses the equipment to satisfy all or a part of the indebtedness. Provided the bank follows the necessary formalities to perfect its security interest in the newly purchased equipment, the bank's PMSI in the equipment is of a higher priority than the other creditors that may hold general security interests in all of the debtor's assets. In the event of the borrower/customer's bankruptcy, the bank may recover the equipment from the bankruptcy estate to satisfy the debt.

Conceptually, there is no difference between the traditional debtor-creditor relationship involving a bank and borrower and

when a manufacturer provides short-term financing to its customer.<sup>11</sup> Thus, to take advantage of the benefits of being a secured creditor, the manufacturer must follow the same requirements to obtain a PMSI in the equipment or other goods that it supplies. What are those requirements? First, there must be a debt. Second, there must be an agreement by which the borrower/customer grants a security interest in the goods to the manufacturer. Third, the manufacturer must timely record a financing statement that adequately describes the collateral in the state in which the borrower/customer is located.<sup>12</sup>

With regard to the first requirement, there is no question that when a manufacturer provides goods to a customer on credit terms, a debt exists.

The second requirement is that there is an agreement by the customer to grant a security interest in goods. How is this agreement created? In many instances, the security interest's terms can simply be included in the terms of the formal contract between the parties. It is recognized, however, that in many cases, such as the automotive industry, manufacturers contract through various proposals, purchase orders, and invoices as opposed to a single controlling contract. In these situations, the contract terms are simply boilerplate provisions included in the forms. The actual terms of the contract lie somewhere within the documents exchanged between the customer and the manufacturer. In these instances, the necessary terms to grant the manufacturer a security interest in the goods can be added to the boilerplate terms and conditions that comprise the manufacturer's standard form proposal, purchase order, and invoice documents.

Note, however, that the terms of a customer's purchase order may vary from the manufacturer's proposal and the invoice. Consequently, the insertion of additional security interest terms into the form documents may not automatically control the "battle of the forms" and may not, in all cases, conclusively establish a security agreement.<sup>13</sup> Therefore, the methodology that inserts the critical terms into the manufacturer's form documents should be carefully scrutinized. When possible, a formal security agreement signed by the customer is preferable to boilerplate security interest terms that are inserted into form purchase order documents.

Finally, the manufacturer will need to record a financing statement in the appropriate

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office in the state in which the debtor/customer is located.<sup>14</sup> In Michigan, the proper location to file the financing statement is the Michigan Department of State, UCC Unit. The UCC-1 financing statement form must clearly describe the collateral. In the case of an equipment manufacturer, the use of serial numbers in the UCC-1 form is strongly encouraged for identification purposes. The financing statement must be filed within twenty days after the debtor takes possession of the collateral.<sup>15</sup> The filing of the financing statement before the debtor takes possession of the collateral is permissible.

Taking a PMSI in goods that will become inventory of the debtor is slightly more complicated. First, the manufacturer must conduct a search of the UCC records to determine which, if any, other creditors claim an interest in the inventory of the debtor. Then, the manufacturer must send an "authenticated notification" to the holders of any conflicting security interest in the customer's inventory.<sup>16</sup> The notice must be received within five years before the debtor/customer receives possession of the inventory.<sup>17</sup> The notice must state that the prospective PMSI holder expects to acquire a PMSI in the debtor/customer's inventory and describe the type of inventory that is to be financed.<sup>18</sup> The PMSI holder must again ensure that it files a financing statement within twenty days after the debtor/customer takes possession of the inventory.<sup>19</sup>

Also, it should be noted that a manufacturer with a PMSI in a "floating mass," such as a fluctuating pool of inventory, is subject to preference attack to the extent the manufacturer improves its position during the ninety-day period before bankruptcy.<sup>20</sup> In other words, if a manufacturer with a perfected security interest in the customer's inventory is better off on the date of the petition than it was ninety days before the petition, there is, by default, a preference.

While the purpose of this article is to provide a manufacturer with a process to attain protection from preference claims in the event of a customer's bankruptcy filing, following these procedures also provides the added benefit in the event the manufacturer remains unpaid for the goods irrespective of its customer's bankruptcy. If the manufacturer is a secured creditor, and a default in payment occurs, the manufacturer/lender can recover the collateral and sell it to pay down the customer's indebtedness.<sup>21</sup>

## **An Alternative Solution under the Michigan Special Tools Lien Act**

Michigan entities that manufacture equipment and deliver the equipment to their customers before receiving final payment may also find it possible to avoid a preference claim if they follow the procedures to perfect a lien in the equipment under the Michigan Special Tools Lien Act.<sup>22</sup>

The purpose of the Michigan Special Tools Lien Act (the "Act") is to provide protection to manufacturers by allowing liens to be imposed on valuable and specially designed and created products used in manufacturing in order to collect amounts owed for the creation of the special tools.<sup>23</sup>

The Act provides a very wide-ranging definition of "special tool." This definition includes any tools, dies, jigs, gauges, gauging, fixtures, special machinery, cutting tools, or metal castings manufactured by a special tool builder.<sup>24</sup> A "special tool builder" is a person who designs, develops, manufactures, or assembles special tools for sale.<sup>25</sup> It is likely that much of the equipment that a manufacturer produces will fall under this definition of "special tool."

Since the lien arises out of the operation of law, there is no requirement that the manufacturer have an agreement with its customer by which the customer expressly provides lien rights to the manufacturer, unlike the case when obtaining a PMSI. However, there is a process that the manufacturer must follow to perfect its lien rights in the "special tool" it manufactures and delivers to its customer.<sup>26</sup>

Under the Act, the manufacturer of the special tool must permanently record on every special tool that it fabricates, repairs or modifies, the special tool builder's name, street address, city, and state.<sup>27</sup> Additionally, the Act specifies that the manufacturer "shall file a financing statement" in the same manner it would perfect a security interest under Michigan's Uniform Commercial Code.<sup>28</sup> It is advisable that the manufacturer record its financing statement as soon as it is able to identify the equipment, even before delivery of the equipment to the customer. In any event, the manufacturer should perfect its lien interest in the equipment by filing the financing statement within twenty days after the customer takes delivery of the equipment.

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amount that the customer owes for the fabrication, repair, and/or modification of the special tool.<sup>29</sup> The lien attaches when the actual or constructive notice is received by the customer (or the end user).<sup>30</sup> The Act provides that the filing of a UCC-1 financing statement constitutes actual and constructive notice of the manufacturer's special tools lien.<sup>31</sup> However, the Act does not preclude other types of "actual" or "constructive" notice of the lien. To further bolster a manufacturer's lien claim, the manufacturer should include a statement in the quotation and invoice documents that the "special tool" produced under the contract is subject to the lien provided in the Act. Arguably, the inclusion of such a statement in the quotation and invoice documents provides the necessary notice such that the failure to correctly file a UCC-1 financing statement may not defeat the manufacturer's lien claim.<sup>32</sup> However, in a very recent decision, the U.S. Bankruptcy Court for the Eastern District of Michigan has held that in order to obtain an enforceable special tools lien, the Act requires a two-step process: the permanent recording of information on the tool, and the filing of a financing statement in accordance with section 9-502 of the Uniform Commercial Code.<sup>33</sup>

As is the case where the manufacturer perfects a PMSI in equipment, in addition to providing protection from preference claims in a bankruptcy, the special tools lien affords a remedy where the manufacturer is unpaid. To enforce the lien, the special tool builder is required to give notice of the lien in writing to the customer<sup>34</sup> by either certified mail or by hand delivery.<sup>35</sup> The notice must state that a lien is claimed, the amount claimed due for the fabrication, repair and/or modification of the special tool, and a demand for payment.<sup>36</sup> If the manufacturer is not paid within ninety days of receipt of the notice, the manufacturer may take possession of the special tool and sell it.<sup>37</sup>

### Comparing a PMSI to the Special Tools Lien

Both obtaining a PMSI and relying on a special tools lien have advantages and disadvantages. Whenever possible, the manufacturer should attempt to obtain and perfect both a PMSI and a special tools lien.

Customers may balk at including language within contract documents that grants the manufacturer a PMSI in the equipment or inventory. In many instances, the custom-

er will insist that its principal financier will not permit any other party to acquire a lien interest in the customer's assets. While it is common that loan covenants with its principal financier may prohibit the customer from granting any additional security interests in the customer's assets, the manufacturer's argument is that it is not acquiring a security interest in any of the customer's existing assets. Rather, the manufacturer is simply seeking to obtain a security interest in goods that are not yet in existence and that the manufacturer will terminate its security interest in the collateral as soon as it receives payment.

Since a special tools lien is created by operation of law and it is not required to be provided for in an agreement between the parties, this discussion will rarely arise between a manufacturer and its customer where the Act's special tools lien is available to a manufacturer. However, it has been reported that at least one original equipment manufacturer has notified tier-one suppliers and tool vendors that, as a matter of policy, its suppliers and tool vendors are prohibited from permanently recording their names and addresses on tools.<sup>38</sup> Complying with this policy will eliminate the ability to claim a special tools lien.

Where equipment is delivered out of Michigan, unless the laws of the destination state provide a similar lien, the manufacturer may not be able to claim a special tools lien.<sup>39</sup> A manufacturer may be able to avoid this problem by inserting language in its contract documents that specifies that Michigan law applies to and governs the contract which provides an avenue for the filing of a special tools lien on the equipment even though it is located in another state.<sup>40</sup> Alternatively, the manufacturer should have its legal counsel scour the laws of the state of the equipment's destination to determine whether that state provides a lien similar to the special tools lien, and if so, take the steps necessary to create and perfect such a lien. Since Revised Article 9 the Uniform Commercial Code has been adopted in one form or another by all fifty states, this is not an issue with the creation of a PMSI, although attention should be given in reviewing the applicable provisions of the state where the UCC-1 financing statement will be filed to ensure the perfection of the PMSI.

Finally, in some circumstances the manufacturer may find it impractical or impossible to recover and sell the recovered equipment

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in the event of non-payment. There may be no other market for the type of equipment manufactured, or the equipment may be subject to asserted intellectual property rights that prohibit the sale of the seized equipment.<sup>41</sup>

### An “Assist” in Reclamation Claims

A manufacturer that retains a PMSI in inventory or perfects a special tools lien in equipment delivered to its customer may also receive an added benefit in making a reclamation claim in the event the customer files for bankruptcy protection after the customer receives possession of the goods, but before it makes payment to the manufacturer. Under the Uniform Commercial Code, a seller has a right to reclaim goods sold on credit to an insolvent buyer by making written demand on the buyer within ten days after the goods are received by the buyer.<sup>42</sup>

The 2005 amendments to the Bankruptcy Code purported to grant even broader reclamation rights in bankruptcy cases than are available under the UCC. First, the Code was amended to expand the reach-back period from ten days to forty-five days.<sup>43</sup> As a result, sellers have more time to reclaim their goods under the Bankruptcy Code than under state law. Specifically, if the buyer files for bankruptcy protection, the seller's reclamation right extends to goods delivered up to forty-five days beforehand. Second, the 2005 amendments also expanded the grace period, giving the seller twenty days after a bankruptcy filing to deliver a reclamation notice where the forty-five-day reclamation period expires after the bankruptcy filing.<sup>44</sup> This effectively gives the seller up to sixty-five days after delivery of goods to a customer (forty-five-day reach-back plus twenty-day period to deliver the reclamation notice) to reclaim them. Additionally, and although not strictly a “reclamation” remedy, the amendments give the seller an administrative priority claim<sup>45</sup> equal to “the value of the goods received by the debtor within twenty days before [the date of the bankruptcy filing] in which the goods have been sold to the debtor in the ordinary course of such debtor's business.”<sup>46</sup>

Traditionally, reclamation is a difficult remedy to obtain. Courts have determined that the goods must be identifiable and in possession of the debtor on the date of the reclamation demand. In other words, goods that are resold by the buyer, incorporated

into finished products, or consumed in the buyer's business operations cannot be reclaimed.<sup>47</sup> The greatest impediment to a seller's reclamation claim, however, is the existence of a secured creditor with a perfected blanket security interest in the buyer's assets, including inventory and equipment.<sup>48</sup> The Bankruptcy Code provides that a seller's right of reclamation is “subject to the prior rights of a holder of a security interest in such goods or the proceeds thereof.”<sup>49</sup>

Cases interpreting the reclamation provisions of the Code have generally not been favorable to reclaiming creditors where there is a pre-petition lien in the debtor's assets. Typically, where there is a secured lender that holds a perfected security interest of a higher priority on the same assets (particularly, inventory) of the debtor as the reclaiming seller, the reclaiming seller loses. In *Simon & Schuster, Inc v Advanced Mktg Servs (In re Advanced Mktg Serv)*,<sup>50</sup> publisher Simon & Schuster delivered \$5.1 million worth of goods to the debtor within the forty-five-day reclamation period, which the publisher timely sought to reclaim after the buyer filed for bankruptcy protection. The bankruptcy court held that Simon & Schuster failed to prove that it would likely succeed on its reclamation claim due to the priority of the senior lenders' liens on substantially all of the debtor's assets, including inventory.<sup>51</sup> The bankruptcy court held that the senior lenders' liens were superior to Simon & Schuster's reclamation claim.<sup>52</sup> Once the senior lenders' liens were satisfied through the sale of inventory, Simon & Schuster's reclamation claim would likely be of no value.<sup>53</sup>

A similar result was reached in *In re Dana Corp.*<sup>54</sup> In *Dana* the debtor objected to reclamation claims filed by hundreds of sellers, arguing that the claims were subject to pre-existing liens on the goods sought to be reclaimed.<sup>55</sup> The court ruled in favor of the debtor, determining that pre-petition collateral, including the reclaimed goods, was subject to the secured creditors' pre-petition liens. The debtor's post-petition financing allowed the debtor to use the lenders' pre-petition collateral, with a replacement lien on all pre- and post-petition collateral and proceeds. The pre-petition indebtedness was refinanced and paid off from the proceeds of the new loan.<sup>56</sup> The court held that the reclaimed goods were either liquidated in satisfaction of the pre-petition indebtedness or were pledged as collateral for the debtor-

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in-possession loan.<sup>57</sup> In either event, the reclaimed goods were effectively disposed of, which rendered the reclamation claims valueless.<sup>58</sup>

To the extent a manufacturer correctly and timely perfects its lien in the goods through either a PMSI or a Special Tools Act lien, the lien of the manufacturer in the goods will be of a higher priority than the pre-existing blanket lien of a customer's secured lender.<sup>59</sup> Thus, the manufacturer should be able to nullify any argument that its reclamation claim is defeated by a pre-existing lien as advanced in *In re Advanced Mktg Servs*, and *In re Dana Corp.*

### Other Considerations

When contemplating methods to avoid bankruptcy preference claims, another strategy that the manufacturer should consider in negotiating the terms of the contract is to make certain that the manufacturer receives as much of the contract price as possible while the manufacturer remains in possession of the equipment. In such instances, the manufacturer will be able to claim that the payments it received while it possessed the equipment are not subject to preference claims because the manufacturer holds a lien on the equipment while it is in the manufacturer's possession. While there is no Michigan case directly on point, this exact issue was discussed by the United States Bankruptcy Court for the Western District of Pennsylvania in *Erie Power Techs, Inc v Shaw Group (In re Erie Power Techs)*.<sup>60</sup> In this case, the plaintiff/debtor filed an action against a power generator manufacturer. Prior to the plaintiff/debtor's bankruptcy filing, the manufacturer entered into a contract with the debtor where the manufacturer was to provide fabrication services on steel piping in accordance with the debtor's specifications.<sup>61</sup> The contract price was in the original amount of \$800,000 to be paid in an initial down-payment of \$160,000, followed by four "milestone" payments when 25 percent, 50 percent, 75 percent and 100 percent of the work was completed. The final payment was due prior to the final shipment.<sup>62</sup>

While the first milestone payment was timely made, on June 12, 2002, the debtor made a single payment for the second and third milestone in the total amount of \$320,000. The debtor made no payments after the June 12 payment, and the manufacturer completed the work under the contract. The debtor filed a Chapter 11 bankruptcy petition

on August 29, 2003. The goods remained in the manufacturer's possession in South Carolina until approximately six months later when, pursuant to a stipulation of the parties, the manufacturer delivered the goods to the debtor on receipt of the final payment.<sup>63</sup>

The debtor later brought a lawsuit against the manufacturer to force the return of the \$320,000 payment paid to the manufacturer on June 12, arguing that it was a preference payment because it was made by the debtor to the manufacturer within ninety days prior to the bankruptcy filing.<sup>64</sup> The manufacturer responded that it held a common law "artisan's lien" under South Carolina law on the goods while the goods were in its possession and, therefore, the transfer at issue was not a preference because the payment did not result in its receipt of any more funds than it would have received in a Chapter 7 bankruptcy.<sup>65</sup> The court recognized the validity of the common law artisan's lien and held in favor of the manufacturer.

The same should hold true in Michigan.<sup>66</sup> Michigan caselaw recognizes a common law lien in favor of persons who provide improvements to "articles."<sup>67</sup> Such a common law lien implies that the person possesses a right to detain or hold an article until it is paid for.<sup>68</sup> Additionally, Michigan has a statutory artisan's lien that may be applicable to manufacturers depending upon the type of goods produced.<sup>69</sup> To the extent a manufacturer receives a payment during the preference period but where the manufacturer retained possession of the goods, the manufacturer should be able to defeat a claim that the payment was preferential. On these bases, and from a practical standpoint, a manufacturer should consider negotiating payment terms such that the purchase price is paid, to the extent possible, while the manufacturer retains possession of the goods to defeat possible future preference claims.

### Conclusion

These are difficult economic times. Michigan's manufacturing industry has been particularly hard hit. The bankruptcy of a key customer can be a costly, if not irreparable, occurrence for a manufacturer. However, manufacturers that understand and are prepared to assert their rights can minimize their losses. Legal counsel can provide vital assistance to manufacturers by helping them protect their businesses from unexpected preference claims. While these suggestions

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may not provide absolute protection, they may lessen a manufacturer's exposure to a preference claim.

## NOTES

1. See, for example, *In re Chrysler, LLC*, Case No. 09-500002, (Bankr SD NY), *In re Metaldyne Corp*, Case No. 09-13412 (Bankr SD NY), *In re Visteon Corp*, Case No. 09-11786 (Bankr D Del), *In re General Motors Corp*, Case No. 09-50026 (Bankr SD NY), *In re Grede Foundries, Inc*, Case No. 09-14337 (Bankr WD Wisc), *In re DURA Automotive Systems, Inc.*, Case No. 06-11202 (Bankr D Del), *In re Delphi Corp*, Case No. 05-44481 (Bankr SD NY), *In re Meridian Automotive Systems, Inc.*, Case No. 05-11169 (Bankr D Del), *In re Tower Automotive, Inc.*, Case No. 05-10578 (Bankr SD NY), and *In re Plastech Engineered Products, Inc*, Case No. 08-42417 (Bankr ED Mich).<sup>2</sup> Or in some cases, the unsecured creditors committee or a liquidation trustee appointed under a plan of reorganization.

3. Or up to one year in the event the payment was made to an "insider." 11 USC 547(b)(4)(B).

4. 11 USC 101 *et seq.*

5. 11 USC 547(f).

6. 11 USC 547(b).

7. These defenses may include what is referred to as the "contemporaneous exchange" defense, the "ordinary course of business" defense, and the "new value" defense. See 11 USC § 547(c) of the U.S. Bankruptcy Code.

8. *Ellis v Ford Motor Credit Comp (In re DeLavern)*, 337 BR 239, 242 (Bankr WD Wash 2005); *Rocin Liquidation Estate v UPAC (In re Rocor)*, 380 BR 567, 572-74 (CA 10 BAP 2007); *Schwinn Plan Comm v Transamerica Ins Fin Corp (In re Schwinn Bicycle Co)*, 200 BR 980, 993 (Bankr ND Ill 1996). See also, *Telesphere Liquidating Trust v Galesi (In re Telesphere)*, 229 B R 173, 180 (Bankr ND Ill 1999).

9. 11 USC 547(b)(5). For further analysis of the function of 11 USC § 547(b)(5) see the recent opinion in *Shapiro v Art Leather Inc (In re Connolly North American, LLC)*, 398 BR 564, 571-572 (Bankr ED Mich 2008).

10. MCL 440.9103 (1) defines two terms that are "essential to the description of what constitutes a purchase-money security interest." Official Comment 3 to Revised § 9-103. The term *purchase-money collateral* means "goods or software that secures a purchase-money obligation incurred with respect to" that property. MCL 440.9103(1)(a). The related term *purchase-money obligation* is defined as "an obligation of an obligor incurred as all or a part of the price of the collateral or values given to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used." MCL 440.9103(1)(b). See P. Mears & S. Dales, *Michigan's Revised Article 9 of the UCC*, § 3.17, p 3-16 (ICLE) (2004).

11. J. Meyer, *A Primer on Purchase Money Security Interests Under Revised Article 9 of the Uniform Commercial Code*, 50 U Kan L Rev 143, 166-167 (2001) provides the following example:

Revised section 9-324(a), which in general tracks former section 9-312(4), provides that a perfected PMSI in goods other than inventory or livestock has priority over a conflicting security interest in the same goods or their identifiable proceeds, if the PMSI was perfected when the debtor obtained possession or within twenty days thereafter. Consider the following hypothetical:

Jan. 2 Dealer borrows \$100,000 from Bank for working capital and grants a security interest in "all equipment now owned or hereafter acquired." Bank

perfects by filing a proper financing statement with the secretary of state on January 5.

Feb. 10 Dealer buys and takes delivery from ABC Manufacturing Co. of a new machine to be used in its business, and agrees to pay for the machine over four years. ABC obtains an enforceable security interest in the machine and files a proper financing statement in the proper place on February 15.

If Dealer goes broke, who has priority as to the new piece of machinery?

Under the first-to-file rule, Bank would win because its security agreement covered after-acquired property and because it filed first. However, ABC can defeat Bank by establishing all the requirements of revised section 9-324(a). First, ABC must establish a PMSI under revised section 9-103. ABC can do this because the new machine is "purchase-money collateral" for a "purchase-money obligation." The security interest secures Dealer's obligation to pay the purchase price. Next, the machine is being used in Dealer's business and therefore is classified as equipment, not inventory. ABC also filed five days after Dealer took delivery, which is well within the twenty-day grace period. Thus, ABC has priority as to the machine because all the requirements of revised section 9-324(a) are satisfied [Footnotes omitted.]

12. If the debtor/customer is a corporation, limited liability company, or other "registered organization" it is "located" in the state of its organization. MCL 440.9307(5).

13. For a discussion of the "battle of the forms" issue see J. Trentacosta & J. Menges, *The Much-Maligned Purchase Order*, 86 Mich B J 32 (2007).

14. See footnote 12, *supra*.

15. MCL 440.9324(1).

16. MCL 440.9324(2)(a).

17. MCL 440.9324(2)(c).

18. MCL 440.9324(2)(d).

19. MCL 440.9324.

20. 11 USC 547(c)(5).

21. MCL 440.9609.

22. MCL 570.541 *et seq.*

23. House Legislative Analysis Section, HB5993 (May 8, 2002).

24. MCL 570.542(c).

25. MCL 570.542(d).

26. For a more complete discussion, see D. Loughlin, *Turning the Screws: Enhanced Rights Under the Michigan Special Tools Lien Act*, Mich Bus L J, Spring 2003, p 26, and W. Hawley, *Michigan Toolmakers' and Moldbuilders' Liens: Practical Considerations*, Mich Bus L J, Fall 2006, p 44.

27. MCL 570.563(1).

28. MCL 570.563(2), citing MCL 440.9502.

29. MCL 570.563(3).

30. Under the Act, the "end user" is a person who uses a special tool as part of his or her manufacturing process. MCL 570.542(b).

31. MCL 570.563(3), (4).

32. This argument is suggested in Roush Manufacturing, Inc.'s Reply to Objection to Roush's Motion for Relief from the Automatic Stay Arguing that Roush's Liens are Invalid in *In re Plastech Engineered Products, Inc, supra*, filed April 22, 2008 (Docket No. 1088).

33. *HS Die & Eng'g, Inc v Ford Motor Co (In re Plastech Engineered Products, Inc)*, 418 BR 235 (Bankr ED Mich 2009).

34. And the "end user," if applicable.

35. MCL 570.565.

36. *Id.*

37. MCL 570.567. The special tool builder can take possession of the special tool without judicial process if it can do so without a breach of the peace. MCL 570.567(a). The process for selling the special tool is set out in detail in MCL 570.569.

38. See J. Gregg, *An Introduction to Tooling Liens in the Automotive Industry (Part I)*, ABI Journal, June 2009, p 28, n 4.

39. See *Buffalo Molded Plastics, Inc v Plastic Mold Tech, Inc (In re Buffalo Molded Plastics, Inc)*, 354 BR 731 (Bankr WD Pa 2006), wherein the bankruptcy court for the Western District of Pennsylvania held that the Michigan Ownership Rights in Dies, Molds and Forms Act, MCL 445.611 et seq, pertaining to plastics mold liens, did not apply once the mold was delivered to Pennsylvania.

40. See J. Gregg, *An Introduction to Tooling Liens in the Automotive Industry (Part II)*, ABI Journal, July/August 2009, p 36, 74.

41. Section 31 of the Michigan Special Tools Lien Act, MCL 570.571, prohibits the sale or possession of the special tool where it would be a violation of federal patent or copyright law.

42. MCL 440.2702(2).

43. 11 USC 546(c).

44. *Id.*

45. An administrative claim is the highest level priority claim (but for certain domestic support obligations) in bankruptcy cases, but ranks under secured claims in entitlement to payment. 11 USC §§ 503(b), 507(a)(2).

46. 11 USC 503(b)(9).

47. *In re Charter Co*, 54 BR 91, 92-93 (Bankr MD Fla 1985); *In re Flagstaff Foodservice Corp*, 14 BR 462 (Bankr SDNY 1981).

48. S. Kimmelman and V. Hamilton, *A Paper Tiger: The Reclamation Seller in Bankruptcy*, The Metropolitan Corporate Counsel, April 2008, p 7.

49. 11 USC 546(c).

50. 360 BR 421 (Bankr D Del 2007).

51. *Id.* at 426.

52. *Id.*

53. See Kimmelman and Hamilton, *supra*.

54. 367 BR 409 (Bankr SDNY 2007).

55. See generally, *id.*

56. *Id.*

57. A practitioner in the 6<sup>th</sup> Circuit should be aware of *Phar-Mor Inc v McKesson Corp*, 534 F3d 502 (6<sup>th</sup> Cir 2008) *cert den* 129 Sct 2053 (2009), wherein the court appears to reject the holding in *In re Dana, supra*, regarding reclamation claims. However, it should be noted that the *Phar-Mor* decision is a pre-Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") (effective October 17, 2005) case. The holding in *Phar-Mor* may not apply to a post-BAPCPA claim. For a more detailed discussion of the possible implications of *Phar-Mor* see L. Gretchko, *Sixth Circuit's Phar-Mor Decision Breathes New Life Into Reclamation Remedy*, ABI Journal, September 2008, p 14.

58. See also Kimmelman and Hamilton, *supra*.

59. See MCL 440.9324(1) and (2) with respect to the priority of a purchase money security interest, and MCL 570.563(6) with respect to the priority of a Special Tools Lien.

60. 364 BR 896 (Bankr WD Pa 2007).

61. *Id.* at 897.

62. *Id.* at 897-898.

63. *Id.*

64. *Id.* at 897.

65. *Id.* at 899. See also 11 USC 547(b)(5).

66. The Sixth Circuit has also recognized the validity and priority of an artisan's lien in *Triad Int'l Maint*

*Corp v Southern Air Transp, Inc (In re Southern Air Transp, Inc)*, 511 F3d 526 (6<sup>th</sup> Cir 2007).

67. See, for example, *Aldine Mfg Co v Phillips*, 118 Mich 162, 76 NW 371 (1898); and *Nickell v Lambrecht*, 29 Mich App 191, 185 NW2d 155 (1970).

68. See 15 Mich Civ Jur, *Liens* § 2 (2008).

69. MCL 570.185 et seq.



Daniel M. Morley is a shareholder in the Traverse City office of Smith Haughey Rice & Roegge where he maintains a commercial law practice. He received a B.S., cum laude, from Michigan Technological University, and a J.D., with distinction, from Thomas M. Cooley Law School.



Kristen A. Campbell is an associate with in the Traverse City office of Smith Haughey Rice & Roegge. She received a B.S., with highest distinction, from Ferris State University, and a J.D., summa cum laude, from Michigan State University College of Law.