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Avoidance Theory According to Steve Nickles

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AVOIDANCE THEORY ACCORDING TO STEVE NICKLES

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Professor Steve Nickles is a much beloved presence in commercial law and certainly the only professor I know who has responded to a scholarly paper by handing baseball caps to the audience in attendance.

The occasion was a conference at the University of Virginia in 1993. I had written my usual paper emphasizing the theoretical failures of law and economics. At one point, I commented on a famous thesis to the effect that the existence of secured lending could be explained by reduction of monitoring costs. This was, in my opinion, a kind of magical claim that, by spending money on vigilance in some undisclosed fashion, risk could be dissipated. I suggested instead that the real point of a security interest is to intimidate debtors into good behavior, and in service of this power vigilance does some good. A security interest represented power to hurt, and power, I thought, was "the main thing."[1]

In his comment on my critique, Professor Nickles seized upon this one phrase. His comment consisted of handing out baseball caps on which was printed the phrase, "Power is the main thing."[2] This seemed to be a critique not only of secured lending but also of the will to power that dresses itself in the guise of policy science—what has recently been called "university discourse."[3]

I was very touched by this baseball cap. I am glad now to be able to return the favor, though in a nonbaseball mode. Alas, it is the function of a commentator to criticize—to show fault. I undertake this somber task with regret, because my regard for Professor Nickles's intellect and record of accomplishment is very

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1 This paper was cleft in twain and published in two different law reviews. *See* David Gray Carlson, *On the Efficiency of Secured Lending*, 80 VA. L. REV. 2179 (1994); David Gray Carlson, *Secured Lending as a Zero Sum Game*, 19 CARDOZO L. REV. 1635 (1998). "Power is the main thing" appears in the latter article. *See id.* at 1679.

2 Professor Nickles proceeded to publish a rather different critique. *See* Edward S. Adams et al., *Wedding Carlson and Schwartz: Understanding Secured Credit as a Fuzzy System*, 80 VA. L. REV. 2233 (1984).

3 On university discourse, see Jeanne L. Schroeder, *The Four Discourses of Law: A Lacanian Analysis of Legal Practice and Scholarship*, 79 TEX. L. REV. 15 (2000).

high. Fortunately, my critiques do not sting. They are more in the nature of encouragement for Professor Nickles to follow a path of analysis that he himself has been influential in establishing.

In his Article, Professor Nickles points out a common phenomenon in bankruptcy jurisprudence: What happens when the words of a statute are at odds with the clear legislative intent? For years, courts have perversely delighted in following the literal words of Congress, no matter how absurd the result. By following the literal words of statutes, courts have gleefully subverted congressional intent. Indeed, it is suggested by speculative philosophy that the surest way to subvert a system is to take it ultraseriously.[4]

In 1994, Congress gave us plenty of occasions to revisit this vicious instinct. The most striking occasion was the attempt by Congress to overrule the famous *Deprizio* case.[5] In this attempt at reversal, the statute literally says one thing, and the legislative history says another.

With his usual perspicuity, Professor Nickles has set forth the nature of this distinction between congressional intent and congressional action. For those who skipped Professor Nickles's article and proceeded directly to the commentary, the problem is this: § 547(b) avoids transfers to *or* for the benefit of a creditor.[6] Transfers to or for the benefit of *ordinary* (noninsider) creditors can be avoided only if made within ninety days of bankruptcy.[7] But transfers to or for the benefit of *insider* creditors can be avoided if within a year of the bankruptcy petition.[8]

In the *Deprizio* case, Judge Frank Easterbrook rocked the staid and conservative world of commercial law by pointing out that a regular creditor who received a transfer *more* than ninety days before bankruptcy had to return it if it benefited an insider creditor. In other words, a creditor who was the initial transferee of someone else's voidable preference had to give it back. Thus, when regular creditors took insider guarantees, they routinely faced a one-year preference period—not a ninety-day period. The guarantee made the regular creditor *worse* off, not better off.

In writing the *Deprizio* opinion, Judge Frank Easterbrook chose to use Bankruptcy Code § 550(a) to illustrate the point.

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4 *See* Slavoj Žižek, *Why Does the Law Need an Obscene Supplement?*, *in* LAW AND THE POSTMODERN MIND: ESSAYS ON PSYCHOANALYSIS AND JURISPRUDENCE 75, 89 (Peter Goodrich & David Gray Carlson eds., 1998). This is the very core of Hegelian dialectics, by the way. Rival philosophies are shown to bear the seeds of their own destruction.

5 *See* Levit v. Ingersoll Rand Fin. Corp., 874 F.2d 1186, 1192 (7th Cir. 1989).

6 *See* 11 U.S.C. § 547(b) (2000).

7 *See id.*

8 *See id.*

Under § 550(a)(1), either the initial transferee *or* the person benefited is liable. Easterbrook made his point convincingly, but he *could* have made the same point from the text of § 547(b), had he chosen to do so. The heart of *Deprizio* is actually to be found in § 547(b), not § 550(a), as Professor Nickles emphasizes.

In seeking to reverse this result, Congress stupidly assumed that the *Deprizio* dilemma was located solely in § 550(a). Therefore, Congress added § 550(c) to the Bankruptcy Code:

> If a transfer made between 90 days and one year before the filing of the petition—
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> (1) is avoided under section 547(b) of this title; and
>
> (2) was made for the benefit of a creditor that at the time of such transfer was an insider;
>
> the trustee may not recover *under subsection (a)* from a transferee that is not an insider.[9]

But, as Professor Nickles points out, if voidable preferences are voidable without the aid of § 550(a), then the amendment is unsuccessful. *Deprizio* still lives and reigns. Only when it is gone may creditors count their gains.

Professor Nickles points out many persuasive reasons why § 547(b) has force independent from § 550(a). For example, actions under § 547(b) have a different statute of limitations than actions under § 550(a). Property avoided under § 547 is preserved for the benefit of the estate under § 551 and is thereby made property of the bankruptcy estate under § 541(a)(4) without any need to refer to § 550(a). These and other points show, without question, that § 550(a) is not the source of bankruptcy avoidance. Elsewhere, I have suggested that the *sole* function of § 550(a) is to add in personam liability. The text of § 547(b) is able to establish only an in rem liability without the aid of § 550(a).[10]

So far, I am in line with Professor Nickles's analysis, and, indeed, he is one of the few scholars who has seen the Copernican truth that § 550(a) is not the center of the avoidance heavens. Nevertheless, the Nickles theory, though an advance over the usual analysis of avoidance, still suffers from a metaphorical confusion traceable to the text of the Bankruptcy Code itself. As a result, Professor Nickles falls prey to some analytical difficulties that are, to coin a phrase, avoidable.

Avoidance of transfers is a fundamental legal idea that occurs most prominently in federal bankruptcy law and, as stated earlier, there is disagreement as to whether § 550(a) is the fount of all

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9 11 U.S.C § 550(c) (2000) (emphasis added).

10 *See* David Gray Carlson, *Bankruptcy's Organizing Principle*, 26 FLA. ST. U. L. REV. 549, 553 (1999).

avoidance wisdom. The idea of avoidance is in actuality a state law idea, stemming from fraudulent conveyance doctrine. Properly analyzed, avoidance stands for the notion that the property of third-party transferees is susceptible to the judicial liens that creditors of the transferor are invited to establish.

Fraudulent conveyance law has always trafficked in a profound metaphorical confusion. The Uniform Fraudulent Conveyance Act ("UFCA"), still the law in New York and many other states, says that, if fraudulent, the conveyance by *D* to *X* should be "set aside."[11] The more recent Uniform Fraudulent Transfer Act ("UFTA") uses the phrase "avoidance."[12] But what do these highly metaphoric terms mean?

Suppose a debtor (*D*) conveys her house to her mother (*X*) for no consideration at a time when *D* is insolvent, in the hope that *D*'s creditors will not get it. This language of setting aside or avoiding a fraudulent conveyance leads to the impression that *D*, who has alienated the property once and for all, owns it once again. Such a conclusion is clearly a metaphorical error. Typically, *D* has alienated the property entirely. Fraudulent conveyance law is strictly an in rem right of *D*'s creditors in the fraudulently conveyed thing. In effect, after *D* conveys property to *X* under conditions deemed fraudulent, *D* no longer owns *any* interest in the conveyed property. *X* now holds the residual or "fee simple" interest in the property conveyed, but the property is made susceptible to any future judicial lien that a creditor of *D* might eventually obtain. If such a creditor's judicial lien successfully attaches to *X*'s property, the creditor may have the property sold in satisfaction of the judgment against *D*. Any surplus after the creditor has been paid must be returned to *X*.

I think the theory promulgated by Professor Nickles has not escaped metaphorical shadows cast by the UFCA. Professor Nickles sees *avoidance* as the assertion of some theory under the Bankruptcy Code—under § 547(b) or § 548(a), for example. Avoidance has three implications. First, avoidance *nullifies*. Nullification "always occurs upon avoidance and predicates the other two consequences."[13] Second, avoidance *preserves*. Preservation is simply the concept of § 551.[14] Whereas in nullification the trustee pretends the debtor never transferred the property, in preservation the trustee reverses field

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[11] UNIF. FRAUDULENT CONVEYANCE ACT § 9(1), 7A U.L.A. 198 (1918).

[12] UNIF. FRAUDULENT TRANSFER ACT § 7(1), 7A U.L.A. 339 (1984).

[13] 1 DAVID G. EPSTEIN, STEVE H. NICKLES & JAMES J. WHITE, BANKRUPTCY § 6-72, at 201 (1992). Professor Nickles is the second of three authors of his treatise, though, I am told, the author of all the sections discussing avoidance.

[14] *See* 11 U.S.C. § 551 (2000) ("Any transfer avoided under section 522, 544, 545, 547, 548, 549, or 724(a) of this title, or any lien void under section 506(d) of this title, is preserved for the benefit of the estate but only with respect to property of the estate.").

and admits that *D did* make the transfer to *X*, but *X* now forfeits the transfer to the bankruptcy trustee. Third, avoidance justifies *recovery*. Recovery is what happens pursuant to § 550. Under § 550, the trustee can win turnovers of property voidably transferred to *X*, which *X* possesses. But "[r]ecovery goes beyond avoidance."[15] It renders nontransferees liable when they "benefited" within the meaning of § 550(a), even though they received no transfers.

Avoidance also exceeds recovery. "Avoidance is always necessary for recovery, but recovery is not always necessary or even useful after avoidance,"[16] Nickles writes. Thus, in hypothecations where *D* possesses the encumbered thing, § 550 is not necessary to disencumber the thing. Nullification suffices.

This taxonomy has its strengths and weaknesses, which I would now like to explore. I have organized my comments according to the triune division suggested by Professor Nickles.

I. NULLIFICATION

Nullification, to my ear, is the same word as avoidance—not merely an attribute of avoidance. To avoid *is* to nullify.

An important issue is the procedure for nullification. If avoidance nullifies, does it do so automatically, or must the trustee bring an adversary proceeding? It is sometimes said that these transfers are *voidable*, not *void*. As one court commented, "Voidable is not the equivalent of void. The latter is a nullity; the former requires some action before the loss of all viability."[17] Similarly, to *nullify* is not the same as asserting the transfer is *null*. "To avoid" or "to nullify"—apparent synonyms—are activities, not descriptions of passive states (or passive nonstates).

Perhaps Professor Nickles will concede that nullification is an active idea that requires a procedure. Still, it need not be a procedure under § 550. A cause of action *in an adversary proceeding* might be sustained under, say, § 547(b) or § 548(a) directly.

But what is the state of a nullifiable conveyance before it is nullified? Is the property in question inside or outside the bankruptcy estate? If the former, the automatic stay prevents any creditor of the debtor (or the third party) from pursuing the property in question. If the latter, the automatic stay does not apply. The matter is exacerbated by § 541(a)(3), which includes as part of the bankruptcy estate "[a]ny interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, or 723 of this title."[18]

15 EPSTEIN ET AL., *supra* note 14, at 201.

16 *Id.* at 201.

17 *In re* Jones & Lamson Mach. Co., 113 B.R. 124, 127 (Bankr. D. Conn. 1990).

18 11 U.S.C. § 541(a)(3) (2000).

The provision suggests that, insofar as § 550(a) is required, nullifiable property is not in the estate *until* the trustee recovers it.

Nevertheless, it must be the case that, prior to nullification, the trustee already owns an interest in the property in question. This can be proved by observing what happens when the debtor conveys tainted property to a third party who then tries to convey the same property to a transferee of a transferee. Suppose *D* transfers a thing to *X* in satisfaction of an antecedent debt, and this transfer is a voidable preference under § 547(b). *X* then sells this thing to *B*, who is a bad faith purchaser for value. According to § 550(a)(2), the trustee can recover from *B*, who is a transferee of a transferee. How could this be, unless the trustee had a nascent interest in the property itself, prior to the conveyance from *X* to *B*?

Rather than using the language of nullification, a cleaner approach is available. We should say that, when *D* conveyed property to *X* in a fraudulent transfer or voidable preference, *D* successfully alienated all her property in the thing. Now *X* is the owner. But *X*'s ownership is *liable* (in the Hohfeldian sense) to judicial liens established by *D*'s creditors.[19] Among these is the hypothetical judicial lien of a bankruptcy trustee.

This is not to say that the judicial lien attaches to the tainted property straight out, before avoidance or nullification. If it did, then the conveyance would be void as soon as the lien attached, not merely voidable. Nevertheless, voidable title in *X* portends some title in the creditors of *D*, which a bankruptcy trustee inherits under § 544. This pre-lien susceptibility in *X*'s property triggers the automatic stay *ab initio* and reserves for the trustee the sole right to pursue the tainted property.

Furthermore, voidability should always imply a power in *X* to convey good title to a bona fide purchaser. This is a standard feature of "voidable title."[20] The concept is also legislated into fraudulent transfer statutes, since, in a fraudulent transfer, *X* has a voidable title.[21] It should also generally be the case that, where a bankruptcy

19 *See* WESLEY N. HOHFELD, FUNDAMENTAL LEGAL CONCEPTIONS AS APPLIED IN JUDICIAL REASONING AND OTHER LEGAL ESSAYS (1923). According to Hohfeld's famous system of opposites and correlatives, all law can be described by eight terms. Arranged by correlatives, any legal relationship between *A* and *B* can be described as follows:

If *A* has a:	right	privilege	power	immunity
Then *B* has a:	duty	no-right	liability	disability

Accordingly, if *X* has a liability to the judicial liens of *D*'s creditors, those creditors have power over *X*.

20 *See, e.g.*, U.C.C. § 2-403(1) (2000) ("A person with voidable title has power to transfer a good title to a good faith purchaser for value.").

21 *See, e.g.*, UNIF. FRAUDULENT CONVEYANCE ACT § 9(1), 7A U.L.A. 198 (1918). The UFTA unhappily extends bona fide purchaser protection to "a person who took in good faith and for a reasonably equivalent value." UNIF. FRAUDULENT TRANSFER ACT §8(a), 7A

trustee has an avoidance theory, the potential defendant should have a power to convey good title to a bona fide purchaser for value.

The Bankruptcy Code provides such a defense in a very limited way. According to § 550(b), transferees of transferees have a bona fide *transfer* defense. This defense goes beyond the bona fide purchaser idea by protecting creditors of *X*.[22] The implication of this extension is that, if *X* is bankrupt, *X*'s bankruptcy trustee is a bona fide transferee of *X* and therefore takes free and clear of *D*'s bankruptcy trustee. This seems unfortunate. Bona fide purchaser protection is about improving markets. Why should nonmarket participants get a windfall from the defrauded creditors of *D*?

But more to the point, if Professor Nickles is right that § 550(a) is not necessary to "nullify" a transfer, then the bankruptcy trustee might disenfranchise the § 550(b) defense by bringing an action under § 547(b). In such cases, bona fide purchaser defenses would have to be implied in many cases, or not provided at all.[23]

At the risk of digression, I would also like to present a question that has always bothered me, but which Professor Nickles's taxonomy actually solves. Suppose *D* grants *A* an unperfected security interest in personal property. The day before *D*'s bankruptcy petition, *A* assigns the security interest to *B*, who knows or should know the security interest is unperfected but does not know that *D* is contemplating bankruptcy. In such a case, is not *B* the transferee of a transferee, who takes the unperfected security interest free and clear of the bankruptcy trustee's avoidance rights? This appears to be the implication of § 550(b). One side effect of Professor Nickles's theory that § 550(a) is not necessary to nullify the security interest is that *B*'s unperfected security interest can indeed be avoided. The security interest can simply be "erased" from the collateral, and *B* could not claim the § 550(b) defense to prevent it. Meanwhile, the suggestion just made—that voidability always implies a bona fide purchaser defense—would have to be ignored. This is perhaps a strength of Professor Nickles's taxonomy.

II. PRESERVATION

Preservation, it seems to me, is a mistake imposed by the Bankruptcy Code in order to counteract its earlier mistake of

U.L.A. 351 (1984). The difference is that *X*'s judicial lien creditor is a protected person who might take a better interest than *D*'s creditor. In effect, the UFTA puts *D*'s creditors and *X*'s creditors in competition for assets supposedly held in trust for *D*'s creditors.

22 The Bankruptcy Code therefore shares the fault of the UFTA. Indeed, the UFTA is largely copied from the Bankruptcy Code.

23 Section 548(c) provides a bona fide transferee defense. Section 549(c) provides a defense to the bona fide purchasers of real property. Otherwise, the avoidance powers do directly refer to bona fide purchaser protection.

nullification or avoidance of transactions. If the conveyance is never avoided or nullified, then it need not be revived.

The textbook account of § 551 is that preservation is necessary when a senior lien is avoidable but a junior lien is not.[24] If the senior lien is merely "avoided"—in the sense of disappearing—then the junior lien would move up in priority and the bankruptcy trustee would not benefit from the avoidance action. Instead, in the unique case of liens, the senior lien is said to be *preserved*. Now the junior creditor does not move up. Rather, the trustee takes over the senior position for the benefit of the unsecured creditors. Incidentally, § 551 is by no means limited to this function. The statute on its face preserves the avoided transfers whether or not they are liens and whether or not there are junior creditors.

If, however, we abandon the "setting aside" metaphor, then there is no need for the "preservation" metaphor. Both concepts stand for the same thing—the susceptibility of third-party property to judicial liens of *D*'s creditors. In truth, where *D* makes some sort of voidable conveyance to *X* and then files for bankruptcy, the bankruptcy estate is comprised in part of *D*'s property and in part of *X*'s property. Avoidance and preservation simply makes this point in a confusing way.

To provide a quick example, suppose *D* grants a voidable, yet perfected senior mortgage to *X*. For example, the mortgage is on *X*'s antecedent debt. *D* subsequently grants a validly perfected junior mortgage to *Y* in exchange for new value. Properly, *X*'s mortgage is not nullified, avoided, or set aside. Rather, the judicial lien of *D*'s creditors (here, the bankruptcy trustee as representative of all such creditors) attaches to *X*'s mortgage. If the trustee were to execute on this judicial lien, the buyer at the execution sale would buy *X*'s position, which could then be asserted against *Y*. This step, however, is usually skipped in bankruptcy proceedings; the trustee is said to own *X*'s mortgage straight out, without any need of an execution sale. The point of this example is that what the Bankruptcy Code calls avoidance and preservation is really nothing but the expropriation of *X*'s security interest by the bankruptcy estate, which then asserts its seniority against *Y*'s security interest.

III. RECOVERY

According to Professor Nickles, recovery both exceeds and is exceeded by the concept of avoidance. Recovery is what happens

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[24] *See* John C. McCoid, II, *Preservation of Avoided Transfers and Liens*, 77 VA. L. REV. 1091, 1092-1102, 1116 (1991).

under § 550. As Nickles conceives it, avoidance is established by § 547, § 548, or one of the other avoidance theories. Many of these sections contain defenses. Only if the trustee survives those defenses is the conveyance voidable. But avoidance, Professor Nickles says, does not guarantee recovery. Section 550 contains several defenses against recovery. The *Deprizio* reform is one of them. There is likewise bona fide transferee protection under § 550(b)(1) for transferees of the initial transferee. There is a defense for the value of improvements made in good faith under § 550(e). Thus, a transaction might be avoided under, say, § 547, but would not be recoverable under § 550.

That avoidance is distinct from recovery is strongly supported by the fact that different statutes of limitations are applicable to § 547, etc., and to § 550. According to § 546(a):

> An action or proceeding under section 544, 545, 547, 548 or 553 may not be commenced after the earlier of—
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> (1) the later of—
>
> (A) 2 years after the entry of the order for relief; or
>
> (B) 1 year after the appointment or election of the first trustee under section 702, 1104, 1163, 1202, or 1302 of this title if such appointment or such election occurs before the expiration of the period specified in subparagraph (A); or
>
> (2) the time the case is closed or dismissed.[25]

Yet from § 550(f) we learn:

> An action or proceeding under this section may not be commenced after the earlier of—
>
> (1) one year after the avoidance of the transfer on account of which recovery under this section is sought; or
>
> (2) the time the case is closed or dismissed.[26]

Hence, it is possible to *avoid* an action under § 547 *and* recover later by filing an action under § 550(a). Hence, avoidance must be one thing and recovery another. Thus, Professor Nickles's taxonomy describes some truth about the structure of the Bankruptcy Code.

Still, there is something wrong with the distinction. To illustrate, compare the case of an unperfected security interest and the voidable conveyance of dollars. First, suppose *D* conveys an unperfected security interest to *X* and then files for bankruptcy. Professor Nickles suggests that *D*'s bankruptcy trustee can nullify the security interest under § 547(b) without the need of a "recovery" under § 550. In contrast, suppose *D* pays dollars to *X* on an antecedent debt, and these dollars are voidable preferences. Now

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25 11 U.S.C. § 546(a) (2000).

26 *Id.* § 550(f).

nullification is insufficient. We might erase *X*'s title to the dollars, but *X* physically possesses them. According to Professor Nickles, "recovery" is necessary.

This implies that "recovery" is a *physical* idea. Where *D* possesses the collateral physically, nullification amounts to mere erasure of the encumbrance. But where *X* is in physical possession—say a pledge on antecedent debt perfected slightly before bankruptcy—a recovery is needed.

This distinction, I believe, falls apart. In the case of *X*'s possession of the disputed property, the bankruptcy trustee does not need to "recover" under § 550(a) in order to gain physical possession of the dollars. Because of "nullification," *X* is in possession of the trustee's property. *X* has a duty to turn it over under § 542(a) of the Bankruptcy Code. Section 550(a) is not needed to establish this result.

Some other aspects of the Nickles description also do not resonate. For instance, Professor Nickles writes, "Avoidance is always necessary for recovery, but recovery is not always necessary or even useful after avoidance."[27] The first part of this formulation seems wrong. For example, suppose *C* lends to *D*, and *S* guarantees the loan. *D* then pays *C* one hundred days before bankruptcy (the *Deprizio* facts). *S* is a guarantor. Does this mean that the trustee cannot pursue *S* until after the trustee has sued *C* to nullify the transaction? At least one case has rejected such a claim flat out.[28]

If, however, Professor Nickles means only that a full cause of action showing a transfer to *C* must be shown in order to sustain the recovery from *S*, the statement is unobjectionable. Nevertheless, if avoidance is an act or event, it surely must be aimed in *C*'s direction. If, indeed, *C*'s transfer has never been nullified, and if, per Nickles, recovery from *S* is dependent on avoidance, then the trustee clearly cannot recover from *S* until the trustee joins *C* in an avoidance action under § 547(b).

IV. INTEGRATION WITH STATE LAW

Another criticism I have of the Nickles theory is that it is too distinctly federal in nature. It insufficiently integrates state law concepts. The need for integration is presented by the challenging case *GAF Linden Employees Federal Credit Union v. Robertson (In re Roberston)*.[29] In *Robertson*, a debtor filed for Chapter 13 protection and obtained confirmation of a plan. In the plan, a

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27 EPSTEIN ET AL., *supra* note 14, at 201.

28 *See* Crafts Plus, Inc. v. Foothill Cap. Corp. (*In re* Crafts Plus, Inc.), 220 B.R. 331, 334 (Bankr. W.D. Tex. 1998).

29 232 B.R. 846 (Bankr. D. Md. 1999).

creditor claiming an unperfected security interest in a truck was treated as an unsecured creditor. The secured creditor did not protest confirmation. Later, it sought a declaration that, because no adversary proceeding was brought to avoid its security interest, the security interest was still valid to secure the creditor's total claim against the debtor. In effect, the secured creditor took the earlier Nickles position that avoidance was a required event; nullification could not be assumed without the adversary proceeding.

Considerable authority exists for the proposition that a secured creditor is entitled to insist that a full adversary proceeding be brought against him in order to avoid a lien.[30] Typically, these cases protect *perfected* and *valid* security interests. The debtor's plan wrongly eliminates the creditor's security interest. Creditors have generally been permitted to have their liens in spite of confirmation on the theory that plans are simply incapable of wiping out the security interest. An adversary proceeding is required.

Judge Duncan Keir, however, reasoned that the plan *could* eliminate the unperfected security interest. He thought that the state law worked to avoid the unperfected security interest without any reference to the Bankruptcy Code at all.[31] Because Uniform Commercial Code ("UCC") § 9-301(3) made a bankruptcy trustee a "lien creditor," the unperfected security interest was already subordinated to the trustee before any adversary proceeding was filed.[32]

So far, Judge Keir had proved only that, under state law, the unperfected secured party was subordinated. How does this translate into the belief that the security interest was completely dead, as the Chapter 13 plan indicated? Judge Keir correctly saw that only a *sale* by a senior lien creditor could terminate the existence of the unperfected secured party. The Chapter 13 plan was itself such a sale. Under the plan, the debtor bought the truck free and clear of the unperfected security interest in exchange for his promise to pay in postpetition wages to the Chapter 13 trustee. In short, Chapter 13 plans are foreclosure sales within the meaning of UCC § 9-504(1).

This case, I think, says something profound about the nature of lien avoidance in bankruptcy and about lien priorities outside of

30 *See, e.g.*, Simmons v. Savell (*In re* Simmons), 785 F.2d 547, 553 (5th Cir. 1985). *See generally* 1 GRANT GILMORE & DAVID GRAY CARLSON, SECURED LENDING CLAIMS IN BANKRUPTCY, 954-65 (2d ed. 2000). *But see In re* Reg'l Bldg. Sys., Inc., 251 B.R. 274 (Bankr. D. Md. 2000) (denying an adversary proceeding is needed so long as notice is given that a reorganization plan will negate a security interest).

31 *Roberston*, 232 B.R. at 850.

32 Actually, it should have sufficed that the bankruptcy trustee is a lien creditor under Bankruptcy Code § 541(a)(1). The reference to the UCC endowment probably adds nothing.

bankruptcy. Voidable titles under state law imply a property right in creditors to "set aside" the conveyance so their judicial liens can attach. But are fraudulent conveyances "void" or merely "voidable"? Or, to pose the question in different terms, does a creditor's judicial lien *instantly* attach to fraudulently conveyed property, or must a creditor "avoid" the conveyance before a judicial lien attaches? The UFCA, for example, hedges its bets by stating that a defrauded creditor may: (a) have the conveyance set aside or obligation annulled to the extent necessary to satisfy his claim, or (b) disregard the conveyance and attach or levy execution upon the property conveyed.[33] Under this provision, where *D* makes a fraudulent conveyance to *X* of personal property, it is not clear that a creditor of *D* must "set aside" the conveyance. It might suffice for the creditor to serve a writ of execution on the sheriff requiring the sheriff to levy *X*'s property. In New York, delivery of the execution to the sheriff creates a defeasible lien on all of *D*'s personal property.[34] It might also suffice to create a lien on all of *X*'s property fraudulently received from *D*. Translated into bankruptcy terms, the bankruptcy trustee would then have a hypothetical judicial lien against any such property of *X* without the need of any adversary proceeding or "recovery" under § 550(a).

If such an interpretation of the UFCA is doubtful, the identical interpretation of the UCC is clear. Judicial liens attach to unperfected security interests instantly upon the bankruptcy petition, as the *Robertson* case shows. Thus, whether an adversary proceeding in bankruptcy is needed should relate to whether avoidance can be accomplished under state law without an adversary proceeding.

Automatic attachment of liens to voidably conveyed property undoubtedly has some disturbing side effects. The *Robertson* conclusion seems comfortable under Article 9, but, in fraudulent conveyance cases, it could engender some surprises. For example, if a Chapter 13 confirmation is a judicial foreclosure sale under state law, then *D* is vested not only with clear title to property previously encumbered with an unperfected security interest—more would be implied. *D* is likewise vested with clear title to *X*'s property that *D* fraudulently transferred to *X*—a rather odd result. Even this might be mitigated somewhat if the debtor is paying to the unsecured creditors whatever they would have received in a Chapter 7 case, as §1325(a)(4) requires. This rule implies that the creditors—not *D*—get the benefit of fraudulent conveyance recovery. But where no one has thought to enforce this rule, *X* is divested of title by the pure

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33 UNIF. FRAUDULENT CONVEYANCE ACT § 9, 7A U.L.A. 198 (1918).

34 *See* N.Y. C.P.L.R. § 5202(a) (McKinney 1999).

fact of the bankruptcy court's confirmation order. *D* would then be the sole beneficiary of *D*'s own fraudulent conveyance.

Here is one place where the § 550(a) imperialists have the jump on Professor Nickles and myself. The case often arises that a reorganization plan conveys all property of the estate to the reconstituted debtor. The debtor then sues some third party on a voidable preference or fraudulent transfer theory. Under the view that Professor Nickles and I share, the confirmation order transfers to the debtor all causes of action, which are property of the estate. The debtor should then be able to recover preferences that he himself made, even though only the debtor is enriched. It may be true that the plan should not have been confirmed under circumstances in which the debtor is permitted the beneficial use of these avoidance theories. It would be easy for a court to insist on a plan that assures that any recoveries after confirmation go to enrich the creditors. But, where the creditors have fixed entitlements under the plan, they cannot benefit from the debtor's postconfirmation recoveries.

The orthodox theory that makes § 550(a) central is able to say that, under § 550(a), only the trustee can recover "for the benefit of the estate." Since, here, the debtor is recovering for the benefit of his own noncreditor self, the debtor's cause of action under § 550(a) must fail.[35] Professor Nickles and I, however, are forced to confess that, if the trustee conveys his voidable preference cause of action to the debtor, the debtor can bring it *under § 547(b) directly*. Our view, if adopted, would require special vigilance by the bankruptcy courts to make sure that the confirmed plan allows creditors to benefit from the postconfirmation avoidance action.

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35 *See, e.g.*, Acequia, Inc. v. Clinton (*In re* Acequia, Inc.), 34 F.3d 800, 811 (9th Cir. 1994); Wellman v. Wellman, 933 F.2d 215, 217-18 (6th Cir. 1991).