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THE OVER-ENCUMBERED TRADE-IN IN CHAPTER 13

Nathan Goralnik*

ABSTRACT

The “hanging paragraph” in Bankruptcy Code § 1325(a) requires many debtors hoping to retain a vehicle under a chapter 13 plan to repay the full value of their auto lender’s secured claim, even if that claim is undersecured. This protection is limited to creditors with a purchase-money security interest in the debtor’s vehicle. Accordingly, bankruptcy courts reviewing a chapter 13 plan must consider the validity of an objecting creditor’s purchase-money security interest. This issue has proven controversial in cases where the lender financed both the debtor’s newly purchased vehicle and excess debt (“negative equity”) a trade-in vehicle. The highly general language of the Uniform Commercial Code affords few clues to the purchase-money status of financed negative equity. To break the impasse, this Article draws on heretofore-neglected evidence from the UCC’s text and drafting history that lends substance to the “consumer compromise” embodied in Revised Article 9. These materials indicate that the UCC maintains strict requirements for according purchase-money status to a consumer loan, and would not accord purchase-money status to financed negative equity. If this conclusion is at odds with the expectations of the drafters of the hanging paragraph, it suggests that they erred in hinging the applicability of a rule of federal bankruptcy law on a loan’s purchase-money status under state law.

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INTRODUCTION 16

I. NEGATIVE EQUITY UNDER THE HANGING PARAGRAPH: THREE APPROACHES 22

II. IS REFINANCED NEGATIVE EQUITY “PURCHASE MONEY?” 26

A. *Does Federal Law Regulate the Content of “Purchase Money”?* 27

B. *“Purchase-Money Obligation” in Article 9* 31

1. *Purchase Money as “Part of the Price of the Collateral”* 32

2. *Purchase Money as “Value Given to Enable”* 35

C. *Parsing Official Comment 3* 39

D. *Negative Equity and the Consumer Compromise* 43

III. DUAL-STATUS OBLIGATIONS UNDER THE HANGING PARAGRAPH 50

IV. CONCLUDING OBSERVATIONS 56

INTRODUCTION

Among the important changes wrought by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (“BAPCPA”) was to make it more expensive for debtors to retain a personal vehicle in chapter 13. Previously, a debtor could “bifurcate” her auto loan under § 506 of the Bankruptcy Code (the “Code”), which provides that a lien creditor has a secured claim only to the extent of the collateral’s replacement value; any deficiency is unsecured.¹ Accordingly, a chapter 13 debtor could “cram down” a plan allowing her to retain her vehicle without repaying the full balance of her car loan.² Since cars depreciate rapidly once driven off the dealer’s lot,³ bifurcation often left auto lenders undersecured and exposed to significant losses in chapter 13.⁴ In response, BAPCPA amended chapter 13’s

¹ 11 U.S.C. § 506(a)(1) (2006) (a lien holder’s allowed claim is secured to the extent of the collateral’s replacement value).

² *Id.* § 1325(a)(5)(B)(ii) (permitting confirmation if “the value . . . distributed under the plan . . . is not less than the allowed amount of such claim”).

³ See H.R. REP. NO. 106-123, pt. 1, at 128 (1999) (“Even though the vehicle is one day old, the amount of the secured creditor’s claim is, under current law, limited to the value of the automobile taking into account the immediate effect of depreciation upon purchase.”); see also Sumit Agarwal et al., *Asymmetric Information and the Automobile Loan Market* 14 (Am. Econ. Ass’n, Conf. Paper, 2005) (“Given the significant depreciation in auto values upon purchase, many borrowers have an auto loan balance greater than the current car value.”).

⁴ See William C. Whitford, *A History of the Automobile Lender Provisions of BAPCPA*, 2007 U. ILL. L. REV. 143, 146 (2007). Moreover, the applicable discount rate “could be far to the south of the interest rate

confirmation requirements to prevent many debtors from stripping down their car loans under § 506.⁵ However, the text and history of the new provision leave considerable uncertainty around the precise obligations of a chapter 13 debtor seeking to retain a vehicle over her auto lender's objection.

Lawmakers proposed a number of measures to protect consumer lenders from cramdown during the drafting of BAPCPA.⁶ The first House bills introduced in 1997 and 1998 would have protected both the principal balance and the contract interest rate from cramdown in an individual case under any Code chapter to the extent that the claim was attributable to a purchase-money loan for personal property acquired within 180 days of filing.⁷ A competing Senate draft contained two significant anti-cramdown provisions. The first was similar to the House proposal, but incorporated a shorter, ninety-day lookback period.⁸ A second provision, added on behalf of the automobile finance industry,⁹ would have prohibited bifurcation altogether in chapter 13 cases.¹⁰ A later Senate draft, also applicable to chapter 13, would have precluded bifurcation of any claim for a personal automobile loan incurred within five years of bankruptcy.¹¹

agreed to by the debtor in the security agreement.” David Gray Carlson, *Cars and Homes in Chapter 13 After the 2005 Amendments to the Bankruptcy Code*, 14 AM. BANKR. INST. L. REV. 301, 340 (2006).

⁵ Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 306(b), 119 Stat. 23, 80 (codified as amended at 11 U.S.C. § 1325(a) (2006)) (“[S]ection 506 shall not apply to a[n allowed] claim . . . if the creditor has a purchase money security interest securing the debt that is the subject of the claim, the debt was incurred within the 910-day [period] preceding the date of the filing of the petition, and the collateral for that debt consists of a motor vehicle . . . acquired for the personal use of the debtor . . .”).

⁶ For the legislative history of BAPCPA's automobile-lending provisions, see *In re Hayes*, 376 B.R. 655, 675 n.29 (Bankr. M.D. Tenn. 2007); Whitford, *supra* note 4, at 164–86. For the general legislative history of BAPCPA, see generally Susan Jensen, *A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 485 (2005).

⁷ Bankruptcy Reform Act of 1998, H.R. 3150, 105th Cong. § 128 (1998); Responsible Borrower Protection Bankruptcy Act, H.R. 2500, 105th Cong. § 110 (1997).

⁸ Consumer Bankruptcy Reform Act of 1998, S. 1301, 105th Cong. § 302(c) (as reported by S. Comm. on the Judiciary, June 4, 1998); see S. REP. No. 105-253, at 32 (1998).

⁹ See Whitford, *supra* note 4, at 177 (citing Harry Stoffer, *Lobbyists Push Industry's Problems with 'Cramdown' into the Spotlight*, AUTOMOTIVE NEWS, Oct. 26, 1998, at 28).

¹⁰ S. 1301, § 302(a) (providing that § 506 shall not apply to “an allowed claim . . . that is secured . . . by reason of a lien on property”); see S. REP. No. 105-253, at 33.

¹¹ S. REP. No. 106-49, at 224 (1999) (“[S]ection 506 shall not apply to a[n allowed] claim . . . if the debt . . . was incurred within the 5-year period preceding the filing of the petition and the collateral for that debt consists of a motor vehicle . . . acquired for the personal use of the debtor . . .”).

The narrower language ultimately adopted emerged in a 2001 draft provision entitled “Restoring the Foundation for Secured Credit.”¹² Finally enacted as an unnumbered “hanging paragraph” following Code § 1325(a), it provided that in the context of cramdown in chapter 13,

section 506 shall not apply to a[n allowed] claim . . . if the creditor has a purchase money security interest securing the debt that is the subject of the claim, the debt was incurred within the 910-day [period] preceding the date of the filing of the petition, and the collateral for that debt consists of a motor vehicle . . . acquired for the personal use of the debtor.¹³

Courts have interpreted the hanging paragraph as preventing a chapter 13 debtor from bifurcating a purchase-money loan for a personal vehicle incurred within 910 days of bankruptcy.¹⁴ Yet this language, described by scholars as “most peculiar”¹⁵ and even “bizarre,”¹⁶ has generated “confusion and incoherence in the law.”¹⁷ A casual reading of the hanging paragraph unearths a tangle of errors, ambiguities, and caveats.¹⁸ For example, even the core

¹² Bankruptcy Abuse Prevention and Consumer Protection Act of 2001, H.R. 333, 107th Cong. § 306(b) (2002) (as reported by H. Comm. On the Judiciary, Feb. 26, 2001); see H.R. REP. NO. 107-617, at 210 (2002) (Conf. Rep.).

¹³ Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 306(b), 119 Stat. 23, 80 (codified as amended at 11 U.S.C. § 1325(a) (2006)). For other types of purchase-money collateral, the hanging paragraph precludes application of § 506 “if the debt was incurred during the 1-year period preceding [the bankruptcy] filing.” *Id.*

¹⁴ See, e.g., *In re Pruitt*, 401 B.R. 546, 562 (Bankr. D. Conn. 2009) (“[A] debtor who proposes in her Chapter 13 plan to retain a 910–Vehicle pursuant to 1325(a)(5)(B) may not engage in Cram–Down, but rather, in order to fully satisfy the 910–Vehicle Claim, must now pay the present value of the *entire, deemed unitary claim, not just the actually secured component* of that claim, as might otherwise have been characterized under Section 506.”).

¹⁵ Carlson, *supra* note 4, at 340.

¹⁶ Jean Braucher, *Rash and Ride-Through Redux: The Terms for Holding on to Cars, Homes and Other Collateral Under the 2005 Act*, 13 AM. BANKR. INST. L. REV. 457, 472 (2005).

¹⁷ *AmeriCredit Fin. Servs., Inc. v. Long (In re Long)*, 519 F.3d 288, 292 (6th Cir. 2008).

¹⁸ For example, one immediately notices that the statute is difficult to cite: its scrivener omitted an alphanumeric designation. Dianne C. Kerns, *Cram-A-Lot: The Quest Continues*, AM. BANKR. INST. J., Nov. 2005, at 10. Additionally, Congress inexplicably adopted the 910-day (2.5-year) lookback provision as a “compromise” between proposals containing three- and five-year periods. Whitford, *supra* note 4 at 184; H.R. REP. NO. 107-617, at 210 (2002) (Conf. Rep.). The “910-day” language required a subsequent technical amendment to insert the missing word “period.” Bankruptcy Technical Corrections Act of 2010, Pub. L. No. 111-327, § 2(a)(44)(A), 124 Stat. 3557, 3562 (2010) (codified as amended at 11 U.S.C.A. § 1325(a) (West 2010)). These errors are far from the only problems evident in the hanging paragraph’s drafting. For further discussion, see Jean Braucher, *A Guide to Interpretation of the 2005 Bankruptcy Law*, 16 AM. BANKR. INST. L. REV. 349, 401–11 (2008); Braucher, *supra* note 16, at 469–74; Carlson, *supra* note 4, at 340–70; Kerns, *supra* note 18; Whitford, *supra* note 4, at 150–51.

“section 506 shall not apply” language, which Congress apparently believed “would prohibit ‘cramdowns,’”¹⁹ or operate as “a prohibition against bifurcat[ion],”²⁰ presents a conundrum. Section 506 does more than provide for the bifurcation of secured claims: it governs the very determination of secured status.²¹ Thus, instead of bolstering the automobile creditor’s security, a literal reading of “section 506 shall not apply” might remove statutory recognition of the creditor’s secured claim.²² This absurd result is foreclosed by the statute’s anti-cramdown purpose, which is plain in the legislative history,²³ but one scholar has commented that “[n]othing could be less plain” in the text itself.²⁴

This Article confronts a still more confounding ambiguity that has produced profound splits among the courts: the hanging paragraph’s application to only those creditors with a “purchase money security interest.”²⁵ This phrase, which is undefined in the Code, generally refers to an interest securing “an obligation . . . incurred as all or part of the price of the collateral or for value given to enable the debtor to acquire . . . the collateral.”²⁶ Under

¹⁹ S. REP. NO. 105-253, at 33 (1998).

²⁰ H.R. REP. NO. 109-31, pt. 1, at 17 (2005).

²¹ See 11 U.S.C. 506 (2006).

²² *In re Long*, 519 F.3d at 293 (“It may be argued that literally, without section 506, there cannot be an ‘allowed secured claim’ at all under § 1325(a)(5).”). For discussion, see Carlson, *supra* note 4, at 344–48.

²³ See *supra* notes 6–12.

²⁴ Braucher, *supra* note 18, at 401. A further peculiarity is that, in withholding bifurcation under § 506, the hanging paragraph protects only the *value* of the secured claim from cramdown. See *generally* Till v. SCS Credit Corp., 541 U.S. 465, 474 (2004) (“The challenge for bankruptcy courts . . . is to choose an interest rate sufficient to compensate the creditor . . .”). Even under the hanging paragraph, “[t]he time of payment and the amount of interest,” for example, “need not conform to the original security agreement. Rather, a (presumably lower) cram down interest rate may be imposed on the car lender.” Carlson, *supra* note 4, at 342. Earlier anti-cramdown proposals avoided this difficulty by clearly providing that “the amount of the allowed secured claim shall be the sum of the unpaid principal balance . . . and accrued and unpaid interest and charges at the contract rate.” Responsible Borrower Protection Bankruptcy Act, H.R. 2500, 105th Cong. § 110 (1997). This proposal further provided that in the case of commingled collateral, “the amount of the allowed secured claim shall be not less than the unpaid principal balance of the purchase price of the personal property acquired and unpaid interest and charges at the contract rate.” *Id.* Yet the silence of the hanging paragraph’s enacted language seemingly leaves the applicable interest rate to the court’s discretion, thus affording less than full protection to auto lenders.

²⁵ 11 U.S.C. § 1325(a).

²⁶ U.C.C. § 9-103(a)(2) (2011). Official Comment 3 adds:

As used in subsection (a)(2), the definition of “purchase-money obligation,” the “price” of collateral or the “value given to enable” includes obligations for expenses incurred in connection with acquiring rights in the collateral, sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, administrative charges, expenses of collection and enforcement, attorney’s fees, and other similar obligations.

the Uniform Commercial Code (the “UCC”), a vendor selling a particular good on credit may acquire a purchase-money security interest in the good that is senior to a more general advance of funds that merely names the good as collateral.²⁷ Courts applying the hanging paragraph have had to consider whether an auto lender holds a valid purchase-money security interest where the loan financed not only the sticker price of the car, but also additional items such as gap insurance,²⁸ extended warranties,²⁹ servicing contracts,³⁰ cash advances,³¹ and antecedent car loans.³²

The “most complex” of these problems relates to trade-in transactions.³³ Because many car buyers have negative equity in their trade-in vehicle (they owe more than the car is worth), they frequently require financing for the negative equity in the trade-in, in addition to the newly purchased vehicle.³⁴ For example, a buyer might owe \$8,000 on an existing vehicle worth \$5,000. If she seeks to trade in her car for another vehicle priced at \$18,000, she may need to finance both the \$18,000 purchase price *and* the \$3,000 in excess debt on the trade-in. In such a common situation, it is far from clear that sums advanced to retire the lien on the trade-in constitute “purchase money,” and the hanging paragraph’s legislative history leaves “no indication Congress gave

U.C.C. § 9-103 cmt. 3. Additionally, a “‘purchase-money security interest’ requires a close nexus between the acquisition of collateral and the secured obligation. Thus, a security interest does not qualify as a purchase-money security interest if a debtor acquires property on unsecured credit and subsequently creates the security interest to secure the purchase price.” *Id.*

²⁷ U.C.C. § 9-324(a). For historical background on the development of this seniority, see generally Grant Gilmore, *The Purchase Money Priority*, 76 HARV. L. REV. 1333 (1963).

²⁸ Compare *Ford Motor Credit Co. v. Dale (In re Dale)*, 582 F.3d 568, 575 (5th Cir. 2009) (extending the hanging paragraph’s protection to financed gap insurance), with *In re Munzberg*, 388 B.R. 529, 548 (Bankr. D. Vt. 2008) (bifurcating the portion of an auto loan attributable to the purchase of gap insurance).

²⁹ Compare *In re Dale*, 582 F.3d at 575 (extending the hanging paragraph’s protection to financed extended warranties), with *In re White*, 352 B.R. 633, 639–40 (Bankr. E.D. La. 2006) (denying application of the hanging paragraph to a financed extended warranty).

³⁰ Compare *In re Munzberg*, 388 B.R. at 544 (extending the hanging paragraph’s protection to a financed service contract), with *GMAC v. Home*, 390 B.R. 191, 205–06 (E.D. Va. 2008) (denying application of the hanging paragraph to financed service contracts), *aff’d in part*, 394 F. App’x 13 (4th Cir. 2010).

³¹ *In re Horn*, 338 B.R. 110, 113–14 (Bankr. M.D. Ala. 2006) (holding that the hanging paragraph does not protect additional cash advances).

³² *In re Vega*, 344 B.R. 616, 621–22 (Bankr. D. Kan. 2006) (holding that the hanging paragraph does not protect value given to refinance a buyer’s other vehicles).

³³ Braucher, *supra* note 18, at 407.

³⁴ Jim Henry, *Credit’s Easing for Auto Customers, Data Show*, AUTOMOTIVE NEWS (July 27, 2011, 10:24 AM), http://www.autonews.com/article/20110727/FINANCE_AND_INSURANCE/110729878/1142. More than one-fifth of trade-in vehicles were “upside down” in June 2011. *Id.*

the negative equity issue any thought at all.”³⁵ This conundrum forms the subject of this Article.

Part I begins by surveying existing approaches to the treatment of financed negative equity under the hanging paragraph. Whether a car loan that rolls in negative equity from an over-encumbered trade-in enjoys the protection of the hanging paragraph has divided the courts and generated an unresolved split among the circuits.³⁶ The case law has primarily looked to UCC § 9-103(a)(2) and its accompanying Official Comment 3 for guidance.³⁷ Yet, as Part II argues, these provisions are too general to furnish a satisfying argument for either position on the purchase-money status of negative equity. This Article charts a different approach. Drawing on heretofore neglected evidence from the text and drafting history § 9-103, I argue that the definition of purchase-money obligations remains highly restrictive in the context of consumer-goods transactions such as the sale of a vehicle, and excludes financed negative equity from purchase-money status.

If sums advanced to finance negative equity are not purchase money, a further question concerns whether a purchase-money security interest survives in the remainder of the loan. In some jurisdictions, the “transformation” rule denies purchase-money status to the entirety of a loan with a non-purchase-money component.³⁸ But in other jurisdictions, the less severe “dual-status” rule provides that such a loan remains a purchase-money obligation to the extent that it finances the new vehicle’s sticker price and related expenses.³⁹ Because the dual-status rule contemplates a car loan having purchase-money and non-purchase-money components, the precise application of the hanging paragraph to such loans is not straightforward.⁴⁰

³⁵ Braucher, *supra* note 18, at 407–08.

³⁶ See *infra* Part I. For an earlier survey of this case law, see Geoffrey M. Collins, Note, *Negative Equity and Purchase-Money Security Interests Under the Uniform Commercial Code and the BAPCPA*, 95 CORNELL L. REV. 161, 175 tbl. (2009); see also Juliet M. Moringiello, *(Mis)use of State Law in Bankruptcy: The Hanging Paragraph Story*, WISC. L. REV. (forthcoming) (manuscript at 972–82), available at <http://ssrn.com/abstract=2032078>.

³⁷ See U.C.C. § 9-103(a)(2) & cmt.3 (2011).

³⁸ See *infra* notes 79–81, 233–36. For background on the transformation rule, see generally Mary Aronov, *The Transformation Rule Applied to Purchase Money Security Interests in Commercial Lending Transactions*, 16 MEM. ST. U. L. REV. 15 (1985).

³⁹ See *infra* notes 66–77.

⁴⁰ See U.C.C. § 9-103 cmt. 7(a) (explaining that, under the dual-status rule, “a security interest may be a purchase-money security interest to some extent and a non-purchase-money security interest to some extent”).

Against this background, Part III makes an uneasy case for according negative-equity loans partial protection from bifurcation—that is, the hanging paragraph protects the purchase-money component from bifurcation, but not the sums used to finance negative equity. Ironically, while the UCC controls the definition of “purchase money,” the purchase-money status of a consumer auto loan has far greater federal- than state-law consequences under existing law. Thus, there is a practical logic to the courts’ tendency to stretch the state-law concept of purchase money to provide auto lenders with greater protection under federal bankruptcy law. Nevertheless, this approach risks upsetting the delicate structure of the purchase-money priority, just as withholding such protection would frustrate the hanging paragraph’s purpose to enhance the rights of undersecured auto lenders. The merit of the dual-status approach is that it furthers Congress’s apparent intent to the extent consistent with a coherent interpretation of the underlying state law.

I. NEGATIVE EQUITY UNDER THE HANGING PARAGRAPH: THREE APPROACHES

The interpretive puzzles posed by the hanging paragraph and its reference to purchase-money security interests involve a vital issue for many going through bankruptcy: how much will they have to pay their auto lender to retain their vehicle under a chapter 13 plan? A bankruptcy court may confirm a plan over the objection of a secured creditor if “the value . . . to be distributed under the plan on account of such claim is not less than the allowed amount of such claim.”⁴¹ Under Code § 506, this amount is generally limited to the replacement value of the collateral securing the debt,⁴² meaning that a debtor frequently does not need to make a secured creditor whole to retain the encumbered property. However, the hanging paragraph imposes more onerous requirements in the case of auto loans: it provides that “section 506 shall not apply” to claims for debt backed by a “purchase money security interest” in a personal motor vehicle and incurred within 910 days of the bankruptcy filing.⁴³ Thus, a debtor hoping to cram down a chapter 13 plan over the objection of her

⁴¹ 11 U.S.C. § 1325(a)(5)(B)(ii) (2006).

⁴² *Id.* § 506(a)(2).

⁴³ *Id.* § 1325(a). The statute withholds application of § 506 for other purchase-money loans incurred within one year of the bankruptcy filing. *Id.*

auto lender must presumably repay the full value of the debt, even if her vehicle is worth far less.⁴⁴

The hanging paragraph's exclusive application to creditors holding a purchase-money security interest in the debtor's vehicle has generated disagreement over the extent to which auto loans that finance negative trade-in equity are immune from bifurcation. First, courts have differed over whether funds used to retire negative equity give rise to purchase-money obligations or ordinary secured loans under the UCC. Second, the jurisdictions that have *not* regarded negative-equity financing as purchase money have divided over whether a loan that includes both purchase money (i.e., the financing for the new vehicle) and non-purchase money (i.e., the financing for negative trade-in equity) loses its purchase-money status *in toto* or only *pro tanto*. These disagreements have given rise to three broad approaches to the treatment of negative trade-in equity.⁴⁵

The most popular approach holds that the hanging paragraph protects the entire auto loan from bifurcation. Eight circuits have taken this position, construing the laws of Georgia,⁴⁶ Illinois,⁴⁷ Kansas,⁴⁸ Missouri,⁴⁹ New York,⁵⁰ North Carolina,⁵¹ Ohio,⁵² Texas,⁵³ and Virginia.⁵⁴ Lower courts have reached

⁴⁴ To be sure, the hanging paragraph does not explain what, other than the replacement value of the collateral, would govern the valuation of the auto lender's secured claim. *See supra* text accompanying notes 19–22. However, the hanging paragraph has been interpreted to render eligible claims “immune from cramdown and bifurcation of their full security interest in [debtors'] cars, including that portion deriving from the negative trade-in value of their prior cars.” *Reiber v. GMAC, LLC (In re Peaslee)*, 585 F.3d 53, 57 (2d Cir. 2009).

⁴⁵ For a concise review of these positions, see *In re Van Dyke*, No. 08-82866, 2009 WL 5206449, at *2 (Bankr. C.D. Ill. Dec. 23, 2009).

⁴⁶ *See Graupner v. Nuvel Credit Corp. (In re Graupner)*, 537 F.3d 1295, 1301 (11th Cir. 2008).

⁴⁷ *See Howard v. AmeriCredit Fin. Servs. (In re Howard)*, 597 F.3d 852, 858 (7th Cir. 2010); *In re Van Dyke*, 2009 WL 5206449, at *4 (following *In re Whipple*); *In re Whipple*, 417 B.R. 86, 96 (Bankr. C.D. Ill. 2009); *In re Smith*, 401 B.R. 343, 355 (Bankr. S.D. Ill. 2008).

⁴⁸ *See Ford v. Ford Motor Credit Corp. (In re Ford)*, 574 F.3d 1279, 1286 (10th Cir. 2009); *AmeriCredit Fin. Servs., Inc. v. Padgett (In re Padgett)*, 408 B.R. 374, 381 (B.A.P. 10th Cir. 2009) (decided prior to *In re Ford*).

⁴⁹ *See Nuvel Credit Co. v. Callicott (In re Callicott)*, 580 F.3d 753, 754 (8th Cir. 2009) (following *In re Mierkowski*); *Ford Motor Credit Co. v. Mierkowski (In re Mierkowski)*, 580 F.3d 740, 743 (8th Cir. 2009); *In re Weiser*, 381 B.R. 263, 271 (Bankr. W.D. Mo. 2007).

⁵⁰ *See Reiber v. GMAC, LLC (In re Peaslee)*, 585 F.3d 53, 57 (2d Cir. 2009).

⁵¹ *See Wells Fargo Fin. Acceptance v. Price (In re Price)*, 562 F.3d 618, 627–28 (4th Cir. 2009).

⁵² *See Nuvel Credit Corp. v. Westfall (In re Westfall)*, 599 F.3d 498, 503 (6th Cir. 2010); *In re Riley*, 428 B.R. 757, 763 (Bankr. N.D. Ohio 2010); *In re Hampton*, No. 07-14990, 2008 WL 5749718, at *4 (Bankr. S.D. Ohio June 16, 2008).

the same result in Alabama,⁵⁵ Florida,⁵⁶ Indiana,⁵⁷ Michigan,⁵⁸ Pennsylvania,⁵⁹ South Carolina,⁶⁰ Utah,⁶¹ Vermont,⁶² and Wisconsin.⁶³ While these decisions primarily interpret the definition of purchase-money obligations in UCC § 9-103(a)(2), a number of authorities have cited state automobile-finance statutes or relied on federal authority for additional support.⁶⁴ The Eleventh Circuit's seminal opinion in *In re Graupner* incorporates all three methods.⁶⁵

The second view denies purchase-money status to the portion of an auto loan used to finance the negative trade-in equity, but holds that the hanging paragraph nevertheless applies to the remaining purchase-money component of the loan. A Ninth Circuit bankruptcy appellate panel took this "dual-status" approach in *In re Penrod*.⁶⁶ Lower courts in Alaska,⁶⁷ Colorado,⁶⁸ Indiana,⁶⁹ Kentucky,⁷⁰ Mississippi,⁷¹ Oregon,⁷² Pennsylvania,⁷³ Tennessee,⁷⁴

⁵³ See *Ford Motor Credit Co. v. Dale (In re Dale)*, 582 F.3d 568, 575 (5th Cir. 2009).

⁵⁴ See *GMAC v. Horne*, 394 F. App'x 13 (4th Cir. 2010) (per curiam).

⁵⁵ See *In re Carlton*, No. 08-10624-DHW, 2008 WL 5045908, at *4 (Bankr. M.D. Ala. Nov. 24, 2008); *In re Harless*, No. BK 07-71959-CMS-13, 2008 WL 3821781, at *2 (Bankr. N.D. Ala. Aug. 13, 2008).

⁵⁶ See *In re Schwalm*, 380 B.R. 630, 635 (Bankr. M.D. Fla. 2008).

⁵⁷ See *In re Myers*, 393 B.R. 616, 622 (Bankr. S.D. Ind. 2008).

⁵⁸ See *Nuvell Credit Co. v. Muldrew (In re Muldrew)*, 396 B.R. 915, 925 (E.D. Mich. 2008).

⁵⁹ See *Porch v. GMAC (In re Porch)*, Ch. 13 Case No. 08-22404JAD, Adv. No. 08-02284JAD, 2009 WL 3614439, at *2 (Bankr. W.D. Pa. Oct. 16, 2009).

⁶⁰ See *In re Vinson*, 391 B.R. 754, 758 (Bankr. D.S.C. 2008).

⁶¹ See *In re Austin*, 381 B.R. 892, 897 (Bankr. D. Utah 2008); *In re Burt*, 378 B.R. 352, 362 (Bankr. D. Utah 2007).

⁶² See *In re Munzberg*, No. 07-10560, 2010 Bankr. LEXIS 5021, at *6 & n.2 (Bankr. D. Vt. Sept. 29, 2010), *reconsideration denied*, 2011 WL 240472 (Bankr. D. Vt. Jan. 21, 2011).

⁶³ *In re Morey*, 414 B.R. 473, 481 (Bankr. E.D. Wis. 2009); *In re Dunlap*, 383 B.R. 113, 119 (Bankr. E.D. Wis. 2008).

⁶⁴ See *In re Whipple*, 417 B.R. 86, 87 (Bankr. C.D. Ill. 2009) (arguing for a federal law definition of "purchase money security interest").

⁶⁵ *Graupner v. Nuvell Credit Corp. (In re Graupner)*, 537 F.3d 1295, 1300-03 (11th Cir. 2008).

⁶⁶ *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 392 B.R. 835, 838 (B.A.P. 9th Cir. 2008). The panel's adoption of the dual-status approach was not an issue on appeal, but the Ninth Circuit affirmed the panel's holding that financed negative equity is not purchase money. *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 611 F.3d 1158, 1160 n.2, 1164 (9th Cir. 2010), *en banc reh'g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

⁶⁷ See *In re Williams*, No. A09-00745-DMD, 2011 WL 5025230, at *1 n.4 (Bankr. D. Alaska Jan. 31, 2011) (noting the probable impact of *Penrod*).

⁶⁸ See *In re McCauley*, 398 B.R. 41, 47 (Bankr. D. Colo. 2008).

⁶⁹ See *In re White*, 417 B.R. 102, 106 (Bankr. S.D. Ind. 2009) (holding that the dual-status rule applied to the confirmed plan).

⁷⁰ See *In re Bandura*, No. 08-50378, 2008 WL 2782851, at *2 (Bankr. E.D. Ky. July 15, 2008).

⁷¹ See *In re Busby*, 393 B.R. 443, 448 (Bankr. S.D. Miss. 2008).

Washington,⁷⁵ West Virginia,⁷⁶ and Wisconsin⁷⁷ have also followed the dual-status approach. Although most of these opinions confined their choice of law to UCC § 9-103(a)(2), a few—including the bankruptcy appellate panel in *Penrod*—have packaged the dual-status approach as a federal rule of decision.⁷⁸

Finally, a few courts have denied the protection of the hanging paragraph altogether, permitting bifurcation of the entire claim. Bankruptcy courts in Alabama,⁷⁹ Florida,⁸⁰ and Tennessee⁸¹ have cited state-law “transformation” rules to hold that the non-purchase-money component vitiates the loan’s purchase-money status. Another Tennessee court,⁸² and one in Maine,⁸³ have reached the same result on federal-law grounds, holding that the hanging paragraph does not protect a loan with a non-purchase-money component,

⁷² See *In re Valiquette*, No. 09-64167-fra13, 2010 WL 695991, at *2 (Bankr. D. Or. Feb. 24, 2010) (following *Penrod*); *In re Riach*, No. 07-61645-aer13, 2008 WL 474384, at *4 (Bankr. D. Or. Feb. 19, 2008); *In re Johnson*, 380 B.R. 236, 250 (Bankr. D. Or. 2007).

⁷³ *GMAC v. Mancini (In re Mancini)*, 390 B.R. 796, 807 (Bankr. M.D. Pa. 2008). *But see* *Porch v. GMAC (In re Porch)*, Ch. 13 Case No. 08-22404JAD, Adv. No. 08-02284JAD, 2009 WL 3614439, at *2 (Bankr. W.D. Pa. Oct. 16, 2009).

⁷⁴ *In re Hayes*, 376 B.R. 655, 674 (Bankr. M.D. Tenn. 2007). *But see In re Mitchell*, 379 B.R. 131, 141 (Bankr. M.D. Tenn. 2007) (denying altogether the application of the hanging paragraph on federal law grounds); *In re Bray*, 365 B.R. 850, 863 (Bankr. W.D. Tenn. 2007) (applying a state law transformation rule).

⁷⁵ *In re Siemers*, No. 11-44935, 2011 WL 5598349, at *3 (Bankr. W.D. Wash. Nov. 17, 2011) (following *Penrod*); *In re Wear*, No. 07-42537, 2008 WL 217172, at *3 (Bankr. W.D. Wash. Jan. 23, 2008).

⁷⁶ *In re Hall*, 400 B.R. 516, 521 (Bankr. S.D. W. Va. 2008).

⁷⁷ See *In re Crawford*, 397 B.R. 461, 468 (Bankr. E.D. Wis. 2008). *But see In re Morey*, 414 B.R. 473, 480 (Bankr. E.D. Wis. 2009); *In re Dunlap*, 383 B.R. 113, 117 (Bankr. E.D. Wis. 2008).

⁷⁸ The bankruptcy appellate panel in *Penrod* proposed that “the Dual Status Rule should be applied as the federal rule,” even in the face of contrary state law. *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 392 B.R. 835, 859 & n.25 (B.A.P. 9th Cir. 2008), *aff’d*, 611 F.3d 1158 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011). The panel’s decision to apply the dual-status approach as federal rule was not at issue on appeal. *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 611 F.3d 1158, 1160 n.2 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011). Bankruptcy courts in Oregon, Vermont, and West Virginia have similarly applied the dual-status rule to effectuate the purposes of BAPCPA. See *In re Hall*, 400 B.R. at 521; *In re Munzberg*, 388 B.R. 529, 546 (Bankr. D. Vt. 2008); *In re Johnson*, 380 B.R. 236, 250 (Bankr. D. Or. 2007); see also *In re Westfall*, 376 B.R. 210, 219 (Bankr. N.D. Ohio 2007) (adopting “use of the dual status rule for the purposes of the hanging paragraph”), *rev’d sub nom. Nuvell Credit Corp. v. Westfall (In re Westfall)*, 599 F.3d 498 (6th Cir. 2010).

⁷⁹ See *In re Tuck*, No. 06-10886-DHW, 2007 WL 4365456, at *3 (Bankr. M.D. Ala. Dec. 10, 2007) (applying a state-law transformation rule).

⁸⁰ See *In re Blakeslee*, 377 B.R. 724, 730–31 (Bankr. M.D. Fla. 2007).

⁸¹ See *In re Bray*, 365 B.R. 850, 863 (Bankr. W.D. Tenn. 2007).

⁸² See *In re Mitchell*, 379 B.R. 131, 141 (Bankr. M.D. Tenn. 2007).

⁸³ See *In re Look*, 383 B.R. 210, 220–21 (Bankr. D. Me. 2008).

regardless of the applicable state-law approach. However, authorities categorically denying the protection of the hanging paragraph have frequently been reversed on appeal.⁸⁴

II. IS REFINANCED NEGATIVE EQUITY “PURCHASE MONEY?”

Valuing an auto loan for cramdown purposes often requires bankruptcy judges to interpret not one, but three interlocking and highly ambiguous statutory texts. The reference to “purchase money” in Bankruptcy Code § 1325(a) directs the interpreter to a vexingly abstract definition given in UCC § 9-103 and an open-ended list of examples in the accompanying Official Comment 3. Instead of providing clarity, this multi-step inquiry has only sent courts deeper into a semantic thicket. The next subparts of this Article show why existing rationales for according purchase-money status to financed negative equity are unconvincing.

This Part concludes by proposing an alternative approach. I argue that a reading of the UCC that is attentive to its historical treatment of consumer-goods transactions yields powerful insight into the definitional boundaries of purchase money in this context. In drafting Revised Article 9, those pushing for a more expansive concept of purchase money successfully assimilated many transaction costs into the items a purchase-money loan could finance, but they were *unsuccessful* with respect to the forms of financial engineering embodied in a trade-in sale with financed negative equity.⁸⁵ Thus, the drafting history of § 9-103 suggests that funds used to retire negative equity are not purchase money under the law of most states. Provisions of § 9-103 addressing the purchase-money status of cross-collateralization and refinancing transactions confirm this understanding.

⁸⁴ See, e.g., *In re Price*, 363 B.R. 734, 746 (Bankr. E.D.N.C. 2007), *aff'd in part, rev'd in part*, No. 5:07-CV-133-BR, 2007 WL 5297071 (E.D.N.C. Nov. 14, 2007), *rev'd*, 562 F.3d 618 (4th Cir. 2009); *In re Sanders*, 377 B.R. 836, 864 (Bankr. W.D. Tex. 2007), *rev'd sub nom.* *Ford Motor Credit v. Sanders (In re Sanders)*, 403 B.R. 435 (W.D. Tex. 2009); *In re Peaslee*, 358 B.R. 545, 555 (Bankr. W.D.N.Y. 2006), *rev'd sub nom.* *Gen. Motors Acceptance Corp. v. Peaslee (In re Peaslee)*, 373 B.R. 252 (W.D.N.Y. 2007), *aff'd sub nom.* *Reiber v. GMAC, LLC (In re Peaslee)*, 585 F.3d 53 (2d Cir. 2009).

⁸⁵ See *infra* note 203.

A. *Does Federal Law Regulate the Content of “Purchase Money”?*

Bankruptcy Code § 1325(a) protects a claim from bifurcation if, among other things, “a purchase money security interest secur[es] the debt that is the subject of the claim,”⁸⁶ yet the Code fails to define “purchase money.” While most authorities consult state law to determine the purchase-money status of financed negative equity, some courts have argued that federal law helps to resolve the issue.⁸⁷ However, because purchase-money obligations are creatures of state law, this Subpart concludes that the purchase-money status of negative trade-in equity eludes resolution on purely federal-law grounds.

The most popular, albeit flawed, federal-law argument favoring the automobile creditor attempts to reconstruct congressional intent based on the general purposes of the hanging paragraph. This argument proceeds, in part, from an assumption that the “architects [of the hanging paragraph] intended only good things for car lenders and other lienholders”⁸⁸ and were hostile to cramdown in chapter 13 cases.⁸⁹ The Eleventh Circuit reasoned in *Graupner* that “the hanging paragraph ultimately seeks to require a debtor electing to retain a ‘910 vehicle’ to pay the creditor the full amount of the claim and not . . . an amount equal to the present value of the car.”⁹⁰ Additionally, since “[r]olling a trade-in’s negative equity into the purchase price of a new vehicle was a common occurrence at the time BAPCPA was enacted in 2005,”⁹¹ courts have expressed reluctance “to read the hanging paragraph in a way that denies its protections to a large percentage of claims held by car lenders.”⁹²

⁸⁶ 11 U.S.C. § 1325(a) (2006).

⁸⁷ The leading example is *In re Whipple*, 417 B.R. 86, 87 (Bankr. C.D. Ill. 2009), which held that “Congress intended the hanging paragraph to be interpreted as a matter of federal law so that ‘purchase money security interest’ is accorded a uniform federal definition.”

⁸⁸ *Graupner v. Nuvel Credit Corp.* (*In re Graupner*), 537 F.3d 1295, 1303 (11th Cir. 2008) (alteration in original) (quoting *AmeriCredit Fin. Servs., Inc. v. Long* (*In re Long*), 519 F.3d 288, 294 (6th Cir. 2008)).

⁸⁹ See *In re Morey*, 414 B.R. 473, 481 (Bankr. E.D. Wis. 2009); *Nuvel Credit Co. v. Muldrew* (*In re Muldrew*), 396 B.R. 915, 924 (E.D. Mich. 2008); *In re Dunlap*, 383 B.R. 113, 118 (Bankr. E.D. Wis. 2008).

⁹⁰ *In re Graupner*, 537 F.3d at 1302 (citing *Trejos v. VW Credit, Inc.* (*In re Trejos*), 374 B.R. 210, 220 (B.A.P. 9th Cir. 2007)); see also *Ford Motor Credit Co. v. Mierkowski* (*In re Mierkowski*), 580 F.3d 740, 745 (8th Cir. 2009) (Bye, J., dissenting). *Graupner*’s reference to a “910 vehicle” refers to “a motor vehicle . . . acquired for the personal use of the debtor” financed by a purchase-money loan “incurred within the 910-day period preceding the date of the filing of the petition.” 11 U.S.C. § 1325(a)(9) (2006).

⁹¹ *In re Graupner*, 537 F.3d at 1303.

⁹² *Wells Fargo Fin. Acceptance v. Price* (*In re Price*), 562 F.3d 618, 628 (4th Cir. 2009); see also *AmeriCredit Fin. Servs., Inc. v. Padgett* (*In re Padgett*), 408 B.R. 374, 381 (B.A.P. 10th Cir. 2009).

Yet even if congressional intent controlled the construction of “purchase money security interest,” this “imaginative reconstruction”⁹³ of Congress’s intent would be less than fully convincing. First, the argument that the creditors should prevail because the “architects [of the hanging paragraph] intended only good things for car lenders and other lienholders”⁹⁴ advances an implicit, winner-takes-all concept of interest group pluralism that is hard to defend on normative or empirical grounds.⁹⁵ As one opinion retorted, “Congress must reconcile many competing interests when drafting legislation. Presuming Congress resolved all policy questions in favor of one constituency is simplistic and likely inaccurate.”⁹⁶ “[N]othing in the statute or the legislative history,” another argued, “says that Congress intended to give car lenders and others not just good things, but everything.”⁹⁷ In drafting the hanging paragraph, Congress had to balance greater protection of auto lenders against the interests of the credit card industry and other lobbies pressing for the enactment of BAPCPA.⁹⁸

Second, the text and legislative history of the hanging paragraph reinforce the conclusion that Congress did not extend the statute’s benefits to every car loan, regardless of its purchase-money status.⁹⁹ The “purchase money security interest” limitation first appeared in S. 3186, introduced in October 2000;¹⁰⁰ an earlier House bill would have extended the hanging paragraph’s protection to *any* claim secured by a motor vehicle within the lookback period.¹⁰¹ “Congress specifically chose to use the term ‘purchase money security interest’ instead of something broader.”¹⁰² Enforcing the hanging paragraph’s limited application to “purchase money security interests” requires careful construction of the term, not airy references to Congress’s general intent to protect creditors.

⁹³ This phrase is borrowed from William N. Eskridge, Jr., *The New Textualism*, 37 UCLA L. REV. 621, 630 (1990).

⁹⁴ *In re Graupner*, 537 F.3d at 1303 (quoting *AmeriCredit Fin. Servs., Inc. v. Long (In re Long)*, 519 F.3d 288, 294 (6th Cir. 2008)).

⁹⁵ See Cass R. Sunstein, *Interpreting Statutes in the Regulatory State*, 103 HARV. L. REV. 405, 447–49 (1989).

⁹⁶ *Ford v. Ford Motor Credit Corp. (In re Ford)*, 574 F.3d 1279, 1294 (10th Cir. 2009) (Tymkovich, J., dissenting).

⁹⁷ *In re Padgett*, 408 B.R. at 393 (Starzynski, J., concurring).

⁹⁸ See Whitford, *supra* note 4, at 181–83.

⁹⁹ See *In re Ford*, 574 F.3d at 1292 (“I cannot conclude the hanging paragraph protects any and every loan secured by an automobile.”).

¹⁰⁰ Bankruptcy Reform Act of 2000, S. 3186, 106th Cong. § 306(b) (2000).

¹⁰¹ Bankruptcy Reform Act of 2000, H.R. 833, 106th Cong. § 306(b) (as passed by Senate, Feb. 2, 2000).

¹⁰² *In re Ford*, 574 F.3d at 1294.

Third, while it is tempting to imagine that Congress would have intended for the hanging paragraph to extend to the large segment of the market represented by trade-in sales with negative equity, even this claim is suspect. The hanging paragraph's 910-day lookback period suggests that "[t]he problem that Congress intended to address was the simple one of the debtor purchasing a vehicle and then shortly thereafter filing a Chapter 13 petition and writing down the value of the vehicle" to avoid paying the full value of the loan.¹⁰³ If this problem is unique to the automobile market, it is because cars depreciate rapidly from the time of sale, leaving auto lenders immediately undersecured. However, in a trade-in sale with negative equity, the excess debt is undersecured from the get-go because it is inherited from the buyer's earlier loan. Moreover, many trade-in transactions roll over negative equity from loans incurred *prior* to the 910-day lookback period.¹⁰⁴ In sum, the problem of excess debt inherited from a trade-in vehicle seems sufficiently dissimilar from that of a deficiency arising within 910 days of the sale to cast doubt on the claim that Congress intended to treat these issues identically.

Fourth, purchase-money status for refinanced negative equity is potentially incongruous with other bankruptcy principles. If a federal-law concept of purchase money existed, it would likely encompass the enabling transfers described in Code § 547, which BAPCPA's drafters seemingly equated with "Purchase Money Security Interests."¹⁰⁵ Among other requirements, these transactions must "secure[] *new value*;" must be "given to enable the debtor to acquire such property;" and must "in fact [be] used by the debtor to acquire such property."¹⁰⁶ However, the definition of "new value" in this context "does not include an obligation substituted for an existing obligation"; that is, it excludes refinancing transactions.¹⁰⁷ Thus, the best candidate for a federal-law

¹⁰³ See also *AmeriCredit Fin. Servs., Inc. v. Padgett* (*In re Padgett*), 408 B.R. 374, 392 (B.A.P. 10th Cir. 2009).

¹⁰⁴ Judge Bea argued in *Penrod* that because "the loan company which held title to the [trade-in vehicle] had a purchase money secur[ity] interest . . . the fact that the old loan is rolled into a new one" should not "make a difference." *AmeriCredit Fin. Servs., Inc. v. Penrod* (*In re Penrod*), 636 F.3d 1175, 1177 (9th Cir. 2011) (Bea, J., dissenting from the denial of en banc rehearing). Yet, it is far from obvious that the hanging paragraph should apply if the "old loan" were incurred more than 910 days before the filing of the petition.

¹⁰⁵ See Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 1222, 119 Stat. 23, 196 (2005) (codified at 11 U.S.C. § 547(c)(3)(B) (2006)); 11 U.S.C. § 547(c)(3)(A) (2006).

¹⁰⁶ *Id.* § 547(c)(3)(A) (emphasis added).

¹⁰⁷ *Id.* § 547(a)(2).

“purchase money security interest” would likely *exclude* the portion of an auto loan that refinanced the debtor’s existing automobile loan.¹⁰⁸

It is difficult then to discern support for the view that BAPCPA itself brought negative equity into the ambit of purchase money. The better approach, adopted by the “great majority” of opinions, recognizes that Congress employed “purchase money security interest” as a state-law term of art.¹⁰⁹ On this view, “[c]ongressional intent cannot expand [state-law] definitions beyond their traditional meanings . . . to include negative equity financing,” regardless of the benefits Congress intended to confer on the hanging paragraph’s beneficiaries.¹¹⁰ Because the purchase-money security interest is a creature of state law, it invites application of *Nobelman v. American Savings Bank*’s guidance suggesting that courts “assume that Congress has left the determination of property rights . . . to state law.”¹¹¹

To be sure, a small minority has held that “purchase money security interest” should have a uniform federal definition “not dependent upon or subject to the variations in . . . state law.”¹¹² Moreover, if Congress had intended to incorporate a state-law term of art, one bankruptcy judge reasoned that it could have done so explicitly: “Congress routinely and expressly incorporates state law when it wants to, and did not do so here.”¹¹³ Yet the hanging paragraph’s enacted text evinces no intent to enforce a separate federal-law definition of the term. For example, during the drafting of BAPCPA, Congress abandoned an early effort to craft a federal-law definition

¹⁰⁸ Cf. *AmeriCredit Fin. Servs., Inc. v. Penrod* (*In re Penrod*), 611 F.3d 1158, 1164 (9th Cir. 2010) (concluding that refinanced negative equity consisted of “old obligations that have been repackaged,” and thus, “would not qualify as new value”), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

¹⁰⁹ See, e.g., *Wells Fargo Fin. Acceptance v. Price* (*In re Price*), 562 F.3d 618, 624 (4th Cir. 2009). The Second Circuit even certified the question of its interpretation to the New York Court of Appeals. *Reiber v. GMAC, LLC* (*In re Peaslee*), 547 F.3d 177, 179 (2d Cir. 2008), *certifying question to Reiber v. GMAC, LLC* (*In re Peaslee*), 913 N.E.2d 387 (N.Y. 2009).

¹¹⁰ *Ford Motor Credit Co. v. Mierkowski* (*In re Mierkowski*), 580 F.3d 740, 747 (8th Cir. 2009) (Bye, J., dissenting); *accord In re White*, 417 B.R. 102, 106 (Bankr. S.D. Ind. 2009) (“Congress chose not to alter or expand the traditional meanings of purchase money obligation and PMSI . . .”).

¹¹¹ *Nobelman v. Am. Sav. Bank*, 508 U.S. 324, 329 (1993) (quoting *Butner v. United States*, 440 U.S. 48, 54 (1979)) (internal quotation marks omitted).

¹¹² *In re Whipple*, 417 B.R. 86, 95 (Bankr. C.D. Ill. 2009); *In re Van Dyke*, No. 08-82866, 2009 WL 5206449, at *4 (Bankr. C.D. Ill. Dec. 23, 2009).

¹¹³ *In re Whipple*, 417 B.R. at 95.

of the claims protected from bifurcation,¹¹⁴ in favor of the enacted language referring to the well-known state-law concept of “purchase money.”¹¹⁵ Thus, it is state law to which the hanging paragraph’s interpreters must inevitably turn.

B. “Purchase-Money Obligation” in Article 9

Article 9 of the UCC governs the definition,¹¹⁶ perfection,¹¹⁷ and priority of purchase-money security interests.¹¹⁸ However, the law “does not provide a precise, encapsulated definition of purchase money security interest, but rather a string of connected definitions.”¹¹⁹ At the time of BAPCPA’s drafting,¹²⁰ Former Article 9-107 defined “purchase money security interest” as a security interest

- (a) taken or retained by the seller of the collateral to secure all or part of its price; or
- (b) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.¹²¹

This language was condensed in Revised Article 9-103(a)(2), which provides that “‘purchase-money obligation’ means an obligation . . . incurred as all or part of the price of the collateral or for value given to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used.”¹²²

¹¹⁴ See Bankruptcy Reform Act of 1999, H.R. 833, 106th Cong. § 122 (as placed on Senate calendar, May 12, 1999) (preventing bifurcation of “an allowed claim to the extent attributable in whole or in part to the purchase price of personal property”).

¹¹⁵ Bankruptcy Reform Act of 2000, S. 3186, 106th Cong. § 306(b) (2000).

¹¹⁶ U.C.C. § 9-103 (2011).

¹¹⁷ *Id.* § 9-309(1).

¹¹⁸ *Id.* § 9-324.

¹¹⁹ *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 611 F.3d 1158, 1161 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

¹²⁰ Revised Article 9 became effective in 2001. U.C.C. § 9-701.

¹²¹ U.C.C. § 9-107 (1972) (current version at U.C.C. § 9-103(a)(2) (2011)). Official Comment 2 added:

When a purchase money interest is claimed by a secured party who is not a seller, he must of course have given present consideration. This section therefore provides that the purchase money party must be one who gives value “by making advances or incurring an obligation”

Id. § 9-107 cmt. 2 (current version at U.C.C. § 9-103 cmt. 3 (2011)). The quoted language excludes from the purchase money category any security interest taken as security for or in satisfaction of a pre-existing claim or antecedent debt. *Id.*

¹²² U.C.C. § 9-103(a)(2) (2011). Official Comment 3 adds:

Following these interpretive guideposts, courts have sought to determine whether financing the negative equity in the debtor's trade-in vehicle (1) represents "all or part of the price of the collateral" or (2) constitutes "value given to enable the debtor to acquire rights in . . . the collateral."¹²³ Most courts have looked to the accompanying Official Comment 3 to help illuminate these highly general provisions. Official Comment 3 notes that a purchase-money obligation might finance "expenses incurred in connection with acquiring rights in the collateral" and "other similar obligations."¹²⁴ Occasionally, courts have also looked to their jurisdiction's automobile-finance statute to determine whether negative equity is part of the vehicle's "price."¹²⁵ Despite the complexity of this inquiry, the courts' disagreement ultimately appears to center on whether financing negative equity is better viewed as incidental to the new-vehicle purchase or as a separate transaction.¹²⁶ Lost in this essentially indeterminate debate are legislative-historical clues. Part II.D argues that these clues favor a more restrictive, formal understanding of "purchase money" that would exclude negative trade-in equity.

1. Purchase Money as "Part of the Price of the Collateral"

While most authorities resort to Official Comment 3 to interpret § 9-103's reference to "the price of the collateral,"¹²⁷ a few opinions have held, unconvincingly, that the phrase's plain meaning precludes according purchase-money status to financed negative equity. One influential opinion, which was subsequently reversed, argued that the term "'price of the collateral' need

As used in subsection (a)(2), the definition of "purchase-money obligation," the "price" of collateral or the "value given to enable" includes obligations for expenses incurred in connection with acquiring rights in the collateral, sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, administrative charges, expenses of collection and enforcement, attorney's fees, and other similar obligations.

Id. § 9-103 cmt. 3. Additionally, a "'purchase-money security interest' requires a close nexus between the acquisition of collateral and the secured obligation. Thus, a security interest does not qualify as a purchase-money security interest if a debtor acquires property on unsecured credit and subsequently creates the security interest to secure the purchase price." *Id.*

¹²³ *Id.* § 9-103(a)(2).

¹²⁴ *Id.* § 9-103 cmt. 3.

¹²⁵ See *infra* Part II.B.1.

¹²⁶ See, e.g., *Ford v. Ford Motor Credit Corp. (In re Ford)*, 574 F.3d 1279, 1285 (10th Cir. 2009) ("We conclude the trade-in exchange is essentially a single transaction.").

¹²⁷ See *infra* Part II.C.

not . . . sweep up more than the common understanding of the phrase.”¹²⁸ The court speculated that “the person on the street might be surprised to learn that a court had concluded that the cost of paying off the excess loan on the trade-in should also count as ‘the price’ of the [new] vehicle itself.”¹²⁹ Similarly, another court has argued that “the definition of purchase money obligation itself limits itself to ‘all or part’ of the price of the collateral, suggesting that the ‘price’ is the upper limit.”¹³⁰ In these opinions, a purchase-money loan is one that finances *only* the price of the collateral securing it; other items, such as legacy debt retired to facilitate the transaction, are excluded from the commonsense meaning of “the price of the collateral.” The trouble with these interpretations is that they cannot account for the language of Official Comment 3, which explicitly stretches the meaning of “price” beyond its plain meaning.¹³¹

In contrast with this plain-meaning analysis, other courts have looked to their jurisdictions’ automobile-finance statutes to determine what “price” means in the technical context of a vehicle sale.¹³² These statutes “typically include definitions of ‘cash price’ or ‘total sales price’ which include negative equity.”¹³³ For example, the bankruptcy court in *Graupner* read Georgia’s automobile-finance statute *in pari materia* with Article 9.¹³⁴ Because the statute explicitly incorporated financed negative equity into the “cash sale

¹²⁸ *In re Sanders*, 377 B.R. 836, 853 (Bankr. W.D. Tex. 2007), *rev’d sub nom.* Ford Motor Credit v. Sanders (*In re Sanders*), 403 B.R. 435 (W.D. Tex. 2009).

¹²⁹ *Id.* at 852.

¹³⁰ AmeriCredit Fin. Servs., Inc. v. Padgett (*In re Padgett*), 408 B.R. 374, 389 (B.A.P. 10th Cir. 2009) (Starzynski, J., concurring).

¹³¹ See U.C.C. § 9-103 cmt. 3 (2011).

¹³² See *Graupner v. Nuvell Credit Corp.* (*In re Graupner*), 537 F.3d 1295, 1299, 1301 & n.3 (11th Cir. 2008) (collecting cases). *Graupner* cited Georgia’s vehicle-finance statute, but this has not been viewed as crucial to its holding. See *In re Carlton*, No. 08-10624-DHW, 2008 WL 5045908, at *3 (Bankr. M.D. Ala. Nov. 24, 2008).

¹³³ Ford Motor Credit Co. v. Mierkowski (*In re Mierkowski*), 580 F.3d 740, 746 (8th Cir. 2009) (Bye, J., dissenting). In contrast, some states’ automobile-finance statutes exclude negative equity from the “price” of a vehicle. See, e.g., *In re Wear*, No. 07-42537, 2008 WL 217172, at *3 (Bankr. W.D. Wash. Jan. 23, 2008) (noting this trend in Washington, Oregon, New York, Georgia, and California); *In re Johnson*, 380 B.R. 236, 244 (Bankr. D. Or. 2007) (citing OR. REV. STAT. § 83.510(1) (2001)).

¹³⁴ *In re Graupner*, 356 B.R. 907, 922 (Bankr. M.D. Ga. 2006), *aff’d sub nom.* Graupner v. Nuvell Credit Corp. (*In re Graupner*), No. 4:07-CV-37CDL, 2007 WL 1858291 (M.D. Ga. June 26, 2007), *aff’d*, 537 F.3d 1295 (11th Cir. 2008).

price” of a retail installment contract,¹³⁵ the court concluded that the definition of “price” under Georgia’s § 9-103(a)(2) included these sums.¹³⁶ Other courts have reached analogous holdings based on their states’ respective statutes.¹³⁷

Yet other circuits have resisted statutory invitations to read the forum state’s automobile-finance statute *in pari materia* with the “price” prong of § 9-103(a)(2). For example, the Seventh Circuit noted that Illinois’s Article 9 gives way to other statutes establishing “a different rule for consumers,”¹³⁸ including the state’s Motor Vehicle Retail Installment Sales Act,¹³⁹ which “allows a car dealer or financier to include negative equity in the amount of the price of the car that he finances, just as he can include an attorney’s fee.”¹⁴⁰ California’s Article 9 also explicitly incorporates the state’s automobile-finance statute.¹⁴¹ It defines a vehicle’s “cash price” to include “payment of a prior credit or lease balance remaining on property being traded in.”¹⁴² Despite the statutes’ seemingly inclusive language, both the Seventh and Ninth Circuits held that the respective statutes defined “price” for the limited purpose of regulating *disclosure* to car buyers; neither regulated the scope of a car lender’s purchase-money priority vis-à-vis other creditors.¹⁴³

¹³⁵ GA. CODE ANN. § 10-1-31(a)(1) (West 2011) (“[C]ash sale price may also include any amount paid . . . on behalf of the buyer to satisfy a lease on or a lien on or a security interest in a motor vehicle used as a trade-in . . .”).

¹³⁶ *In re Graupner*, 356 B.R. at 922–23.

¹³⁷ See, e.g., *In re Mierkowski*, 580 F.3d at 743 (“[I]nterpreting ‘price’ in Article 9 to include negative equity is consistent with the definition of ‘time sale price’ in [the Missouri Motor Vehicle Time Sales Act.]”); *In re Morey*, 414 B.R. 473, 481 (Bankr. E.D. Wis. 2009) (reading the Wisconsin Consumer Act *in pari materia* with Wisconsin’s version of Article 9); *In re Smith*, 401 B.R. 343, 352–53 (Bankr. S.D. Ill. 2008) (reading an Illinois automobile-finance statute *in pari materia* with Article 9); *In re Cohrs*, 373 B.R. 107, 110 (Bankr. E.D. Cal. 2007) (quoting CAL. CIV. CODE § 2981(e) (West 2006)); *Reiber v. GMAC, LLC* (*In re Peaslee*), 913 N.E.2d 387, 390 (N.Y. 2009) (noting that New York’s Motor Vehicle Retail Installment Sales Act defines “price” to include financed negative equity).

¹³⁸ *Howard v. AmeriCredit Fin. Servs.* (*In re Howard*), 597 F.3d 852, 856 (7th Cir. 2010) (quoting 810 ILL. COMP. STAT. 5/9-201(b)(2) (2001)).

¹³⁹ 815 ILL. COMP. STAT. ANN. 375/2.8, 2.10 (West, Westlaw through P.A. 97-1132 of the 2012 Reg. Sess.).

¹⁴⁰ *In re Howard*, 597 F.3d at 856–57.

¹⁴¹ CAL. COM. CODE § 9201(b) (West 2012).

¹⁴² *Id.* CIV. § 2981(e).

¹⁴³ *AmeriCredit Fin. Servs., Inc. v. Penrod* (*In re Penrod*), 611 F.3d 1158, 1163 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011); *In re Howard*, 597 F.3d at 857; *accord Ford Motor Credit Co. v. Mierkowski* (*In re Mierkowski*), 580 F.3d 740, 747 (8th Cir. 2009) (Bye, J., dissenting); *In re Crawford*, 397 B.R. 461, 467 (Bankr. E.D. Wis. 2008).

At most then, the rules governing negative equity in state automobile-finance statutes provide “evidence that negative equity is indeed a common element of a credit purchase of a car.”¹⁴⁴ Perhaps reinforcing this conclusion, Official Comment 3 provides an extensive list of expenses included in the “‘price’ of collateral.”¹⁴⁵ This suggests an intention to define the term rather than to incorporate existing meanings.

2. Purchase Money as “Value Given to Enable”

Many courts have looked to language in § 9-103(a)(2) defining purchase money as “value given to enable the debtor to acquire rights in . . . the collateral,”¹⁴⁶ seizing on its seemingly more accommodating language.¹⁴⁷ These courts have held that paying off the negative equity in a trade-in “enables” the transaction by discharging the lien on the trade-in so that the buyer may exchange it for the new car. “[T]he payoff of Debtors’ negative equity in their trade-in vehicle ‘enabled’ them to purchase the vehicle,” one court held, because it “played an integral role in the overall transaction.”¹⁴⁸ Specifically, “[r]eleasing the lien on the trade-in vehicle allows the dealer to sell it and, in turn, makes the purchase of the new vehicle possible.”¹⁴⁹ Many courts have observed that there is often no other way for a car buyer to dispose of her over-encumbered trade-in vehicle.¹⁵⁰

In contrast, other courts have argued that paying off the negative equity in the trade-in vehicle is a separate transaction completed to accommodate the borrower’s circumstances rather than to facilitate the sale of the new vehicle.¹⁵¹ For example, one widely cited opinion urged that to satisfy the UCC’s definition, “the value must be used to acquire *rights* in the collateral, as

¹⁴⁴ *In re Howard*, 597 F.3d at 857.

¹⁴⁵ U.C.C. § 9-103 cmt. 3 (2011).

¹⁴⁶ *Id.* § 9-103(a)(2).

¹⁴⁷ *See, e.g.*, *Nuvell Credit Corp. v. Westfall (In re Westfall)*, 599 F.3d 498, 503 (6th Cir. 2010); *Ford Motor Credit Co. v. Dale (In re Dale)*, 582 F.3d 568, 575 (5th Cir. 2009); *Wells Fargo Fin. Acceptance v. Price (In re Price)*, 562 F.3d 618, 625 (4th Cir. 2009).

¹⁴⁸ *In re Westfall*, 599 F.3d at 505; *see also In re Dale*, 582 F.3d at 575; *In re Price*, 562 F.3d at 625–26; *Reiber v. GMAC, LLC (In re Peaslee)*, 913 N.E.2d 387, 390 (N.Y. 2009).

¹⁴⁹ *In re Westfall*, 599 F.3d at 505; *see also In re Morey*, 414 B.R. 473, 480 (Bankr. E.D. Wis. 2009).

¹⁵⁰ *See, e.g.*, *Howard v. AmeriCredit Fin. Servs. (In re Howard)*, 597 F.3d 852, 857 (7th Cir. 2010).

¹⁵¹ *See e.g.*, *In re Sanders*, 377 B.R. 836, 855 (Bankr. W.D. Tex. 2007), *rev’d sub nom.* *Ford Motor Credit v. Sanders (In re Sanders)*, 403 B.R. 435 (W.D. Tex. 2009).

opposed to, for example, *enabling the transaction* that ultimately results in the borrowers acquiring rights in the collateral.”¹⁵²

The view that refinancing the borrower’s existing car loan is “readily separable from the purchase transaction itself,”¹⁵³ and thus is not purchase money, turns on the intuition that a car buyer need not trade in or refinance her existing vehicle to purchase a new one. All aspects of the trade-in transaction—the purchase of a new vehicle, the sale of an existing vehicle, and the refinancing of the existing vehicle—can occur separately. For example, a borrower may opt to refinance her existing vehicle while purchasing an additional vehicle (e.g., for a family member).¹⁵⁴ In such a case, the entire loan does not enable the purchase of the new vehicle nor is the “value given” “in fact so used.”¹⁵⁵ Alternatively, a debtor seeking to reduce her loan balance might sell her over-encumbered vehicle and refinance the negative equity without purchasing a new car.¹⁵⁶ Finally, a debtor not looking to sell *or* buy a car can refinance her vehicle to obtain cash.¹⁵⁷ Notably, none of these scenarios includes the necessary link between the refinancing of the existing vehicle and the purchase of a new one. Instead, each of these refinancing transactions merely facilitates the car owner’s financial goals by, respectively, consolidating two car loans, reducing a loan balance, and obtaining a cash advance. These examples suggest that a debtor financing the negative equity in

¹⁵² *Id.* In response, the Fourth Circuit argued that “[f]rom a practical perspective, that distinction is meaningless. If negative equity financing enabled the transaction in which the new car was acquired, then, in reality, the negative equity financing also enabled the acquisition of rights in the new car.” *In re Price*, 562 F.3d at 625; *accord* AmeriCredit Fin. Servs., Inc. v. Penrod (*In re Penrod*), 636 F.3d 1175, 1179 (9th Cir. 2011) (Bea, J., dissenting from the denial of en banc rehearing). Another panel has noted that even if financing negative equity is not strictly necessary to enable the purchase of a new vehicle, recognizing that such transactions are often *practically* indispensable is appropriate because it “comports with the factual realities of the industry practice of financing negative equity.” AmeriCredit Fin. Servs., Inc. v. Padgett (*In re Padgett*), 408 B.R. 374, 380 (B.A.P. 10th Cir. 2009).

¹⁵³ *In re Peaslee*, 913 N.E.2d at 391 (Smith, J., dissenting).

¹⁵⁴ *See, e.g., In re Vega*, 344 B.R. 616, 617 (Bankr. D. Kan. 2006).

¹⁵⁵ *Id.* at 622.

¹⁵⁶ *See, e.g., Joe Sangl, Selling a Car with Negative Equity Isn’t Easy, but It’s Possible*, ANDERSON INDEP. MAIL (Sept. 10, 2008, 6:24 PM), <http://www.independentmail.com/news/2008/sep/10/selling-car-negative-equity-isnt-easy-its-possible/>.

¹⁵⁷ *In re Horn*, 338 B.R. 110, 112 (Bankr. M.D. Ala. 2006) (debtor repeatedly refinanced her auto loan with additional cash advances); *see also* Ford Motor Co. v. Mierkowski (*In re Mierkowski*), 580 F.3d 740, 744 (8th Cir. 2009) (Bye, J., dissenting).

her vehicle does not necessarily do so to enable the purchase of the new car,¹⁵⁸ and thus is incurring something other than a purchase-money loan.

The problem with this logic is that *any* purchase-money loan could be characterized as facilitating unrelated financial goals. For instance, a borrower might finance her vehicle, instead of paying out of pocket, to maintain liquidity for other major expenses. A trade-in may serve similar purposes. For example, a debtor owing a monthly payment of \$1,000 on her existing vehicle might not wish to pay an additional \$900 monthly payment on a new vehicle. If she can trade in her existing vehicle and work off the negative equity at a rate of \$200 per month, however, the consolidated payment of \$1,100 per month might bring the new vehicle more easily within reach. Trade-in transactions, like car loans in general, allow buyers to pay over time, thereby making cars affordable to those with limited means or high expenses.¹⁵⁹

Still, “value given to enable” seemingly requires some limiting principle, lest it explode the concept of purchase money. Judges have proffered numerous examples of transactions that “enable” the sale of a new vehicle in the same way that a financed trade-in does, but are intuitively distinct from purchase money.¹⁶⁰ Perhaps the best argument for narrowly construing “value given to enable” is that many enabling transactions are potentially “in derogation of the rights and interests of other creditors.”¹⁶¹ That is, the privileges attached to purchase-money status must be carefully conserved in the context of refinancing loans and similar transactions because they implicate the inter-creditor conflicts that are Article 9’s core subject matter.¹⁶² Formulated too broadly, a purchase-money priority for refinancing transactions could undo the general rule that an earlier secured creditor “has priority over later creditors in the assets in which it has security.”¹⁶³ Hence, interpretive

¹⁵⁸ See *Ford v. Ford Motor Credit Corp.* (*In re Ford*), 574 F.3d 1279, 1289 (10th Cir. 2009) (Tymkovich, J., dissenting).

¹⁵⁹ Cf. *Howard v. AmeriCredit Fin. Servs.* (*In re Howard*), 597 F.3d 852, 858 (7th Cir. 2010).

¹⁶⁰ See, e.g., *In re Ford*, 574 F.3d at 1291 (refinancing credit card debt); *In re Westfall*, 365 B.R. 755, 762 (Bankr. N.D. Ohio 2007) (life-saving appendectomy), *rev’d sub nom.* *Nuvel Credit Corp. v. Westfall* (*In re Westfall*), 599 F.3d 498 (6th Cir. 2010).

¹⁶¹ *AmeriCredit Fin. Servs., Inc. v. Padgett* (*In re Padgett*), 408 B.R. 374, 392 (B.A.P. 10th Cir. 2009) (Starzynski, J., concurring).

¹⁶² This explains the intuition that value given to refinance an existing loan is “not ‘in fact so used’ as further required by the statute. The monies are used to extinguish a pre-existing debt.” *In re White*, 417 B.R. 102, 105 (Bankr. S.D. Ind. 2009); see also *In re Ford*, 574 F.3d at 1289.

¹⁶³ Alan Schwartz, *A Theory of Loan Priorities*, 18 J. LEGAL STUD. 209, 209 (1989).

caution should be taken before according purchase-money status to any transaction that seemingly enables the purchase of a vehicle.¹⁶⁴

However, the more straightforward problem with equating purchase money with “value given to enable” is that the provision was drafted to merely extend the purchase-money security interest to third-party lenders;¹⁶⁵ it does not give broader, alternative content to the concept of purchase money. This is apparent in the statute’s evolution. Former Article 9-107 distinguished between a purchase-money security interest “taken . . . by the seller of the collateral to secure all or part of its price”¹⁶⁶ and one “taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in . . . the . . . collateral.”¹⁶⁷ This distinction survives in Revised Article 9. For example, an Official Comment to Article 9-324 distinguishes between “purchase-money security interests securing the price of collateral (i.e., created in favor of the seller)” and “purchase-money security interests that secure enabling loans.”¹⁶⁸ Thus, the “value given to enable” prong “is employed to encompass third party financing, not to expand the scope of purchase money security interests.”¹⁶⁹

Other evidence reinforces this conclusion. If “value given to enable” expanded the definition of purchase money, then the “all or part of the price” language would be superfluous, since any loan financing “all or part of the price of the collateral” would represent “value given to enable” its purchase. Even if the “value given to enable” prong offered an alternative basis on which *sellers* could claim purchase-money status, Official Comment 3 precludes reading this basis more broadly than the “all or part of the price” prong. It provides that, “[a]s used in subsection (a)(2), the definition of ‘purchase-money obligation,’ the ‘price’ of collateral or the ‘value given to enable’

¹⁶⁴ The treatment of refinancing and similar transactions under § 9-103 is the subject of Part II.D.

¹⁶⁵ See *Howard v. AmeriCredit Fin. Servs. (In re Howard)*, 597 F.3d 852, 855–56 (7th Cir. 2010) (“The ‘value given’ part of the definition is intended to make clear that the obligation can be to a finance company, as in this case, rather than to the seller.”); Gilmore, *supra* note 27, at 1373–74.

¹⁶⁶ See U.C.C. § 9-107(a) (1972) (current version at U.C.C. § 9-103(a)(2) (2011)).

¹⁶⁷ *Id.* § 9-107(b) (current version at U.C.C. § 9-103(a)(2) (2011)). In the case of a third-party financier, an Official Comment to Article 9-107 describes limitations on how “a secured party who is not a seller” may “give[] value.” *Id.* § 9-107 cmt. 2.

¹⁶⁸ U.C.C. § 9-324 cmt. 13 (2011).

¹⁶⁹ *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 611 F.3d 1158, 1164 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

includes [the same things].”¹⁷⁰ In sum, even the apparently expansive language of the “value given to enable” prong offers auto lenders far less than initially meets the eye.

C. Parsing Official Comment 3

Informing the interpretation of § 9-103, the accompanying Official Comment 3 explains that

the “price” of collateral or the “value given to enable” includes obligations for expenses incurred in connection with acquiring rights in the collateral, sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, administrative charges, expenses of collection and enforcement, attorney’s fees, and other similar obligations.¹⁷¹

Noting the capacious phrasing of “obligations for expenses incurred in connection with acquiring rights in the collateral” and “other similar obligations,” many courts have held that the inclusion of these categories implies that “the definitions of ‘price’ and ‘value’ should be interpreted broadly.”¹⁷² In addition, the Comment provides that a “‘purchase-money security interest’ requires a close nexus between the acquisition of collateral and the secured obligation.”¹⁷³ This Subpart considers the import of each of these provisions in turn.

Official Comment 3’s reference to “obligations for expenses incurred in connection with acquiring rights in the collateral” forms the basis of prominent decisions favoring automobile creditors.¹⁷⁴ As the Fifth Circuit noted, such expenses form “a stand alone category” not limited by “language like ‘such as’ or ‘including’ between that phrase and the additional listed expenses.”¹⁷⁵ The Seventh Circuit observed that the term “seems a pretty good description of

¹⁷⁰ U.C.C. § 9-103 cmt. 3.

¹⁷¹ *Id.*

¹⁷² *Graupner v. Nuvell Credit Corp. (In re Graupner)*, 537 F.3d 1295, 1302 (11th Cir. 2008) (quoting *In re Myers*, 393 B.R. 616, 621 (Bankr. S.D. Ind. 2008)).

¹⁷³ U.C.C. § 9-103 cmt. 3.

¹⁷⁴ *See, e.g., Howard v. AmeriCredit Fin. Servs. (In re Howard)*, 597 F.3d 852, 857 (7th Cir. 2010); *Ford Motor Credit Co. v. Dale (In re Dale)*, 582 F.3d 568, 575 (5th Cir. 2009); *Ford v. Ford Motor Credit Corp. (In re Ford)*, 574 F.3d 1279, 1284–85 (10th Cir. 2009) (examining Kansas law, which adopted the UCC); *Wells Fargo Fin. Acceptance v. Price (In re Price)*, 562 F.3d 618, 627 (4th Cir. 2009) (examining North Carolina law, which adopted the UCC); *In re Graupner*, 537 F.3d at 1301–02.

¹⁷⁵ *In re Dale*, 582 F.3d at 575.

negative equity. It is an obligation assumed by the buyer of the car in connection with his acquiring ownership.”¹⁷⁶ The Eleventh Circuit saw “no persuasive reason why . . . the refinancing of reasonable, bona fide negative equity in connection with the purchase of the new vehicle should not qualify as ‘expenses’ within the meaning of the comment.”¹⁷⁷ In contrast, the Ninth Circuit and others have expressed skepticism that the payoff of a buyer’s trade-in could even “be characterized as an ‘expense.’”¹⁷⁸ The bankruptcy appellate panel in *Penrod* argued that “such a major part of the purchase price can hardly be a form of ‘expense’ incurred in order to acquire the car.”¹⁷⁹

Courts have also found significance in the Comment’s reference to “other similar obligations.”¹⁸⁰ For example, the Eleventh Circuit took this language to indicate that “[t]he expenses identified in Comment 3 are merely examples of additional components of the ‘price’ of the collateral.”¹⁸¹ While some opinions viewed the modifier “similar” as limiting the Comment’s open-ended definition to necessary transaction costs,¹⁸² the majority rejects this approach. For example, the Eleventh Circuit argued that the presence of “attorney’s fees” in Official Comment 3 “belies the notion that ‘price’ or ‘value’ is narrowly viewed as only those [traditional] expenses that *must* be paid to drive the car off the lot.”¹⁸³ The Tenth Circuit noted that “[t]he term ‘transaction costs[]’ . . . is entirely absent from the statute and the Official Comment. Had the drafters of the U.C.C. intended to limit a purchase-money security interest

¹⁷⁶ *In re Howard*, 597 F.3d at 857.

¹⁷⁷ *In re Graupner*, 537 F.3d at 1302; *see also In re Dale*, 582 F.3d at 575; *In re Ford*, 574 F.3d at 1285; *In re Price*, 562 F.3d at 626.

¹⁷⁸ *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 611 F.3d 1158, 1162 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011); *Reiber v. GMAC, LLC (In re Peaslee)*, 913 N.E.2d 387, 391 (N.Y. 2009) (Smith, J., dissenting).

¹⁷⁹ *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 392 B.R. 835, 848 (B.A.P. 9th Cir. 2008), *aff’d*, 611 F.3d 1158 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

¹⁸⁰ *See, e.g., Nuvel Credit Corp. v. Westfall (In re Westfall)*, 599 F.3d 498, 504 (6th Cir. 2010); *In re Dale*, 582 F.3d at 574–75; *Ford Motor Credit Co. v. Mierkowski (In re Mierkowski)*, 580 F.3d 740, 742 (8th Cir. 2009); *In re Graupner*, 537 F.3d at 1301–02.

¹⁸¹ *In re Graupner*, 537 F.3d at 1302; *accord In re Westfall*, 599 F.3d at 504; *In re Dale*, 582 F.3d at 574–75; *In re Mierkowski*, 580 F.3d at 742; *In re Peaslee*, 913 N.E.2d at 389.

¹⁸² *See, e.g., In re Ford*, 574 F.3d at 1289 (Tymkovich, J., dissenting); *In re White*, 417 B.R. 102, 105 (Bankr. S.D. Ind. 2009); *In re Mitchell*, 379 B.R. 131, 137 n.8 (Bankr. M.D. Tenn. 2007); *In re Peaslee*, 913 N.E.2d at 391 (Smith, J., dissenting).

¹⁸³ *In re Graupner*, 537 F.3d at 1302 (alteration in original) (quoting *In re Myers*, 393 B.R. 616, 620 (Bankr. S.D. Ind. 2008)); *see also In re Dale*, 582 F.3d at 574 (quoting *id.* at 1302).

to cash price plus transaction costs, they could easily have done so.”¹⁸⁴ Some courts have even held that “the listed expenses in Comment 3 have no common feature beyond an attenuated connection to the acquisition or maintenance of the vehicle.”¹⁸⁵ On this view, there is no principled reason to exclude negative equity from the “other similar obligations” that a purchase-money loan might finance.

Yet the character of the enumerated expenses in Official Comment 3 suggests that “expenses incurred in connection” and “other similar obligations” cannot function as a catchall category lacking a limiting principle. Such a principle is easily discernable than the case law would suggest; namely, the expenses listed in the Comment encompass those expenses necessary for each party to realize the value of the transaction. The sale of a vehicle incurs “sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, [and] administrative charges,” while enforcing the terms of the sale may incur “expenses of collection and enforcement, [and] attorney’s fees.”¹⁸⁶ Granting the car lender priority as to these expenses secures the lender’s entire exposure for costs incidental to the sale and the enforcement of its terms.¹⁸⁷ Negative equity financing “simply does not fit within that rubric.”¹⁸⁸ Thus, while policymakers might disagree over whether negative equity *should* be given purchase-money status, Official Comment 3 appears to not address this issue. Its language focuses on incidental expenses, not the complex and sensitive question of the purchase-money character of a refinancing transaction, which I address in Part II.D.

Before turning to that issue, a brief coda is merited for Official Comment 3’s additional requirement that a purchase-money security interest “requires a close nexus between the acquisition of collateral and the secured

¹⁸⁴ *In re Ford*, 574 F.3d at 1285.

¹⁸⁵ *In re Westfall*, 599 F.3d at 504 (quoting *In re Dale*, 582 F.3d at 574).

¹⁸⁶ U.C.C. § 9-103 cmt. 3 (2011).

¹⁸⁷ *See AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 611 F.3d 1158, 1163 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011); *Ford Motor Credit Co. v. Mierkowski (In re Mierkowski)*, 580 F.3d 740, 746 (8th Cir. 2009); *In re Ford*, 574 F.3d at 1289 (Tymkovich, J., dissenting).

¹⁸⁸ *In re Penrod*, 611 F.3d at 1163; *see also id.* at 1162–63 (In contrast, “negative equity will ‘typically be larger, and more readily separable from the purchase transaction itself, than such things as sales tax, duties and finance charges.’” (quoting *Reiber v. GMAC, LLC (In re Peaslee)*, 913 N.E.2d 387, 391 (N.Y. 2009) (Smith, J., dissenting))).

obligation.”¹⁸⁹ Courts adopting the majority position have correctly discerned “a ‘close nexus’ between the negative equity in the Debtor’s trade-in vehicle and the purchase of his new vehicle,” noting that “[t]he financing was part of the same transaction and may be properly regarded as a ‘package deal.’”¹⁹⁰ A few courts have responded that the “close nexus” requirement is not satisfied because “[t]here is no necessary connection between this refinancing and the car’s acquisition.”¹⁹¹ Others have argued, based on the Comment’s predecessor in Former Article 9,¹⁹² that the “close nexus” requirement is not met because the negative equity in a trade-in is “antecedent debt,” which is inherently distinct from purchase money.¹⁹³

Like other debates about the meaning of § 9-103(a)(2) and Official Comment 3, the debate over the “close nexus” requirement is unmoored from the true import of this provision. Like the “value given to enable” prong of Revised Article 9-103,¹⁹⁴ the “close nexus” requirement of Official Comment 3 is simply an artifact of Former Article 9’s provisions for purchase-money loans by non-sellers. The predecessor to Comment 3 denied purchase-money status where “a secured party who [was] not a seller” sought to take “security for or

¹⁸⁹ U.C.C. § 9-103 cmt. 3.

¹⁹⁰ *Graupner v. Nuvel Credit Corp.* (*In re Graupner*), 537 F.3d 1295, 1302 (11th Cir. 2008); *see also In re Westfall*, 599 F.3d at 505; *In re Mierkowski*, 580 F.3d at 743; *In re Ford*, 574 F.3d at 1285; *Wells Fargo Fin. Acceptance v. Price* (*In re Price*), 562 F.3d 618, 627 (4th Cir. 2009); *In re Cohrs*, 373 B.R. 107, 109–10 (Bankr. E.D. Cal. 2007); *In re Peaslee*, 913 N.E.2d at 390.

¹⁹¹ *AmeriCredit Fin. Servs., Inc. v. Penrod* (*In re Penrod*), 392 B.R. 835, 852 (B.A.P. 9th Cir. 2008), *aff’d*, 611 F.3d 1158 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011); *see also In re Sanders*, 377 B.R. 836, 857 (Bankr. W.D. Tex. 2007), *rev’d sub nom.* *Ford Motor Credit v. Sanders* (*In re Sanders*), 403 B.R. 435 (W.D. Tex. 2009).

¹⁹² U.C.C. § 9-107 cmt. 2 (1972) (excluding “from the purchase money category any security interest taken as security for or in satisfaction of a preexisting claim or antecedent debt”) (current version at U.C.C. § 9-103 cmt. 3 (2011)).

¹⁹³ *See, e.g., In re Penrod*, 611 F.3d at 1163; *In re Ford*, 574 F.3d at 1289, 1291 (Tymkovich, J., dissenting); *AmeriCredit Fin. Servs., Inc. v. Padgett* (*In re Padgett*), 408 B.R. 374, 389 (B.A.P. 10th Cir. 2009) (Starzynski, J., concurring); *In re Penrod*, 392 B.R. at 849; *In re White*, 417 B.R. 102, 105 (Bankr. S.D. Ind. 2009); *In re Hall*, 400 B.R. 516, 520 (Bankr. S.D. W. Va. 2008); *In re Crawford*, 397 B.R. 461, 465 (Bankr. E.D. Wis. 2008); *GMAC v. Mancini* (*In re Mancini*), 390 B.R. 796, 805 (Bankr. M.D. Pa. 2008); *In re Munzberg*, 388 B.R. 529, 539 (Bankr. D. Vt. 2008); *In re Wear*, No. 07-42537, 2008 WL 217172, at *3 (Bankr. W.D. Wash. Jan. 23, 2008); *In re Johnson*, 380 B.R. 236, 243 (Bankr. D. Or. 2007); *In re Lavigne*, Nos. 07-30192, 07-31402, 07-31247, 06-32914, 2007 WL 3469454, at *6 (Bankr. E.D. Va. Nov. 14, 2007), *aff’d in part, rev’d in part sub nom.* *GMAC v. Horne*, 390 B.R. 191 (E.D. Va. 2008), *aff’d*, 394 F. App’x 13 (4th Cir. 2010); *see also In re Mierkowski*, 580 F.3d at 744 (Bye, J., dissenting); *In re Graupner*, 537 F.3d at 1301 (admitting that “the question [of] whether negative equity on a trade-in vehicle is ‘debt for the money required to make the purchase’ of the new vehicle, or . . . ‘antecedent debt[.]’ . . . is . . . a close call”).

¹⁹⁴ *See supra* text accompanying notes 165–70.

in satisfaction of a preexisting claim or antecedent debt.”¹⁹⁵ Now phrased as a “close nexus” requirement, Comment 3 continues to govern the case where “a debtor acquires property on unsecured credit and subsequently creates the security interest to secure the purchase price.”¹⁹⁶ Ultimately, both formulations amount to a requirement that the value given by a third-party lender must be “present”¹⁹⁷ or otherwise have “a close nexus”¹⁹⁸ to the acquisition of the collateral. The lender cannot lend on a non-purchase-money basis and then later take a purchase-money security interest.¹⁹⁹ Thus, a historically sensitive reading of the “close nexus” requirement reveals a consistent rule of law that is irrelevant to the purchase-money status of negative equity.²⁰⁰

D. Negative Equity and the Consumer Compromise

It would appear that courts debating the purchase-money status of negative equity have been barking up the wrong textual trees. Frequently, as in the case of the “value given to enable” and “close nexus” tests, statutory language that at first appears dispositive turns out merely to reflect unrelated rules of law inherited from Former Article 9.²⁰¹ While reading Revised Article 9 against Former Article 9 highlights the confused state of the case law on negative equity, it also illuminates the neglected provisions of Revised Article 9 that *are* relevant to the status of negative equity. Revised Article 9 was not cut from whole cloth. Rather, its drafters were working against a body of background law that conceptualized purchase money in highly restrictive, formalistic terms, which Revised Article 9 largely preserved in the context of consumer finance. The minority of states that adopted a more permissive consumer finance regime did so explicitly. However, the majority version of Revised

¹⁹⁵ U.C.C. § 9-107 cmt. 2 (current version at U.C.C. § 9-103 cmt. 3 (2011)).

¹⁹⁶ U.C.C. § 9-103 cmt. 3 (2011).

¹⁹⁷ U.C.C. § 9-107 cmt. 2 (1972) (current version at U.C.C. § 9-103 cmt. 3 (2011)); *cf.* U.C.C. § 9-103 cmt. 3 (2011) (“[A] security interest does not qualify as a purchase-money security interest if a debtor acquires property on unsecured credit and subsequently creates the security interest to secure the purchase price.”).

¹⁹⁸ U.C.C. § 9-103 cmt. 3 (2011).

¹⁹⁹ *See* Gilmore, *supra* note 27, at 1373–74.

²⁰⁰ Thus the majority of courts are correct that “[debt] owed on account of negative equity does not, in fact, amount to a refinance of antecedent debt” because “[p]rior to financing the negative equity in connection with their purchase of the new vehicle, Debtors owed [the creditor] nothing.” *Nuvel Credit Corp. v. Westfall (In re Westfall)*, 599 F.3d 498, 505 (6th Cir. 2010). Put differently, the “close nexus” requirement and the “antecedent debt” prohibition do not govern a purchase-money security interest immediately taken by the seller of the collateral, such as when a car dealer completes a trade-in transaction. *See AmeriCredit Fin. Servs., Inc. v. Padgett (In re Padgett)*, 408 B.R. 374, 389 (B.A.P. 10th Cir. 2009) (Starzynski, J., concurring).

²⁰¹ *See supra* Part II.B.2.C.

Article 9 is best read as maintaining prior law excluding financed negative equity from the limited category of purchase money.

Although largely ignored by the courts, perhaps the most persuasive evidence that Revised Article 9-103 does not expand the “price of the collateral” to encompass financed negative equity comes from the text itself. Two little-discussed provisions, subsections (b) and (f), explicitly contemplate two ways in which an obligation financing an over-encumbered trade-in departs from a prototypical purchase-money transaction: it involves both *cross-collateralization* and *refinancing*.²⁰² The specificity of these sections belies the popular view that statutory recognition for negative-equity financing is buried in Official Comment 3’s general reference to “expenses incurred in connection with acquiring rights in the [new vehicle].”²⁰³ Instead, these provisions compel the conclusion that Revised Article 9 preserves prior lines of authority that denied purchase-money status, in whole (under the transformation rule) or in part (under the dual-status rule), to cross-collateralized and refinanced purchase-money obligations.²⁰⁴

First, financing negative trade-in equity departs from a traditional purchase-money loan because it involves a form of cross-collateralization: it uses one item of value (the debtor’s new vehicle) to secure debt incurred in the acquisition of other property (the trade-in). Courts applying Former Article 9-107 frequently denied purchase-money status in such cases on the basis that an item of purchase-money collateral could not secure more than “all or part of [its] price.”²⁰⁵ In the consumer-finance context, the prohibition against cross-

²⁰² U.C.C. § 9-103(b), (f).

²⁰³ *Id.* § 9-103 cmt. 3.

²⁰⁴ Under the transformation rule, “the PMSI status is lost . . . whenever the collateral purports to secure more than its own price. This event can occur . . . where a debt is merely refinanced or consolidated (i.e. cross-collateralized) with other debts.” Christopher Harry, Comment, *To Be (Transformed), or Not to Be: The Transformation Versus Dual-Status Rules for Purchase-Money Security Interests Under Kansas’ Former and Revised Article 9*, 50 U. KAN. L. REV. 1095, 1105 (2002) (footnote omitted). “In contrast to the transformation rule, under the dual-status approach, a PMSI is *not* necessarily extinguished . . .” *Id.* at 1107; *see also* G. Ray Warner, *Consumer Avoidance of Non-Purchase-Money Security Interests Under Revised Article 9*, AM. BANKR. INST. J., Nov. 2001, at 22, 22.

²⁰⁵ *See, e.g.*, Southtrust Bank of Ala., Nat’l Ass’n v. Borg-Warner Acceptance Corp., 760 F.2d 1240, 1242 (11th Cir. 1985) (commercial context); Roberts Furniture Co. v. Pierce (*In re* Manuel), 507 F.2d 990, 993 (5th Cir. 1975) (consumer context). For a discussion of purchase-money collateral and pricing in context of consumers and commercial transactions, *see* Aronov, *supra* note 38, at 24; Marion W. Benfield, Jr., *Consumer Provisions in Revised Article 9*, 74 CHI.-KENT L. REV. 1255, 1292 (1999); Gerald T. McLaughlin, “Add On” Clauses in Equipment Purchase Money Financing: *Too Much of a Good Thing*, 49 FORDHAM L. REV. 661, 692–99 (1981); Ann E. Conaway Stilson, *The “Overloaded” PMSI in Bankruptcy: A Problem in Search of A*

collateralization was thought to prevent creditors from oppressively casting a net over many of a debtor's assets in an attempt to satisfy a deficiency.²⁰⁶ Thus, courts limited the "purchase money" designation to loans secured by the *particular collateral* that they financed. This restriction is reflected in Revised Article 9-103(b)(1), which requires that a purchase-money obligation be mutually traceable to an item of purchase-money collateral: "A security interest in goods is a purchase-money security interest . . . to the extent that the goods are purchase-money collateral *with respect to* that security interest."²⁰⁷

Whether a new vehicle can be purchase-money collateral "with respect to" the negative equity in the trade-in is answered squarely in Official Comment 4. This Comment considers the case where one item of purchase-money collateral (Item-1) secures the price of another item of purchase-money collateral (Item-2), which has been sold to a buyer in the ordinary course of business.²⁰⁸ Comment 4 explains that "to the extent that Item-1 secures the price of Item-2, [the] security interest in Item-1 *would not* be a purchase-money security interest under subsection (b)(1)," even though "Item-2 *itself* was subject to a purchase-money security interest."²⁰⁹ Against this background, Revised Article 9-103(b)(2) accommodated cross-collateralization of business inventory,²¹⁰ where requiring a rigid relationship between a particular debt and particular property came to be viewed as too onerous.²¹¹ However, subsection (b)(1) continues to deny purchase-money status to cross-collateralized obligations in the context of consumer goods and other types of collateral.²¹²

Second, in the consumer-finance context, Revised Article 9-103 preserves background law that provided that refinancing, consolidating, or restructuring an earlier loan potentially destroys its purchase-money status. Under Former Article 9-107, creditors frequently attempted to refinance and consolidate

Resolution, 60 TEMP. L.Q. 1, 24–33 (1987); Mark B. Wessman, *Purchase Money Inventory Financing: The Case for Limited Cross-Collateralization*, 51 OHIO ST. L.J. 1283, 1307–13 (1990); Bernard A. Burk, Note, *Preserving the Purchase Money Status of Refinanced or Commingled Purchase Money Debt*, 35 STAN. L. REV. 1133, 1143 & n.43 (1983).

²⁰⁶ See Stilson, *supra* note 205, at 24. A major benefit of claiming a purchase-money security interest over a wide pool of the debtor's assets is to prevent avoidance of non-purchase-money liens under the Bankruptcy Code § 522(f). See Wessman, *supra* note 205, at 1336.

²⁰⁷ U.C.C. § 9-103(b)(1) (emphasis added).

²⁰⁸ *Id.* § 9-103 cmt. 4.

²⁰⁹ *Id.* (emphasis added).

²¹⁰ See *id.* § 9-103(b)(2).

²¹¹ For further discussion, see generally Wessman, *supra* note 205.

²¹² See U.C.C. § 9-103(b)(1) & cmt. 4.

outstanding debt in a series of separate purchase-money loans. These transactions often produced “the functional equivalent of cross-collateralization” because the “[c]onsolidated debt [was] secured by all remaining collateral.”²¹³ In such cases, courts found that, because each item of collateral secured more than its price, the resulting obligation was not for purchase money.²¹⁴ Revised Article 9-103(f) provided that “a purchase-money security interest does not lose its status as such, even if . . . the purchase-money obligation has been renewed, refinanced, consolidated, or restructured,” but limited this safe harbor to “a transaction *other* than a consumer-goods transaction.”²¹⁵

The failure of Revised Article 9 to sanction “cross-collateralization, refinancing, or the like”²¹⁶ in the consumer-goods context was the product of “eight years of work” and reflected “an important issue for consumer transactions.”²¹⁷ A proposal to preserve purchase-money status in such cases “was left by the wayside” when a consensus did not emerge.²¹⁸ Instead, a savings clause in subsection (h) explained that the safe harbor’s “limitation . . . to transactions other than consumer-goods transactions is intended to leave to the court the determination of the proper rules in consumer-goods transactions” and that “[t]he court . . . may continue to apply established approaches.”²¹⁹

This drafting history explains the intuition, reflected in some opinions, that the drafters of Revised Article 9 would not have concealed a provision according purchase-money status to certain refinancing transactions in Official Comment 3’s vague references to “expenses.” “Given that financing negative equity is increasingly common,” one court reasoned, “it was not an oversight that the legislature did not include negative equity in the list of ‘expenses

²¹³ Wessman, *supra* note 205, at 1315.

²¹⁴ Benfield, *supra* note 205, at 1292; Wessman, *supra* note 205, at 1313 n.233, 1315. Whether the purchase-money character of such transactions is destroyed in whole or in part depends on the jurisdiction’s choice among the transformation and dual-status rules. *See generally In re Short*, 170 B.R. 128, 132–34 (Bankr. S.D. Ill. 1994) (reviewing each rule).

²¹⁵ U.C.C. § 9-103(f)(3) (emphasis added).

²¹⁶ *Id.* § 9-103 cmt. 7(a).

²¹⁷ Charles W. Mooney, Jr., *The Consumer Compromise in Revised U.C.C. Article 9: The Shame of It All*, 68 OHIO ST. L.J. 215, 222 (2007).

²¹⁸ *Id.*; *see also* Richard H. Nowka, *Allowing Dual Status for Purchase-Money Security Interests in Consumer-Goods Transactions*, 13 TRANSACTIONS: TENN. J. BUS. L. 13, 32–35 (2011).

²¹⁹ U.C.C. § 9-103(h).

incurred in connection with acquiring rights in the collateral’ set forth in Official Comment 3.”²²⁰ Instead, Official Comment 3 “is silent as to existing debt . . . because the drafters did not intend to include that type of expense within the confines of the statute.”²²¹ The battle to extend purchase-money status to refinanced consumer loans was waged—and lost—in the drafting of Revised Article 9-103. Thus, the express references to cross-collateralization and refinancing in Revised Article 9-103 exclude a reading of Official Comment 3 that would extend the purchase-money concept to these transactions in the consumer-goods context. Instead, the drafters “follow[ed] the general position that Revised Article 9 should not change present rules, which are seen as protective of consumers.”²²²

The cross-collateralization and refinancing provisions of Revised Article 9-103 have not yet featured prominently in the construction of the hanging paragraph, suggesting the foregoing interpretation may be vulnerable to critique. One potential counterargument is that it begs the question to characterize the payoff of negative equity as an instance of “cross-collateralization, refinancing, or the like,”²²³ rather than as an “expense[] incurred in connection with acquiring rights in the collateral.”²²⁴ However, the former characterization is highly specific and supported by both the example in Official Comment 3 and the legislative history of Revised Article 9, whereas the “expenses incurred” language is highly general and seems to cover incidental expenses instead of alternative financing structures.²²⁵ Moreover, even if the cross-collateralization and refinancing provisions are merely clues to legislative meaning, they clearly reflect a background assumption that a purchase-money obligation could “lose its status as such” if cross-collateralized or “renewed, refinanced, consolidated, or restructured.”²²⁶ This evidence hardly supports the view that a refinancing transaction that

²²⁰ *In re Johnson*, 380 B.R. 236, 245–46 (Bankr. D. Or. 2007) (citing *In re Blakeslee*, 377 B.R. 724, 728–29 (Bankr. M.D. Fla. 2007)); see also *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 392 B.R. 835, 848 (B.A.P. 9th Cir. 2008), *aff’d*, 611 F.3d 1158 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

²²¹ *In re White*, 417 B.R. 102, 104 (Bankr. S.D. Ind. 2009).

²²² Benfield, *supra* note 205, at 1294.

²²³ U.C.C. § 9-103 cmt. 7(a).

²²⁴ *Id.* § 9-103 cmt. 3.

²²⁵ See *supra* Part II.C.

²²⁶ U.C.C. § 9-103(f).

consolidates and cross-collateralizes two loans generates a purchase-money obligation.

A second counterargument is that the provisions of Revised Article 9 governing cross-collateralized and refinanced transactions relate only to the choice between the dual-status and transformation rules. To be sure, this is the context in which subsection (f) is generally cited.²²⁷ But the choice among these rules would never arise if these transactions were unambiguously purchase-money loans. Moreover, Official Comment 4 goes to the substance of the purchase-money question, providing that, except with respect to inventory, a “security interest in Item-1 would not be a purchase-money security interest” “to the extent that Item-1 secures the price of Item-2,” which has been sold to a buyer in the ordinary course.²²⁸ Finally, subsection (f) would still provide more specific evidence of legislative meaning than Official Comment 3’s oblique reference to “expenses incurred.” The unmistakable import of these provisions is that cross-collateralization and refinancing threaten the purchase-money status of the original debt.²²⁹ The text and legislative history of Revised Article 9-103 therefore support the conclusion that “established approaches,”²³⁰ not subtle emanations from the phrase “expenses incurred,” should govern the treatment of over-encumbered trade-in loans.

Unfortunately for automobile creditors, Revised Article 9’s failure to accord purchase-money status to cross-collateralized and refinanced consumer loans invites significant inconsistency among the “established approaches,”²³¹ in different jurisdictions.²³² The more severe approach, the transformation rule, “holds that a security interest that is part purchase-money and part non-purchase-money completely loses its purchase-money character and is entirely transformed into a non-purchase-money security interest.”²³³ Once popular in

²²⁷ See, e.g., *In re Munzberg*, 388 B.R. 529, 544–45 (Bankr. D. Vt. 2008); *In re Pajot*, 371 B.R. 139, 158 (Bankr. E.D. Va. 2007), *aff’d in part, rev’d in part sub nom.* GMAC v. Horne, 390 B.R. 191 (E.D. Va. 2008), *aff’d in part, appeal dismissed in part*, 394 F. App’x 13 (4th Cir. 2010); U.C.C. § 9-103 cmts. 7(b) & 8.

²²⁸ U.C.C. § 9-103 cmt. 4.

²²⁹ See *id.* § 9-103 cmt. 7(b).

²³⁰ *Id.* § 9-103(h).

²³¹ *Id.*

²³² Wessman, *supra* note 205, at 1315 & n.241 (describing “a patchwork of transformation rule cases and dual status rule cases”).

²³³ *In re Pajot*, 371 B.R. 139, 157 (Bankr. E.D. Va. 2007), *aff’d in part, rev’d in part sub nom.* GMAC v. Horne, 390 B.R. 191 (E.D. Va. 2008), *aff’d in part, appeal dismissed in part*, 394 F. App’x 13 (4th Cir. 2010).

refinancing cases,²³⁴ the transformation rule has met widespread criticism and waning application.²³⁵ Courts applying the transformation rule in negative-equity cases are frequently reversed and are clearly in the minority.²³⁶ Moreover, local variants of Revised Article 9 exclude application of the transformation rule in some states. While most states restrict the subsection (f) safe harbors for refinancing transactions to “a transaction other than a consumer-goods transaction,”²³⁷ nine states protect the status of refinanced purchase-money obligations in the consumer-goods context as well. These nine states are Florida,²³⁸ Idaho,²³⁹ Indiana,²⁴⁰ Kansas,²⁴¹ Louisiana,²⁴² Maryland,²⁴³ Nebraska,²⁴⁴ North Dakota,²⁴⁵ and South Dakota.²⁴⁶ Their version of subsection (f) preserves the purchase-money status of a refinanced obligation and compels application of the dual-status rule.²⁴⁷ Under the more common dual-status approach,²⁴⁸ the purchase-money character of the loan is preserved so long as some feasible method exists for allocating payments between the purchase-money and non-purchase-money components of the balance.²⁴⁹ In dual-status cases, the choice of allocation method is significant because it can

²³⁴ See, e.g., *Matthews v. Transamerica Fin. Servs. (In re Matthews)*, 724 F.2d 798, 800 (9th Cir. 1984); *In re Huddle*, No. 06-11076-SSM, 2007 WL 2332390, at *3 (Bankr. E.D. Va. Aug. 13, 2007); see also *In re Short*, 170 B.R. 128, 133 (Bankr. S.D. Ill. 1994) (collecting cases).

²³⁵ See, e.g., Russell A. Hakes, *According Purchase Money Status Proper Priority*, 72 OR. L. REV. 323, 365 (1993).

²³⁶ See *supra* text accompanying notes 79–84.

²³⁷ U.C.C. § 9-103(f) (2011).

²³⁸ FLA. STAT. ANN. § 679.1031(6) (West 2003).

²³⁹ IDAHO CODE ANN. § 28-9-103(f) (West, Westlaw through end of 2012 2d Regular Sess. of the 61st Leg.).

²⁴⁰ IND. CODE ANN. § 26-1-9.1-103(f) (West, Westlaw current with all 2012 legislation).

²⁴¹ KAN. STAT. ANN. § 84-9-103(f) (West, Westlaw through 2012 regular session).

²⁴² LA. REV. STAT. ANN. § 10:9-103(f) (West, Westlaw through the 2011 First Extraordinary and Regular Sess.).

²⁴³ MD. CODE ANN., COM. LAW § 9-103(f) (West, Westlaw through all chapters of the 2012 Regular Sess. and the First and Second Special Sess. of the General Assembly).

²⁴⁴ NEB. REV. STAT. U.C.C. § 9-103(f) (West, Westlaw through the 102nd Leg. Second Regular Sess. (2012)).

²⁴⁵ N.D. CENT. CODE ANN. § 41-09-03(6) (West, Westlaw through the 2011 Regular and Special Sess. of the 62d Legis. Assembly).

²⁴⁶ S.D. CODIFIED LAWS § 57A-9-103(f) (Westlaw through the 2012 Regular Sess. and Supreme Court Rule 12-10).

²⁴⁷ See, e.g., *Citifinancial Auto v. Hernandez-Simpson*, 369 B.R. 36, 46 (D. Kan. 2007).

²⁴⁸ See *supra* text accompanying notes 66–78.

²⁴⁹ See, e.g., *In re Acaya*, 369 B.R. 564, 571 (Bankr. N.D. Cal. 2007); *In re Tuck*, No. 06-10886-DHW, 2007 WL 4365456, at *4 (Bankr. M.D. Ala. Dec. 10, 2007).

radically alter the value of the purchase-money and non-purchase-money components of the balance remaining at the time of the bankruptcy filing.²⁵⁰

In contrast to the prevailing emphasis on Article 9-103 and the accompanying Official Comment 3, reading these provisions against their predecessors in Former Article 9-107 helpfully directs the interpreter's attention to the most relevant statutory authorities on the status of negative trade-in equity. In particular, it highlights the stringency of the former law's definition of purchase money and the varying extent to which Revised Article 9 relaxes these requirements. While the new provisions offer a more liberal regime for inventory lending and other non-consumer finance, the drafters were unable to agree on comparable moves with respect to consumer-goods transactions. Thus, the "consumer compromise" embodied in Revised Article 9 preserves traditional approaches to consumer finance that would likely deny purchase-money status to a trade-in loan that refinances old debt and secures it with newly purchased collateral.

III. DUAL-STATUS OBLIGATIONS UNDER THE HANGING PARAGRAPH

If the portion of an auto loan that finances negative trade-in equity is not purchase money, a remaining question concerns whether, and to what extent, this defect deprives the loan of protection under the hanging paragraph. Courts in jurisdictions applying the transformation rule should have no difficulty in resolving this inquiry, since the transformation rule extinguishes the creditor's purchase-money security interest.²⁵¹ Application of the hanging paragraph becomes problematic, however, in the context of the dual-status rule.²⁵² Although every court applying a state-law dual-status rule has permitted bifurcation of the non-purchase-money portion of the loan under § 506, some of these courts have assumed that this result flows directly from the state law dual-status rule,²⁵³ while others have adopted it as a kind of Goldilocks

²⁵⁰ *In re Pajot*, 371 B.R. 139, 162 tbls.1 & 2 (Bankr. E.D. Va. 2007), *aff'd in part, rev'd in part sub nom. GMAC v. Home*, 390 B.R. 191 (E.D. Va. 2008), *aff'd in part, appeal dismissed in part*, 394 F. App'x 13 (4th Cir. 2010).

²⁵¹ *See supra* note 233.

²⁵² *See, e.g., In re Look*, 383 B.R. 210, 220 (Bankr. D. Me. 2008).

²⁵³ *See supra* notes 66–78.

approach to the hanging paragraph.²⁵⁴ The latter authorities have reasoned that “the objectives of Congress in passing the hanging paragraph are best served” under such an approach, since it allows automobile creditors to escape bifurcation to the extent of their purchase-money security interest.²⁵⁵ Despite its popularity among lower courts, however, no circuit court has adopted the dual-status approach: in *Penrod*, the only circuit court decision favoring a debtor, the bankruptcy appellate panel’s dual-status approach was not examined on appeal.²⁵⁶ Furthermore, some courts have argued for an all-or-nothing reading; that is, the hanging paragraph should apply to the claim either in its entirety or not at all.²⁵⁷ While there is considerable support for the view that a claim for even a dual-status auto loan should receive full protection from bifurcation, this Part concludes that the non-purchase-money component of a dual-status obligation is eligible for bifurcation under Code § 506.

The textual argument for protecting a dual-status auto loan from bifurcation draws support from the hanging paragraph’s apparently categorical language: “[S]ection 506 shall not apply . . . if the creditor has a purchase money security interest securing the debt.”²⁵⁸ A few opinions have argued that this condition is satisfied even if the creditor’s purchase-money security interest is commingled with non-purchase-money interests under the dual-status rule. In one particularly well-articulated decision, an Illinois bankruptcy court reasoned that the hanging paragraph “cleaves the universe of loans into two subsets: those that are purchase money and those that are not,” ultimately holding that, “[w]here the lender advances funds used by the borrower to buy the car, the loan (and the security interest) is purchase money.”²⁵⁹ Similarly, in reasoning

²⁵⁴ See, e.g., *AmeriCredit Fin. Servs., Inc. v. Penrod* (*In re Penrod*), 392 B.R. 835, 859 (B.A.P. 9th Cir. 2008), *aff’d*, 611 F.3d 1158 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

²⁵⁵ *In re Hall*, 400 B.R. 516, 521 (Bankr. S.D. W. Va. 2008).

²⁵⁶ *AmeriCredit Fin. Servs., Inc. v. Penrod* (*In re Penrod*), 611 F.3d 1158, 1160 n.2 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011).

²⁵⁷ Compare *In re Sanders*, 377 B.R. 836, 859 (Bankr. W.D. Tex. 2007) (“The word ‘if’ implies that the purchase money collateral either secures the debt underlying [the] claim or it does not.”), *rev’d sub nom.* *Ford Motor Credit v. Sanders* (*In re Sanders*), 403 B.R. 435 (W.D. Tex. 2009), with *In re Dale*, No. H-07-3176, 2008 WL 4287058, at *4 n.12 (S.D. Tex. Aug. 14, 2008) (holding that the hanging paragraph applies if any part of the creditor’s claim is secured by a purchase-money security interest), *aff’d on other grounds*, *Ford Motor Credit Co. v. Dale* (*In re Dale*), 582 F.3d 568 (5th Cir. 2009).

²⁵⁸ 11 U.S.C. § 1325(a) (2006).

²⁵⁹ *In re Whipple*, 417 B.R. 86, 96 (Bankr. C.D. Ill. 2009).

not relied upon by the Fifth Circuit,²⁶⁰ the district court in *In re Dale* held that the hanging paragraph applies if *any part* of the loan is purchase money.²⁶¹

These opinions supply a plausible reading of the statute: even if the creditor's claim was only partly secured by a purchase-money security interest under a state-law dual-status rule, it is still reasonable to state that such "creditor has a purchase money security interest securing the debt that is the subject of the claim."²⁶² While the dual-status rule normally has federal-law implications in the context of § 522(f), which permits avoidance of certain non-purchase-money liens,²⁶³ the language of the hanging paragraph is arguably distinguishable because it applies to—and thus protects—the entire "claim," and not merely the purchase-money lien.²⁶⁴

The hanging paragraph's legislative history also poses problems for advocates of a dual-status approach to negative-equity loans. The earliest draft explicitly contemplated a dual-status approach, providing that § 506(a) "shall not apply to an allowed claim *to the extent* attributable in whole *or in part* to the purchase price of personal property acquired by the debtor within 180 days of the filing of the petition."²⁶⁵ It further proposed that, in the case of commingled debt, "the amount of the allowed secured claim shall be not less than the unpaid principal balance *of the purchase price of the personal property* acquired," and not the entire amount of the claim.²⁶⁶ This dual-status language later appeared in a Senate draft, S. 1301,²⁶⁷ alongside a competing formula similar to that ultimately enacted, which proposed that "section 506 shall not apply to a claim" that is "secured . . . by reason of a lien on

²⁶⁰ *In re Dale*, 582 F.3d at 572.

²⁶¹ *In re Dale*, 2008 WL 4287058, at *4 n.12; *see also In re Sanders*, 403 B.R. at 439. This reasoning also appears in Judge Bea's dissent from the denial of rehearing in *AmeriCredit Financial Services, Inc. v. Penrod* (*In re Penrod*), 636 F.3d 1175, 1178 (9th Cir. 2011) (Bea, J., dissenting from the denial of en banc rehearing), *en banc reh'g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011), as well as Judge Starzynski's concurrence in *AmeriCredit Financial Services, Inc. v. Padgett* (*In re Padgett*), 408 B.R. 374, 386 (B.A.P. 10th Cir. 2009) (Starzynski, J., concurring).

²⁶² 11 U.S.C. § 1325(a).

²⁶³ *Id.* § 522(f)(1)(B).

²⁶⁴ *See id.* § 1325(a) (emphasis added).

²⁶⁵ Responsible Borrower Protection Bankruptcy Act, H.R. 2500, 105th Cong. § 110 (1997) (emphasis added).

²⁶⁶ *Id.*

²⁶⁷ Consumer Bankruptcy Reform Act of 1998, S. 1301, 105th Cong. § 302(c) (as reported by S. Comm. on the Judiciary, June 4, 1998) ("[Section 506](a) shall not apply to an allowed claim to the extent attributable in whole or in part to the purchase price of personal property acquired by the debtor during the 90-day period preceding the date of filing . . .").

property.”²⁶⁸ Congress ultimately chose the latter course, enacting a “section 506 shall not apply” formula described as effecting “a prohibition against bifurcati[on].”²⁶⁹ Thus, Congress considered, and abandoned, a proposal that would have explicitly adopted the dual-status approach. While one court has cautioned that “[t]here is no legislative commentary revealing the purpose of this substitution of concepts,”²⁷⁰ the abandonment of an explicit dual-status formula in favor of more categorical language reinforces a natural reading of the text.

However, the categorical reading is not without its own problems. Significantly, this approach risks upsetting the usual priority schemes embedded in the Bankruptcy Code and Article 9.²⁷¹ For example, under this view, a purchase-money automobile loan commingled with thousands of dollars in cash advances secured by the vehicle could escape bifurcation entirely.²⁷² This peculiar outcome is inconsistent with the bankruptcy principle that “creditors of equal status should receive comparable recoveries,” which forbids “discrimination among unsecured creditors through classification of their claims.”²⁷³ More pertinently, such a reading does violence to the state-law principle that the first to file is first in priority, transforming the purchase-money exception into a floodgate. In contrast, the dual-status rule comports well with applicable law and broader bankruptcy principles.

As noted above, the dual-status rule is potentially at odds with the hanging paragraph’s language protecting the auto lender’s entire claim. Perhaps the best solution, then, is to invoke the rule in the debtor’s objection to the auto lender’s proof of claim. In *In re White*, the bankruptcy court sustained the debtors’ objection and approved a plan that simply divided the auto lender’s claim into secured and unsecured components, treating the balance attributable to the negative equity as unsecured.²⁷⁴ Crucially, this procedure is distinct from § 506 bifurcation because it does not strip down the auto lender’s claim to the

²⁶⁸ *Id.* § 302(a).

²⁶⁹ H.R. REP. NO. 109-31, pt. 1, at 17 (2005).

²⁷⁰ *In re Hayes*, 376 B.R. 655, 675 n.29 (Bankr. M.D. Tenn. 2007).

²⁷¹ See *In re White*, 417 B.R. 102, 106 (Bankr. S.D. Ind. 2009).

²⁷² Note that a state-law transformation rule would still preclude application of the hanging paragraph. *In re Horn*, 338 B.R. 110, 112 (Bankr. M.D. Ala. 2006) (debtor repeatedly refinanced her auto loan with additional cash advances).

²⁷³ See *In re Steele*, No. 08-40282-DML-13, 2008 WL 2486060, at *3 (Bankr. N.D. Tex. June 12, 2008) (collecting cases).

²⁷⁴ See *In re White*, 417 B.R. at 106–07.

value of the collateral—it simply excises the negative-equity component from the lender’s allowed secured claim. In this way, the state-law dual-status rule could prevent the creditor from folding a non-purchase-money security interest into a purchase-money claim, operating in a manner “somewhat analogous to claim bifurcation under § 506.”²⁷⁵

A potential counterargument to this approach is that Congress has preempted the dual-status rule via “occupation of the field of bankruptcy claim determination,”²⁷⁶ such that “State Law deficiency claim concepts [are] wholly displaced by the plenary *bankruptcy* law standards of claim *characterization*.”²⁷⁷ On this view, one could argue that state-law dual-status rules have no role in the determination of the automobile creditor’s claim: if there is a right to payment and thus a claim, then “the value . . . of property to be distributed under the plan on account of such claim” must not be “less than the allowed amount of such claim.”²⁷⁸ Yet the hanging paragraph’s command that “section 506 shall not apply”²⁷⁹ could easily be read as giving way to alternative state-law schemes, so that the extent of the purchase-money security interest, rather than a federal claim determination, applies. Such a reading also avoids the potentially absurd result of withholding bifurcation of a claim overstuffed with non-purchase-money debts.

The polar-opposite reading—that the hanging paragraph wholly *excludes* loans with a non-purchase-money component²⁸⁰—is even less persuasive. Some courts have held that the hanging paragraph does not apply to a dual-status loan, reasoning that “a purchase money security interest that secures *part of the debt*” does not have “a purchase money security interest securing *the debt*,” as required by the hanging paragraph.²⁸¹ Like other courts who have applied the hanging paragraph to the entire loan, these courts seize upon the

²⁷⁵ *In re Pan Am Corp.*, 124 B.R. 960, 971 n.9 (Bankr. S.D.N.Y. 1991), *aff’d in part*, 125 B.R. 372 (S.D.N.Y. 1991), *aff’d*, 929 F.2d 109 (2d Cir. 1991).

²⁷⁶ *In re Pruitt*, 401 B.R. 546, 555 (Bankr. D. Conn. 2009).

²⁷⁷ *Id.* at 559.

²⁷⁸ 11 U.S.C. § 1325(a)(5)(B)(ii) (2006).

²⁷⁹ *Id.* § 1325(a).

²⁸⁰ The conclusion that the hanging paragraph is inapplicable to any loan with a non-purchase-money component is not the same as a “transformation” rule because it is “derived from . . . the Bankruptcy Code itself. It does not come from an interpretation of the UCC or an application of the transformation rules developed in state decisional law.” *In re Sanders*, 377 B.R. 836, 860 n.21 (Bankr. W.D. Tex. 2007), *rev’d sub nom. Ford Motor Credit v. Sanders (In re Sanders)*, 403 B.R. 435 (W.D. Tex. 2009).

²⁸¹ *Id.* at 859 (quoting 11 U.S.C. § 1325(a)).

statute's all-or-nothing phrasing, which applies “*if* the creditor has a purchase money security interest,” rather than “to the extent of” such interest.²⁸² Thus, they conclude, if “there is a portion of [the automobile creditor's] claim that is not secured by its purchase money security interest, the claim is not the type of claim protected by the hanging paragraph.”²⁸³ These opinions demonstrate the indeterminacy that comes from a plain-meaning analysis of the hanging paragraph. Its categorical language seems equally suited to interpretations that would grant full protection, or no protection, to a dual-status loan. It is difficult to imagine, however, that Congress intended to penalize trade-in creditors by singling out their claims for bifurcation.²⁸⁴ Thus, as one court observed, it seems implausible “that any mix of non-purchase money debt [sh]ould taint the whole and cost the lender the protection Congress intended.”²⁸⁵

The choice between full protection and a dual-status regime is a close one, and it is perhaps surprising that more courts have not held that the hanging paragraph protects the entire claim, regardless of its non-purchase-money contents. The dual-status interpretation is more appealing, however, because it protects car lenders from bifurcation to the extent of the purchase-money security interest, rather than assuming that Congress intended no limitations on the types of claims protected by the hanging paragraph.²⁸⁶ Furthermore, the careless drafting of the hanging paragraph has rightly limited some courts' willingness to draw all-or-nothing conclusions from its text.²⁸⁷ For example, the bankruptcy appellate panel in *Penrod* reasoned, “[T]he hanging paragraph is not a text that lightly gives up its meaning, let alone a plain meaning, and the use of standard interpretive conventions is not likely to yield a canonical

²⁸² *Id.* (quoting 11 U.S.C. § 1325(a)); *see also In re Look*, 383 B.R. 210, 220 (Bankr. D. Me. 2008); *In re Mitchell*, 379 B.R. 131, 140 (Bankr. M.D. Tenn. 2007).

²⁸³ *In re Sanders*, 377 B.R. at 860; *accord In re Look*, 383 B.R. at 220–21; *In re Mitchell*, 379 B.R. at 140–41; *In re Peaslee*, 358 B.R. 545, 559 (Bankr. W.D.N.Y. 2006), *rev'd sub nom.* Gen. Motors Acceptance Corp. v. Peaslee (*In re Peaslee*), 373 B.R. 252 (W.D.N.Y. 2007), *aff'd sub nom.* Reiber v. GMAC, LLC (*In re Peaslee*), 585 F.3d 53 (2d Cir. 2009).

²⁸⁴ *See In re Steele*, No. 08-40282-DML-13, 2008 WL 2486060, at *6 n.13 (Bankr. N.D. Tex. June 12, 2008) (Even if “there is no indication that Congress intended to *encourage* negative equity trade-ins, neither is there any suggestion in the Code or legislative history that Congress intended to *discourage* such loans by penalizing their makers”).

²⁸⁵ *See id.* at *6; *accord In re Johnson*, 380 B.R. 236, 250 (Bankr. D. Or. 2007).

²⁸⁶ *See In re Johnson*, 380 B.R. at 249.

²⁸⁷ *See supra* text accompanying notes 15–24.

reading strong enough to support such a drastic [transformation] rule.”²⁸⁸ One might reach the same conclusion with respect to a reading that would protect the entire claim from bifurcation. Yet courts applying the dual-status rule may not need to confront these interpretive issues if, as in *White*, they simply treat the negative-equity component of each loan as a separate, non-purchase-money claim from the outset.

IV. CONCLUDING OBSERVATIONS

An obligation incurred to retire the lien on a trade-in vehicle is not purchase money because it is not incurred as “part of the price of the collateral.”²⁸⁹ Revised Article 9-103 permitted cross-collateralization in inventory financing²⁹⁰ and abolished the transformation rule with respect to refinanced obligations in the non-consumer-goods context.²⁹¹ However, with respect to consumer goods, the law preserved the conceptual incompatibility between purchase money and “cross-collateralization, refinancing, or the like”²⁹² and authorized courts to “continue to apply established approaches” to such transactions.²⁹³ Although Official Comment 3 expanded the definition of “price” to allow a purchase-money obligation to finance a range of incidental expenses,²⁹⁴ it did not introduce a new rule authorizing cross-collateralization and refinancing in the consumer context. Such proposals were advanced, and defeated, in the drafting of Revised Article 9.²⁹⁵

Courts applying the dual-status rule to isolate a purchase-money car loan from its negative-equity component have held that the hanging paragraph protects the claim from bifurcation to the extent of the balance of the purchase-money portion.²⁹⁶ This position is not without difficulties, as Congress seemingly protected the entire “claim” from bifurcation and rejected competing proposals that would have explicitly incorporated the dual-status

²⁸⁸ *AmeriCredit Fin. Servs., Inc. v. Penrod (In re Penrod)*, 392 B.R. 835, 858 (B.A.P. 9th Cir. 2008), *aff’d*, 611 F.3d 1158 (9th Cir. 2010), *en banc reh’g denied*, 636 F.3d 1175 (9th Cir. 2011), *cert. denied*, 132 S. Ct. 108 (2011); *see also In re Johnson*, 380 B.R. at 250.

²⁸⁹ U.C.C. § 9-103(a)(2) (2011).

²⁹⁰ *Id.* § 9-103(b)(2).

²⁹¹ *Id.* § 9-103(f)(3).

²⁹² *Id.* § 9-103 cmt. 7(a).

²⁹³ *Id.* § 9-103(h).

²⁹⁴ *Id.* § 9-103 cmt. 3.

²⁹⁵ Mooney, *supra* note 217, at 222.

²⁹⁶ *See supra* notes 66–78.

rule. However, one may equally surmise that Congress was not concerned with forcing chapter 13 debtors to repay the full balance of loans incurred—often more than 910 days before the bankruptcy filing—to purchase cars that they have since traded in. Furthermore, given the hanging paragraph’s imprecise drafting, interpreters should pause before reading the statute in so categorical a manner as to protect claims overstuffed with non-purchase-money debt.²⁹⁷ Instead, the dual-status rule should allow courts to extend the hanging paragraph’s protection to bona fide purchase-money loans without forcing debtors to pay legacy debts in full to retain their vehicles over their creditors’ objections.

It is ironic that Congress committed the scope of the hanging paragraph’s protection of “purchase money security interest[s]” to state law because purchase-money status has few state-law implications for car lenders.²⁹⁸ Since any after-acquired-property clause in a consumer loan becomes ineffective after ten days,²⁹⁹ an automobile creditor will not have difficulty gaining priority in the new vehicle, even if the lender does not have purchase-money status. Thus, under Article 9, “[p]urchase money status for security interests in consumer goods is significant only for automatic perfection . . . not for priority.”³⁰⁰ The most important consequences of the purchase-money question flow not from Article 9, but from the Bankruptcy Code, namely §§ 522(f) and 1325(a).³⁰¹ Along these lines, one court even held that “state law rules regarding the application of either the transformation rule or dual status rule are simply irrelevant” to the task of determining “whether [the creditor] qualifies for the special protection afforded . . . under the 910-day provision of the Bankruptcy Code, a question of federal law.”³⁰² On the other hand, the hanging paragraph’s reference to “purchase money” has the appealing characteristic of allowing the states to contribute to the bankruptcy-law principles applicable to vehicle lending within their respective jurisdictions.

²⁹⁷ See *supra* notes 15–24, 287–88.

²⁹⁸ See Moringiello, *supra* note 36, manuscript at 1006 (arguing that purchase-money status “is completely irrelevant to consumer transactions” under the UCC).

²⁹⁹ U.C.C. § 9-204(b)(1) & cmt. 3.

³⁰⁰ Hakes, *supra* note 235, at 359–60.

³⁰¹ 11 U.S.C. §§ 522(f)(1)(B), 1325(a) (2006).

³⁰² *In re Sanders*, 377 B.R. 836, 858 (Bankr. W.D. Tex. 2007), *rev’d sub nom.* *Ford Motor Credit v. Sanders* (*In re Sanders*), 403 B.R. 435 (W.D. Tex. 2009). Reinterpreting the *Butner* principle, at least one commentator has argued that the hanging paragraph’s reference to “purchase money” should not be defined by state law. See Moringiello, *supra* note 36.

Protecting this contribution requires bankruptcy courts to sensitively interpret states' differing approaches to consumer finance. Under Revised Article 9, these approaches are frequently less permissive than bankruptcy courts addressing the negative-equity issue have acknowledged.