UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION

IN RE:	)	
	)	
Pluma, Inc.,	)	Case No. 99-11104C-11G
	)	
Debtor.	)	
	)	

MEMORANDUM OPINION

This case came before the court on June 13, 2000, for hearing upon an objection by the Debtor, Pluma, Inc., to a claim by Premium Wear, Inc., for a secured claim or a priority claim in the amount of $54,203.28 based upon reclamation rights under § 546(c). R. Bradford Leggett appeared on behalf of the Debtor, K. Lane Klotzberger appeared on behalf of Premium Wear, Inc., David M. Grogan appeared on behalf of the Unsecured Creditors' Committee, and Douglas R. Ghidina appeared on behalf of the Bank of America and the Bank Group.

NATURE OF THE CONTROVERSY

The Debtor contends that Premium Wear, Inc. is not entitled to any relief under § 546(c) and therefore is not entitled to either secured or priority status.

FACTS

1. Prior to ceasing operations, Debtor was a vertically integrated manufacturer and distributor of fleece and jersey active

wear.

2. In May 1997, Debtor purchased various assets and assumed various liabilities from Stardust Corporation, a Wisconsin corporation, which expanded Debtor's nationwide wholesale distributorship into undecorated sportswear. The purchased assets, which included real and personal property comprising a manufacturing facility in Wisconsin, were operated as a separate division called the Stardust Division. It is undisputed that Stardust was sufficiently integrated with Pluma after the purchase for Pluma to be liable for all of Stardust's debts and obligations arising thereafter.

3. Debtor's Stardust Division purchased shirts in large quantities from Premium Wear, which is located in Minnesota. At the time of Debtor's petition, Stardust owed Premium Wear $159,435.16 as a result of multiple shipments of clothing for which no payment had been made. Of these shipments, four were delivered on May 13, 1999, and had a total contract price of $54,435.16. These four shipments were comprised of a total of 4,440 Munsingwear shirts.

4. Debtor filed a voluntary petition for relief under Chapter 11 on May 14, 1999.

5. Upon learning of Debtor's filing, Premium Wear mailed on May 21, 1999, written demand for reclamation of the 4,400 shirts delivered on May 13th. The letter demanded that Stardust retain the shirts until Premium Wear secured possession thereof. Authority for reclamation cited in the letter was 11 U.S.C. § 546(c), Wis. Stat. § 402.702, and Minn. Stat. § 336.2-702.

6. Premium Wear filed a proof of claim in this case on July 20, 1999, in the amount of $159,435.16. Of that amount, Premium Wear alleged that $54,203.28 should be allowed as a secured claim because of its reclamation rights related to the 4,400 shirts.

7. There is no evidence that Premium Wear had any contact with Stardust or Pluma during the interval between the demand letter on May 21, 1999, and the filing of the proof of claim on July 20, 1999.

8. The Debtor objected to Premium Wear's claim to the extent that the claim was asserted as secured or priority based upon reclamation under § 546(c).

9. Premium Wear filed a response to Debtor's objection on March 2, 2000, followed by a second response on April 27, 2000.

PROCEDURAL POSTURE

On June 13, 2000, a hearing was held regarding Premium Wear's

claim and the Debtor's objection. At the hearing, the parties agreed that the only documents filed with the Court regarding Premium Wear's claim were Premium Wear's proof of claim, Debtor's objection to the claim and Premium Wear's two responses to Debtor's objection, which included attached documentation. The only evidence offered at the hearing were the attachments to the Premium Wear response and a copy of an affidavit from Michael P. Coaty, counsel for Premium Wear in Wisconsin, regarding the fact that various bankruptcy notices had been sent to Premium Wear's lockbox in Minnesota rather than to him despite his having filed a notice of appearance on September 8, 1999. Debtor objected to paragraph six of the affidavit, and the objection was sustained. The original of this affidavit was filed with the court on June 27, 2000, and has been considered by the court along with Premium Wear's proof of claim and responses.

DISCUSSION

As an initial matter, it was agreed by the parties that none of the shirts remain in the possession of the Debtor. There being no actual shirts remaining in Debtor's possession, Premium Wear conceded that actually reclaiming the shirts is foreclosed. Premium Wear argued, however, that it should nonetheless be granted a priority claim under § 503(b). Premium Wear claims to have fully

complied with both Minnesota and Wisconsin state law[1] and to have a right to reclamation under state law. In its second Brief in Support of Claim, Premium Wear states that "Section 546(c) of the Bankruptcy Code provides that a party with a state-law right to reclamation may assert that right in bankruptcy, provided that the seller's demand for reclamation was in writing." Premium Wear then refers the Court to § 546(c)(2), which states that when a court denies "reclamation to a seller with such a right of reclamation that has made such a demand," the court must provide the seller with either a priority claim or a lien on property.[2] According to

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[1]Minn. Stat. Ann. § 336.2-702 (West 2000) and Wis. Stat. Ann. § 402.702 (West 2000) respectively, both of which are based on Article 2, Section 702 of the Model Uniform Commercial Code, which addresses reclamation rights and insolvent buyers.

[2]Section 546 states:

(c) Except as provided in subsection (d) of this section, the rights and powers of a trustee under sections 544(a), 545, 547, and 549 of this title are subject to any statutory or common-law right of a seller of goods that has sold goods to the debtor, in the ordinary course of such seller's business, to reclaim such goods if the debtor has received such goods while insolvent, but-

(1) such seller may not reclaim any such goods unless such seller demands in writing reclamation of such goods-

(A) before 10 days after receipt of such goods by the debtor; or

(B) is such 10-day period expires after the commencement of the case, before 20 days after receipt of such goods by the debtor; and

(2) the court may deny reclamation to a seller with such a right of reclamation that has made such a demand only if the court-

(A) grants the claim of such a seller priority as a

Premium Wear, since it has been denied this state-law reclamation right, the court must provide it with a priority claim pursuant to § 546(c)(2).

In opposition to this argument, the Debtor maintains that § 546(c) requires that a right to reclamation exist and that Premium Wear had the burden of proving it had a right to reclamation, which it failed to do. The court finds Debtor's arguments to be correct and decisive in this matter.

It is well settled that § 546(c) provides the sole remedy for a seller seeking to reclaim goods from a debtor in bankruptcy. See In re Julien Co., 44 F.3d 426, 432 (6th Cir. 1995); Rawson Food Serv., Inc., 846 F.2d 1343, 1346 (11th Cir. 1988); In re Morken, 182 B.R. 1007, 1014 (Bankr. D. Minn. 1995); In re Video King of Ill., Inc., 100 B.R. 1008, 1013 (Bankr. N.D. Ill. 1989). Courts have consistently held that any grant of lien or priority claim under § 546(c)(2) is conditioned upon the claiming party first establishing a right to reclamation under §546(c). Since § 546(c)(2) provides for a lien or priority claim only when the court has denied a valid claim of reclamation under § 546(c), establishing a § 546(c) right to reclamation is a precondition for

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claim of a kind specified in section 503(b) of this title; or
(B) secures such claim by a lien.

any lien or priority claim that § 546(c) provides as an alternative remedy. See Morken, 182 B.R. at 1018; Video King, 100 B.R. at 1016. One of the prerequisites for establishing a 546(c) right to reclamation is that the reclaiming party must have a common law or statutory right to reclamation. See, e.g., Rawson, 846 F.2d at 1347; In re McLouth Steel Prods. Corp., 213 B.R. 978, 983 (E.D. Mich. 1997); In re Arlco, Inc., 239 B.R. 261, 266 (Bankr. S.D.N.Y. 1999).

While Premium Wear has stated in its briefs and at the hearing that it has complied with state law and has a state law right of reclamation, these statements are conclusory and not supported by the evidence. The court accepts that Premium Wear did abide by those requirements listed in its briefs, namely that demand was made within ten days of Debtor's receipt of the goods, the goods were sold on credit, and that the Debtor was insolvent at the time of receipt (although no evidence was presented on this latter issue). However, the three requirements listed by Premium Wear do not comprise all of the requirements for proving a state law right to reclamation. Instead, the cases impose four requirements for obtaining treatment under § 546(c) as follows:

> (1) the goods must have been sold in the ordinary course of business;

(2) the goods must have been received by the buyer while insolvent;

(3) a written demand for reclamation must have been made within ten days of receipt of the goods by buyer; and

(4) the buyer must have been in possession of the goods at the time the buyer received the demand or the goods not be in the hands of a good faith purchaser or buyer in the ordinary course of business.

See, e.g., In re Adventist Living Centers, Inc., 52 F.3d 159, 162 (7th Cir. 1995); In re Pester Refining Co., 964 F.2d 842, 845 (8th Cir. 1992); Video King, 100 B.R. at 1013. Other courts use slightly different variations on this list, but all still require that the goods be in the possession of the buyer at the time demand is made. See, e.g., Rawson, 846 F.2d at 1347; Vanco Trading, Inc. v. Monheit, 1999 WL 464531 (D. Conn. June 17, 1999); McLouth, 213 B.R. at 983; Arlco, 239 B.R. at 266; In re Victory Markets, Inc., 212 B.R. 738, 741 (Bankr. N.D.N.Y. 1997). This is because reclamation is an in rem right that must be invoked immediately and prior to disposition of the goods. See In re Crofton & Sons, Inc., 139 B.R. 567, 569 (M.D. Fla. 1992); Action Indus., Inc. v. Dixie Enters., Inc., 22 B.R. 855, 859 (Bankr. S.D. Ohio 1982).

The requirement that the goods still be in the possession of the buyer at the time demand is made is a state law requirement—not an additional requirement of the Bankruptcy Code. See In re Landy

Beef Co., 30 B.R. 19, 20 n.4 (Bankr. D. Mass. 1983); In re Flagstaff Food Serv. Corp., 14 B.R. 462, 465 (Bankr. S.D.N.Y. 1981); 5 Collier on Bankruptcy ¶ 546.04[2][a](Lawrence P. King et al. eds., 15th ed. rev. 2000).

The prevailing rule is that the reclaiming party has the burden of proving that the goods were in the possession of the buyer at the time demand was received by the buyer. See Adventist, 52 F.3d at 163 ("The seller in a reclamation case bears the burden of proving that the debtor possessed the goods when it received the reclamation demand. This is a fairly stringent requirement because a seller's evidence must indicate that this critical fact on which its recover depends is true, and not merely that it is possible it is so.'")(quoting In re Flagstaff Food Serv. Corp., 56 B.R. 899, 908 (Bankr. S.D.N.Y. 1986)); Rawson, 846 F.2d at 1348; Arlco, 239 B.R. at 266; Victory Markets, 212 B.R. at 741. The burden is to prove by the preponderance of the evidence. See Adventist, 52 F.3d at 162; Arlco, 239 B.R. at 266; Video King, 100 B.R. at 1013. There is no presumption that the goods remain in the possession of the debtor just because delivery has been made. See Adventist, 52 F.3d at 162; Rawson, 846 F.2d at 348.

In the present case, Premium Wear failed to provide any evidence that the shirts in question were still in the Debtor's

possession at the time written demand was made on May 21, 1999. Premium Wear thus failed to meet its burden of proving a right to reclaim any goods under § 546(c) of the Code.

A reclaiming party that fails to prove that goods were in the possession of a bankruptcy debtor at the time demand was made fails to prove a state law right to reclamation and therefore fails to meet the most basic prerequisite to § 546(c) remedies. Since Premium Wear has failed to establish that it had a state law right to reclamation, this court's denial of Premium Wear's right to reclamation is not a denial of a valid right of reclamation under § 546(c), and § 546(c)(2) therefore is not called into play. See Pester, 964 F.2d at 847. As a result, Premium Wear's request for a priority claim pursuant to § 546(c)(2) must be denied. Though Premium Wear did not raise the issue, any claim for a lien pursuant to § 546(c)(2)(A) would be denied on the same grounds.[3]

CONCLUSION

In accordance with the foregoing, an order will be entered contemporaneously herewith denying the claim of Premium Wear, Inc.

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[3]Because a determination as to whether or not the Bank Group had a perfected security interest in the inventory of Stardust does not affect the outcome of the issue at hand, namely whether or not Premium Wear should be allowed a secured or priority claim in the amount of $54,203.28, the court need not address that question.

to the extent that it seeks secured or priority status and allowing a general unsecured claim in the amount of $159,435.16.

This 21st day of July, 2000.

WILLIAM L. STOCKS
United States Bankruptcy Judge

Judge's Copy

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MIDDLE DISTRICT OF NORTH CAROLINA
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ORDER

In accordance with the memorandum opinion filed contemporaneously herewith, it is ORDERED, ADJUDGED AND DECREED as follows:

(1) The claim of Premium Wear, Inc. is disallowed to the extent that it seeks secured or priority status; and

(2) Premium Wear, Inc. is allowed a general unsecured claim in the amount of $159,435.16.

This 21st day of July, 2000.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge