Fordham Law Review

Volume 50 | Issue 4 Article 6

1982

The Buyer-Secured Party Conflict and Section 9-307(1) of the UCC: Identifying when a Buyer Qualifies for Protection as a Buyer in Ordinary Course

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THE BUYER-SECURED PARTY CONFLICT AND SECTION 9-307(1) OF THE UCC: IDENTIFYING WHEN A BUYER QUALIFIES FOR PROTECTION AS A BUYER IN ORDINARY COURSE

INTRODUCTION

The buyer in ordinary course of business[1] (BIOC) exception of section 9-307(1) of the Uniform Commercial Code[2] (Code) allows a qualifying buyer to cut off a lender's fully perfected interest[3] in an item of collateral securing a loan.[4] As such, it represents a powerful

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1. The Uniform Commercial Code defines buyer in ordinary course as "a person who in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interest of a third party in the goods buys in ordinary course from a person in the business of selling goods of that kind." U.C.C. § 1-201(9) (1977).

2. *Id.* § 9-307(1). This section provides in pertinent part that "[a] buyer in ordinary course of business . . . takes free of a security interest created by his seller even though the security interest is perfected and even though the buyer knows of its existence." *Id.*

3. A security interest is "an interest in personal property or fixtures which secures payment or performance of an obligation." *Id.* § 1-201(37). The security agreement is always effective against the debtor. T. Quinn, Uniform Commercial Code Commentary and Law Digest ¶¶ 9-201[A][2]-[3] (1978). For maximum legal protection against third parties, however, the security interest must be perfected. *Id.* ¶ 9-303[A], at 9-152. The act of perfection, which consists of publication of the creditor's interest in the collateral, gives the world notice that the debtor does not have unencumbered ownership of the goods. L. Denonn, Secured Transactions Under the UCC 39 (rev. ed. 1970); T. Quinn, *supra*, ¶ 9-101[A][4][e]; Knapp, *Protecting the Buyer of Previously Encumbered Goods: Another Plea for Revision of UCC Section 9-307(1)*, 15 Ariz. L. Rev. 861, 872 (1973). A security interest may be perfected in one of three basic ways. The two principal methods are filing and possession. The third is automatic perfection by operation of law, which is limited to certain types of collateral and circumstances. B. Clark, The Law of Secured Transactions Under the Uniform Commercial Code ¶ 2.5, at 2-16 (1980); W. Davenport & D. Murray, Secured Transactions 115 (1978); L. Denonn, *supra*, at 39; T. Quinn, *supra*, ¶¶ 9-101[A][4][e], -302[A][1]-[3]; Knapp, *supra*, at 872; *see* U.C.C. § 9-303 (1977). In order for a security interest to be perfected, it must attach. U.C.C. § 9-303(1) (1977); T. Quinn, *supra*, ¶ 9-303[A][1]. Attachment is the point at which a security interest first arises. U.C.C. § 9-303 official comment 1 (1977). Under § 9-203, it occurs when there is an effective security agreement, value has been given and the debtor has rights in the collateral. *Id.* § 9-203(1); Anzivino, *When Does a Debtor Have Rights in the Collateral Under Article 9 of the Uniform Commercial Code?*, 61 Marq. L. Rev. 23, 23-24 (1977). In the 1962 version of the Code, these provisions are in § 9-204. U.C.C. § 9-204 (1962); T. Quinn, *supra*, ¶ 9-203[A][3].

4. U.C.C. § 9-307(1) official comment 1 (1977). The concept of buyer in ordinary course of business represents an important exception to the doctrine of caveat emptor. 1 N.Y. L. Rev. Comm'n, Study of the Uniform Commercial Code, Leg. Doc. No. 65, at 227 (1955) [hereinafter cited as 1955 Report].

assault[5] on the sanctity of the Article 9 security interest.[6] Whether a buyer has qualified as a BIOC, therefore, is a vitally important determination.[7]

A typical section 9-307(1) scenario is as follows: *B*, a buyer,[8] agrees to buy a specific model television set from Acme Appliances, Inc. (*S*)[9] and tenders a check for the full price. After *B* leaves, *S* designates a particular television set to be delivered to *B* the next week.[10] *S* is able to maintain a full line of television sets and other appliances in his inventory[11] by virtue of a financing arrangement with a bank (*L*) under which the appliances serve as collateral for the loan.[12] The security agreement[13] and financing statement[14] provide *L* with a

5. One commentator referred to this exception as a "massive loophole" to which a security interest in business inventory is subject. *62,000 Tons of Sand*, 14 U.C.C. L. Letter, June 1980, at 1 [hereinafter cited as U.C.C. L. Letter].

6. Section 9-201 provides that "[e]xcept as otherwise provided by this Act a security agreement is effective according to its terms between the parties, against purchasers of the collateral and against creditors." U.C.C. § 9-201 (1977). A security agreement is "an agreement which creates or provides for a security interest." *Id.* § 9-105(1)(*l*). Section 9-201 "states the general validity of a security agreement." *Id.* § 9-201 official comment. Exceptions are only allowed by specific provision of the Code. *See id.* The buyer in ordinary course of business exception is an example of such a provision.

7. Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 265, 288 N.Y.S.2d 525, 529 (Sup. Ct. 1968); Antigo Co-op Credit Union v. Miller, 86 Wis. 2d 90, 91, 271 N.W.2d 642, 643 (1978).

8. The Uniform Commercial Code defines a buyer as "a person who buys or contracts to buy goods." U.C.C. § 2-103(1)(a) (1977).

9. A seller is defined by the Uniform Commercial Code as "a person who sells or contracts to sell goods." *Id.* § 2-103(1)(d).

10. Designation identifies the goods to the contract. *Id.* § 2-501(1)(b).

11. The Code defines goods as " 'inventory' if they are held by a person who holds them for sale or lease . . . or if they are raw materials, work in process or materials used or consumed in a business." *Id.* § 9-109(4). Whether goods are inventory is a function of whether they are held for sale in the ordinary course of business. *Id.* § 9-109 official comment 3.

12. Floor-plan financing is a common method of secured financing under which a lender advances funds to enable a dealer to purchase and replenish his inventory. R. Speidel, R. Summers & J. White, Teaching Materials on Commercial and Consumer Law 217 (2d ed. 1974) [hereinafter cited as R. Speidel]; Note, *Secured Transactions—Importance of Possession or Title to Buyer in the Ordinary Course of Business*, 14 Suffolk U. L. Rev. 695, 695 n.4 (1980) [hereinafter cited as *Possession or Title*]; *see* European-Am. Bank & Trust Co. v. Sheriff of Nassau, 97 Misc. 2d 549, 550, 411 N.Y.S.2d 851, 852-53 (Sup. Ct. 1978); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 262, 288 N.Y.S.2d 525, 526-27 (Sup. Ct. 1968); Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 843 (R.I. 1979).

13. Although the security agreement expressly secures the proceeds of sale, the 1972 version of Article 9 of the Uniform Commercial Code provides that proceeds are automatically included. U.C.C. § 9-203(3) (1972). This is in contrast to the 1962 version of § 9-203(1)(b), which at a minimum required that the word "proceeds" be mentioned in the agreement. U.C.C. § 9-203(1)(b) (1962); T. Quinn, *supra* note 3, ¶ 9-203[A][1][d]. The reason this change was made was that "it is assumed that the parties [intended to include proceeds] unless otherwise agreed." U.C.C. app. II § 9-203, reasons for 1972 change (1977).

14. The financing statement is the paper that is placed in the public records. T.

security interest in both the inventory and the proceeds of sale.[15] The financing statement has been filed[16] in accordance with Code perfection requirements.[17] Before the television is delivered to *B*, *S* defaults on the loan, and *L* moves to repossess everything in *S*'s inventory.[18] Included in the inventory is the television designated for *B*, which is still on the premises pending delivery.

Quinn, *supra* note 3, ¶ 9-203[A][5], at 9-96. The 1972 version of the Code provides that each financing statement must include the signature of the debtor, the names and addresses of both parties and a description of the collateral. U.C.C. § 9-402(1) & official comment 1 (1972); T. Quinn, *supra* note 3, ¶ 9-402[A][1], at 9-265. Either the security agreement itself or the standard abbreviated form, UCC-1, may be filed. U.C.C. § 9-402 official comment 2 (1977); T. Quinn, *supra* note 3, ¶ 9-203[A][5], at 9-96, ¶ 9-402[A][4]. Usually it is the latter. *Id.* ¶ 9-402[A][1], at 9-265.

15. The Code provides that " '[p]roceeds' includes whatever is received upon the sale, exchange, collection or other disposition of collateral or proceeds. . . . Money, checks, deposit accounts, and the like are 'cash proceeds'. All other proceeds are 'non-cash proceeds'." U.C.C. § 9-306(1) (1977). Floor-plan financing arrangements usually contemplate that the proceeds of sale will be applied toward repayment of the loan. Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 843 n.2 (R.I. 1979); 2 G. Gilmore, Security Interests in Personal Property § 26.1, at 677 (1965); T. Quinn, *supra* note 3, ¶ 9-307[A][1] (Supp. 1981); R. Speidel, *supra* note 12, at 211, 217; Knapp, *supra* note 3, at 874; *Possession or Title*, *supra* note 12, at 695 n.4. Proceeds, however, may also be used to replenish the seller's inventory. J. Honnold, Cases and Materials on the Law of Sales and Sales Financing 599 (4th ed. 1976). A financing arrangement that includes proceeds is an example of a "floating lien." *See* 2 W. Hawkland, A Transactional Guide to the Uniform Commercial Code 701-02 (1964). A "floating lien," which the Code validates, is a security interest that is maintained throughout the inventory cycle. *Id.* It begins with the raw materials, continues in the goods as they go through the process of change and become finished goods, follows into proceeds and goes back to newly purchased raw materials. 1 G. Gilmore, *supra*, § 11.7, at 359; W. Hawkland, *supra*, at 701-02; J. Honnold, *supra*, at 598-99; T. Quinn, *supra* note 3, ¶ 9-108[A][2]; R. Speidel, *supra* note 8, at 210-11; *see* Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 268, 288 N.Y.S.2d 525, 532-33 (Sup. Ct. 1968).

16. Part 4 of Article 9 of the Code sets forth the rules on filing. U.C.C. §§ 9-401 to -408 (1977). States may adopt one of three alternative filing systems provided in section 9-401. Id. § 9-401; *see* T. Quinn, *supra* note 3, ¶¶ 9-401[A][1]-[3]. All three alternatives involve filing with the Secretary of State. U.C.C. § 9-401 first alternative subsection (1)(b) (1977); *id.* second alternative subsection (1)(c); *id.* third alternative subsection (1)(c). They differ primarily as to the types of collateral that must be filed in local county offices. *Compare id.* first alternative subsection (1)(a) (including, *inter alia*, timber or minerals) *with id.* second alternative subsections (1)(a)-(b) (including, *inter alia*, equipment used in farming operations, timber or minerals) *with id.* third alternative subsections (1)(a)-(c) (including, *inter alia*, equipment used in farming operations, timber or minerals, and providing for filing in county where debtor resides or has a place of business). The official comments discuss the advantages and disadvantages of each of the three alternatives. *Id.* § 9-401 official comments. Other Code sections in part 4 outline the formal requisites of financing statements, *id.* § 9-402, what constitutes filing, *id.* § 9-403, and termination statements. *Id.* § 9-404.

17. Filing is one method by which perfection may occur. *See* U.C.C. § 9-302(1) (1977).

18. A secured party has the right to take possession of collateral upon the debtor's default. *Id.* § 9-503.

The situation becomes a priority battle[19] between *L* and *B*, with each claiming rights in the television: *B* as a buyer in ordinary course of business under section 9-307(1);[20] *L* as a secured party under section 9-306(2).[21] If section 9-307(1) is applicable, *B* will take delivery of the television free of *L's* security interest. *L*, however, still has a right to the proceeds of the sale.[22] If section 9-307(1) is not applicable, *L* will be able to repossess the television as well as claim the proceeds.[23]

The determination of whether *B* is a buyer in ordinary course of business depends on the answers to two questions: (1) Who is a BIOC;[24] and (2) when does a buyer attain this preferred status?[25] A buyer qualifies as a BIOC pursuant to Code section 1-201(9)[26] if he in "good faith"[27] and "without knowledge" that the sale to him violates a

19. *See, e.g.*, Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 747-48 (3d. Cir. 1979); European-Am. Bank & Trust Co. v. Sheriff of Nassau, 97 Misc. 2d 549, 550-51, 411 N.Y.S.2d 850, 852-53 (Sup. Ct. 1978); Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 868-69, 396 N.Y.S.2d 319, 320 (Sup. Ct. 1977); Adams v. City Nat'l Bank, 565 P.2d 26, 27-28 (Okla. 1977); Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 843-44 (R.I. 1979).

20. U.C.C. § 9-307(1) (1977); *see supra* note 2.

21. Section 9-306(2) of the Code provides that generally "a security interest continues in collateral notwithstanding sale, exchange or other disposition . . . and also continues in any identifiable proceeds including collections received by the debtor." U.C.C. § 9-306(2) (1977).

22. *See, e.g.*, Martin Marietta Corp. v. New Jersey Nat'l Bank, 505 F. Supp. 946, 952 (D.N.J.), *aff'd in relevant part*, 653 F.2d 779 (3d Cir. 1981); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492, 211 S.E.2d 430, 433 (1974); Associates Discount Corp. v. Old Freeport Bank, 421 Pa. 609, 612, 220 A.2d 621, 623 (1966); B. Clark, *supra* note 3, ¶ 3.4, at 3-18; E. Reiley, Guidebook to Security Interests in Personal Property § 8.3, at 8-7 (1981).

23. *See* U.C.C. § 9-306(2) (1977). Although *L* may claim both proceeds and collateral, there may be only one satisfaction. *Id.* official comment 3.

24. T. Quinn, *supra* note 3, ¶ 9-307[A][7], at 9-189; *see, e.g.*, Taft v. Jake Kaplan, Ltd. (*In re* Dexter Buick-GMC Truck Co.), 2 Bankr. 253, 255 (Bankr. D.R.I. 1980); Hempstead Bank v. Andy's Car Rental Sys., 35 A.D.2d 35, 36, 312 N.Y.S.2d 317, 318 (1970); European-Am. Bank & Trust Co. v. Sheriff of Nassau, 97 Misc. 2d 549, 552, 411 N.Y.S.2d 851, 853 (Sup. Ct. 1978).

25. T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-135 (Supp. 1981); Skilton, *Buyer in Ordinary Course of Business Under Article 9 of the Uniform Commercial Code (And Related Matters)*, 1974 Wis. L. Rev. 1, 16; *see* Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 478, 392 N.E.2d 344, 345 (1979); Chrysler Corp. v. Adamatic, Inc., 59 Wis. 2d 219, 238-39, 208 N.W.2d 97, 106 (1973).

26. U.C.C. § 1-201(9) (1977); *see supra* note 1.

27. U.C.C. § 1-201(9) (1977). Good faith is defined as "honesty in fact in the conduct or transaction concerned." *Id.* § 1-201(19). Article 2 of the Code contains a definition of good faith that superimposes a requirement of "observance of reasonable commercial standards of fair dealing in the trade" on the Article 1 requirement of honesty in fact. *Id.* § 2-103(1)(b). This definition applies only to merchants. *See id.* The courts disagree over whether to apply the Article 1 or Article 2 standard of good faith when dealing with a merchant buyer in an Article 9 situation. Skilton, *supra* note 25, at 24-28. *Compare* Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 751-52 (3d Cir. 1979) (applying Article 1 definition), *and* Sherrock v.

secured party's interest,[28] "buys in ordinary course"[29] "from a person in the business of selling goods of that kind."[30] In addition, the security interest must be "created by [the] seller,"[31] in accordance with section 9-307(1). It looks as though *B* qualifies as a BIOC.

Commercial Credit Corp., 290 A.2d 648, 651 (Del. 1972) (same), *with* Swift v. J.I. Case Co., 266 So. 2d 379, 381 (Fla. Dist. Ct. App. 1972) (applying Article 2 definition), *and* Hempstead Bank v. Andy's Car Rental Sys., 35 A.D.2d 35, 37-38, 312 N.Y.S.2d 317, 320 (1970) (same).

28. U.C.C. § 1-201(9) (1977); *e.g.*, Rex Fin. Corp. v. Marshall, 406 F. Supp. 567, 581 (W.D. Ark. 1976); O.M. Scott Credit Corp. v. Apex Inc., 97 R.I. 442, 448, 198 A.2d 673, 677 (1964); Cash Loan Co. v. Boser, 34 Wis. 2d 410, 419, 149 N.W.2d 605, 610 (1967). One commentator argues that the "no knowledge" requirement is implicit in the good faith requirement. Felsenfeld, *Knowledge as a Factor in Determining Priorities Under the Uniform Commercial Code*, 42 N.Y.U. L. Rev. 246, 248-49 (1967).

29. U.C.C. § 1-201(9) (1977). To be considered buying in ordinary course of business, the buyer should buy from the seller's usual place of business, on a day and at a time that is customary in the area and typical in the trade. 1 R. Anderson, Uniform Commercial Code §§ 1-201:22, :25 (2d ed. 1970); Skilton, *supra* note 16, at 29-30. Examples of non-qualifying sales are bulk sales, sales in liquidation, and sales at excessively low prices. Tanbro Fabrics Corp. v. Deering Milliken, Inc., 39 N.Y.2d 632, 637, 350 N.E.2d 590, 592, 385 N.Y.S.2d 260, 262 (1976). Whether a buyer is found to buy in the ordinary course depends on the circumstances of the case as of the purchase date. *Compare* Martin Marietta Corp. v. New Jersey Nat'l Bank, 505 F. Supp. 946, 949-52 (D.N.J.) (commercial construction buyer's purchase of 150,000 tons of sand from commercial seller of sand was not bulk sale but sale in ordinary course of business), *aff'd in relevant part*, 653 F.2d 779 (3d Cir. 1981), *and* Tanbro Fabrics Corp. v. Deering Milliken, Inc., 39 N.Y.2d 632, 636-37, 350 N.E.2d 590, 592-93, 385 N.Y.S.2d 260, 262-63 (1976) (fabric converter's purchase of excess goods from another converter was customary in the trade and therefore in ordinary course of business), *with* National Bank of Commerce v. First Nat'l Bank & Trust Co., 446 P.2d 277, 280, 282 (Okla. 1968) (purchase of an automobile from a seller who operated an automobile repair business and did not have a new car dealer's license was not in ordinary course of business), *and* Whitmire v. Keylon, 12 U.C.C. Rep. Serv. (Callaghan) 1203, 1207 (Tenn. Ct. App. 1973) (purchase of a one-half interest in a houseboat was not in ordinary course of business).

30. U.C.C. § 1-201(9) (1977). The requirement limits the BIOC exception to sales that are made by sellers regularly engaged in selling such goods and excludes casual sales. R. Anderson, *supra* note 29, § 1-201:26. *Compare* American Nat'l Bank & Trust Co. v. Mar-K-Z Motors & Leasing Co., 11 Ill. App. 3d 1046, 1048-49, 298 N.E.2d 209, 210-11 (1973) (seller held to be in business of selling automobiles where articles of incorporation specified that seller was in business of leasing and selling), *aff'd*, 57 Ill. 2d 29, 309 N.E.2d 567 (1974), *with* Hempstead Bank v. Andy's Car Rental Sys., 35 A.D.2d 35, 39, 312 N.Y.S.2d 317, 321 (1970) (seller held not to be in business of selling automobiles because periodic sales were incidental to leasing business). One commentator explains the requirement as a preference for buyers who buy in normal trading channels. Skilton, *supra* note 25, at 23.

31. U.C.C. § 9-307(1) (1977); B. Clark, *supra* note 3, § 3.4[3]; Skilton, *supra* note 25, at 7-9. Commentators have criticized the fact that the reach of § 9-307(1) is limited to security interests created by the buyer's seller. Dugan, *Buyer-Secured Party Conflicts Under Section 9-307(1) of the Uniform Commercial Code*, 46 U. Colo. L. Rev. 333, 345-47 (1975); Knapp, *supra* note 3, at 884-85; Vernon, *Priorities, The Uniform Commercial Code and Consumer Financing*, 4 B.C. Indus. &

The question of when a buyer becomes a BIOC is not as easy to answer as the question of who may become one.[32] A sales transaction involves specific and identifiable points in time, each of which represents a unique event in the Code scheme.[33] These include time of contracting, identification, passage of title, delivery, receipt and acceptance.[34] Because the Code fails to give guidance as to when BIOC status arises,[35] it is arguable that a buyer could become a buyer in ordinary course at any one of these times.

Jurisdictions differ as to the most appropriate point at which to recognize BIOC status. Neither courts nor commentators have advanced time of contracting. Delivery and receipt have been expressly rejected.[36] This leaves passage of title[37] and identification,[38] both of

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Com. L. Rev. 531, 534-36 (1963). Thus if a buyer buys from a seller who bought the goods from another seller who encumbered the goods, the buyer will be denied the protection of § 9-307(1). Exchange Bank v. Jarrett, 588 P.2d 1006, 1009 (Mont. 1979); National Shawmut Bank v. Jones, 108 N.H. 386, 388, 236 A.2d 484, 485-86 (1967); Dugan, *supra*, at 345-46; Knapp, *supra* note 3, at 884; Vernon, *supra*, at 535. This result has been criticized on the basis that one who buys goods encumbered by other than the immediate seller is just as innocent and subject to the same equities as one who buys directly from the seller who creates the security interest. Even if the buyer tries to search the records for outstanding liens, he will learn nothing because the security interest will have been filed under the debtor's name, of which the buyer is ignorant. Dugan, *supra*, at 347; Knapp, *supra* note 3, at 887. Commentators therefore argue that the language "created by his seller" should be deleted from § 9-307(1) to expand its protection. *Id.* at 892; Vernon, *supra*, at 536. Commentators also argue for the elimination of the exclusion of buyers of farm goods from the protection of § 9-307(1). Dolan, *Section 9-307(1)—U.C.C.'s Obstacle to Agricultural Commerce in the Open Market,* 72 Nw. U. L. Rev. 706, 735-36 (1977); Dugan, *supra*, at 337-44.

32. U.C.C. L. Letter, *supra* note 5, at 1.

33. *See* T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-135 to -136 (Supp. 1981).

34. *See id.*; Skilton, *supra* note 25, at 16.

35. T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-135 to -136 (Supp. 1981); Skilton, *supra* note 25, at 15-21.

36. Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 178, 580 P.2d 8, 10 (1978); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 494-96, 211 S.E.2d 430, 434-35 (1974); Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 478-79, 392 N.E.2d 344, 345-46 (1979); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968); Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979); *see* Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 751 (3d Cir. 1979); Tanbro Fabrics Corp. v. Deering Milliken, Inc., 39 N.Y.2d 632, 636, 350 N.E.2d 590, 592-93, 385 N.Y.S.2d 260, 262-63 (1976); Makransky v. Long Island Reo Truck Co., 58 Misc. 2d 338, 339-40, 295 N.Y.S.2d 240, 241-42 (Sup. Ct. 1968).

37. *See* International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492-94, 211 S.E.2d 430, 433-34 (1974); Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 870-71, 396 N.Y.S.2d 319, 320-21 (Sup. Ct. 1977); Chrysler Corp. v. Adamatic, Inc., 59 Wis. 2d 219, 238-39, 208 N.W.2d 97, 106-07 (1973). *International Harvester Credit Corp.*, although decided under the title approach, recognized the possibility of deciding "without resort to the technical niceties of definitions in the Sales article of the U.C.C." 133 Ga. App. at 494, 211 S.E.2d at 434.

38. Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 749 (3d Cir.

which have been utilized in the cases, as viable points in time for determination of BIOC status. If passage of title is favored, *B* will lose because the Code provides that title generally passes on delivery,[39] and in this case, delivery has not yet taken place. If, however, the court favors identification, *B* will win because the television was identified when S designated a particular television for delivery to *B*.[40]

The question of when *B* becomes a BIOC also arises when *B* buys on credit.[41] To illustrate, the hypothetical should be modified so that *B*, instead of paying by check, agrees to pay on an installment basis.[42] *B* executes a note, formalizing his obligation to pay for the television over time,[43] and a security agreement, giving *S* the right to repossess the goods should *B* default.[44] *S* may sell the security agreement and the note, which together are termed "chattel paper,"[45] to either the inventory lender or a retail financer.[46] Although security agreements

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1979); Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979).

39. U.C.C. § 2-401(2) (1977).

40. *See id.* § 2-501(1)(b).

41. *See* Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 178, 580 P.2d 8, 10 (1978); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968); T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-134 to -135 (Supp. 1981); Skilton, *supra* note 25, at 76-78.

42. *See* Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 176, 580 P.2d 8, 8 (1978); Wickes Corp. v. General Elec. Credit Corp., 363 So. 2d 56, 57 (Fla. Dist. Ct. App. 1978); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 489, 211 S.E.2d 430, 431 (1974); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 262, 288 N.Y.S.2d 525, 526-27 (Sup. Ct. 1968); Associates Discount Corp. v. Old Freeport Bank, 421 Pa. 609, 611, 220 A.2d 621, 623 (1966); T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-134 (Supp. 1981); R. Speidel, *supra* note 12, at 217-18; Skilton, *supra* note 25, at 77.

43. *See* International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 489, 211 S.E.2d 430, 431 (1974); R. Speidel, *supra* note 12, at 217; Levie, *Security Interests in Chattel Paper*, 78 Yale L.J. 935, 936 (1969).

44. *See* Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 176, 580 P.2d 8, 8 (1978); Wickes Corp. v. General Elec. Credit Corp., 363 So. 2d 56, 57 (Fla. Dist. Ct. App. 1978); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 489, 211 S.E.2d 430, 431 (1974); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 262, 288 N.Y.S.2d 525, 527 (Sup. Ct. 1968); Associates Discount Corp. v. Old Freeport Bank, 421 Pa. 609, 611, 220 A.2d 621, 622 (1966); T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-134 (Supp. 1981); R. Speidel, *supra* note 12, at 217; Levie, *supra* note 43, at 936; Skilton, *supra* note 25, at 78; *supra* note 18 and accompanying text.

45. Chattel paper is defined as "a writing or writings which evidence both a monetary obligation and a security interest in . . . specific goods." U.C.C. § 9-105(1)(b) (1977). Chattel paper therefore results from the credit purchase of an item evidenced by a promissory note and the security agreement. R. Speidel, *supra* note 12, at 217-18; *see* Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 176-77, 580 P.2d 8, 8-9 (1978); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 489, 211 S.E.2d 430, 431 (1974); 2 G. Gilmore, *supra* note 15, § 27.1, at 718; Levie, *supra* note 43, at 935-37.

46. 2 G. Gilmore, *supra* note 15, § 27.1, at 719-20; J. Honnold, *supra* note 15, at 645; Levie, *supra* note 43, at 955-56.

often provide that *S* will sell the chattel paper to *L*,[47] when in need of cash *S* is more likely to sell to the retail financer,[48] who then becomes, for the purposes of the Code, the chattel paper purchaser.[49] Upon default by either *S* on the loan agreement with *L*, or *B* on the installment contract, determination of the priorities between *L* and the chattel paper purchaser in the chattel paper and the underlying goods may turn on the determination of when BIOC status arises.[50]

This Note reviews the purposes and policies underlying the Code as a whole, and in particular the BIOC exception and Article 9. It then analyzes the six possible points on the transactional continuum to determine which is most satisfactory in terms of the underlying purposes and policies of the Code, predictability of results, and equity. Finally, this Note concludes that of the six possible points in time, identification satisfies the above criteria most successfully.

I. Purposes and Policies of the Code

To ensure that businesses function as planned[51] and to minimize the possibility of disputes,[52] parties to commercial contracts must be able to determine their rights and obligations with a reasonable degree of certainty.[53] Because "commerce knows nothing of State boundaries,"[54] it is also important that the applicable law be uniform when a transaction is conducted across state lines.[55] The commercial case law[56] of the nineteenth century and the "uniform" commercial stat-

47. J. Honnold, *supra* note 15, at 645; R. Speidel, *supra* note 12, at 218; Skilton, *supra* note 25, at 77; *see* 2 G. Gilmore, *supra* note 15, § 27.1, at 718-20.

48. 2 G. Gilmore, *supra* note 15, § 27.1, at 720; J. Honnold, *supra* note 15, at 645.

49. *See* International Harvester Credit Corp. v. Associates Fin. Servs. Corp., 133 Ga. App. 488, 489, 211 S.E.2d 430, 431 (1974); U.C.C. § 9-308 (1977); 2 G. Gilmore, *supra* note 15, § 27.1, at 728.

50. *See* Skilton, *supra* note 25, at 76-78; *see, e.g.*, Rex. Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 177, 580 P.2d 8, 9 (1978); International Harvester Credit Corp. v. Associates Fin. Servs., 133 Ga. App. 488, 492, 211 S.E.2d 430, 433 (1974); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 269, 288 N.Y.S.2d 525, 533 (Sup. Ct. 1968).

51. R. Speidel, *supra* note 12, at 5, 646; *see* Hawkland, *Uniform Commercial "Code" Methodology*, 1962 U. Ill. L.F. 291, 294.

52. R. Speidel, *supra* note 12, at 5, 646; M. Chalmers, Address on the Codification of Mercantile Law, 19 Law Q. Rev. 10, 15 (1903).

53. Finance Co. of Am. v. Hans Mueller Corp., 471 F.2d 546, 552 (4th Cir. 1972); Lockyer v. Offley, 99 Eng. Rep. 1079, 1083 (1786); R. Speidel, *supra* note 12, at 5, 646; M. Chalmers, *supra* note 52, at 14-15; *see* Hawkland, *supra* note 51, at 294, 320.

54. M. Chalmers, *supra* note 52, at 18.

55. *Id.; see* R. Speidel, *supra* note 12, at 657; Hawkland, *supra* note 51, at 294.

56. The commercial case law system developed in the wake of the Industrial Revolution. Hawkland, *supra* note 51, at 293-94. The number of cases grew rapidly. Gilmore, *Legal Realism: Its Cause and Cure*, 70 Yale L.J. 1037, 1040-41 (1961); Hawkland, *supra* note 51, at 293-94. Because a precedent-based case law system can

utes[57] that followed failed to achieve the necessary certainty and uniformity. The Uniform Commercial Code was intended to remedy this failure.[58]

The Code drafters attempted to add a measure of predictability to commercial law,[59] while ensuring sufficient flexibility in its application.[60] These aims are expressed in the Code's stated purposes and policies: "to simplify, clarify and modernize the law governing commercial transactions;" "to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;" and "to make uniform the law among the various jurisdictions."[61] The Code also mandates that it "be liberally construed and applied to promote its underlying purposes and policies."[62] This directive per-

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only function with a manageable number of precedents, the burgeoning number of cases caused the system to break down. Gilmore, *supra*, at 1041. In addition, the decisions were not uniform from state to state. *Id.* at 1043-44; Hawkland, *supra* note 51, at 293-94. This patchwork of nonuniform decisions impeded interstate commercial activity. *Id.* at 294.

57. The uniform state statutes were enacted in an attempt to remedy the failure of the commercial case law system. Gilmore, *supra* note 56, at 1043-44; Hawkland, *supra* note 51, at 296. The National Conference of Commissioners of Uniform State Laws, formed in the 1890's, presented the Uniform Sales Act in 1906. R. Speidel, *supra* note 12, at 18. This statute, the principal commercial act, was adopted by only 36 states. Hawkland, *supra* note 51, at 297. Others were adopted by only a handful of states. *Id.* In addition, the statutes were not comprehensive. For example, the Uniform Sales Act covered only 60% of sales transactions. *Id.* at 299. Finally, because the statutes were not constructed systematically, they sometimes conflicted with each other. *Id.* at 298-99. Thus, the "uniform" statutes failed to satisfy the needs of an increasingly mercantile society. *Id.* at 299.

58. Commonwealth v. Jett, 230 Pa. Super. 373, 375, 326 A.2d 508, 509 (1974); Hawkland, *supra* note 51, at 299-300; *see* Redisco, Inc. v. United Thrift Stores, Inc., 363 F.2d 11, 14 (3d Cir. 1966); Arcuri v. Weiss, 198 Pa. Super. 506, 510, 184 A.2d 24, 26 (1962); Mid Continent Aircraft Corp. v. Curry County Spraying Serv., Inc., 572 S.W.2d 308, 312 (Tex. 1978); Kripke, *The Principles Underlying the Drafting of the Uniform Commercial Code*, 1962 U. Ill. L.F. 321, 330-31.

59. Hawkland, *supra* note 51, at 299-300, 320.

60. U.C.C. § 1-102 official comment 1 (1977); Kripke, *supra* note 58, at 329-30; *e.g.*, *In re* Stegman, 15 U.C.C. Rep. Serv. (Callaghan) 225, 228-29 (S.D. Fla. 1974); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 264-65, 288 N.Y.S.2d 525, 529 (Sup. Ct. 1968); Erb v. Stoner, 19 Pa. D. & C.2d 25, 31 (1958). Although the Code was designed "to be a semi-permanent piece of legislation," it "provide[s] its own machinery for expansion of commercial practices." U.C.C. § 1-102 official comment 1 (1977). One such mechanism is § 1-102(3), which states that "[t]he effect of provisions of this Act may be varied by agreement." *Id.* § 1-102(3); *see id.* § 1-102 official comment 2.

61. U.C.C. § 1-102(2) (1977).

62. *Id.* § 1-102(1). Courts are well aware of this important mandate. *E.g.*, Universal Lightning Rod, Inc. v. Rischall Elec. Co., 24 Conn. Supp. 399, 401, 192 A.2d 50, 51 (Cir. Ct. 1963); Servbest Foods, Inc. v. Emessee Indus., Inc., 82 Ill. App. 3d 662, 671, 403 N.E.2d 1, 8 (1980); Minsel v. El Rancho Mobile Home Center, Inc., 32 Mich. App. 10, 13, 188 N.W.2d 9, 11 (1971); Putnam Ranches, Inc. v. Corkle, 189 Neb. 533, 535, 203 N.W.2d 502, 503 (1973); Baillie Lumber Co. v. Kincaid Carolina Corp., 4 N.C. App. 342, 353, 167 S.E.2d 85, 92-93 (1969).

tains not only to the purposes and policies underlying the Code as a whole, but also to those of its component sections.[63]

The Uniform Commercial Code has aspects of a "true code," in that it has its own stated purposes and policies, preempts the field of commercial law, and is constructed systematically.[64] Accordingly, it is recommended that courts modify their legal method when construing the Code. As a threshold matter, it must be determined whether the answer to a particular problem is contained within the Code.[65] If it is, courts should look to the text of the Code as the "best evidence of what it means."[66] If the Code does not address a specific situation, however, courts should use analogy.[67] It is also suggested that courts should attribute less precedential value to their own decisions[68] and give weight to Code decisions of other states.[69] This recommendation is based on the idea that "the uniform 'right' decision ranks higher than the local 'best' decision."[70]

Article 9 of the Code was designed "to provide a simple and unified structure within which the immense variety of present-day secured financing transactions can go forward with less cost and with greater certainty."[71] Pre-Code secured financing had been characterized by conflicting and arbitrary requirements for each of the numerous fi-

63. U.C.C. § 1-102 official comment 1 (1977).

64. Hawkland, *supra* note 51, at 299; *see* Gilmore, *supra* note 56, at 1042-43.

65. *In re* Hardin, 8 U.C.C. Rep. Serv. (Callaghan) 857, 861 (Bankr. E.D. Wis. 1971), *aff'd*, 458 F.2d 938 (7th Cir. 1972); Herington Livestock Auction Co. v. Verschoor, 179 N.W.2d 491, 493 (Iowa 1970); Lincoln Bank & Trust Co. v. Queenan, 344 S.W.2d 383, 385 (Ky. 1961).

66. Hawkland, *supra* note 51, at 319; *accord* Gilmore, *supra* note 56, at 1043.

67. Gilmore, *supra* note 56, at 1043; Hawkland, *supra* note 51, at 314-18; *see* U.C.C. § 1-102 official comment 1 (1977). In determining whether a potentially applicable Code provision should apply in a given situation, a court should consider whether the underlying policy of the section applies to the case at hand. *See* Hawkland, *supra* note 51, at 317. Courts are also directed to supplement the provisions of the Code with "principles of law and equity," unless "displaced by the particular provisions of [the] Act." U.C.C. § 1-103 (1977). These principles include, for example, the law merchant, estoppel, coercion and mistake. *Id.*; Hawkland, *supra* note 51, at 312-13.

68. Hawkland, *supra* note 51, at 318-20. Because court decisions do not become part of the legislation, but are merely persuasive, the role of stare decisis is somewhat limited. *See* Gilmore, *supra* note 56, at 1043.

69. *E.g.*, A.J. Armstrong Co. v. Janburt Embroidery Corp., 97 N.J. Super. 246, 259, 234 A.2d 737, 744 (Law Div. 1967); Commonwealth v. National Bank & Trust Co., 469 Pa. 188, 194, 364 A.2d 1331, 1335 (1976); Hawkland, *supra* note 51, at 319-20.

70. Hawkland, *supra* note 51, at 319.

71. U.C.C. § 9-101 official comment (1977); *accord* Wabasso State Bank v. Caldwell Packing Co., 308 Minn. 349, 357, 251 N.W.2d 321, 325 (1976); *see, e.g.*, Redisco, Inc. v. United Thrift Stores, Inc., 363 F.2d 11, 14 (3d Cir. 1966); Needle v. Lasco Indus., Inc., 10 Cal. App. 3d 1105, 1107, 89 Cal. Rptr. 593, 594 (1970); Uniroyal, Inc. v. Michigan Bank, N.A., 12 U.C.C. Rep. Serv. (Callaghan) 745, 750 (Mich. Cir. Ct. 1972).

nancing devices.[72] Article 9 brought consistency to this field of law by recognizing distinctions between devices only when of functional utility.[73]

Section 9-201 of the Code provides that a "security agreement is effective . . . between the parties, against purchasers of the collateral and against creditors."[74] This rule states the general validity of security agreements,[75] which are the means by which security interests are created.[76] A security interest gives a lender the right to take possession of goods serving as collateral in the event of a debtor's default.[77] In commercial financing, one of the most frequently used lending arrangements is floor-plan financing, under which the debtor's inventory serves as collateral for the loan.[78] Although such an arrangement does not normally prohibit the seller from selling his inventory,[79] the lender may include in the security agreement certain restrictions,[80] such as a requirement that the seller obtain express authorization from the lender before completing a sale.[81]

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72. U.C.C. § 9-101 official comment (1977). Examples of the various pre-Code financing devices include the chattel mortgage, the conditional sale, and the trust receipt. *Id.* The evolving complexity of available financing transactions reflected in numerous statutory provisions resulted in higher costs and much uncertainty as to the rights of the parties. *Id.* Furthermore, despite the large number of financing forms, gaps in financing certain types of transactions remained. *Id.*

73. *Id.*; Alaska State Bank v. General Ins. Co., 579 P.2d 1362, 1365 (Alaska 1978); L. Denonn, *supra* note 3, § 5.1, at 34; 1 G. Gilmore, *supra* note 15, § 9.2, at 290, § 11.1, at 333; *see* W. Davenport & D. Murray, *supra* note 3, § 3.01, at 87. "The Code has eliminated the older, technical and restrictive categories of security agreements. Gone are the definitional difficulties and transactional fictions of the chattel mortgage, the conditional sale, and the trust receipt. In their stead is a general set of rules for the creation of a security interest in the secured party." Uniroyal, Inc. v. Michigan Bank, N.A., 12 U.C.C. Rep. Serv. (Callaghan) 745, 750 (Mich. Cir. Ct. 1972); *accord* Redisco, Inc. v. United Thrift Stores, Inc., 363 F.2d 11, 14 (3d Cir. 1966). See T. Quinn, *supra* note 3, ¶ 9-101[A], for a discussion of the basic changes Article 9 made to pre-Code secured financing law.

74. U.C.C. § 9-201 (1977).

75. *Id.* § 9-201 official comment.

76. *Id.* § 9-105(1)(*l*).

77. *Id.* § 9-503; T. Quinn, *supra* note 3, ¶ 9-503[A], at 9-311.

78. *See supra* note 12.

79. The secured party expects that the goods will be sold and that his interest will then attach to the proceeds. 1955 Report, *supra* note 4, at 228; 2 G. Gilmore, *supra* note 15, § 26.1, at 677; *Possession or Title*, *supra* note 12, at 695 n.4; *see* J. Honnold, *supra* note 15, at 598-99; R. Speidel, *supra* note 12, at 217.

80. *See* R. Posner, Economic Analysis of Law 294 (2d ed. 1977); *Possession or Title*, *supra* note 12, at 700.

81. *See* Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 843 n.2 (R.I. 1979). The security agreement may also provide, for example, that retail, but not wholesale, sales are allowed, *see* O.M. Scott Credit Corp. v. Apex Inc., 97 R.I. 442, 444, 198 A.2d 673, 675 (1964), or that sales must be in the ordinary course of business. *See* Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 752 (3d Cir. 1979).

This extension of credit on the strength of underlying inventory enables sellers to acquire the merchandise they sell.[82] In the absence of the protection afforded security interests by the Code, it is presumable that certain lenders might not be as willing to lend.[83] In such a case, certain sellers would not be in a position to sell.[84] This result would interfere with our exchange economy, in which "[s]ales of goods and contracts for their sale are the most common and most significant of all commercial transactions."[85] To avoid this result, Article 9 incorporates an "unambiguous bias in favor of the secured party"[86] and makes the security agreement a "very powerful document."[87]

Exceptions to the general rule recognizing the validity of security agreements are therefore allowed only under special circumstances and by express provision.[88] One such provision is the BIOC exception of section 9-307(1),[89] which was designed to allow buyers of goods to take free of security interests created by their sellers, even though those interests are perfected.[90] This provision serves the dual purpose

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82. *See supra* note 12.
83. R. Speidel, *supra* note 12, at 73-74.
84. *Id.* at 74.
85. *Id.* at 644.
86. Dugan, *supra* note 31, at 333; *see* Copeland v. Stewart, 124 Cal. Rptr. 860, 866 (Ct. App. 1975); McFadden v. Mercantile-Safe Deposit & Trust Co., 260 Md. 601, 624, 273 A.2d 198, 209 (1971).
87. T. Quinn, *supra* note 3, ¶ 9-201[A], at 9-84.
88. U.C.C. § 9-201 official comment (1977). One such provision is § 9-301, which allows certain persons to take priority over unperfected security interests. *Id.* § 9-301; W. Davenport & D. Murray, *supra* note 3, § 3.03, at 95; T. Quinn, *supra* note 3, ¶¶ 9-301[A][1]-[10] (1978 & Supp. 1981). Other circumstances where the secured party might not prevail are covered under § 9-312, which determines priorities among conflicting security interests in the same collateral. U.C.C. § 9-201 official comment (1977). Lastly, the security interest may be defeated by certain claimants who are given protected status, *id.*, including purchasers of chattel paper, *id.* § 9-308; T. Quinn, *supra* note 3, ¶¶ 9-308[A][2]-[5], and purchasers of instruments. U.C.C. § 9-309 (1977); T. Quinn, *supra* note 3, ¶¶ 9-309[A]-[A][1] (1978 & Supp. 1981). This group of protected buyers also includes buyers of goods, U.C.C. § 9-201 official comment (1977), known as buyers in the ordinary course of business. *Id.* § 9-307; T. Quinn, *supra* note 3, ¶¶ 9-307[A][1]-[13] (1978 & Supp. 1981).
89. U.C.C. § 9-307(1) (1977). The BIOC exception contained in § 9-307(1) has been referred to as the principal exception to the general rule of validity of security agreements under § 9-201. Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 477, 392 N.E.2d 344, 345 (1979). The BIOC exception has also been called "the buyer's best friend." T. Quinn, *supra* note 3, ¶ 9-307[A][2]. Additionally, the buyer in ordinary course has been termed "one of the favorites in the dramatis personae of the UCC." Skilton, *supra* note 25, at 2.
90. U.C.C. § 9-307 official comment 1 (1977); B. Clark, *supra* note 3, ¶ 3.4, at 3-18; T. Quinn, *supra* note 3, ¶ 9-307[A][2]; Skilton, *supra* note 25, at 12.

of "encourag[ing] the marketability of goods"[91] and "support[ing] the reliance interest of buyers who assume that they have clear title to the goods they purchase."[92] Buyers expect that their sellers have the right to sell the goods they offer for sale.[93] In addition, because restrictions in the security agreement do not appear in the filed financing statement,[94] the buyer has no way of discovering restrictions negotiated between the lender and the seller-debtor.[95] Therefore, because buyers may be at a disadvantage when inventory serves as collateral, the BIOC exception of section 9-307(1), "rest[ing] on principles of justice and utility,"[96] "favor[s] the safeguarding of sales transactions over the safeguarding of secured transactions."[97]

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91. B. Clark, *supra* note 3, ¶ 3.4, at 3-18; *accord In re* Kline, 1 U.C.C. Rep. Serv. (Callaghan) 628, 634 (E.D. Pa. 1956); 2 N.Y. L. Rev. Comm'n, Report and Record of Hearings on the Uniform Commercial Code, Leg. Doc. No. 65, at 1018 (1954).

92. B. Clark, *supra* note 3, ¶ 3.4, at 3-18; *accord* Knapp, *supra* note 3, at 887; *see* Dugan, *supra* note 31, at 346.

93. Haynes v. General Elec. Credit Corp., 432 F. Supp. 763, 767 (W.D. Va. 1977), *aff'd*, 582 F.2d 869 (4th Cir. 1978); Northern Ill. Corp. v. Bishop Distrib. Co., 284 F. Supp. 121, 125 (W.D. Mich. 1968); Texas Nat'l Bank v. Aufderheide, 235 F. Supp. 599, 604 (E.D. Ark. 1964); Bitzer-Croft Motors, Inc. v. Pioneer Bank & Trust Co., 82 Ill. App. 3d 1, 12, 401 N.E.2d 1340, 1348 (1980); Sebrite Corp. v. Transouth Fin. Corp., 272 S.C. 483, 487, 252 S.E.2d 873, 875 (1979). The policy of § 9-307(1) is that "where the debtor has express, implied, or apparent authority to sell the collateral, a buyer in the ordinary course of business takes free of the security interest." Comm'n on Unif. State Laws, New York Annotations to Uniform Commercial Code and Report to Legislature of New York State, Leg. Doc. No. 65, at 275 (1961). The authority to sell can flow from the status of the goods as inventory, Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 843 n.2 (R.I. 1979); Matthews v. Arctic Tire, Inc., 106 R.I. 691, 694, 262 A.2d 831, 833 (1970); 1955 Report, *supra* note 4, at 228, as well as the fact that the seller has claimed proceeds. *Id.; see supra* note 79 and accompanying text.

94. Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 752 n.3 (3d Cir. 1979); Bank of Utica v. Castle Ford, Inc., 36 A.D.2d 6, 9, 317 N.Y.S.2d 542, 545 (1971); Hempstead Bank v. Andy's Car Rental Sys., 35 A.D.2d 35, 38, 312 N.Y.S.2d 317, 320 (1970).

95. Bank of Utica v. Castle Ford, Inc., 36 A.D.2d 6, 9, 317 N.Y.S.2d 542, 545 (1971); Hempstead Bank v. Andy's Car Rental Sys., 35 A.D.2d 35, 38, 312 N.Y.S.2d 317, 320 (1970); Sebrite Corp. v. Transouth Fin. Corp., 272 S.C. 483, 486-87, 252 S.E.2d 873, 875 (1979). Because buyers gain nothing from searching the files for liens, they are not considered to lack good faith for failing to do so. Hempstead Bank v. Andy's Car Rental Sys., 35 A.D.2d 35, 38, 312 N.Y.S.2d 317, 320 (1970).

96. Skilton, *supra* note 25, at 3.

97. *Id.* at 4. Section 9-307(1) of the Code has its roots in the Uniform Trust Receipts Act provision governing buyers in the ordinary course of trade, Unif. Trust Receipts Act § 9(2)(a) (1933), 9C U.L.A. 255 (1957), and the Uniform Conditional Sales Act provision governing buyers for value in the ordinary course of business. Unif. Conditional Sales Act § 9 (1918), 2 U.L.A. 15 (1922). Thus, the BIOC exception represents the continuation of a statutory tradition of protecting buyers. Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979); 1955 Report, *supra* note 4, at 227-30; 2 G. Gilmore, *supra* note 15, §§ 26.3-4; Skilton, *supra* note 25, at 4-7.

Article 9's attempt to accommodate the conflicting rights of buyers and secured lenders has been termed "a finely integrated plan for the determination of the priorities and equities of the parties to secured transactions."[98] Its principal mechanism, section 9-307(1), is usually effective in adjusting the tension between buyers of inventory and secured lenders who claim rights in the inventory.[99] Because it is unclear when BIOC status arises,[100] however, the buyer's ability to prevail under this exception is questionable when he has not yet obtained possession of the goods he has purchased. *B* will want to obtain possession of the television he has contracted to buy. Similarly, if *S* defaults on his loan, *L* will want to exercise his Code reclamation rights.[101] In order to resolve this conflict, it is necessary to determine exactly when a buyer may properly partake of the protection provided to buyers in the ordinary course. The resolution of this question will lead to increased uniformity and predictability, two important mandates handed down by the drafters of the Code.

II. The Points in Time

A sales transaction involves a series of identifiable events. In the hypothetical in the Introduction, the first step, the making of the contract, occurs when *B* agrees to purchase the television. The next step, identification of the goods to the contract, occurs when *S* designates a particular television set for delivery to *B* by either noting on the sales agreement the serial number of *B*'s new television or actually setting a television aside. The next step in the transaction, passage of title, occurs when the television is delivered. Delivery is accomplished by *S*'s act of loading the television into his delivery truck for shipment to *B*, as per prior agreement. Receipt occurs when *B* permits the delivery people to bring the television into his house. Acceptance, the final step, occurs after a reasonable period for inspection, when *B*, satisfied with the television, does not reject it. Although these events usually occur successively, they will be addressed in order of increasing importance to determination of BIOC status.

A. *Acceptance*

Acceptance represents the end point on the transactional continuum.[102] The Code provides that it may occur in three different

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98. Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968).

99. *See id.*; Note, *Merchant-Buyer's Good Faith Duty to Inquire Under 9-307: A Confusion of Concepts*, 27 U. Miami L. Rev. 524, 528-29 (1973).

100. *See* B. Clark, *supra* note 3, ¶ 3.4[2], at 3-21 to -22; T. Quinn, *supra* note 3, ¶ 9-307[A][8] (1978 & Supp. 1981); Skilton, *supra* note 25, at 15-19.

101. *See supra* note 18.

102. T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981). This is of

ways.[103] The first method, express acceptance, occurs when *B* signifies by word or act that he is satisfied with the television.[104] Acceptance may also occur by operation of law if the buyer fails to make an effective rejection after a reasonable opportunity to inspect.[105] Finally, a buyer may be held to have technically accepted[106] by an act inconsistent with S's ownership.[107]

There is no authority for requiring acceptance of goods before conferring BIOC status.[108] Courts may avoid acceptance because the precise moment of acceptance is not easily pinpointed. Assuming neither express nor technical acceptance, the period of time during which acceptance may occur varies depending on the amount of time reasonably necessary to inspect the goods.[109] A reasonable period has been held to be as short as one day[110] and as long as nine months after receipt.[111] Because the determination of what constitutes a reasonable time depends on the particular circumstances of each case,[112] a requirement of acceptance would add an unnecessary variable to determination of BIOC status.

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course barring revocation of acceptance, which is available under limited circumstances. *See* U.C.C. § 2-608 (1977).

103. U.C.C. § 2-606(1) (1977); *see, e.g.*, Miron v. Yonkers Raceway, Inc., 400 F.2d 112, 117 (2d Cir. 1968); Linscott v. Smith, 3 Kan. App. 2d 1, 4, 587 P.2d 1271, 1274 (1978); Fred J. Miller, Inc. v. Raymond Metal Prods. Co., 265 Md. 523, 527, 290 A.2d 527, 529 (1972).

104. U.C.C. § 2-606(1)(a) & official comment 1 (1977); *see, e.g.*, Pratt v. Winnebago Indus., Inc., 463 F. Supp. 709, 714 (W.D. Pa. 1979); Sessa v. Riegle, 427 F. Supp. 760, 767 (E.D. Pa. 1977), *aff'd mem.*, 568 F.2d 770 (3d Cir. 1978); Rozmus v. Thompson's Lincoln-Mercury Co., 209 Pa. Super. 120, 123-24, 224 A.2d 782, 784 (1966).

105. U.C.C. § 2-606(1)(b) (1977); *see, e.g.*, T.J. Stevenson & Co. v. 81,193 Bags of Flour, 629 F.2d 338, 357-58 (5th Cir. 1980); Green Chevrolet Co. v. Kemp, 241 Ark. 62, 65, 406 S.W.2d 142, 144 (1966); Linscott v. Smith, 3 Kan. App. 2d 1, 4, 587 P.2d 1271, 1274 (1978).

106. T. Quinn, *supra* note 3, ¶ 2-606[A][1].

107. U.C.C. § 2-606(1)(c) (1977); *e.g.*, Gerard Constr. Inc. v. Motor Vessel Va., 490 F. Supp. 475, 476-77 (W.D. Pa.), *aff'd*, 636 F.2d 1208 (3d Cir. 1980); Linscott v. Smith, 3 Kan. App. 2d 1, 4, 587 P.2d 1271, 1274 (1978); *see* Rozmus v. Thompson's Lincoln-Mercury Co., 209 Pa. Super. 120, 123-24, 224 A.2d 782, 784 (1966).

108. *See* T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981).

109. *See, e.g.*, T.J. Stevenson & Co. v. 81,193 Bags of Flour, 629 F.2d 338, 357 (5th Cir. 1980); Miron v. Yonkers Raceway, Inc., 400 F.2d 112, 118 (2d Cir. 1968); La Villa Fair v. Lewis Carpet Mills, Inc., 219 Kan. 395, 403, 548 P.2d 825, 832 (1976); White Devon Farm v. Stahl, 88 Misc. 2d 961, 964-65, 389 N.Y.S.2d 724, 727-28 (Sup. Ct. 1976); Don's Marine, Inc. v. Haldeman, 557 S.W.2d 826, 829 (Tex. Civ. App. 1977).

110. Miron v. Yonkers Raceway, Inc., 400 F.2d 112, 118 (2d Cir. 1968).

111. La Villa Fair v. Lewis Carpet Mills, Inc., 219 Kan. 395, 403, 548 P.2d 825, 832 (1976).

112. U.C.C. § 2-513 official comment 3 (1977); *e.g.*, T.J. Stevenson & Co. v. 81,193 Bags of Flour, 629 F.2d 338, 357 (5th Cir. 1980); Miron v. Yonkers Raceway, Inc., 400 F.2d 112, 118 (2d Cir. 1968); White Devon Farm v. Stahl, 88 Misc. 2d 961, 964-65, 389 N.Y.S.2d 724, 727-28 (Sup. Ct. 1976).

Furthermore, use of acceptance as a reference point postpones BIOC status until late in the transaction.[113] This result minimizes the effect of the Article 9 BIOC exception, thereby undermining the policy of protecting buyers from hidden interests in goods.[114] In addition, requiring acceptance would penalize the buyer who, exercising his Article 2 rights,[115] delays acceptance until he has completed a thorough inspection.[116] To protect himself against *L*'s right to repossess if *S* defaults during the period that *B* is inspecting, *B* may have to expressly accept before completing a thorough inspection. *B*'s rights against *S*, however, become severely circumscribed at the point of acceptance.[117] Thus, a requirement of acceptance would place *B* in the untenable position of having to choose between either the protection afforded by Article 2 or that of Article 9.

B. *Delivery and Receipt*

Unlike acceptance, delivery and receipt are readily discernible events. Delivery consists of the seller's conduct in putting and holding the goods at the buyer's disposition.[118] In contrast, receipt entails buyer's gaining possession of the goods.[119] Receipt, therefore, usually presupposes delivery.[120] In fact, "the seller may . . . fulfill his obliga-

113. T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981).

114. *See supra* notes 92-97 and accompanying text.

115. U.C.C. § 2-513 (1977).

116. *See* R. Speidel, *supra* note 12, at 951-52.

117. *See* T. Quinn, *supra* note 3, ¶ 2-607[A][1], at 2-355 to -356. Before acceptance, the buyer may reject if the goods fail to conform to the contract in any way. U.C.C. § 2-601 (1977). If, however, the buyer accepts the goods, § 2-607(2) provides that he is precluded from rejecting them. *Id.* § 2-607(2). He may, however, revoke his acceptance, but only where the defect substantially impairs the value of the goods. *Id.* § 2-608.

118. U.C.C. § 2-503 (1977). The general rule of § 2-503 provides that "the seller put and hold conforming goods at the buyer's disposition and give the buyer any notification reasonably necessary to enable him to take delivery. The manner, time and place for tender are determined by the agreement and this Article . . . ." *Id.* § 2-503(1). The nature of the sales contract will determine the seller's delivery obligation. T. Quinn, *supra* note 3, ¶ 2-503[A][2]. In a shipment contract, in which the seller is not required to deliver the goods to a particular destination, his obligation is discharged when he "put[s] the goods in the possession of . . . a carrier." U.C.C. § 2-504(a) (1977). In a destination contract, the seller's delivery obligation is not discharged until he tenders the goods at the point of destination. *Id.* § 2-503(3). When goods are in possession of a bailee, § 2-503(4) applies. *Id.* § 2-503(4). Code delivery rules also appear in other sections of Article 2. *E.g.*, *id.* § 2-307 (delivery in single lot or several lots); *id.* § 2-308 (absence of specified place for delivery); *id.* § 2-507 (effect of seller's tender; delivery on condition).

119. U.C.C. § 2-103(1)(c) (1977). "The act or state of possessing is a condition of facts under which one can exercise power over property . . . to the exclusion of all other persons . . . ." Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 870, 396 N.Y.S.2d 319, 321 (Sup. Ct. 1977).

120. *See* U.C.C. § 2-103 official comment 2 (1977).

tions to 'deliver' even though the buyer may never 'receive' the goods"[121]—for example, when goods are destroyed in transit after the seller has transferred them to a common carrier. Although the concepts thus are not synonymous,[122] they are often used interchangeably.[123] Courts and commentators routinely reject imposition of a delivery or receipt requirement[124] in determining BIOC status.

It could be argued, however, that delivery should be a prerequisite to a finding of BIOC status because it represents "the time when seller has finally committed himself in regard to specific goods."[125] This theory underlies the Code rule that title generally passes on delivery.[126] Another Code subsection, however, provides that title may pass as early as the time of contracting,[127] because under certain

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121. *Id.*

122. Mechanics Nat'l Bank v. Gaucher, 7 Mass. App. Ct. 143, 148, 386 N.E.2d 1052, 1056 (1979); Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 871, 396 N.Y.S.2d 319, 321 (Sup. Ct. 1977).

123. In considering whether the buyer was a BIOC, the court in Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 478, 392 N.E.2d 344, 346 (1979), used the term "received delivery." In Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 178, 580 P.2d 8, 10 (1978), the court, in holding that *possession* was not necessary, relied on Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968), which had held that *delivery* was not necessary for BIOC status.

124. Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 178, 580 P.2d 8, 10 (1978); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 494-96, 211 S.E.2d 430, 434-35 (1974); Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 478-79, 392 N.E.2d 344, 345-46 (1979); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968); Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979); *see* Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 751 (3d Cir. 1979); Tanbro Fabrics Corp. v. Deering Milliken, Inc., 39 N.Y.2d 632, 636, 350 N.E.2d 590, 592-93, 385 N.Y.S.2d 260, 262-63 (1976); Makransky v. Long Island Reo Truck Co., 58 Misc. 2d 338, 339-40, 295 N.Y.S.2d 240, 241-42 (Sup. Ct. 1968); 1955 Report, *supra* note 4, at 232; 2 G. Gilmore, *supra* note 15, § 26.6, at 696; T. Quinn, *supra* note 3, ¶ 9-307[A][8] (1978 & Supp. 1981); Dolan, *The Uniform Commercial Code and the Concept of Possession in the Marketing and Financing of Goods*, 56 Tex. L. Rev. 1147, 1155-56 (1978); Jackson & Peters, *Quest for Uncertainty: A Proposal for Flexible Resolution of Inherent Conflicts Between Article 2 and Article 9 of the Uniform Commercial Code*, 87 Yale L.J. 907, 950-53 (1978); Warren, *Cutting Off Claims of Ownership Under the Uniform Commercial Code*, 30 U. Chi. L. Rev. 469, 473 & n.23 (1963). One commentator argues that possession appears to be necessary for attainment of BIOC status in a § 2-403(2) entrustment, such as a bailment. Smith, *Title and the Right to Possession Under the Uniform Commercial Code*, 10 B.C. Indus. & Com. L. Rev. 39, 60-61 (1968). Other courts and commentators have interpreted Smith as saying that possession is a requirement in the Article 9 BIOC context as well. *See* Chrysler Corp. v. Adamatic, Inc., 59 Wis. 2d 219, 239, 208 N.W.2d 97, 106-07 (1973); Dolan, *supra*, at 1155 n.35; *Possession or Title*, *supra* note 12, at 698 n.23. Such an interpretation, however, is unwarranted; Smith's comment was expressly limited to § 2-403(2). *See* Smith, *supra*, at 60-61.

125. U.C.C. § 2-401 official comment 4 (1977).

126. *See id.*

127. *Id.* § 2-401(3)(b).

circumstances, the seller may be committed to a sale of specific goods at that time.[128] Thus, delivery does not always represent the point when S is committed and therefore should not be a requirement for BIOC status.

The rationale of the passage of title on delivery rule is also unpersuasive in the context of the BIOC exception because that section does not include the delivery requirement found in its predecessor, a provision of the Uniform Trust Receipts Act.[129] It is most likely that the Code drafters' omission of this requirement was intentional.[130] Other Code provisions that protect buyers expressly require delivery,[131] "highlight[ing] the absence of the delivery requirement in section 9-307(1)."[132] A court, by imposing a delivery requirement, would therefore be taking an action in contravention of legislative intent and prerogative.[133]

It has been suggested that receipt may be necessary for BIOC status because the definition of buyer in ordinary course in section 1-201(9) states that buying "includes receiving goods . . . under a pre-existing contract for sale."[134] In its study of the Uniform Commercial Code, the New York Law Revision Commission speculated that the receipt clause may have been inserted to mark the point when a buyer becomes sufficiently committed to payment of the price to be considered a buyer in the ordinary course of business.[135] Courts that have rejected the necessity of receipt, however, have apparently found the buyer sufficiently committed when he has done everything he is obli-

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128. *Id.* § 2-401 official comment 4.

129. Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979); 1955 Report, *supra* note 4, at 232; 2 G. Gilmore, *supra* note 15, § 26.6, at 696; Dolan, *supra* note 124, at 1155-56; Warren, *supra* note 124, at 473 & n.23; *Possession or Title*, *supra* note 12, at 698. The Uniform Trust Receipt Act's version of the BIOC exception, Unif. Trust Receipt Act § 9(a)(2) (1933), 9C U.L.A. 255 (1957), protected only buyers "to whom goods [were] sold and delivered." *Id.* § 1, 9C U.L.A. at 230.

130. Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979); 1955 Report, *supra* note 4, at 232; 2 G. Gilmore, *supra* note 15, § 26.6, at 696; Dolan, *supra* note 124, at 1155-56; Warren, *supra* note 124, at 473 & n.23.

131. *E.g.*, U.C.C. § 7-205 (1977); *id.* § 7-504(2)(b); *id.* § 9-301(1)(c).

132. Dolan, *supra* note 124, at 1188; *accord* 1955 Report, *supra* note 4, at 239-40; Jackson & Peters, *supra* note 124, at 950; Skilton, *supra* note 25, at 20.

133. In Continental Oil Co. v. Citizens Trust & Savs. Bank, 397 Mich. 203, 244 N.W.2d 243 (1976), the court refused to require that a financing statement be refiled when the secured party changed its name. The court stated: "We decline to engraft a court-established requirement upon the provisions of the U.C.C. which regulate commercial transactions within the marketplace. We leave such action to the Legislature, should it choose to do so." *Id.* at 209, 244 N.W.2d at 245; *accord* Leech v. White (*In re* Thermal Barriers, Inc.), 8 Bankr. 294, 296 (Bankr. E.D. Mich. 1981).

134. U.C.C. § 1-201(9) (1977); 1955 Report, *supra* note 4, at 235-36.

135. 1955 Report, *supra* note 4, at 235-36.

gated to do prior to receipt.[136] Moreover, the New York Law Revision Commission noted that if its conjecture concerning the purpose of the receipt clause were correct, "the rule appears to be conservative."[137] Finally, a requirement of receipt, or even delivery, would unduly delay determination of BIOC status,[138] in contravention of the section 9-307(1) policy of protecting buyers[139] and the basic Code policy of encouraging sales of goods.[140]

C. *Time of Contracting*

The time of contracting, the earliest point at which a buyer could conceivably sever a secured party's security interest, is usually not seriously considered as an alternative.[141] It is not entirely clear, however, why it is in disuse. In its favor is the Code definition of buyer contained in section 2-103(1)(a): "a person who buys or *contracts to buy* goods."[142] As has been noted, however, "[i]t is not an easy jump . . . to conclude that the definition of the term 'buyer' should influence the definition of the separate term 'buyer in ordinary course.' "[143] Moreover, the BIOC definition in section 1-201(9) refers only to a person who buys.[144] The New York Law Revision Commission has suggested that the absence of a reference to "contracting to buy" indicates that use of time of contracting to determine BIOC status may be appropriate only in the case of a present sale,[145] where the buyer becomes the owner immediately.[146] Moreover, time of

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136. *See* Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 178, 580 P.2d 8, 10 (1978); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 496, 211 S.E.2d 430, 435 (1974); Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 480, 392 N.E.2d 344, 347 (1979); Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 870-71, 396 N.Y.S.2d 319, 321 (Sup. Ct. 1977).

137. 1955 Report, *supra* note 4, at 235-36.

138. Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979); T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981); Dolan, *supra* note 124, at 1157.

139. *See supra* notes 89-97 and accompanying text.

140. *Possession or Title, supra* note 12, at 698 & n.25; *see supra* note 91 and accompanying text.

141. *See* Chrysler Corp. v. Adamatic, Inc., 59 Wis. 2d 219, 238-39, 208 N.W.2d 97, 106-07 (1973); T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981).

142. U.C.C. § 2-103(1)(a) (1977) (emphasis added); *see* T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981). One commentator argues that the definition of buyer as one "who contracts to buy" does not necessarily lead to the conclusion that an "executory buyer" qualifies as a BIOC as soon as the contract for sale is made. Skilton, *supra* note 25, at 15; *see* Jackson & Peters, *supra* note 124, at 952 n.162.

143. Jackson & Peters, *supra* note 124, at 952 n.162.

144. U.C.C. § 1-201(9) (1977).

145. 1955 Report, *supra* note 4, at 236.

146. T. Quinn, *supra* note 3, ¶ 2-106[A][1]; *see, e.g.*, O'Brien v. Isaacs, 32 Ill. 2d 105, 107, 203 N.E.2d 890, 891 (1965); Groth v. Stillson, 20 Mich. App. 704, 707, 174 N.W.2d 596, 598 (1969); Miles v. Starks, 590 S.W.2d 223, 225-26 (Tex. Civ. App.

contracting is of limited utility even in a present sale, because it coincides with either time of identification[147] or passage of title,[148] both of which are more readily accepted by the courts.

When there is not a present sale, the rights of a buyer are too immature at the time of contracting to justify attainment of BIOC status.[149] Section 2-105(2) of the Code requires that "[g]oods . . . be both existing and identified before any interest in them can pass."[150] Goods may exist at time of contracting without being identified,[151] as when *B* has agreed to buy a television, but before *S* has designated a specific television for delivery to *B*. Additionally, the goods that *B* has contracted to buy may not yet exist in the form in which they will be sold.[152] For example, *B* may order a cake.[153] Before *S* sets aside some flour and begins baking, section 2-105(2) would prevent passing of an interest to *B*.[154] Therefore, under Article 2, before goods are existing and identified, a buyer is a buyer in name only;[155] his interest in the

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1979), *cert. denied*, 449 U.S. 875 (1980). This is in contrast to a future sale, in which the buyer becomes the owner at a future date. T. Quinn, *supra* note 3, ¶ 2-106[A][1]. Both present and future sales are considered contracts of sale and are therefore covered by Article 2. U.C.C. § 2-106(1) (1977); *e.g.*, Fender v. Colonial Stores, Inc., 138 Ga. App. 31, 32, 225 S.E.2d 691, 693 (1976); Giant Food, Inc. v. Washington Coca-Cola Bottling Co., 273 Md. 592, 603-04, 332 A.2d 1, 8 (1975); Melms v. Mitchell, 266 Or. 208, 216 n.2, 512 P.2d 1336, 1340 n.2 (1973).

147. *See* Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 749-51 (3d Cir. 1979); Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 844 (R.I. 1979). Identification occurs at the time of contracting if the sale is of goods already existing and identified. U.C.C. § 2-501(1)(a) (1977).

148. *See* Jones v. One Fifty Foot Gulfstar Motor Sailing Yacht, 625 F.2d 44, 49 (5th Cir. 1980); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 493, 211 S.E.2d 430, 433-34 (1974). Title passes at time of contracting when (i) delivery is to be made without moving the goods, (ii) the goods are identified, and (iii) no documents are to be delivered. U.C.C. § 2-401(3)(b) (1977).

149. *See* T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981).

150. U.C.C. § 2-105(2) (1977).

151. *See* Melms v. Mitchell, 266 Or. 208, 216 n.2, 512 P.2d 1336, 1340 n.2 (1973); City of Richmond v. Petroleum Marketers, Inc., 221 Va. 372, 374, 269 S.E.2d 389, 390 (1980).

152. In such a situation, the goods, for example, chocolate and sugar, or quartz crystals, will ultimately be sold as manufactured products—that is, candy and watches respectively. W. Davenport & D. Murray, *supra* note 3, § 2.09, at 67-68; T. Quinn, *supra* note 3, ¶ 9-315[A].

153. *See* T. Quinn, *supra* note 3, ¶ 9-315[A].

154. U.C.C. § 2-105(2) (1977). Although the goods need not be in a deliverable state to be identified, *id.* § 2-501 official comment 4; Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979), one commentator has indicated that identification does not occur by the mere manufacturing of goods from which a certain buyer's order will be filled. 2 R. Anderson, *supra* note 29, § 2-501:9, at 64. In fact, identification does not occur until the first step of production using the raw materials, and only if the production is done according to specifications contained in the buyer's contract for the goods. *Id.* §§ 2-501:4, at 61, :9 at 64.

155. *See* Dolan, *supra* note 124, at 1156.

goods has not yet arisen.[156] Thus, determination of BIOC status at time of contracting would give the buyer rights through section 9-307(1) at a point in time at which Article 2 does not recognize an interest.[157] Moreover, because under Article 9 a secured party may have a perfected security interest in the raw materials[158]—that is, the flour—prior to identification of the materials to the buyer's contract, use of time of contracting in the BIOC context would also unduly interfere with Article 9's policy of giving validity to security interests.[159]

D. *Passage of Title*

Passage of title is the point in time that has engendered the most controversy with respect to determination of BIOC status. On the one hand, the Code minimizes the importance of title.[160] As stated in an official comment, "the rights and remedies of the parties to the contract of sale, as defined in [Article 2] . . . rest on the contract and its performance . . . and not on stereotyped presumptions as to the location of title."[161] On the other hand, the Code provides that a " 'sale' consists in the passing of title from the seller to the buyer for a price."[162] Because qualification as a buyer in ordinary course re-

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156. *See* U.C.C. § 2-105(2) (1977).

157. *Cf.* Dolan, *supra* note 124, at 1192-93 & n.243 (passage of title should not govern § 9-307(1) situations because "title does not govern the rights of the buyer under Article 2").

158. R. Speidel, *supra* note 12, at 212. The security interest in the raw materials carries over into the finished goods. U.C.C. §§ 9-315 (1977); W. Davenport & D. Murray, *supra* note 3, § 2.09, at 67-68; T. Quinn, *supra* note 3, at ¶ 9-315[A].

159. *See supra* notes 74-75, 86-87 and accompanying text.

160. *E.g.*, Anderson v. First Jacksonville Bank, 243 Ark. 977, 980, 423 S.W.2d 273, 274-75 (1968); Giant Food, Inc. v. Washington Coca-Cola Bottling Co., 273 Md. 592, 604, 332 A.2d 1, 8 (1975); William F. Wilke, Inc. v. Cummins Diesel Engines, Inc., 252 Md. 611, 615-16, 250 A.2d 886, 889 (1969); Zabriskie Chevrolet, Inc. v. Smith, 99 N.J. Super. 441, 446, 240 A.2d 195, 198 (1968); Nationwide Mut. Ins. Co. v. Hayes, 276 N.C. 620, 632, 174 S.E.2d 511, 518 (1970); T. Quinn, *supra* note 3, ¶ 2-401[A][1]; Dolan, *supra* note 124, at 1192; Jackson & Peters, *supra* note 124, at 912; Skilton, *supra* note 25, at 17-18; *see* U.C.C. § 2-101 official comment (1977); *id.* § 2-401 & official comment 1; *id.* § 2-505 official comment 1; *id.* § 9-202 & official comment.

161. U.C.C. § 2-505 official comment 1 (1977). The court in Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 288 N.Y.S.2d 525 (Sup. Ct. 1968), stated that "a buyer who makes a purchase . . . in good faith with a full understanding it is a binding contract, who knowingly signs a retail installment payment obligation and trades in an old car in addition must . . . be deemed a buyer in the ordinary course of business, *without regard to the technicalities of when title is to pass.*" *Id.* at 270, 288 N.Y.S.2d at 534 (emphasis added); *accord* Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 177-78, 580 P.2d 8, 9-10 (1978); Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 478-79, 392 N.E.2d 344, 345-46 (1979).

162. U.C.C. § 2-106(1) (1977).

quires a sale,[163] courts that emphasize the importance of title in the definition of sale require passage of title before conferring BIOC status.[164] Inclusion of title in the definition of sale, however, was intended to serve the limited purpose of distinguishing a transaction that is properly characterized as a sale for Article 2 purposes from one in which transfer of ownership is not contemplated, as in a bailment or lease.[165] "[B]eyond that [title] serves no function"[166] and its use in the determination of BIOC status "flies in the face of the drafters' antipathy to the use of 'title' as a Code problem solver."[167]

The Code title rules may provide a certain degree of flexibility in that title may pass at any time after identification to which the parties agree[168] or, under limited circumstances, at time of contracting.[169] The general rule, however, is that title passes when the seller has completed his performance with respect to physical delivery of the goods.[170] This rule may lead to harsh results when delivery has not yet occurred. For example, in *Chrysler Corp. v. Adamatic, Inc.*,[171] the leading case decided under the title theory,[172] the buyer had

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163. *Id.* § 1-201(9); Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 870, 396 N.Y.S.2d 319, 320 (Sup. Ct. 1977); Chrysler Corp. v. Adamatic, Inc., 59 Wis. 2d 219, 239, 208 N.W.2d 97, 106 (1973); B. Clark, *supra* note 3, § 3.4[2], at 3-22; Dolan, *supra* note 124, at 1154; Skilton, *supra* note 25, at 16; *Possession or Title*, *supra* note 12, at 697.

164. International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492-94, 211 S.E.2d 430, 433-34 (1974); Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 870, 396 N.Y.S.2d 319, 320 (Sup. Ct. 1977); Chrysler Corp. v. Adamatic, Inc., 59 Wis. 2d 219, 239, 208 N.W.2d 97, 106 (1973); *cf.* Jones v. One Fifty Foot Gulfstar Motor Sailing Yacht, 625 F.2d 44, 47 (5th Cir. 1980) (legal title required in admiralty petitory action).

165. T. Quinn, *supra* note 3, ¶ 2-106[A][1]; *see* U.C.C. § 2-401 official comment 1 (1977).

166. T. Quinn, *supra* note 3, ¶ 2-106[A][1].

167. *Id.* ¶ 9-307[A][8], at S9-136 (Supp. 1981); *accord* 1955 Report, *supra* note 4, at 451; Skilton, *supra* note 25, at 17-18.

168. U.C.C. § 2-401(1) (1977); *e.g.*, Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 177, 580 P.2d 8, 8-9 (1978); Bowman v. American Home Assurance Co., 190 Neb. 810, 813, 213 N.W.2d 446, 448 (1973); Graves Constr. Co. v. Rockingham Nat'l Bank, 220 Va. 844, 849-50, 263 S.E.2d 408, 412 (1980).

169. U.C.C. § 2-401(3)(b) (1977). "[T]itle passes at the time and place of contracting" where delivery is to be made without moving the goods, the goods are already identified and no documents are to be delivered. *Id.* BIOC status has been found at time of contracting under § 2-401(3)(b). Jones v. One Fifty Foot Gulfstar Motor Sailing Yacht, 625 F.2d 44, 49 (5th Cir. 1980); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492-94, 211 S.E.2d 430, 433-34 (1974).

170. U.C.C. § 2-401(2) (1977); *e.g.*, Coast Scopitone, Inc. v. Self, 127 Ga. App. 124, 127, 192 S.E.2d 513, 515 (1972); Underwood v. Commonwealth, 390 S.W.2d 635, 639 (Ky. 1965); Gantman v. Paul, 203 Pa. Super. 158, 161-62, 199 A.2d 519, 520 (1964).

171. 59 Wis. 2d 219, 208 N.W.2d 97 (1973).

172. *See* Integrity Ins. Co. v. Marine Midland Bank-W., 90 Misc. 2d 868, 870-71,

tendered substantially all of the contract price,[173] and both parties agreed that identification had taken place.[174] In addition, the buyer had obtained possession of the goods by a replevin action.[175] The court, however, viewed the replevin as "an unusual and drastic mode of recourse to secure the rights of a purchaser,"[176] and further noted that the parties had apparently intended title to pass on delivery.[177] The court, therefore, determined that title had not yet passed and that the buyer failed to qualify as a BIOC.[178] Nevertheless, as the *Chrysler* court itself recognized, "[f]rom the viewpoint of equity, this is an unsatisfactory result."[179] The buyer did not prevail despite having discharged his obligation under the contract because delivery, a relatively late point in the transaction, had not yet occurred.

E. *Identification*

Identification "specif[ies] the goods to which the contract refers so that the contract can apply to no others,"[180] and represents the point at which the buyer first acquires property rights in the goods he has contracted to buy.[181] Section 2-501 of the Code provides a set of rules outlining how and when identification occurs.[182] When the buyer selects an item out of the seller's inventory in a present sale, identification occurs at the time of contracting.[183] Otherwise, identification occurs when the seller fills the buyer's order by designating particular goods for delivery to the buyer,[184] or in any other way and at any time to which the parties agree.[185]

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396 N.Y.S.2d 319, 321 (Sup. Ct. 1977); B. Clark, *supra* note 3, § 3.4[2], at 3-22; T. Quinn, *supra* note 3, ¶ 9-307[A][8] (1978 & Supp. 1981); Dolan, *supra* note 124, at 1154-59; Jackson & Peters, *supra* note 124, at 952; Skilton, *supra* note 25, at 16-21.

173. 59 Wis. 2d at 226, 241-42, 208 N.W.2d at 100, 108.

174. *Id.* at 240, 208 N.W.2d at 107; *see* T. Quinn, *supra* note 3, ¶ 9-307[A][8], at 9-192; Skilton, *supra* note 25, at 16.

175. 59 Wis. 2d at 228, 208 N.W.2d at 101.

176. *Id.* at 241, 208 N.W.2d at 107.

177. *Id.*

178. *See id.* at 241-42, 208 N.W.2d at 108.

179. *Id.*

180. Rivera, *Identification of Goods and Casualty to Identified Goods Under Article Two of the UCC*, 13 Ind. L. Rev. 637, 640 (1980) (emphasis omitted); *accord* Servbest Foods, Inc. v. Emessee Indus., Inc., 82 Ill. App. 3d 662, 670, 403 N.E.2d 1, 7 (1980); 2 R. Anderson, *supra* note 29, § 2-501:4, at 60-61.

181. T. Quinn, *supra* note 3, ¶ 2-501[A][1]. Identification represents the time when the "buyer obtains a special property and an insurable interest" in existing goods. U.C.C. § 2-501(1) (1977). It is also the point at which an interest in goods may first pass under Article 2. *Id.* § 2-105(2).

182. U.C.C. § 2-501 (1977); T. Quinn, *supra* note 3, ¶¶ 2-501[A][1]-[2].

183. U.C.C. § 2-501(1)(a) (1977); T. Quinn, *supra* note 3, ¶ 2-501[A][2].

184. U.C.C. § 2-501(1)(b) (1977); 2 R. Anderson, *supra* note 29, § 2-501:4, at 61; T. Quinn, *supra* note 3, ¶ 2-501[A][2].

185. U.C.C. § 2-501(1) (1977).

Use of identification in determining BIOC status appears to be the modern trend.[186] The court in *Holstein v. Greenwich Yacht Sales, Inc.*[187] confronted the buyer-secured party conflict. After rejecting title, delivery and receipt as requirements for BIOC status,[188] the court concluded that the buyer qualified as a buyer in the ordinary course at the time of identification of the goods to the contract.[189] This conclusion was based on the court's recognition of the equities of the conflict: "The risk of loss . . . quite properly should be on the lender rather than on the buyer."[190]

A number of factors compel assignment of the risk to the secured party. The lender makes an informed decision[191] to assume the risk of engaging in inventory financing because of the possibility of profiting

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186. *See* Martin Marietta Corp. v. New Jersey Nat'l Bank, 612 F.2d 745, 749 (3d Cir. 1979); Holstein v. Greenwich Yacht Sales, Inc., 404 A.2d 842, 845 (R.I. 1979); Dolan, *supra* note 124, at 1154-57; Schimberg, *Secured Transactions*, 35 Bus. Law. 1165, 1175 (1980); *Possession or Title, supra* note 12, at 698-700.

187. 404 A.2d 842 (R.I. 1979).

188. *Id.* at 845. The court referred to possession, *id.*, but this concept implies receipt. *See supra* note 119 and accompanying text.

189. 404 A.2d at 845. The court based much of its reasoning on the article by Dolan, *supra* note 124. *See id.* at 845 n.7.

190. 404 A.2d at 845; *accord* Rome Bank & Trust Co. v. Bradshaw, 143 Ga. App. 152, 157, 237 S.E.2d 612, 615 (1977); Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 481, 392 N.E.2d 344, 347 (1979); Dugan, *supra* note 31, at 361-62; Skilton, *supra* note 25, at 3-4; *cf.* Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 178, 580 P.2d 8, 10 (1978) (in contest between retail and inventory financers, court allocated risk of loss to inventory financer); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 496, 211 S.E.2d 430, 435 (1974) (same); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968) (same).

191. Lenders usually have access to a great deal of financial data regarding the debtor's financial status, including financial statements, various asset ratios and credit agency reports. P. Smith, Economics of Financial Institutions and Markets 149-50 (1971); Gordon, *The Prepaying Buyer: Second Class Citizenship Under Uniform Commercial Code Article 2*, 63 Nw. U. L. Rev. 565, 577-78 (1968); Helman, *Ostensible Ownership and the Uniform Commercial Code*, 83 Com. L.J. 25, 30-32 (1978). In view of this readily available and comprehensive information, the argument that finding BIOC status when the goods are in the seller's possession might be misleading to lenders is unpersuasive. Gordon, *supra*, at 577; Helman, *supra*, at 25, 32. This concept, known as the doctrine of ostensible ownership, addresses the situation in which "a party, who [is] in possession of another's property, is held out as the owner of the property under such circumstances as would be reasonably calculated to induce creditors to extend credit to him on the faith of his apparent ownership." Helman, *supra*, at 25. The theory should not be used as a bar to finding BIOC status before buyer takes possession of the goods because it is clear that modern lenders do not rely on inventory in a seller's showroom in making credit decisions, but instead rely on the financial data discussed above. Gordon, *supra*, at 577; Helman, *supra*, at 32. *But see* Chrysler Corp. v. Adamatic, Inc., 59 Wis. 2d 219, 240, 208 N.W.2d 97, 107 (1973) (court found the ostensible ownership argument persuasive and therefore required possession by the buyer, at least as applied to the facts of that case).

from the associated paper purchases;[192] the buyer merely places himself on the market to buy goods, in the process of which he is exposed to the risk of buying encumbered goods.[193] Additionally, the lender is in a better position than the buyer to protect against the risk of loss.[194] He may monitor the seller's activities by, for example, requiring various financial reports and conducting physical audits of the inventory.[195] The mere fact that the security agreement contains restrictions on the seller's conduct regarding the collateral underlying the loan, however, does not mean that the seller is prohibited from selling the goods.[196] Accordingly, because information concerning possible restrictions is rarely, if ever, available to the buyer,[197] he cannot effectively protect himself against buying goods in violation of a security agreement.

Finally, the lender is in a better position to neutralize the effect of loss of the goods. When a buyer is found to be a BIOC and thus allowed possession of the goods, the secured lender will still be granted a recovery because floor-plan financing agreements usually provide that the lender will have access to the proceeds of sale.[198] Even when this is not possible,[199] as when the proceeds are dissipated before default,[200] the lender can build the cost of losses into the cost of credit by adjusting interest rates in accordance with the degree of risk per-

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192. *Possession or Title*, *supra* note 12, at 695 n.4. The profit made by the lender on chattel paper purchases greatly surpasses that made on inventory financing. 2 G. Gilmore, *supra* note 15, § 27.1, at 719; R. Speidel, *supra* note 12, at 218, 257; Biborosch, *Floor Plan Financing*, 77 Banking L.J. 725, 727 (1960); Levie, *supra* note 43, at 955-56. It has been referred to as the "pot of gold at the end of the . . . rainbow." Gilmore, *The Commercial Doctrine of Good Faith Purchase*, 63 Yale L.J. 1057, 1102 (1954).

193. *See supra* notes 92-95 and accompanying text.

194. Dugan, *supra* note 31, at 361.

195. International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 496, 211 S.E.2d 430, 435 (1974); Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 480-81, 392 N.E.2d 344, 347 (1979); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968); Biborosch, *supra* note 192, at 736-40; Dolan, *supra* note 124, at 1159; Jackson & Kronman, *Secured Financing and Priorities Among Creditors*, 88 Yale L.J. 1143, 1150 (1979); Levie, *supra* note 43, at 956 & n.38; *Possession or Title*, *supra* note 8, at 700.

196. *See supra* note 79 and accompanying text.

197. *See supra* notes 93-95 and accompanying text.

198. *See supra* note 15.

199. See International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492, 211 S.E.2d 430, 433 (1974); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 269-70, 288 N.Y.S.2d 525, 533-34 (Sup. Ct. 1968); Associates Discount Corp. v. Old Freeport Bank, 421 Pa. 609, 612, 220 A.2d 621, 623-24 (1966), in which inventory financers lost to retail financers their rights in chattel paper as proceeds under § 9-308(b).

200. *See* 2 G. Gilmore, *supra* note 15, § 27.1, at 720; Skilton, *supra* note 25, at 77.

ceived.[201] Moreover, the lender may decline to lend.[202] Buyers are not in such a position. If he is not held to be a BIOC, the buyer receives no recovery.[203] In the absence of recovery, not all buyers are able to pass on the loss.[204]

Although use of identification would lead to equitable results in the buyer-secured party conflict, it has been suggested that such an approach may be inappropriate[205] in view of the Code drafters' observation in an official comment that identification is of "limited effect."[206] This comment has been subject to controversy, however, because identification is a threshold event that is required for a number of valuable Code rights to arise.[207] For example, Article 2 provides that on identification, a buyer may obtain the right to goods on the seller's insolvency.[208] He may also pursue a replevin action[209] and sue third parties for injury to goods.[210] Furthermore, once goods have been identified, a seller may pursue an action for the price.[211] Article 2 also provides that on identification a creditor may, under limited circumstances, void sales made by his debtor-seller.[212] In addition,

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201. R. Posner, *supra* note 80, at 293-94; Jackson & Kronman, *supra* note 195, at 1148-51; *see* P. Smith, *supra* note 191, at 148-53; Dugan, *supra* note 31, at 361-62.

202. International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 496, 211 S.E.2d 430, 435 (1974); Herman v. First Farmers State Bank, 73 Ill. App. 3d 475, 480, 392 N.E.2d 344, 347 (1979); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 270, 288 N.Y.S.2d 525, 534 (Sup. Ct. 1968); *see* P. Smith, *supra* note 191, at 148-51; Jackson & Kronman, *supra* note 195, at 1149-51.

203. There are, however, other Code sections under which buyers who fail to qualify under § 9-307(1) might prevail, although they too have high hurdles. U.C.C. § 9-301(1)(c) (1977) (if security interest is unperfected, buyer prevails "to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected"); *id.* § 9-306(2) (if sale is authorized by secured party, buyer prevails); *see* E. Reiley, *supra* note 22, § 8.3, at 8-7 to -8.

204. This is at least the case with individual retail buyers. *See* Dugan, *supra* note 31, at 362. As for commercial buyers, who comprise the balance of the BIOC class, the cases routinely find BIOC status notwithstanding potential ability to spread the losses of buying encumbered goods. *E.g.*, Texas Nat'l Bank v. Aufderheide, 235 F. Supp. 599, 604 (E.D. Ark. 1964) (dealer of aircraft); Bitzer-Croft Motors, Inc. v. Pioneer Bank & Trust Co., 82 Ill. App. 3d 1, 12, 401 N.E.2d 1340, 1348 (1980) (same); Associates Discount Corp. v. Rattan Chevrolet, Inc., 462 S.W.2d 546, 549 (Tex. 1970) (wholesale dealer of automobiles).

205. T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981).

206. U.C.C. § 2-501 official comment 2 (1977) ("In view of the limited effect given to identification . . . , the general policy is to resolve all doubts in favor of identification.").

207. T. Quinn, *supra* note 3, ¶ 2-501[A][1]; Dolan, *supra* note 124, at 1154, 1157-58; Rivera, *supra* note 180, at 639.

208. U.C.C. § 2-502 (1977); Rivera, *supra* note 180, at 639.

209. U.C.C. § 2-716(3) (1977); Rivera, *supra* note 180, at 639.

210. U.C.C. § 2-722(a) (1977); T. Quinn, *supra* note 3, ¶ 2-501[A][1], at 2-268.

211. U.C.C. § 2-709(1)(b) (1977); T. Quinn, *supra* note 3, ¶ 2-501[A][1], at 2-268; Rivera, *supra* note 180, at 639.

212. Dolan, *supra* note 124, at 1158; *Possession or Title, supra* note 12, at 699-700; *see* U.C.C. § 2-402(2) (1977).

under Article 9, the security interest of a secured party attaches at the point when goods purchased by his debtor are identified to the contract.[213] Irrespective of the comment's assertion regarding "limited effect,"[214] therefore, determination of BIOC status as of identification is consistent with the Code scheme of recognizing important rights at that point in the transaction.

Moreover, because identification occurs at a relatively early point in the contract,[215] its use as a reference point for determining BIOC status gives maximum vitality to the Code policy of protecting buyers from hidden interests in goods.[216] It is arguable, however, that severing security interests at the point of identification may discourage inventory financing.[217] Because a lender's principal objective is to purchase its debtor-seller's chattel paper at attractive rates,[218] such a result seems unlikely. Furthermore, because a lender's ability to protect itself[219] and to recoup its losses[220] places it in an advantageous position, the equities favor the buyer.[221] Finally, finding BIOC status as of identification would further the general Code policy of expand-

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213. U.C.C. § 9-203 (1977). A security interest attaches upon the coalescence of an effective security agreement, value and debtor's rights in the goods. *See supra* note 3. Because identification will usually mark the time when the debtor first gains rights in the goods he purchases, it will also usually mark the time when the secured party's interest attaches. Dolan, *supra* note 124, at 1157-58; Rivera, *supra* note 180, at 639; *see In re* Pelletier, 5 U.C.C. Rep. Serv. (Callaghan) 327, 337 (Bankr. D. Me. (1968).

214. Although the official comments are persuasive and aid in the interpretation of the Code, they are not controlling. Thompson v. United States, 408 F.2d 1075, 1084 n.15 (8th Cir. 1969); First State Bank v. Clark, 91 N.M. 117, 119, 570 P.2d 1144, 1146 (1977).

215. T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-136 (Supp. 1981); Dolan, *supra* note 124, at 1157; *Possession or Title, supra* note 12, at 698 & n.25.

216. *See supra* note 92 and accompanying text.

217. *Possession or Title, supra* note 12, at 699-700; *see* Dolan, *supra* note 124, at 1157.

218. *See supra* note 192 and accompanying text.

219. *See supra* notes 194-95 and accompanying text.

220. *See supra* notes 198-201 and accompanying text.

221. The New York Court of Appeals, in Tanbro Fabrics Corp. v. Deering Milliken, Inc., 39 N.Y.2d 632, 350 N.E.2d 590, 385 N.Y.S.2d 260 (1976), determined that a buyer may prevail as a BIOC even when the secured party is in possession of the goods. *Id.* at 634-36, 350 N.E.2d at 591-92, 385 N.Y.S.2d at 261. One commentator, who advanced identification as the most appropriate reference point for determination of BIOC status, Dolan, *supra* note 124, at 1157-59, criticized the *Tanbro* decision, and argued that the identification rule should exclude those buyers whose sellers were not in possession of the goods at the time of the sale. *Id.* at 1186-92; *accord* Kriendler, *The Uniform Commercial Code and Priority Rights Between the Seller in Possession and a Good Faith Third-Party Purchaser*, 82 Com. L.J. 86, 89-90 (1977); Kripke, *Should Section 9-307(1) of the Uniform Commercial Code Apply Against a Secured Party in Possession?*, 33 Bus. Law. 153, 160 (1977). Other commentators, however, approve of the *Tanbro* holding. Birnbaum, *Section 9-307(1) of the Uniform Commercial Code Versus Possessory Security Interests—A Reply to*

ing commerce[222] by minimizing buyers' fears of buying encumbered goods.[223] Its use in the BIOC context thus "promote[s] the interests of buyers, . . . the interests of a commercial society. . . . [and] fosters sales,"[224] maintaining the delicate balance between buyers and secured parties intended by the Code drafters.[225]

III. ANOTHER CONTEXT: SECURED PARTY v. CHATTEL PAPER PURCHASER

The determination of when a buyer becomes a BIOC may affect the determination of whether a chattel paper purchaser will prevail over an inventory financer.[226] As in the modified hypothetical in the Introduction, when *S* is in need of cash, he will often sell the chattel paper to a third party, the chattel paper purchaser.[227] The chattel paper purchaser obtains a derivative security interest in the goods.[228] If *S* defaults on the loan agreement with *L*, and *B* is found to be a BIOC, *L's* security interest in the goods will be severed.[229] When the proceeds of the sale of the chattel paper have been dissipated by *S*,[230] *L* will claim the chattel paper itself as proceeds of the sale.[231] The battle is then between *L* and the chattel paper purchaser for the chattel paper.[232]

Professor Homer Kripke, 33 Bus. Law. 2607 (1977); Gottleib, *Section 9-307(1) and Tanbro Fabrics: A Further Response*, 33 Bus. Law. 2611 (1977). Espousing the better view, one commentator argued that to amend § 9-307(1) to exclude the secured party in possession from its reach "would not help but [would] hamper and frustrate normal business sales activities." *Id.* at 2615.

222. *See supra* note 61 and accompanying text.

223. *See* Dolan, *supra* note 124, at 1157; *Possession or Title*, *supra* note 12, at 698 & n.25; *cf.* Sebrite Corp. v. Transouth Fin. Corp., 272 S.C. 483, 487, 252 S.E.2d 873, 875 (1979) (requiring innocent purchaser or retail lender to investigate seller's ability to sell unencumbered goods would "stagnate retail sales so necessary to commerce").

224. Dolan, *supra* note 124, at 1157.

225. *See supra* notes 98-99 and accompanying text.

226. *See supra* note 41 and accompanying text.

227. *See supra* note 48 and accompanying text.

228. *See* U.C.C. § 9-105 official comment 3 (1977); Skilton, *supra* note 25, at 77-78.

229. U.C.C. § 9-307(1) (1977); *see* Wickes Corp. v. General Elec. Credit Corp., 363 So. 2d 56, 57 (Fla. Dist. Ct. App. 1978); International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492, 211 S.E.2d 430, 433 (1974); Associates Discount Corp. v. Old Freeport Bank, 421 Pa. 609, 612, 220 A.2d 621, 623 (1966).

230. *See supra* note 200 and accompanying text.

231. International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492, 211 S.E.2d 430, 433 (1974); Associates Discount Corp. v. Old Freeport Bank, 421 Pa. 609, 612, 220 A.2d 621, 623 (1966); 2 G. Gilmore, *supra* note 15, § 27.1, at 720; Levie, *supra* note 43, at 955-56; Skilton, *supra* note 25, at 77-78.

232. Rex Fin. Corp. v. Mobile Am. Corp., 119 Ariz. 176, 176, 580 P.2d 8, 8 (1978); 2 G. Gilmore, *supra* note 15, § 27.1, at 718; Skilton, *supra* note 25, at 76-77;

Section 9-308 of the Code provides that chattel paper purchasers who give value and take possession of the paper in the ordinary course of their business prevail over inventory lenders.[233] This preference for the chattel paper purchaser over the inventory financer[234] is designed to promote competition in consumer financing[235] and to prevent the inventory financer from monopolizing the acquisition of seller's chattel paper.[236] Therefore, under section 9-308, the chattel paper purchaser wins the chattel paper.

If *B* had failed to qualify as a BIOC, however, *L*'s original security interest in the goods would continue.[237] In that case, although the chattel paper purchaser would still prevail as to the chattel paper itself, his derivative interest in the goods would appear to be encumbered by *L*'s continuing interest.[238] Yet, sections 9-306(5)(b) and (d) provide that if the chattel paper purchaser takes the necessary steps to perfect his interest in the goods underlying the paper, his interest in the goods will be superior to that of the inventory lender.[239] Some courts have used these sections to allow chattel paper purchasers to repossess goods.[240] Commentators have also recognized this section as determinative of the priorities between these two secured parties.[241] One commentator, however, while recognizing that sections 9-306(5)(b) and (d) operate in conjunction with section 9-308,[242] has suggested that courts, in determining that the chattel paper purchaser prevailed over the inventory lender, were in fact relying on the buyer in ordinary course having first severed the inventory lender's interest in the goods.[243] In criticizing this result, the commentator pointed out that if the buyer had not qualified as a BIOC, the chattel paper purchaser might not have prevailed.[244]

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see T. Quinn, *supra* note 3, ¶ 9-307[A][8], at S9-134 to -135 (Supp. 1981); Levie, *supra* note 43, at 955-56.

233. U.C.C. § 9-308(b) (1977).

234. T. Quinn, *supra* note 3, ¶ 9-308[A][4].

235. Skilton, *supra* note 25, at 78 n.189.

236. *Id.; see* 2 G. Gilmore, *supra* note 15, § 27.1, at 719-20.

237. Skilton, *supra* note 25, at 78. This is unless the sale was otherwise authorized under § 9-306(2). U.C.C. § 9-306(2) (1977); Skilton, *supra* note 25, at 78.

238. Skilton, *supra* note 25, at 78.

239. U.C.C. § 9-306(5)(b), (d) (1977); 4 R. Anderson, *supra* note 29, § 9-306:22; W. Hawkland, *supra* note 15, at 731-32.

240. International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 492 & n.1, 211 S.E.2d 430, 433 & n.1 (1974); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 269, 288 N.Y.S.2d 525, 533 (Sup. Ct. 1968).

241. 4 R. Anderson, *supra* note 29, § 9-306:22; W. Hawkland, *supra* note 15, at 730-32; Skilton, *supra* note 25, at 83 & n.199.

242. Skilton, *supra* note 25, at 83 & n.199.

243. *Id.* at 77-78. In these cases, the buyer had qualified as a BIOC. International Harvester Credit Corp. v. Associates Fin. Servs. Co., 133 Ga. App. 488, 496, 211 S.E.2d 430, 435 (1974); Chrysler Credit Corp. v. Sharp, 56 Misc. 2d 261, 269, 288 N.Y.S.2d 525, 533 (Sup. Ct. 1968).

244. Skilton, *supra* note 25, at 79, 87.

In the event that this analysis is correct, the chattel paper purchaser's ability to prevail over the inventory lender will depend on the buyer's qualification as a BIOC. It is important, therefore, to find BIOC status at identification to the contract. As a relatively early point in the transaction,[245] it will allow the chattel paper purchaser to prevail more frequently, thereby serving the purpose underlying section 9-308.[246]

CONCLUSION

The fundamental purpose of the Code is to facilitate the proper functioning of the marketplace by promoting uniformity and certainty. Because the BIOC exception of Article 9 does not specify when a buyer may partake of its protection, the needed certainty is sorely lacking. Analysis of the points on the transactional continuum, the

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245. *See supra* note 215 and accompanying text.

246. *See supra* notes 233-36 and accompanying text. The question of when a buyer becomes a BIOC also arises in an entrustment situation. The Code provides that "[a]ny entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business." U.C.C. § 2-403(2) (1977). This provision takes effect when, for example, a person leaves a watch with a jeweler for repair, and the jeweler then sells it to a buyer. If the buyer qualifies as a BIOC, he takes the watch free and clear of the owner's interest. 1955 Report, *supra* note 4, at 458; T. Quinn, *supra* note 3, ¶ 2-403[A][3]. The purpose of § 2-403 is to "protect a person from a third-party interest in goods purchased from the general inventory of a merchant regardless of that merchant's actual authority to sell those goods." Mattek v. Malofsky, 42 Wis. 2d 16, 19, 165 N.W.2d 406, 408 (1969). It has been stated that passage of title is not necessary for a buyer to prevail under § 2-403. Jackson & Peters, *supra* note 124, at 952 & n.163. One commentator, however, has argued that the buyer must be in possession to qualify as a BIOC under § 2-403. Smith, *supra* note 124, at 61. In most instances, however, such a requirement is moot, because the buyer is already in possession of the goods by the time the owner learns of the sale. *See, e.g.*, Simson v. Moon, 137 Ga. App. 82, 83, 222 S.E.2d 873, 873 (1975), *appeal dismissed*, 236 Ga. 786, 225 S.E.2d 314 (1976); Rockwin Corp. v. Kincaid, 124 Ga. App. 570, 570, 184 S.E.2d 509, 510 (1971); Mattek v. Malofsky, 42 Wis. 2d 16, 19, 165 N.W.2d 406, 408 (1969). Furthermore, § 25 of the Uniform Sales Act, the predecessor of § 2-403, expressly required delivery. Uniform Sales Act § 25 (1906), 1 U.L.A. 390 (1950). It is arguable that the omission of such an express requirement in § 2-403 was intentional. *Cf.* 1955 Report, *supra* note 4, at 232 (discussing absence of delivery requirement in § 1-201(9) BIOC definition in § 9-307 context). A requirement that identification have occurred, however, is reasonable. Because the question of whether § 2-403 will allow a buyer to prevail usually arises in a present sale, the buyer will be in possession and identification will have taken place. *See supra* note 183 and accompanying text. In rare instances, however, identification will have taken place before the buyer is in possession, as when he contracts to buy a used car that the owner has entrusted to the seller. *See supra* note 184 and accompanying text. Allowing the buyer to prevail in such a case is justified by the policy of § 2-403(2) of giving strong protection to the innocent buyer, who relies on the seller's apparent authority in an entrustment situation. *See* Simson v. Moon, 137 Ga. App. 82, 85-86, 222 S.E.2d 873, 875 (1975), *appeal dismissed*, 236 Ga. 786, 225 S.E.2d 314 (1976).

Code scheme and the parties' equities indicates that identification of goods to the contract is the proper point at which BIOC status should arise. The selection of identification recognizes the buyer's Article 2 rights as well as the mercantile nature of the secured lender's interest. Lenders are in the favorable position of being able to protect themselves and to recoup their losses. In contrast, buyers stand to lose all that they bring to the transaction.

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