

Quest for Uncertainty: A Proposal for Flexible Resolution of Inherent Conflicts Between Article 2 and Article 9 of the Uniform Commercial Code*

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Anglo-American jurisprudence, because of its common law tradition, has focused on the variety of law-giving roles that courts play. In the process of adjudication, courts regularly perform a rulemaking as well as a dispute-resolution function.¹ Legislation is similarly bifocused. Some laws are intended to provide specific instructions about particular conduct, which is to be sanctioned in designated ways. But much legislation is more broadly rulemaking, intended instead to provide guideposts for reasoned decisionmaking by those entrusted with judicial administration.² Broadly drafted statutes are perhaps most familiar in the context of enabling legislation for administrative agencies. Commercial statutes, particularly commercial codes, may also be seen as enabling legislation, providing a presumptive framework for private or official rulemaking, rather than as binding rules that determine, by statutory fiat, the outcome of precisely specified confrontations.³

In the American history of the codification of commercial law, "uniform" statutes have been drafted in both styles. The Uniform Sales Act⁴ was an open-ended restatement of common law sales principles,

* A table of citations to the Uniform Commercial Code may be found at the end of this article. The Code will hereinafter be cited by section number only. References to Article 9 will be to the 1972 (rather than the 1962) Official Text, unless otherwise stated.

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1. See Eisenberg, *Private Ordering Through Negotiation: Dispute-Settlement and Rule-Making*, 89 HARV. L. REV. 637 (1976).

2. The universally uneasy relationship between legislation and judicial lawmaking is reviewed in a recent article focusing on the confrontation between the California Civil Code and the developing case law of comparative negligence. See England, *Li v. Yellow Cab Co.—A Belated and Inglorious Centennial of the California Civil Code*, 65 CALIF. L. REV. 4 (1977).

3. See Gilmore, *Commercial Law in the United States: Its Codification and Other Misadventures*, in ASPECTS OF COMPARATIVE COMMERCIAL LAW: SALES, CONSUMER CREDIT, AND SECURED TRANSACTIONS 449 (J. Ziegel & W. Foster eds. 1969).

4. The Uniform Sales Act, which was modeled on the British Sale of Goods Act, was approved and recommended for adoption by the National Conference of Commissioners

while the Uniform Negotiable Instruments Law⁵ contained detailed commands about the determination of negotiability and its consequences. Each model has its problems: predictably, the Sales Act was often ignored, while the Negotiable Instruments Law was often burdensome. The Uniform Commercial Code continues this pattern of eclecticism, putting together articles of markedly different styles and aspirations. For example, Article 5, on letters of credit, is hardly a codification at all,⁶ while Article 3, on commercial paper, continues the peremptory style of prior learning on negotiable instruments.⁷ Whether or not a Code so divided will survive is a question that only time will answer, although it is worth noting that Article 5 has already proven adaptable to an entirely new form of credit, known as a stand-by credit, while Article 3 must be revised to accommodate electronic innovation.

Inevitably, some factual patterns give rise to conflicts that eclecticism cannot dissipate. One transaction that recurrently crosses article lines is a contract for the sale of goods that can either become, or come into confrontation with, a security interest. Article 2, the sales article, consistent with its historical antecedents and responsive to its applicability to conspicuously diverse commercial interactions, leans heavily to statements of principle and presumptive guidelines. Its pattern is to define a few core concepts with core consequences, which are then located in a broader network of open-ended constructs with multifaceted implications.⁸ It is, in sum, a rulemaking statute in the common law tradition.

on Uniform State Laws in 1906. It was ultimately adopted in 36 states and the District of Columbia; most of these adoptions came in the 1910s and 1920s. The Act has now everywhere been superseded by the Uniform Commercial Code.

5. The Uniform Negotiable Instruments Law, familiarly known as the NIL, was modeled on the British Bills of Exchange Act, and was approved and recommended for adoption by the National Conference of Commissioners on Uniform State Laws in 1896. The NIL was the Commissioners' first important statute, and their most successful; it was adopted in every state, the last being Georgia in 1924. The NIL has now everywhere been superseded by the Uniform Commercial Code. Even in Louisiana, which has resisted enactment of the Code in its entirety, enactment of Articles 1, 3, 4, and 5 has displaced the NIL. See 4 LA. REV. STAT. ANN. §§ 10:1-101 to 1-209, 3-101 to 5-117 (West Supp. 1977).

6. The scope section of Article 5, § 5-102, is extraordinarily gingerly in defining its authority. Subsection (3) provides:

This Article deals with some but not all of the rules and concepts of letters of credit as such rules or concepts have developed prior to this act or may hereafter develop. The fact that this Article states a rule does not by itself require, imply or negate application of the same or a converse rule to a situation not provided for or to a person not specified by this Article.

7. The sections of Article 3, in contrast with those of Article 2, only rarely contain the prefatory words "unless otherwise agreed." The basic scope section, § 3-104, provides in subsection (1) that "[a]ny writing to be a negotiable instrument within this Article *must* [meet specified requirements of form]." (Emphasis added).

8. For example, the pattern of remedies available to parties aggrieved by breach of a sales contract is set by the assumption that most sales contracts are negotiated and performed (or not performed) against the background of a functioning marketplace for the

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Article 9, the secured transactions article, consistent with its historical antecedents and responsive to the unitary but absolute requirement that security interests survive attack in bankruptcy, leans heavily to positivist prescription of rules that dictate outcomes. Its primary function is to assure secured creditors that they can defeat lien creditors, since the rights of lien creditors furnish the basic test that determines the upset powers of the trustee in bankruptcy⁹ (and of the assessor of federal tax liens, another formidable foe¹⁰). Pre-Code litigation taught incontrovertibly that protection in bankruptcy could not be assured through indeterminate solutions.¹¹ The pattern for Article 9 was thus set by the inexorable demand to deal dispositively with lien creditors. This pattern not only shaped the provisions of Article 9 on perfection, which determine the rights of lien creditors, but also affected with equal rigor the form of provisions on priority among other competing claimants to collateral. Thus the difference in orientation between Articles 2 and 9 is pervasive. There is some attempt at accommodation in the principal bridging section, section 9-113,¹² but that section, while acknowledging the likelihood that commercial transactions will encounter inconsistent regulation under the two articles, offers guidance that is too skeletal and imprecise to resolve the varieties of conflict that regularly arise. Nowhere else is there a systematic effort to mesh the two articles or to cope with their differing orientations and styles.

The most rudimentary commercial contract readily illustrates that

contract goods and goods like them. See Peters, *Remedies for Breach of Contracts Relating to the Sale of Goods Under the Uniform Commercial Code: A Roadmap for Article Two*, 73 YALE L.J. 199, 253-68 (1963). When Article 2 has tried to draw a hard line, as between disclaimers and clauses limiting liability for default, it has been notoriously unsuccessful. See, e.g., *Dessert Seed Co. v. Drew Farmers Supply, Inc.*, 248 Ark. 858, 454 S.W.2d 307 (1970); *Adams v. J.I. Case Co.*, 125 Ill. App. 2d 388, 261 N.E.2d 1 (1970).

9. Section 9-301(3) of the Code includes in its definition of a "lien creditor" "a trustee in bankruptcy from the date of the filing of the petition." The Bankruptcy Act, in turn, gives the trustee in bankruptcy upset powers measured by the rights of a creditor who, on the date of bankruptcy, had obtained a lien by legal or equitable proceedings. Bankruptcy Act § 70(c), 11 U.S.C. § 110(c) (1970). The Bankruptcy Act tests transactions as preferential, when they involve property other than real property, by asking whether a subsequent lien obtained by legal or equitable proceedings could have become "superior." *Id.* § 60(a), 11 U.S.C. § 96(a) (1970).

10. The Federal Tax Lien Act of 1966 defines a valid security interest as one that "has become protected under local law against a subsequent judgment lien arising out of an unsecured obligation." I.R.C. § 6323(h)(1).

11. The case of *First Nat'l Bank v. O'Keefe (In re New Haven Clock & Watch Co.)*, 253 F.2d 577 (2d Cir. 1958), is an especially horrendous example. Despite meticulous procedures designed to conform to accepted practices and local law, the secured creditor was required to defend his financing arrangement, an assignment of accounts receivable, before a bankruptcy referee, a federal district court, and a court of appeals. The secured creditor ultimately prevailed, but at considerable expense in litigation.

12. The language and the significance of § 9-113 will be explored in detail below. Other sections of the Code that relate Articles 2 and 9 include §§ 2-401 and 2-403.

interactions between Articles 2 and 9 need be neither complex nor esoteric. Consider a simple contract for the sale of chattels. ABC Manufacturing Corporation agrees with Family Furniture Mart, Inc., to manufacture and deliver in a single shipment 500 adequately described living room sofas.¹³ It is likely that ABC's manufacturing process will, at some point, generate output capable of being earmarked as that destined for Family Furniture.¹⁴ Any number of commercial parties involved with Family Furniture may then assert an interest in the sofas. Family Furniture may previously have contracted with a secured creditor who took, for value, an effective and perfected Article 9 security interest in Family Furniture's present and future inventory.¹⁵ Family Furniture will expect to make sales of furniture to its customers, who may buy for cash, on time, or with funds obtained through independent secured financing.¹⁶ Family Furniture is also likely to have trade creditors on the lookout for new assets to subject to judicial liens.¹⁷ On the other side, ABC Manufacturing is apt to have commercial relationships with buyers other than Family Furniture. The Uniform Commercial Code assumes in Article 2 that sellers like ABC have ready access to a resale market.¹⁸ ABC may sell the sofas on that market despite its contract with Family Furniture,¹⁹ or as a way of working out disputes that arise out of their contract.²⁰ Thus even under the most ordinary circumstances, virtually any sales contract may gen-

13. It will be assumed that the ABC-Family Furniture contract meets the Statute of Frauds requirements of § 2-201.

14. Section 2-501(1) provides that the buyer obtains "a special property and an insurable interest in goods" when they become identified to the contract. For goods not in existence when the contract is made, identification occurs, unless otherwise explicitly agreed, "when goods are shipped, marked or otherwise designated by the seller as goods to which the contract refers." Section 2-501(1)(b).

15. Article 9 permits security agreements that encompass after-acquired as well as present collateral. See §§ 9-203, 9-204.

16. Article 9 repeals the rule of *Benedict v. Ratner*, 268 U.S. 353 (1925), under which the validity of a security agreement turned on the debtor's accountability for secured collateral. See § 9-205; *id.*, Comment 1. In inventory financing, the expected commercial pattern is the sale of the secured collateral, with the security interest then shifting to the proceeds of the sale. See § 9-306.

17. Whenever a debtor acquires rights in collateral, creditors may bargain for a voluntary transfer or insist on an involuntary transfer. See § 9-311.

18. The seller is entitled to recover the price from a defaulting buyer only where the goods have been accepted or damaged after the risk of loss has passed to the buyer. Ordinarily, the seller is expected to resell. See § 2-709(2).

19. A seller who, like ABC, is a merchant, see § 2-104(1), can resell goods in his possession so as to pass good title to a buyer in the ordinary course of business, despite a pre-existing contract of sale. See § 2-403(2).

20. One of the remedies available to the seller on the buyer's default is resale. See §§ 2-703(d), 2-706.

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erate a significant array of competing claims; the claimants described above in no way exhaust the possibilities.²¹

The law that governs competing interests in the ABC-Family Furniture contract is the law of Articles 2 and 9 of the Uniform Commercial Code. ABC is an Article 2 seller,²² probably an Article 2 merchant,²³ and possibly, as section 9-113 provides, a person with “[a] security interest arising solely under the Article on Sales” that is nonetheless “subject to the provisions of [Article 9].”²⁴ Family Furniture is an Article 2 buyer,²⁵ and may be an Article 9 debtor,²⁶ as well as an Article 9 seller and a transferor of chattel paper. As one might expect, these various roles carry different implications about rights in the sofas, which are goods under Article 2²⁷ and collateral under Article 9.²⁸ Necessarily, rules about rights in the “property” transferred by the

21. ABC may have unpaid creditors, who may levy on goods in ABC's possession despite the existence of a contract for their sale. *See* § 2-402. Consignment arrangements, *see* §§ 2-326, 2-327, 9-114, may occasion further complexities.

22. Section 2-103(1)(d) provides:

“Seller” means a person who sells or contracts to sell goods.

23. Section 2-104(1) provides:

“Merchant” means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.

24. Section 9-113 provides:

Security Interests Arising Under Article on Sales

A security interest arising solely under the Article on Sales (Article 2) is subject to the provisions of this Article except that to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods

(a) no security agreement is necessary to make the security interest enforceable; and

(b) no filing is required to perfect the security interest; and

(c) the rights of the secured party on default by the debtor are governed by the Article on Sales (Article 2).

25. Section 2-103(1)(a) provides:

“Buyer” means a person who buys or contracts to buy goods.

26. Section 9-105(1)(d) provides:

“Debtor” means the person who owes payment or other performance of the obligation secured, whether or not he owns or has rights in the collateral, and includes the seller of accounts or chattel paper. Where the debtor and the owner of the collateral are not the same person, the term “debtor” means the owner of the collateral in any provision of the Article dealing with the collateral, the obligor in any provision dealing with the obligation, and may include both where the context so requires

27. Section 2-105(1) provides:

“Goods” means all things (including specially manufactured goods) which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities (Article 8) and things in action. “Goods” also includes the unborn young of animals and growing crops and other identified things attached to realty as described in the section on goods to be severed from realty (Section 2-107).

28. Section 9-105(1)(c) provides:

“Collateral” means the property subject to a security interest, and includes accounts and chattel paper which have been sold

sales contract impinge also on claims for monetary damages between ABC and Family Furniture, but monetary claims will not be central to our discussion here.²⁹

Despite their conspicuous differences, Articles 2 and 9 share one important principle. Both articles explicitly renounce reliance on the metaphysics of "title"³⁰ and look instead to factual signposts as empirical guides to commercial relationships.³¹ For both articles, physical location of contract goods is a significant indicator of statutory rights, particularly when third-party interests are at stake.³² It therefore seems

29. Monetary claims are likely to present difficulties of their own arising out of conflicting instructions under Article 2 and Article 9. For example, consider the problem that arises if a buyer disputes the amount of his monetary obligation on the ground that some part of the seller's performance under the contract has been nonconforming. Such a buyer, upon giving adequate notice, is entitled to elect to keep defective goods, *see* § 2-607(3), and to pursue a claim for damages measured by §§ 2-714 and 2-715.

Under Article 2, the buyer may enforce his claim for damages by withholding payment from the seller. Section 2-717 provides:

The buyer on notifying the seller of his intention to do so may deduct all or any part of the damages resulting from any breach of the contract from any part of the price still due under the same contract.

This section means that failure by the buyer to pay in full, while the amount of the offset for damages is in dispute, is not a breach by the buyer, and does not privilege countermeasures by the disappointed seller. The section codifies the common law position of cases like *Lander v. Samuel Heller Leather Co.*, 314 Mass. 592, 50 N.E.2d 962 (1943). Possibly excessive withholding by the buyer might trigger a seller's right to request adequate assurance of performance under § 2-609, but that section would, at most, permit suspension of further performance by the seller.

By contrast, Article 9 allows a seller who is a secured party to invoke draconian measures, such as repossession of collateral, whenever the debtor (the buyer) is in default. *See* § 9-503. Article 9 does not in terms define default. Consistent reading of §§ 9-501, 9-502, and 9-503 suggests strongly that default is determined by the terms of the security agreement. *See* 2 G. GILMORE, *SECURITY INTERESTS IN PERSONAL PROPERTY* 1190-95 (1965). It is standard learning that security agreements unconditionally make nonpayment of any installment when due an event of default, regardless of the bona fides of the buyer's reasons for nonpayment. *See* R. HENSON, *SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE* 235-36 (1973). Article 9 may, therefore, make it impossible for a buyer who has signed a security agreement to exercise rights given to him by Article 2, even though Article 9, in § 9-206(2), expressly preserves the substantive claims on which the buyer's rights are most apt to be premised.

There has been remarkably little litigation to test resolution of this conflict between Articles 2 and 9. The issue was in fact raised in *Fuentes v. Shevin*, 407 U.S. 67, 87 n.17 (1972); *id.* at 99-103 (White, J., dissenting), but was not reached, since the Court found fatal defects in the process by which repossession had been accomplished. *Lindsey v. Normet*, 405 U.S. 56 (1972), decided during the same term of the Court, and cited in the *Fuentes* case, allowed a limited hearing on limited issues (had the tenant defaulted on the rent?) to pass constitutional muster. Whatever may be the magnitude of the constitutional due process requirement for a hearing before definitive dispossession, the common law question of the underlying contract rights is yet to be seriously examined.

30. *See* §§ 2-401, 9-202.

31. For a discussion of some of these empirical guides under Article 2, *see* Peters, *supra* note 8. Article 9 rules vary (as under § 9-103) with types of collateral, rather than with the form in which a security agreement is cast. *See* § 9-102(2).

32. *See, e.g.*, the rules on risk of loss in Article 2, §§ 2-509 and 2-510, and on the role of possession in perfection in Article 9, §§ 9-205, 9-301(2), and 9-305.

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useful to analyze the ABC-Family Furniture contract in each of the following circumstances:

- (1) ABC never delivers the contract goods to Family Furniture;
- (2) ABC unconditionally delivers the contract goods to Family Furniture;
- (3) ABC delivers the contract goods on special condition to Family Furniture; and
- (4) ABC regains possession of the contract goods from Family Furniture.

In each case it will be assumed that ABC has chosen not to enter into an Article 9 secured transaction of normal configuration in its dealings with Family Furniture.³³ We propose to explore the costs and risks of that choice, to determine the urgency with which all unpaid sellers ought to contemplate conversion into secured lenders. (We do not mean to suggest, of course, that secured lending is any kind of panacea; its trade-offs are well recognized, and dissimilar.³⁴) In order to do so, we will use the following frame of reference, suggested by the customary law of secured lending, to test the rights of an unpaid seller at each of the four stages of the sales transaction:

- (1) the validity of the unpaid seller's proprietary claim against anyone;
- (2) the perfection of the unpaid seller's claim against lien creditors;
- (3) the enforceability of the unpaid seller's interest against the sold goods because of the buyer's default;
- (4) the priority of the unpaid seller's rights against other takers from the buyer.

This framework emphasizes Article 9's great strength: its recognition that different kinds of competing claims should be adjudicated by different standards, that security interests need not rise or fall as unitary entities. We propose to investigate the claims of the unpaid seller as a medium for infusing the flexibility of Article 2 into the categorical rulemaking of Article 9.

33. It is clear that a seller of goods has the capacity to reserve or acquire a security interest under §§ 1-201(37) and 9-102.

34. The perfected secured creditor faces a variety of competitors for priority under §§ 9-307 to 9-316. His rights on default are limited by the provisions of Part 5 of Article 9. But on perfection he has rights superior to those of a subsequent lien creditor, including a trustee in bankruptcy. See § 9-301. See generally G. GILMORE, *supra* note 29.

I. The Validity of the Unpaid Seller's Proprietary Claim to Sold Goods

The unpaid seller was entitled at common law and under the Sales Act to a possessory lien on sold goods. As Williston put it:

The ground upon which an unpaid seller is allowed a lien and kindred remedies is the inherent injustice of depriving him of goods with which he has not finally parted where it is evident that he has not been or will not be paid the price for them when it is due.³⁵

The seller's common law lien attached automatically when the seller became unpaid and terminated automatically when the seller delivered the contract goods to the buyer or the buyer's agent. At common law, then, ABC would have had a seller's lien before delivery to Family Furniture and would have become an unsecured creditor without a lien thereafter.³⁶

A. *ABC in Possession Before Delivery*

The Uniform Commercial Code has no specific counterpart to the provisions of the Sales Act on seller's liens. Article 2 characteristically eschews the language of "lien" and instead includes, in section 2-703's laundry list of seller's remedies upon buyer's breach, the rights of an "aggrieved" seller to "withhold delivery" and to "cancel."³⁷ ABC's rights are not appreciably affected by this change in nomenclature. Clearly, ABC can "withhold delivery" only of goods within its control. The seller's rights over goods appropriately "withheld," which we will

35. 3 S. WILLISTON, *THE LAW GOVERNING SALES OF GOODS AT COMMON LAW AND UNDER THE UNIFORM SALES ACT* 99 (rev. ed. 1948).

36. The Uniform Sales Act, in §§ 52-56 and §§ 61-62, codified the common law without substantial change.

37. Section 2-703 provides:

Seller's Remedies in General

Where the buyer wrongfully rejects or revokes acceptance of goods or fails to make a payment due on or before delivery or repudiates with respect to a part or the whole, then with respect to any goods directly affected and, if the breach is of the whole contract (Section 2-612), then also with respect to the whole undelivered balance, the aggrieved seller may

- (a) withhold delivery of such goods;
- (b) stop delivery by any bailee as hereafter provided (Section 2-705);
- (c) proceed under the next section respecting goods still unidentified to the contract;
- (d) resell and recover damages as hereafter provided (Section 2-706);
- (e) recover damages for non-acceptance (Section 2-708) or in a proper case the price (Section 2-709);
- (f) cancel.

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explore below in the section on enforceability,³⁸ are very much like those that inhere in a seller's common law lien. Similar constraints in fact limit the right to "cancel," which appears at first glance to promise a substantial expansion of ABC's pre-Code position. Although the text of section 2-703 does not expressly require that the seller be in possession of the goods in order to assert his right to cancel, other sections in Article 2 imply such limitations.³⁹ The section governing replevin of sold goods affords rights to an aggrieved buyer rather than to an aggrieved seller;⁴⁰ there is no general authority anywhere in Article 2 for the unpaid seller to retake goods from the buyer after delivery.⁴¹ Two exceptional cases, the cash sale⁴² and the sale induced by mis-

38. See pp. 942-47 *infra*.

39. See Peters, *supra* note 8, at 216-22 (describing implications of seller's right to cancel). The term "cancellation" is defined in § 2-106(4):

"Cancellation" occurs when either party puts an end to the contract for breach by the other and its effect is the same as that of "termination" except that the cancelling party also retains any remedy for breach of the whole contract or any unperformed balance.

The general remedial implications, or nonimplications, of cancellation are further spelled out in § 2-720:

Effect of "Cancellation" or "Rescission" on Claims for Antecedent Breach

Unless the contrary intention clearly appears, expressions of "cancellation" or "rescission" of the contract or the like shall not be construed as a renunciation or discharge of any claim in damages for an antecedent breach.

40. The relevant section, § 2-716, is headed "*Buyer's Right to Specific Performance or Replevin*." (Emphasis added.) Although headings are often not formally enacted, they are nonetheless suggestive. Furthermore, § 2-716 is one of the sections referred to in § 2-711, which lists the buyer's remedies in general. The text of § 2-716 provides:

Buyer's Right to Specific Performance or Replevin

(1) Specific performance may be decreed where the goods are unique or in other proper circumstances.

(2) The decree for specific performance may include such terms and conditions as to payment of the price, damages, or other relief as the court may deem just.

(3) The buyer has a right of replevin for goods identified to the contract if after reasonable effort he is unable to effect cover for such goods or the circumstances reasonably indicate that such effort will be unavailing or if the goods have been shipped under reservation and satisfaction of the security interest in them has been made or tendered.

41. The section that lists the seller's remedies in general, § 2-703, contains no mention of a right of replevin. It does not even refer to the special cases of reclamation, §§ 2-507 and 2-702. It is possible, however, to argue that a general right of replevin is saved by § 1-103, which provides:

Supplementary General Principles of Law Applicable

Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions. The difficulty with this argument is that neither the common law in general nor the law merchant in particular gave the unpaid seller a continuing lien on goods in his buyer's possession. *E.g.*, *Southern Lumber Co. v. Colvin*, 104 Ark. 130, 148 S.W. 496 (1912); see R. NORDSTROM, *HANDBOOK OF THE LAW OF SALES* 498-500 (1970).

42. The cash sale transaction is discussed in detail below. See pp. 922-30 *infra*. The text of § 2-507(2) strongly implies a right to reclaim:

Where payment is due and demanded on the delivery to the buyer of goods or docu-

representation of solvency,⁴³ do give rise to special rights to retake. But their exceptional nature and the stringent conditions by which they are hedged underline the absence of a general nonpossessory lien.

Article 9, surprisingly, more closely approximates the linguistic structure of the Uniform Sales Act than that of Article 2. The proprietary rights of the unpaid seller are primarily codified, under Article 9, in section 9-113. That section, added long after the basic drafting of Article 9 had been completed, bridges Article 2 and Article 9 by positing the existence of a "security interest arising solely under the Article on Sales."⁴⁴ The absence in the article on sales of a clearly demarcated class of Article 2 security interests either went unnoticed or was thought irrelevant. Undaunted by the ambiguity of their referent, the drafters of Article 9 determined that, whatever "arising solely" might encompass, the resultant interest was a security interest under Article 9. The consequent applicability of the rules and requirements of Article 9 might, however, be suspended "to the extent that and so long as the buyer does not have or does not lawfully obtain possession of the goods." Suspension, under section 9-113, affects questions of validity, perfection, and enforcement; significantly, it does not affect questions of priority. Nor, of course, does that suspension significantly undermine the basic determination of section 9-113 to look to Article 9 rather than to Article 2 as the first source of learning on borderline transactions.

Whatever the scope of "security interest arising solely under the Article on Sales" might be, undoubtedly the common law seller's lien

ments of title, his right as against the seller *to retain or dispose of them* is conditional upon his making the payment due.

(Emphasis added.)

43. The sale on credit induced by misrepresentation of solvency is discussed in detail below. See pp. 922-30 *infra*. Section 2-702(2) expressly provides a right to reclaim:

Where the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days after the receipt, but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply. Except as provided in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.

44. Section 9-113 provides:

Security Interests Arising Under Article on Sales

A security interest arising solely under the Article on Sales (Article 2) is subject to the provisions of this Article except that to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods

- (a) no security agreement is necessary to make the security interest enforceable; and
- (b) no filing is required to perfect the security interest; and
- (c) the rights of the secured party on default by the debtor are governed by the Article on Sales (Article 2).

Section 9-113 first appeared in the 1957 Official Text of the Code.

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must be the paradigmatic security interest so arising. What other commercial interest more closely resembles a security interest and yet describes special claims of a seller that obtain “to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods”? If the unpaid seller continues in possession of sold goods, it is logical to validate his claim to the goods regardless of how his interest is characterized. Where Article 2 permits continued “withholding” of goods from a repudiating or defaulting buyer, it would be wrongheaded to devalue the seller’s rights merely because of a reflexive characterization of his interest as an Article 9 security interest. Section 9-113 obviates this danger by expressly waiving the Article 9 requirement of a written security agreement for a seller in possession.⁴⁵ This waiver, while clarifying and sensible, is in fact superfluous. Even under Article 9, the requirement of a written security agreement is waived whenever the secured party is in possession of the collateral.⁴⁶ As a pledgee, ABC needs no further Article 9 credentials to have a valid security interest.

It is fortunate that, terminology apart, both Article 2 and Article 9 continue the validity of the seller’s possessory lien, since Article 2, at least, also continues the common law implications of this lien for subsequent takers from the seller. If ABC resells the sofas, either out of spite or because it is aggrieved by Family Furniture’s misconduct, buyers in the ordinary course of business from ABC get good title under section 2-403.⁴⁷ Although it might be possible to treat differently the claims of ABC and those of ABC’s customers, consistent resolution is obviously preferable.

B. *ABC Delivers Goods Unconditionally*

If the seller’s possessory lien is the paradigmatic interest validated by section 9-113, the seller’s putative claim after unconditional delivery to

45. Section 9-113(a).

46. Section 9-203(1)(a).

47. The relevant provisions of § 2-403 apply if ABC is a merchant, as defined in § 2-104(1), and if the buyer is a buyer in the ordinary course of business, as defined in § 1-201(9). Section 2-403 then provides, in the relevant subsections:

(2) Any 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.

(3) “Entrusting” includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor’s disposition of the goods have been such as to be larcenous under the criminal law.

Under these provisions, the issue is the possessory seller’s power to resell, rather than the seller’s actual or implied authority to do so.

the buyer is the interest that is with equal rigor invalidated. Even assuming that the seller could conjure up a security interest arising under Article 2, the ameliorative provisions of section 9-113 apply only "so long as the debtor does not have or does not lawfully obtain possession of the goods"; after unconditional delivery, ABC hasn't a leg to stand on.⁴⁸ Validity under Article 9, apart from the possessory shelter of Article 2, requires a written security agreement⁴⁹ evidencing a kind of agreement that will not remotely have crossed the minds of either ABC or Family Furniture in the context of an open-credit sale. Even if a written contract of sale could be distorted into compliance with Article 9, an unlikely eventuality,⁵⁰ further problems of perfection, enforcement, and priority would confirm the common law position that surrender of goods usually signals the end of the seller's proprietary claim.

Some way stations were developed at common law that, under certain circumstances, allowed delivery to be conditional and thus reversible. One of these was the conditional sale, a sale on credit coupled with the stipulation that title was reserved in the seller until the contract price was fully paid.⁵¹ In most states, the condition reserving title was effective not only against the buyer himself, but also against purchasers from, and creditors of, the buyer. During the first half of this century, this special protection of the conditional seller was gradually eroded, and recording of the conditional sales contract came to be required, at least to defeat innocent third-party claimants.⁵²

48. Of course ABC might negotiate for an ordinary Article 9 security interest to preserve its claims after delivery; it is assumed throughout that this option has not been exercised.

49. Section 9-203.

50. Under § 9-203, a nonpossessory security interest requires a written security agreement, signed by the debtor, that describes the collateral. A contract of sale might well furnish an adequate description, and memorialize an agreement, but it would probably not be a security agreement. That term is defined in § 9-105(1)(l) as "an agreement which creates or provides for a security interest." See, e.g., *In re Shelton*, 472 F.2d 1118 (8th Cir. 1973); *In re Mitchell*, 458 F.2d 700 (10th Cir. 1972). Parol evidence might suggest that a security agreement was intended, see, e.g., *Peterson v. Ziegler*, 39 Ill. App. 3d 379, 350 N.E.2d 356 (1976), but intent to provide security is not lightly to be implied. See, e.g., *Tate v. Gallagher*, 116 N.H. 165, 355 A.2d 417 (1976).

51. See 1 G. GILMORE, *supra* note 29, at 68-85; 2 S. WILLISTON, *supra* note 35, at 265-309.

52. See 1 G. GILMORE, *supra* note 29, at 68. A uniform statute on conditional sales, the Uniform Conditional Sales Act, was approved and recommended for adoption by the National Conference of Commissioners on Uniform State Laws in 1918. It was adopted in only 12 jurisdictions and is now superseded by the Code. Section 5 of the Act provided:

Conditional sales void as to certain persons. Every provision in a conditional sale reserving property in the seller, shall be void as to any purchaser from or creditor of the buyer, who, without notice of such provision, purchases the goods or acquires by attachment or levy a lien upon them, before the contract or a copy thereof shall be filed as hereinafter provided, unless such contract or copy is so filed within ten days after the making of the conditional sale.

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Today the seller of goods who seeks protection by dint of a contract reserving title is not in a substantially different position than any other seller upon delivery to the buyer. In Article 2, the seller encounters the drafters' general aversion to rights turning on claims of title. Section 2-401, which opens with a preamble disassociating "the rights, obligations and remedies of the seller, the buyer, purchasers or other third parties" from title, relegates the conditional seller to the inhospitable turf of Article 9. "Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest."⁵³ This limitation endows the buyer, upon delivery, with the status of a secured debtor under Article 9 and allows the debtor and takers under the debtor to impose all of the customary Article 9 constraints upon secured sellers.⁵⁴ Whether a seller reserving a security interest arising under Article 2 or a "regular"

UNIFORM CONDITIONAL SALES ACT § 5. Many states that did not adopt the Uniform Conditional Sales Act enacted local laws of similar import. See 3 S. WILLISTON, *supra* note 35, at 743-55.

53. The relevant parts of § 2-401 provide:

Each provision of this Article with regard to the rights, obligations and remedies of the seller, the buyer, purchasers or other third parties applies irrespective of title to the goods except where the provision refers to such title. Insofar as situations are not covered by the other provisions of this Article and matters concerning title become material the following rules apply:

(1) Title to goods cannot pass under a contract for sale prior to their identification to the contract (Section 2-501), and unless otherwise explicitly agreed the buyer acquires by their identification a special property as limited by this Act. Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest. Subject to these provisions and to the provisions of the Article on Secured Transactions (Article 9), title to goods passes from the seller to the buyer in any manner and on any conditions explicitly agreed on by the parties.

54. The definition of "security interest" in § 1-201(37) expressly incorporates the provisions of § 2-401. The subsection states:

"Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (Section 2-401) is limited in effect to a reservation of a "security interest". The term also includes any interest of a buyer of accounts or chattel paper which is subject to Article 9. The special property interest of a buyer of goods on identification of such goods to a contract for sale under Section 2-401 is not a "security interest", but a buyer may also acquire a "security interest" by complying with Article 9. Unless a lease or consignment is intended as security, reservation of title thereunder is not a "security interest" but a consignment is in any event subject to the provisions on consignment sales (Section 2-326). Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

Article 9 incorporates this definition into its scope section, § 9-102. Subsection (2) of § 9-102 contains an illustrative list of security interests created by contract; that list includes "conditional sale."

secured party under Article 9 denied special shelter under Article 2, ABC cannot avoid the majority of Article 9 problems. True, the reservation of title, if in writing and signed by the buyer, is likely to have enough descriptive content to qualify as a security agreement.⁵⁵ However, the buyer's possession under a conditional sale requires perfection by filing of ABC's security interest and implicates the Article 9 default rules, to be discussed below, in exactly the same way as any unconditional delivery.⁵⁶

On occasion sellers may temporize by initiating a process of delivery that postpones the total relinquishment of possession to the buyer. The seller who receives derogatory information about his buyer's creditworthiness may stop delivery of goods in transit and thereby regain his possessory stance.⁵⁷ The seller who ships goods "under reservation,"

55. Section 9-203.

56. The array of instructions from § 1-201(37) to § 2-401 to § 9-102 probably means that the interest of a conditional seller is not a security interest arising "solely" under the Article on Sales, as § 9-113 requires. An Article 9 security interest of the ordinary kind must be perfected by filing a financing statement, *see* §§ 9-401 to 9-408, and enforced by protective default rules, *see* §§ 9-501 to 9-507. In the case of a security interest that does arise "solely" under Article 2, the ordinary Article 9 rules are suspended "to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods." Section 9-113. This suspension would surely not apply, even if a conditional sale contract were to qualify under § 9-113, once goods were delivered to the buyer. A buyer's possession subject to a seller's "retention or reservation . . . of . . . title," § 2-401, is authorized and lawful possession. The rules of perfection and default are therefore the same whether the conditional seller comes into Article 9 via § 9-102 or via § 9-113.

57. Section 2-705 provides:

Seller's Stoppage of Delivery in Transit or Otherwise

(1) The seller may stop delivery of goods in the possession of a carrier or other bailee when he discovers the buyer to be insolvent (Section 2-702) and may stop delivery of carload, truckload, planeload or larger shipments of express or freight when the buyer repudiates or fails to make a payment due before delivery or if for any other reason the seller has a right to withhold or reclaim the goods.

(2) As against such buyer the seller may stop delivery until

- (a) receipt of the goods by the buyer; or
- (b) acknowledgment to the buyer by any bailee of the goods except a carrier that the bailee holds the goods for the buyer; or
- (c) such acknowledgment to the buyer by a carrier by reshipment or as warehouseman; or
- (d) negotiation to the buyer of any negotiable document of title covering the goods.

(3) (a) To stop delivery the seller must so notify as to enable the bailee by reasonable diligence to prevent delivery of the goods.

(b) After such notification the bailee must hold and deliver the goods according to the directions of the seller but the seller is liable to the bailee for any ensuing charges or damages.

(c) If a negotiable document of title has been issued for goods the bailee is not obliged to obey a notification to stop until surrender of the document.

(d) A carrier who has issued a non-negotiable bill of lading is not obliged to obey a notification to stop received from a person other than the consignor.

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typically by procuring a negotiable bill of lading to his own order covering the contract goods, in effect retains control over the goods until the document is tendered and accepted.⁵⁸ Such a seller has, while he holds the document, another form of security interest “arising solely under the Article on Sales.”⁵⁹ If the buyer never obtains possession in either of these cases, the seller’s position should be the same as if the seller had remained totally in possession *ab initio*.

These seller’s options are essentially variations on the theme of delivery and possession. Until there is delivery, the seller can retain possession with minimal interference, regardless of how his interest is characterized; a seller who is especially risk averse, and who has the market power to do so, can refuse any delivery until full payment of the contract price. Delivery dramatically increases the seller’s vulnerability to competing claims by subjecting him to the Article 9 rules on secured creditors, which provide little comfort for ordinary sellers. The question remains whether there are any circumstances in which the buyer’s possession is so limited, his rights so ephemeral, that the seller should be entitled to extricate himself from the disastrous consequences that otherwise attend his nonpossessory status, whether or not he holds an Article 2 security interest. Two candidates that emerge for special treatment, under both the common law of sales and the provisions of Article 2, are the cash sale and the credit sale fraudulently induced by misrepresentation of solvency. Although neither of these transactions was treated under common law as coming within seller’s liens, each did

58. Section 2-505 provides:

Seller’s Shipment Under Reservation

(1) Where the seller has identified goods to the contract by or before shipment:

- (a) his procurement of a negotiable bill of lading to his own order or otherwise reserves in him a security interest in the goods. His procurement of the bill to the order of a financing agency or of the buyer indicates in addition only the seller’s expectation of transferring that interest to the person named.
- (b) a non-negotiable bill of lading to himself or his nominee reserves possession of the goods as security but except in a case of conditional delivery (subsection (2) of Section 2-507) a non-negotiable bill of lading naming the buyer as consignee reserves no security interest even though the seller retains possession of the bill of lading.

(2) When shipment by the seller with reservation of a security interest is in violation of the contract for sale it constitutes an improper contract for transportation within the preceding section but impairs neither the rights given to the buyer by shipment and identification of the goods to the contract nor the seller’s powers as a holder of a negotiable document.

59. Section 9-113. Comment 1 to § 9-113 provides a variety of clues to the coverage of § 9-113, some of which appear to tie § 9-113 to particular language of “security interest” in Article 2, others of which appear to pursue a more functional analysis. Although we are inclined to disagree with inclusion of conditional sales, *see* note 56 *supra*, we note the Comment’s more plausible references to §§ 2-505, 2-703, 2-705, and 2-706.

permit a seller who acted promptly and properly to replevy goods from a buyer in possession.⁶⁰

C. *ABC Delivers Goods on Special Condition*

The contours of the two sales on special condition were well developed at common law. The cash sale was a transaction in which the parties were said to have contemplated a simultaneous exchange of the goods for the contract price.⁶¹ Under a cash sale, no title ever passed to the buyer until payment was made, and the retaking seller was therefore entitled to retake his property when payment was not forthcoming. To exercise his right to retake, the cash seller was required to act speedily, for acquiescence in the buyer's possession despite nonpayment rapidly turned the transaction into a credit sale and the seller into an unsecured creditor.⁶² Similarly, the cash seller could not entrust his unpaying buyer with "indicia of ownership" that might indicate more than a claim to merely temporary possession, without again losing the

60. See 1 G. GILMORE, *supra* note 29, at 64; Gilmore, *The Commercial Doctrine of Good Faith Purchase*, 63 YALE L.J. 1057, 1060 (1954). At common law it was understood that the cash sale was to be distinguished from the conditional sale, on the basis that in a cash sale no right of possession is contemplated until the price is paid; whereas, in a conditional sale the buyer is expected to have possession as soon as the bargain is made. The cash sale contemplates no credit; the conditional sale contemplates credit as far as the possession and use of the goods by the buyer is concerned, though no credit in regard to the transfer of title.

2 S. WILLISTON, *supra* note 35, at 325 (footnote omitted). See also 2 F. MECHEM, A TREATISE ON THE LAW OF SALE OF PERSONAL PROPERTY 1259, 1285, 1361-62, 1363 (1901); Corman, *Cash Sales, Worthless Checks and the Bona Fide Purchaser*, 10 VAND. L. REV. 55 (1956). Misrepresentations of solvency that induce the seller to extend credit were held at common law to be a form of fraud and to allow the deceived seller to avoid the sale. 3 S. WILLISTON, *supra* note 35, at 448. And, under the doctrine enunciated in *California Conserving Co. v. D'Avanzo*, 62 F.2d 528 (2d Cir. 1933), it was not necessary to demonstrate an intent not to pay if the facts showed that, by reason of his financial situation, the buyer could not have hoped to pay. See Braucher, *Reclamation of Goods from a Fraudulent Buyer*, 65 MICH. L. REV. 1281, 1283 (1967). The seller's power of avoidance was seen as an equitable claim, subject to intervening rights obtained by good faith purchasers from the defrauding buyer. See, e.g., *Oswego Starch Factory v. Lendrum*, 57 Iowa 573, 10 N.W. 900 (1881). The buyer's title position was clear: he obtained voidable title and could pass indefeasible title. The seller's power of avoidance was not put in terms of title at all. 3 S. WILLISTON, *supra* note 35, at 503.

61. L. VOLD, HANDBOOK OF THE LAW OF SALES 160 (2d ed. 1959). The common law history is nowhere codified in the Uniform Sales Act.

62. See, e.g., *French v. Lewis*, 218 Pa. 141, 67 A. 45 (1907). For a discussion of the commercial limitations routinely imposed on enforcement of the cash seller's right to retake, see 2 S. WILLISTON, *supra* note 35, at 337-42; Gilmore, *supra* note 60, at 1060-62. Williston argued vigorously but unsuccessfully that acceptance of a check that turned out to be uncollectable was a waiver of a cash sale because it amounted to acquiescence, albeit induced by fraud, in the buyer's possession and title. See 2 S. WILLISTON, *supra* note 35, at 342-45. See also Note, *The "Cash Sale" Presumption in Bad Check Cases: Doctrinal and Policy Anomaly*, 62 YALE L.J. 101 (1952).

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special status of cash seller.⁶³ The sale induced by fraud was a transaction in which the buyer obtained possession and some form of voidable title by misrepresenting his intention to pay or his capacity to do so.⁶⁴ The materiality of this misrepresentation as an inducement to a credit sale established the defrauded seller's right to rescind and to retake the contract goods. Doubts about the precise characterization of the defrauding buyer's title led to differences in the treatment of various takers under the buyer⁶⁵ but did not otherwise impair the seller's right to reclaim his goods if he acted within a reasonable time after receiving notice of the fraud. The theoretical difference between these two sales on special condition was a difference of title: in the former the buyer had none, in the latter he had some. This difference was more significant for subsequent purchasers and lien creditors than for the buyer himself. In direct confrontations between seller and buyer, the same basic principles counseled equitable enforcement of the seller's clearly exceptional claims. Equitable enforcement, by circumscribing the use of the disappointed seller's claim to retake, perhaps served as well as a safety valve. In contrast to the contract expressly denominated a conditional sale, these transactions were never considered to confer liens⁶⁶ and therefore escaped the pre-Code regulation of transactions characterized as invidious secret liens.

Article 2 of the Uniform Commercial Code deals explicitly with both cash sales and fraudulent sales. Despite the Code's virtual abandonment of title, the two transactions are at least nominally described separately. Sections 2-507⁶⁷ and 2-511⁶⁸ are the starting points for investigating the

63. See *Guckeen Farmers Elevator Co. v. Cargill, Inc.*, 269 Minn. 127, 133-36, 130 N.W.2d 69, 73-75 (1964); L. VOLD, *supra* note 61, at 175. Entrusting led to estoppel; typically the litigation involved confrontations with purchasers from the buyer, rather than with the buyer himself.

64. Because the seller's power to reclaim was tied to fraud, which implies intentional misconduct by the buyer, it was unclear at common law how to characterize the transaction of sale induced by over-optimism about financial prospects, rather than by duplicity. See, e.g., *California Conserving Co. v. D'Avanzo*, 62 F.2d 528 (2d Cir. 1933); *Manly v. Ohio Shoe Co.*, 25 F.2d 384 (4th Cir. 1928).

65. The equities of various takers under the buyer are discussed in L. VOLD, *supra* note 61, at 402-04.

66. See, e.g., *Southern Lumber Co. v. Colvin*, 104 Ark. 130, 148 S.W. 496 (1912); *Greater Louisville Auto Auction, Inc. v. Ogle Buick, Inc.*, 387 S.W.2d 17 (Ky. 1965).

67. Section 2-507 provides:

Effect of Seller's Tender; Delivery on Condition

(1) Tender of delivery is a condition to the buyer's duty to accept the goods and, unless otherwise agreed, to his duty to pay for them. Tender entitles the seller to acceptance of the goods and to payment according to the contract.

(2) Where payment is due and demanded on the delivery to the buyer of goods or documents of title, his right as against the seller to retain or dispose of them is conditional upon his making the payment due.

68. Section 2-511 adds presumptions for payment by check:

cash sale doctrine, while section 2-702⁶⁹ is the starting point for investigating the fraudulent sale doctrine. Between the immediate parties, section 2-507(2) provides that the cash buyer's "right as against the seller to retain or dispose of [goods or documents of title] is conditional upon his making the payment due," without spelling out the remedies available to the seller, while section 2-702(2) gives the defrauded seller a right to reclaim goods received on credit if a demand is "made within ten days after the receipt" of the goods, without spelling out the conditional nature of the buyer's tenure. Comment 3 to section 2-507 suggests a link between the two sections by opining that "[t]he provision of this Article for a ten day limit within which the seller may reclaim goods delivered on credit to an insolvent buyer is also applicable here," where the transaction is a cash sale.⁷⁰ This comment, carried forward from earlier drafts of Article 2 in which section 2-702 required reclamation and not just demand within ten days,⁷¹ clearly points to

Tender of Payment by Buyer; Payment by Check

(1) Unless otherwise agreed tender of payment is a condition to the seller's duty to tender and complete any delivery.

(2) Tender of payment is sufficient when made by any means or in any manner current in the ordinary course of business unless the seller demands payment in legal tender and gives any extension of time reasonably necessary to procure it.

(3) Subject to the provisions of this Act on the effect of an instrument on an obligation (Section 3-802), payment by check is conditional and is defeated as between the parties by dishonor of the check on due presentment.

69. Section 2-702 provides:

Seller's Remedies on Discovery of Buyer's Insolvency.

(1) Where the seller discovers the buyer to be insolvent he may refuse delivery except for cash including payment for all goods theretofore delivered under the contract, and stop delivery under this Article (Section 2-705).

(2) Where the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days after the receipt, but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply. Except as provided in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.

(3) The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403). Successful reclamation of goods excludes all other remedies with respect to them.

70. Comment 3 in its entirety provides:

Subsection (2) deals with the effect of a conditional delivery by the seller and in such a situation makes the buyer's "right as against the seller" conditional upon payment. These words are used as words of limitation to conform with the policy set forth in the bona fide purchase sections of this Article. Should the seller after making such a conditional delivery fail to follow up his rights, the condition is waived. The provision of this Article for a ten day limit within which the seller may reclaim goods delivered on credit to an insolvent buyer is also applicable here.

Section 2-507, Comment 3.

71. In the 1952 Official Draft of the Uniform Commercial Code, § 2-702 read:

Seller's Remedies on Discovery of Buyer's Insolvency

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section 2-702(2). Indeed, there is no other ten-day period in the text of Article 2 to which the comment could refer. Although reliance on comment to supply links missing from the text is suspect, in this case both good sense and the similarity in vulnerability to third-party claimants under section 2-403⁷² suggest that, remedially, cash sales and fraudulent sales should be treated alike. Within ten days and without any other formalities, sellers on special condition can by demand commence the retaking of contract goods from their buyers.⁷³

If the cash sale or the fraudulent sale creates a security interest "arising solely under" Article 2, however, the authority to reclaim under Article 2 may be undermined by Article 9. If section 9-113⁷⁴ applies in full force once the buyer is in possession, then his possession is irreversible, because the seller's security interest is invalid without

- (1) Where the seller discovers the buyer to be insolvent he may
 - (a) refuse delivery except for cash including payment for all goods theretofore delivered under the contract, and stop delivery under this Article (Section 2-705); and
 - (b) subject to the rights of a buyer in ordinary course or other good faith purchaser or lien creditor under this Article (Section 2-403), and within ten days after receipt, *reclaim any goods received by the buyer on credit*, but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply.
- (2) Successful reclamation of goods excludes all other remedies with respect to them. (Emphasis added.)

72. The provisions of § 2-403(1) protect good faith purchasers from sellers who have voidable title or who are in possession pursuant to a cash sale or to a transfer procured through fraud:

A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

- (a) the transferor was deceived as to the identity of the purchaser, or
- (b) the delivery was in exchange for a check which is later dishonored, or
- (c) it was agreed that the transaction was to be a "cash sale", or
- (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

73. The 10-day limitation is a convenient solution, but is not universally available. Under § 2-702, this period is extended indefinitely if the seller received a written misrepresentation of solvency within three months before delivery. There is no hint in the text or comments of Article 2 about the relevance of such a misrepresentation in a cash sale.

74. Section 9-113 provides:

Security Interests Arising Under Article on Sales

A security interest arising solely under the Article on Sales (Article 2) is subject to the provisions of this Article except that to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods

- (a) no security agreement is necessary to make the security interest enforceable; and
- (b) no filing is required to perfect the security interest; and
- (c) the rights of the secured party on default by the debtor are governed by the Article on Sales (Article 2).

a written security agreement and is subject to Article 9 rules on default and liquidation of contract goods now characterized as collateral.

Why should an interest that is never characterized by Article 2 as creating a "security interest" fall into the snares of section 9-113? The definition of a security interest in Article 1 is expansive. It encompasses any "interest in personal property . . . which secures payment or performance of an obligation," without regard to consensual designation or distinguishing features of form.⁷⁵ As noted earlier, the common law seller's lien and right of stoppage in transit, neither of which is labeled a "security interest" in Article 2, do fall within section 9-113.⁷⁶ The conditional sale, although denominated a security interest in section 2-401, is a normal Article 9 security interest rather than one "arising solely under" Article 2.⁷⁷ Although the reference to a security interest in section 2-505(1), concerning documentary reservations, and in section 2-711(3), concerning buyers' possessory liens, happens to fit both Article 2 and Article 9, this identity of language is surely fortuitous. To the extent that reclamation rights are analogous to seller's liens, the fact that Article 2 does not characterize them as "security interests" cannot insulate them from section 9-113. The drafting pattern of Article 2 emphasizes the consequences rather than the labeling of commercial relationships. ABC cannot be spared the travails of Article 9 simply because sections 2-507 and 2-702 speak to rights rather than to security interests.

Justice Braucher⁷⁸ offers two other reasons for differentiating reclamation rights from security interests:

75. Section 1-201 (37) defines security interest:

"Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (Section 2-401) is limited in effect to a reservation of a "security interest". The term also includes any interest of a buyer of accounts or chattel paper which is subject to Article 9. The special property interest of a buyer of goods on identification of such goods to a contract for sale under Section 2-401 is not a "security interest", but a buyer may also acquire a "security interest" by complying with Article 9. Unless a lease or consignment is intended as security, reservation of title thereunder is not a "security interest" but a consignment is in any event subject to the provisions on consignment sales (Section 2-326). Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

76. See pp. 920-21 & notes 57-59 *supra*.

77. See note 36 *supra*.

78. Mr. Justice Braucher, as Professor Braucher of the Harvard Law School, was one of the two Coordinators for revisions of the Uniform Commercial Code for its 1962 Official Text. He has been chairman of several committees to consider Article 2, both

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First, a right to rescind is a right to undo the transaction—to reclaim the goods as a substitute for the price—not a right to “secure” payment of the price as required by the definition of “security interest”; under section 2-702(3), successful reclamation “excludes all other remedies.” Second, any such security interest is not the result of a transaction “intended to create a security interest” and is not “created by contract” within the meaning of section 9-102, which defines the scope of Article Nine on secured transactions.⁷⁹

The second suggestion seems plainly wrong: if a security interest arises “solely” under Article 2, by definition it is *not* the result of a transaction “intended to create a security interest,” nor is it “created by contract.” Section 9-113⁸⁰ is an alternate route into Article 9, which by-

before 1962 and in connection with the work of the Permanent Editorial Board since then. The Permanent Editorial Board was urged, as early as 1962, to consider amendment of § 2-702(3) to delete its reference to “lien creditor.” Professor Braucher was chairman of the subcommittee that persuaded the Permanent Editorial Board in 1966 to recommend amendment of § 2-702. See REPORT NO. 3 OF THE PERMANENT EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE ix, 3-4 (1967).

79. Braucher, *supra* note 60, at 1290 (footnote omitted). These reasons have become the accepted wisdom, usually with no further discussion or reference. See, e.g., *United States v. Wyoming Nat'l Bank*, 505 F.2d 1064 (10th Cir. 1974); *Johnston & Murphy Shoes, Inc. v. Meinhard Commercial Corp.* (*In re Mel Goode Shoes, Inc.*), 403 F.2d 658, 660 (6th Cir. 1968); *Guy Martin Buick, Inc. v. Colorado Springs Nat'l Bank*, 184 Colo. 166, 176, 519 P.2d 354, 359-60 (1974) (en banc); *Evans Prod. Co. v. Jorgensen*, 245 Ore. 362, 421 P.2d 978 (1966); *Ranchers & Farmers Livestock Auction Co. v. First St. Bank*, 531 S.W.2d 167, 169 (Tex. Civ. App. 1975); Kennedy, *The Interest of a Reclaiming Seller Under Article 2 of the Code*, 30 BUS. LAW. 833, 844 (1975); Note, *Selected Priority Problems in Secured Financing Under the Uniform Commercial Code*, 68 YALE L.J. 751, 757-58 (1959). A recent important case concluded, however, that a putative reclaiming seller did have an unperfected security interest, but one achieved under § 2-401(1). *Stowers v. Mahon* (*In re Samuels & Co.*), 526 F.2d 1238, 1246-47 (5th Cir.) (en banc), *cert. denied*, 429 U.S. 834 (1976). Although Judge Godbold in *Samuels* rejected the argument that security interests must be “consensually” created, he appeared unaware of the possibility that the reclamation right itself would be a security interest. *But see In re Hardin*, 8 U.C.C. Rep. 857, 862 (E.D. Wis. 1971) (bankruptcy referee), *aff'd sub nom. Shapiro v. Union Bank & Sav. Co.* (*In re Hardin*), 458 F.2d 938 (1972); Peters, *supra* note 8, at 220; Shanker, *A Reply to the Proposed Amendment of UCC Section 2-702(3): Another View of Lien Creditor's Rights vs. Rights of a Seller to an Insolvent*, 14 W. RES. L. REV. 93, 102-04 (1962).

It is worth noting that Justice Braucher's reasons were proposed as two (out of three) suggestions for avoiding what he thought would otherwise be a problem with the application of § 9-203. See Braucher, *supra* note 60, at 1290. Apart from that perceived problem—which, he also recognized, could be handled by treating the reclamation right as a security interest exempted by § 9-113 from the filing requirements of Article 9—there is no indication that Justice Braucher thought that he was passing down undisputed wisdom.

80. Section 9-113 provides:

Security Interests Arising Under Article on Sales

A security interest arising solely under the Article on Sales (Article 2) is subject to the provisions of this Article except that to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods

- (a) no security agreement is necessary to make the security interest enforceable; and
- (b) no filing is required to perfect the security interest; and
- (c) the rights of the secured party on default by the debtor are governed by the Article on Sales (Article 2).

passes the requirements of section 9-102.⁸¹ By necessary implication, section 9-102 is superseded whenever section 9-113 applies.

The proposition that a right to rescind cannot be a security interest is more plausible, but it, too, is ultimately unpersuasive. It is not inconsistent with the idea of a security interest, as section 9-505⁸² recognizes, that one remedy for a secured party may be the return and retention of secured property.⁸³ Moreover, as section 9-113(c) expressly

81. Section 9-102 provides:

Policy and Subject Matter of Article

(1) Except as otherwise provided in Section 9-104 on excluded transactions, this Article applies

- (a) to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel paper or accounts; and also
- (b) to any sale of accounts or chattel paper.

(2) This Article applies to security interests created by contract including pledge, assignment, chattel mortgage, chattel trust, trust deed, factor's lien, equipment trust, conditional sale, trust receipt, other lien or title retention contract and lease or consignment intended as security. This Article does not apply to statutory liens except as provided in Section 9-310.

(3) The application of this Article to a security interest in a secured obligation is not affected by the fact that the obligation is itself secured by a transaction or interest to which this Article does not apply.

Nothing in the definition of a security interest in § 1-201(37) requires a security interest to be consensual in origin. See *Stowers v. Mahon (In re Samuels & Co.)*, 526 F.2d 1238, 1247 (5th Cir.) (en banc), cert. denied, 429 U.S. 834 (1976).

82. Section 9-505 describes the circumstances under which, after default, a secured party may retain secured collateral in satisfaction of the secured obligation. It provides:

Compulsory Disposition of Collateral; Acceptance of the Collateral as Discharge of Obligation

(1) If the debtor has paid sixty per cent of the cash price in the case of a purchase money security interest in consumer goods or sixty per cent of the loan in the case of another security interest in consumer goods, and has not signed after default a statement renouncing or modifying his rights under this Part a secured party who has taken possession of collateral must dispose of it under Section 9-504 and if he fails to do so within ninety days after he takes possession the debtor at his option may recover in conversion or under Section 9-507(1) on secured party's liability.

(2) In any other case involving consumer goods or any other collateral a secured party in possession may, after default, propose to retain the collateral in satisfaction of the obligation. Written notice of such proposal shall be sent to the debtor if he has not signed after default a statement renouncing or modifying his rights under this subsection. In the case of consumer goods no other notice need be given. In other cases notice shall be sent to any other secured party from whom the secured party has received (before sending his notice to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. If the secured party receives objection in writing from a person entitled to receive notification within twenty-one days after the notice was sent, the secured party must dispose of the collateral under Section 9-504. In the absence of such written objection the secured party may retain the collateral in satisfaction of the debtor's obligation.

83. See, e.g., *Carnation Plastic Mfg. Co. v. Giltex, Inc. (In re Giltex, Inc.)*, 17 U.C.C. Rep. 887, 890 n.6 (S.D.N.Y. 1975); *In re Hardin*, 8 U.C.C. Rep. 857, 862 (E.D. Wis. 1971) (bankruptcy referee), *aff'd sub nom. Shapiro v. Union Bank & Sav. Co. (In re Hardin)*, 458 F.2d 938 (7th Cir. 1972) ("[t]hus a seller on credit is given the same rights that a secured creditor would have, namely, the right to repossess the goods"); Shanker, *supra* note 79, at 102-06.

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acknowledges, the rights upon default preserved by Article 2 differ from the constellation of rights existing in Article 9. In the transactions to which section 9-113 applies, where the seller's right is to withhold delivery or to stop goods in transit or to retain control through documents, the seller's remedy is to retain or to retrieve the contract goods. It is true that in all of these cases the seller's remedy of retention is not doctrinally, although it may be practically, his exclusive remedy. Yet in every respect other than exclusivity, the seller's right to reclaim under a cash sale or a fraudulent sale closely resembles the interests that are otherwise characterized as security interests "arising solely" under Article 2 and are incorporated in Article 9 through section 9-113. And whatever may be obscure about section 9-113, it does manifest an intention to cover at least some transactions in which some buyers temporarily receive possession, of which they may then be divested.

The critical language in section 9-113 is contained in the statement that there may be security interests arising solely under Article 2 in which the debtor "does not have or does not lawfully obtain possession of the goods."⁸⁴ Under either alternative, the hybrid security interest is valid without the normal security agreement and is perfected without a financing statement. If, on the other hand, the debtor obtains unfettered possession, the normal Article 9 requirements for validation and perfection govern even under section 9-113. The seller reclaiming under sections 2-507 or 2-702 appears to be a prime candidate to assert a claim that the buyer-debtor did not "lawfully obtain possession"; indeed, no other claim founded in Article 2 seems to come close. As Justice Braucher pointed out, a right of reclamation routinely arises as a result of behavior that is impliedly fraudulent, even though intent to deceive is not an express prerequisite of the seller's cause of action.⁸⁵

84. This language in the alternative is derived from § 56 of the Uniform Sales Act, which described the circumstances under which an unpaid seller's lien was lost. Section 56 provided:

When lien is lost.—(1) The unpaid seller of goods loses his lien thereon—

(a) When he delivers the goods to a carrier or other bailee for the purpose of transmission to the buyer without reserving the property in the goods or the right to the possession thereof;

(b) When the buyer or his agent lawfully obtains possession of the goods;

(c) By waiver thereof.

(2) The unpaid seller of goods, having a lien thereon, does not lose his lien by reason only that he has obtained judgment or decree for the price of the goods.

This history illuminates the otherwise puzzling alternative phraseology in § 9-113, which suggests similar treatment for both nonpossession and unlawful possession. It would be possible to read the phrase "does not have . . . possession" in § 9-113 to throw any hybrid transaction entirely into Article 9 as soon as possession, however procured, had passed to the buyer. But such a reading would leave the rest of the phrase, "or does not lawfully obtain possession," without operative meaning, and should therefore be avoided.

85. Braucher, *supra* note 60, at 1282-84, 1290. See also § 2-702, Comment 2; King, *Reclamation Petition Granted: In Defense of the Defrauded Seller*, RECL. L.J., July 1970, at

"Unlawful" possession must refer principally to fraudulent conduct by the Family Furnitures of this world, since outright theft entitles ABC to a claim in conversion rather than to a security interest.

In sum, the seller reclaiming under the special conditions of a cash sale or a fraudulent sale has the right to reclaim only under the circumstances dictated by Article 2. Compliance with the Article 2 requirements, principally its ten-day demand period, allows ABC to re-take the contract sofas from Family Furniture. ABC has a section 9-113 security interest but is excused, by section 9-113 itself, from compliance with Article 9 validation requirements. Section 9-113 may introduce priority complications for ABC, but it does not alter proprietary rights between ABC and Family Furniture.⁸⁶

81, 82. Once the cash seller is otherwise assimilated to the position of a credit seller in a sale induced by fraud, there is no reason why the cash seller should not also be able to rely on this presumption of fraud.

86. The reclamation right that is provided by §§ 2-507 and 2-702 is a right that runs textually only to "the goods." However, if that right is a security interest arising solely under Article 2, so that Article 9 is made applicable (apart from default rules) by § 9-113, then it is plausible to believe that the reclamation right "continues in any identifiable proceeds," § 9-306(2), until either the termination of the reclamation right under Article 2 or the expiration of "ten days after receipt of the proceeds by the debtor," § 9-306(3), whichever occurs first. Section 9-306(2) and (3) provide:

(2) Except where this Article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof unless the disposition was authorized by the secured party in the security agreement or otherwise, and also continues in any identifiable proceeds including collections received by the debtor.

(3) The security interest in proceeds is a continuously perfected security interest if the interest in the original collateral was perfected but it ceases to be a perfected security interest and becomes unperfected ten days after receipt of the proceeds by the debtor unless

- (a) a filed financing statement covers the original collateral and the proceeds are collateral in which a security interest may be perfected by filing in the office or offices where the financing statement has been filed and, if the proceeds are acquired with cash proceeds, the description of collateral in the financing statement indicates the types of property constituting the proceeds; or
- (b) a filed financing statement covers the original collateral and the proceeds are identifiable cash proceeds; or
- (c) the security interest in the proceeds is perfected before the expiration of the ten day period.

Except as provided in this section, a security interest in proceeds can be perfected only by the methods or under the circumstances permitted in this Article for original collateral of the same type.

In *In re Samuels & Co.*, in which it appeared that the cattle had "long since been butchered and processed and sold through the normal course of business"—presumably to buyers in the ordinary course of business—the issue concerned the priority of interest in proceeds between the reclaiming cattle farmers and C.I.T. Corporation. *Stowers v. Mahon (In re Samuels & Co.)*, 510 F.2d 139, 144 (5th Cir.), *rev'd en banc*, 526 F.2d 1238 (5th Cir. 1975), *cert. denied*, 429 U.S. 834 (1976). The court did not address the question whether the reclamation right automatically attached itself, via Article 9, to the proceeds of resale. Here, again, where the Code does not speak to a situation in which Articles 2 and 9 appear to point in different directions, resort to the underlying policies would suggest that, absent unusual circumstances, the reclamation right should, like other perfected security interests, shift to proceeds upon resale.

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D. *ABC Reacquires Goods from Family Furniture*

In all other cases in which the seller reacquires goods from a buyer at some time lawfully in possession, the seller's rights are more problematic. At common law, the seller's lien was sometimes said to be revived by repossession, although it was unclear whether revival implied a new lien or renewal of an old lien.⁸⁷ Whatever the rationale, in the language of a leading case, "[t]his rule probably serves commercial convenience, and we accept it."⁸⁸

Consideration of the revival of a seller's lien has usually arisen in the context of reacquisition triggered by the buyer's default. The buyer may refuse to pay out of obduracy (or a "temporary cash bind"), or he may wrongfully claim that nonconformity in the tendered goods excuses his obligation to pay. But reacquisition may also occur because of the seller's default if the buyer rightfully rejects the goods or revokes his acceptance, or because of a consensual modification totally apart from, or in settlement of, a dispute about the contract of sale.

Article 2 of the Code, which says nothing directly about seller's liens, predictably says little about the inferences to be drawn from the seller's repossession. Although Article 2 discourages rejection⁸⁹ and may thereby diminish the likelihood that goods will be reacquired by the seller, it does not preclude rejection entirely. According to section 2-401(4), "[a] rejection or other refusal by the buyer to receive or retain the goods, whether or not justified, or a justified revocation of acceptance reverts title to the goods in the seller."⁹⁰ And section 2-602(3) adds that

87. 3 S. WILLISTON, *supra* note 35, at 107-08.

88. *Jones v. LeMay-Lieb Corp.*, 301 Mass. 133, 135, 16 N.E.2d 634, 635 (1938).

89. *See Peters*, *supra* note 8, at 206-16.

90. Section 2-401 provides, in its entirety:

Passing of Title; Reservation for Security; Limited Application of This Section

Each provision of this Article with regard to the rights, obligations and remedies of the seller, the buyer, purchasers or other third parties applies irrespective of title to the goods except where the provision refers to such title. Insofar as situations are not covered by the other provisions of this Article and matters concerning title become material the following rules apply:

(1) Title to goods cannot pass under a contract for sale prior to their identification to the contract (Section 2-501), and unless otherwise explicitly agreed the buyer acquires by their identification a special property as limited by this Act. Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest. Subject to these provisions and to the provisions of the Article on Secured Transactions (Article 9), title to goods passes from the seller to the buyer in any manner and on any conditions explicitly agreed on by the parties.

(2) Unless otherwise explicitly agreed title passes to the buyer at the time and place at which the seller completes his performance with reference to the physical delivery of the goods, despite any reservation of a security interest and even though a document of title is to be delivered at a different time or place; and in particular and despite any reservation of a security interest by the bill of lading

(a) if the contract requires or authorizes the seller to send the goods to the buyer

"[t]he seller's rights with respect to goods wrongfully rejected are governed by the provisions of this Article on Seller's remedies in general (Section 2-703)."⁹¹ Section 2-703, in turn, permits an aggrieved seller to "resell and recover damages" and to "cancel."⁹² Between the

but does not require him to deliver them at destination, title passes to the buyer at the time and place of shipment; but

(b) if the contract requires delivery at destination, title passes on tender there.

(3) Unless otherwise explicitly agreed where delivery is to be made without moving the goods,

(a) if the seller is to deliver a document of title, title passes at the time when and the place where he delivers such documents; or

(b) if the goods are at the time of contracting already identified and no documents are to be delivered, title passes at the time and place of contracting.

(4) A rejection or other refusal by the buyer to receive or retain the goods, whether or not justified, or a justified revocation of acceptance reverts title to the goods in the seller. Such reversion occurs by operation of law and is not a "sale".

91. Section 2-602(3) is part of a section dealing generally with rightful rejection. That section provides, in its entirety:

Manner and Effect of Rightful Rejection

(1) Rejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the buyer seasonably notifies the seller.

(2) Subject to the provisions of the two following sections on rejected goods (Sections 2-603 and 2-604),

(a) after rejection any exercise of ownership by the buyer with respect to any commercial unit is wrongful as against the seller; and

(b) if the buyer has before rejection taken physical possession of goods in which he does not have a security interest under the provisions of this Article (subsection (3) of Section 2-711), he is under a duty after rejection to hold them with reasonable care at the seller's disposition for a time sufficient to permit the seller to remove them; but

(c) the buyer has no further obligations with regard to goods rightfully rejected.

(3) The seller's rights with respect to goods wrongfully rejected are governed by the provisions of this Article on Seller's remedies in general (Section 2-703).

This statement of the seller's rights is reinforced by a similar provision in § 2-709(3), dealing with the seller's action for the price, which provides yet another indication of the reversion of the seller's rights over sold goods. Section 2-709 provides:

Action for the Price

(1) When the buyer fails to pay the price as it becomes due the seller may recover, together with any incidental damages under the next section, the price

(a) of goods accepted or of conforming goods lost or damaged within a commercially reasonable time after risk of their loss has passed to the buyer; and

(b) of goods identified to the contract if the seller is unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.

(2) Where the seller sues for the price he must hold for the buyer any goods which have been identified to the contract and are still in his control except that if resale becomes possible he may resell them at any time prior to the collection of the judgment. The net proceeds of any such resale must be credited to the buyer and payment of the judgment entitles him to any goods not resold.

(3) After the buyer has wrongfully rejected or revoked acceptance of the goods or has failed to make a payment due or has repudiated (Section 2-610), a seller who is held not entitled to the price under this section shall nevertheless be awarded damages for non-acceptance under the preceding section.

92. Section 2-703 provides:

Seller's Remedies in General

Where the buyer wrongfully rejects or revokes acceptance of goods or fails to make a payment due on or before delivery or repudiates with respect to a part or the whole,

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immediate parties, these sections serve to give the seller the same rights to which he would have been entitled at common law as a revived lienor.⁹³

This analysis of the seller's rights under Article 2 and the analogy to lien status raise Article 9 questions. How, if at all, does a reacquiring seller fit into section 9-113?⁹⁴ Does a reacquiring seller have a security interest under any circumstances?

Once a seller has managed to reacquire contract goods for any legitimate reason, he is likely to view inquiries into his security status as surprising and gratuitous. The buyer's possessory interlude is now, after all, totally superseded by the seller's concededly authorized reacquisition. The logic of reacquisition of title and possession suggests that the repossessing seller is an owner rather than a secured party. Yet under section 9-113 there is no metaphysical inconsistency between ownership and possession on the one hand and security status on the other. If the seller's justifiable withholding of delivery furnishes the paradigm for Article 9 supervision, as an Article 9 security interest, of a security interest "arising solely under the Article on Sales," the seller's reacquisition can hardly escape similar characterization.

The language of section 9-113 arguably accommodates the vicissitudes of the reacquiring seller. It provides that Article 9 rules on validation, perfection, and default do not apply "so long as the debtor

then with respect to any goods directly affected and, if the breach is of the whole contract (Section 2-612), then also with respect to the whole undelivered balance, the aggrieved seller may

- (a) withhold delivery of such goods;
- (b) stop delivery by any bailee as hereafter provided (Section 2-705);
- (c) proceed under the next section respecting goods still unidentified to the contract;
- (d) resell and recover damages as hereafter provided (Section 2-706);
- (e) recover damages for non-acceptance (Section 2-708) or in a proper case the price (Section 2-709);
- (f) cancel.

93. The common law cases seem to have revolved principally around the seller's right to resell and to measure damages by losses, if any, under the resale. This issue was complicated by the reliance of the common law on title to determine monetary claims after breach. See G. GILMORE & C. BLACK, *THE LAW OF ADMIRALTY* 102-08 (2d ed. 1975). The cases do not seem to have arisen in contexts involving the rights of third parties.

94. Section 9-113 provides:

Security Interests Arising Under Article on Sales

A security interest arising solely under the Article on Sales (Article 2) is subject to the provisions of this Article except that to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods

- (a) no security agreement is necessary to make the security interest enforceable; and
- (b) no filing is required to perfect the security interest; and
- (c) the rights of the secured party on default by the debtor are governed by the Article on Sales (Article 2).

does not have . . . possession." If "so long as" implies that the debtor's possession is reversible, then, upon reacquisition, the seller's Article 2 rights are not seriously compromised. Although such a seller may have to take into account the interests of other parties that arose while the buyer was in possession,⁹⁵ his reacquisition is still to be distinguished from the retaking associated with ordinary Article 9 security interests.⁹⁶

It is of course by no means clear that section 9-113 was drafted to accommodate the reacquiring seller rather than to hedge uncertainties about delivery and tender. The ambiguous reach of "so long as" may well be influenced by the circumstances of the reacquisition. Retaking as a resolution of disagreement about the quality or suitability of ABC's sofas may well trigger different responses than repossession consequent to the "mere" failure of Family Furniture to pay, even if, in this latter case, repossession is consensual rather than forcible. Inquiry into attendant circumstances is certainly consistent with the methodology of Article 2, even if it proves disconcerting to the Article 2 seller. Yet such inquiry should avoid imposing risks that are genuinely unforeseeable. Between ABC and Family Furniture, reacquisition that is authorized by Article 2 should foreclose fishing expeditions into the status of the seller's interest under Article 9. At least as to the validity of proprietary claims between the immediate parties, if not as to the claims of third parties, "so long as" in section 9-113 should be read to protect the reasonable expectations of the reacquiring seller.

II. Perfection of the Unpaid Seller's Proprietary Claim to Sold Goods

The proprietary claims of the unpaid seller against his buyer are reasonably well established by both Article 2 and Article 9 of the Code. The competing claims of lien creditors of the buyer are, like all third-party claims, more obscure. There is little overall guidance in Article 2 about the rights of creditors except in the few transactions that the Article singles out as so fraught with fraudulent overtones that creditors need special protection. Apart from these transactions, involving sellers left in possession of sold goods⁹⁷ and agents entrusted with consigned

95. Third-party claims will be discussed in the remainder of this article.

96. If the repossessing seller comes within the "except" clause of § 9-113, Article 9 rules about validation, perfection, and default are all waived.

97. Section 2-402 incorporates the common law principle of ostensible ownership, which allows creditors of a seller to levy on sold goods if the seller's retention of possession is or can be deemed fraudulent. Section 2-402 provides:

Rights of Seller's Creditors Against Sold Goods

(1) Except as provided in subsections (2) and (3), rights of unsecured creditors of the seller with respect to goods which have been identified to a contract for sale are

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goods,⁹⁸ Article 2 refers creditors to rights set out in Article 9.⁹⁹ This omission cannot be justified by an absence of foreseeable conflict between the unpaid seller and the creditors of his buyer. As one example,

subject to the buyer's rights to recover the goods under this Article (Sections 2-502 and 2-716).

(2) A creditor of the seller may treat a sale or an identification of goods to a contract for sale as void if as against him a retention of possession by the seller is fraudulent under any rule of law of the state where the goods are situated, except that retention of possession in good faith and current course of trade by a merchant-seller for a commercially reasonable time after a sale or identification is not fraudulent.

(3) Nothing in this Article shall be deemed to impair the rights of creditors of the seller

- (a) under the provisions of the Article on Secured Transactions (Article 9); or
- (b) where identification to the contract or delivery is made not in current course of trade but in satisfaction of or as security for a pre-existing claim for money, security or the like and is made under circumstances which under any rule of law of the state where the goods are situated would apart from this Article constitute the transaction a fraudulent transfer or voidable preference.

98. Sections 2-326 and 9-114 deal with consignments, transactions in which an agent is entrusted with goods for the purpose of sale. Creditors of the agent may subject those goods to their claims if the agent appears to have the characteristics of a merchant dealing in goods of that kind and if precautionary warnings have not been given. Section 9-114 deals with questions of priority in consigned goods; § 2-326 defines the rights of general creditors as follows:

Sale on Approval and Sale or Return; Consignment Sales and Rights of Creditors

(1) Unless otherwise agreed, if delivered goods may be returned by the buyer even though they conform to the contract, the transaction is

- (a) a "sale on approval" if the goods are delivered primarily for use, and
- (b) a "sale or return" if the goods are delivered primarily for resale.

(2) Except as provided in subsection (3), goods held on approval are not subject to the claims of the buyer's creditors until acceptance; goods held on sale or return are subject to such claims while in the buyer's possession.

(3) Where goods are delivered to a person for sale and such person maintains a place of business at which he deals in goods of the kind involved, under a name other than the name of the person making delivery, then with respect to claims of creditors of the person conducting the business the goods are deemed to be on sale or return. The provisions of this subsection are applicable even though an agreement purports to reserve title to the person making delivery until payment or resale or uses such words as "on consignment" or "on memorandum". However, this subsection is not applicable if the person making delivery

- (a) complies with an applicable law providing for a consignor's interest or the like to be evidenced by a sign, or
- (b) establishes that the person conducting the business is generally known by his creditors to be substantially engaged in selling the goods of others, or
- (c) complies with the filing provisions of the Article on Secured Transactions (Article 9).

(4) Any "or return" term of a contract for sale is to be treated as a separate contract for sale within the statute of frauds section of this Article (Section 2-201) and as contradicting the sale aspect of the contract within the provisions of this Article on parol or extrinsic evidence (Section 2-202).

99. The rights of third-party claimants generally in Article 2 are located in Part 4 of that Article. Subsection (4) of § 2-403 makes a sweeping reference to several articles, including Article 9, for the law that "govern[s]" the "rights of . . . lien creditors." Section 2-403 in its entirety provides:

Power to Transfer; Good Faith Purchase of Goods; "Entrusting"

(1) A purchaser of goods acquires all title which his transferor had or had power

consider the case of ABC, as an unpaid seller, once goods are marked and identified for shipment to Family Furniture. Identification gives Family Furniture rights described by Article 2 under the rubric of "special property," which may well be difficult to distinguish from title.¹⁰⁰ It is not unlikely that judicial process of some sort will enable

to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

- (a) the transferor was deceived as to the identity of the purchaser, or
- (b) the delivery was in exchange for a check which is later dishonored, or
- (c) it was agreed that the transaction was to be a "cash sale", or
- (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

(2) Any 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.

(3) "Entrusting" includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be larcenous under the criminal law.

(4) The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9), Bulk Transfers (Article 6) and Documents of Title (Article 7).

100. Under § 2-401(1), identification is a prerequisite to the passage of title, while the consequence of identification is normally to give the buyer "a special property as limited by this Act." Section 2-401(1) provides:

Each provision of this Article with regard to the rights, obligations and remedies of the seller, the buyer, purchasers or other third parties applies irrespective of title to the goods except where the provision refers to such title. Insofar as situations are not covered by the other provisions of this Article and matters concerning title become material the following rules apply:

(1) Title to goods cannot pass under a contract for sale prior to their identification to the contract (Section 2-501), and unless otherwise explicitly agreed the buyer acquires by their identification a special property as limited by this Act. Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest. Subject to these provisions and to the provisions of the Article on Secured Transactions (Article 9), title to goods passes from the seller to the buyer in any manner and on any conditions explicitly agreed on by the parties.

Identification is defined and described in § 2-501:

Insurable Interest in Goods; Manner of Identification of Goods

(1) The buyer obtains a special property and an insurable interest in goods by identification of existing goods as goods to which the contract refers even though the goods so identified are non-conforming and he has an option to return or reject them. Such identification can be made at any time and in any manner explicitly agreed to by the parties. In the absence of explicit agreement identification occurs

- (a) when the contract is made if it is for the sale of goods already existing and identified;
- (b) if the contract is for the sale of future goods other than those described in paragraph (c), when goods are shipped, marked or otherwise designated by the seller as goods to which the contract refers;
- (c) when the crops are planted or otherwise become growing crops or the young are conceived if the contract is for the sale of unborn young to be born within twelve months after contracting or for the sale of crops to be harvested

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a creditor with a judgment against Family Furniture to reach this "special property."¹⁰¹ If Family Furniture is not only indebted but also insolvent, then Family Furniture's trustee in bankruptcy will make similar demands. In these unhappy circumstances, several courts have chosen to look to local pre-Code law rather than to Article 9, on the theory that Article 9 applies only to security interests created by Article 9.¹⁰² It is fair to say that these courts have not taken section 9-113 fully into account.¹⁰³

In fact, the unpaid seller who is assimilated into Article 9 because he has a security interest arising solely under the Article on Sales receives considerable protection by the provisions of section 9-113. The rights of a lien creditor turn, under section 9-301,¹⁰⁴ on whether the com-

within twelve months or the next normal harvest season after contracting whichever is longer.

(2) The seller retains an insurable interest in goods so long as title to or any security interest in the goods remains in him and where the identification is by the seller alone he may until default or insolvency or notification to the buyer that the identification is final substitute other goods for those identified.

(3) Nothing in this section impairs any insurable interest recognized under any other statute or rule of law.

There is little further codification of the consequences of "special property" in Article 2. Under § 2-502, a prepaying buyer of goods in which he has a special property may possibly recover the identified goods from an insolvent seller. The functional dimensions of this right are precarious at best. See Jackson & Kronman, *A Plea for the Financing Buyer*, 85 YALE L.J. 1 (1975). Section 2-722 spells out the consequences of an insurable risk for claims against third parties who damage identified goods. Otherwise, there is only the definition of "security interest" in § 1-201(37), which stipulates, *inter alia*, that "[t]he special property interest of a buyer of goods on identification of such goods to a contract for sale under Section 2-401 is not a 'security interest', but a buyer may also acquire a 'security interest' by complying with Article 9." By contrast, the buyer who has made payments for goods in his possession, which the buyer chooses rightfully to reject or to revoke, has what § 2-711(3) denominates a "security interest." Comment 1 to § 9-113 suggests that this security may be encompassed within the range of security interests "arising solely under the Article on Sales," with the seller as debtor and the buyer as secured creditor.

101. The Code does not anywhere purport to determine when a judicial lien attaches or what property a judicial lienor may reach. See Note, *Nonconsensual Liens Under Article 9*, 76 YALE L.J. 1649, 1665-68 (1967). The common law rules manifest "hopeless prolixity and diversification." Riesenfeld, *Collection of Money Judgments in American Law—A Historical Inventory and a Prospectus*, 42 IOWA L. REV. 155, 155 (1957).

102. See, e.g., *Johnston & Murphy Shoes, Inc. v. Meinhard Commercial Corp.* (*In re Mel Golde Shoes, Inc.*), 403 F.2d 658 (6th Cir. 1968); *In re Kravitz*, 278 F.2d 820 (3d Cir. 1960).

103. See *In re Federal's Inc.*, 553 F.2d 509 (6th Cir. 1977).

104. Section 9-301 provides:

Persons Who Take Priority Over Unperfected Security Interests; Rights of "Lien Creditor"

(1) Except as otherwise provided in subsection (2), an unperfected security interest is subordinate to the rights of

(a) persons entitled to priority under Section 9-312;

(b) a person who becomes a lien creditor before the security interest is perfected;

(c) in the case of goods, instruments, documents, and chattel paper, a person who is not a secured party and who is a transferee in bulk or other buyer not in

peting interest is perfected at the time the creditor levies. Under section 9-113, the seller's hybrid security interest is perfected without the filing of a financing statement, so long as the seller's interest is possessory.¹⁰⁵ Like the ordinary secured creditor who perfects his interest by possession of pledged collateral,¹⁰⁶ the Article 2 seller has a perfected interest, and therefore priority over lien creditors, so long as he withholds or regains the contract goods. ABC need not fear the wrath, or the lien, of Family Furniture's creditors unless those creditors manage to levy on ABC's sofas while they are in the possession of Family Furniture or its agent.

The most difficult case is that of delivery on special condition—the cash sale or the credit sale induced by misrepresentation of solvency. If creditors levy or bankruptcy ensues while Family Furniture is temporarily in possession, who should prevail? This question, variously answered at common law and in successive drafts of Article 2, deserves to be laid to rest. A majority of legislatures first enacted a version of

ordinary course of business or is a buyer of farm products in ordinary course of business, to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected;

(d) in the case of accounts and general intangibles, a person who is not a secured party and who is a transferee to the extent that he gives value without knowledge of the security interest and before it is perfected.

(2) If the secured party files with respect to a purchase money security interest before or within ten days after the debtor receives possession of the collateral, he takes priority over the rights of a transferee in bulk or of a lien creditor which arise between the time the security interest attaches and the time of filing.

(3) A "lien creditor" means a creditor who has acquired a lien on the property involved by attachment, levy or the like and includes an assignee for benefit of creditors from the time of assignment, and a trustee in bankruptcy from the date of the filing of the petition or a receiver in equity from the time of appointment.

(4) A person who becomes a lien creditor while a security interest is perfected takes subject to the security interest only to the extent that it secures advances made before he becomes a lien creditor or within 45 days thereafter or made without knowledge of the lien or pursuant to a commitment entered into without knowledge of the lien.

105. A possessory security interest arising solely under the Article on Sales falls within the exemption of § 9-113(b):

Security Interests Arising Under Article on Sales

A security interest arising solely under the Article on Sales (Article 2) is subject to the provisions of this Article except that to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods

(a) no security agreement is necessary to make the security interest enforceable; and

(b) no filing is required to perfect the security interest; and

(c) the rights of the secured party on default by the debtor are governed by the Article on Sales (Article 2).

106. With the exception of a few special security interests that enjoy automatic perfection, see §§ 9-302(1), 9-304, security interests are ordinarily perfected either by filing or by the secured party's taking or retaining possession. Section 9-305 permits perfection through possession for every form of collateral except accounts and general intangibles. The only distinction between perfection by filing and perfection by possession is that there is no relation back for perfection by possession.

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section 2-702 that specifically foreclosed reclamation by a defrauded seller once a lien creditor had intervened.¹⁰⁷ When it was discovered that this priority decision reversed well-established common law cases to the contrary, the offending language was dropped from section 2-702.¹⁰⁸ If legislative history means anything, it means that the drafters, newly enlightened, intended to instruct that lien creditors should lose, or at least that they should not prevail, absent unusual equities. Perhaps it is difficult for courts to draw inferences from language that, like the Cheshire cat, is no longer there.¹⁰⁹

If the matter of perfection is considered from the vantage of Article 9 and section 9-113, it seems as plausible here as it was when we were considering the validity of the seller's interest to say that the buyer-debtor's possession is sufficiently "unlawful" so that the seller's security interest is perfected without the filing of a financing statement.¹¹⁰

107. In the 1962 Official Text of the Code, § 2-702(3) read:

The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser or lien creditor under this Article (Section 2-403). Successful reclamation of goods excludes all other remedies with respect to them.

(Emphasis added.)

108. The history of the drafting and amendment of § 2-702 is described in Braucher, *supra* note 60, at 1285-88.

109. Unfortunately, in a large number of jurisdictions the original language of § 2-702, and the reference to "lien creditor," have remained unamended. These jurisdictions have no direct mandate to prefer the reclaiming seller over a lien creditor, but must instead analyze what upset powers, if any, a lien creditor is entitled to assert.

Under the amended § 2-702(3), the battleground has shifted to the question whether the reclamation right of § 2-702(2) is a statutory lien, voidable under § 67c(1)(A) of the Bankruptcy Act, 11 U.S.C. § 107(c)(1)(A) (1970), or a disguised, state-created priority invalidated by § 64 of the Bankruptcy Act, *id.* § 104. See, e.g., *In re Federal's Inc.*, 553 F.2d 509 (6th Cir. 1977); *Alfred M. Lewis, Inc. v. Holzman (In re Telemart Enterprises, Inc.)*, 524 F.2d 761 (9th Cir. 1975); *In re National Bellas Hess, Inc.*, 17 U.C.C. Rep. 430 (S.D.N.Y. 1975) (bankruptcy judge). *Contra*, *Carnation Plastic Mfg. Co. v. Giltex, Inc. (In re Giltex, Inc.)*, 17 U.C.C. Rep. 887 (S.D.N.Y. 1975); *In re Good Deal Supermarkets Inc.*, 384 F. Supp. 887 (D.N.J. 1974). For divergent views on this topic, see, e.g., Anderson, *The Reclaiming Seller Under UCC Section 2-702 vs. His Four Horsemen of the Apocalypse*, 8 ST. MARY'S L.J. 271 (1976); Countryman, *Buyers and Sellers of Goods in Bankruptcy*, 1 N.M.L. REV. 435 (1971); Hawkland, *The Relative Rights of Lien Creditors and Defrauded Sellers—Amending the Uniform Commercial Code to Conform to the Kravitz Case*, 67 COM. L.J. 86 (1962); Note, *Uniform Commercial Code—§ 2-702: Conflict with § 67c(1)(A) of the Federal Bankruptcy Act*, 53 N.C.L. REV. 169 (1974).

110. Under § 9-113, if the debtor "does not lawfully obtain possession," then § 9-113(b) waives the requirement of filing for perfection. Section 9-113 provides:

Security Interests Arising Under Article on Sales

A security interest arising solely under the Article on Sales (Article 2) is subject to the provisions of this Article except that to the extent that and so long as the debtor does not have or does not lawfully obtain possession of the goods

- (a) no security agreement is necessary to make the security interest enforceable; and
- (b) no filing is required to perfect the security interest; and
- (c) the rights of the secured party on default by the debtor are governed by the Article on Sales (Article 2).

Temporary perfection without filing or possession is expressly validated for practical commercial reasons elsewhere in Article 9.¹¹¹ In fact, if the reclaiming seller acts to repossess within ten days, his posture is functionally indistinguishable from that of a purchase money secured creditor who files a financing statement within ten days after the debtor takes possession.¹¹² This analysis loses persuasiveness, however, if the seller's reclamation is indefinitely delayed, as is permissible under section 2-702 when the seller has relied on a written misrepresentation of solvency,¹¹³ or if the seller privately demands reclamation but then does not actually reclaim. It would be consistent with pre-Code case law on cash sales¹¹⁴ and general principles of estoppel incorporated

111. Temporary perfection without filing or possession is permitted for 21 days for a security interest in instruments or negotiable documents under § 9-304. Similarly, a security interest in proceeds is continuously perfected under § 9-306 for 10 days after receipt by the debtor. Good and sufficient commercial reasons support preferment of the secured to the lien lender under these circumstances. Short-term protection from transactions induced by fraud may be equally worthy of preferment. The choice is one of policy, on which reasonable people have been known to differ, as Justice Braucher shows, *see Braucher, supra* note 60, at 1281 & n.2. In any case, a choice in favor of the reclaiming seller would not do fundamental violence to the Article 9 scheme of perfection.

112. Under § 9-301(2), a secured party who "files with respect to a purchase money security interest before or within ten days after the debtor receives possession of the collateral . . . takes priority over the rights of . . . a lien creditor" that arose in the gap between possession and filing. Technically, this grace period is available only to the secured party who perfects by filing and not to one who perfects by taking possession. *See* § 9-305; 1 G. GILMORE, *supra* note 29, at 445-49. Still, given the special constraints that limit the class of purchase money security interests, *see* § 9-107, the reclaiming seller may be exempted from the obloquy that has befallen the equitable pledgor. Furthermore, it is not entirely clear that Article 9 totally supersedes the doctrine of equitable lien. *See, e.g., General Ins. Co. v. Lowry*, 412 F. Supp. 12 (S.D. Ohio 1976); *Warren Tool Co. v. Stephenson*, 11 Mich. App. 274, 161 N.W.2d 133 (1968).

Although repossession within 10 days is not required, action beyond the demand might reasonably be required to be asserted promptly. *See, e.g., In re Behring & Behring*, 5 U.C.C. Rep. 600, 606 (N.D. Tex. 1968) (bankruptcy referee), *aff'd*, 445 F.2d 1096 (5th Cir.), *cert. denied*, 404 U.S. 991 (1971).

113. Section 2-702 provides:

Seller's Remedies on Discovery of Buyer's Insolvency

(1) Where the seller discovers the buyer to be insolvent he may refuse delivery except for cash including payment for all goods theretofore delivered under the contract, and stop delivery under this Article (Section 2-705).

(2) Where the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days after the receipt, but if misrepresentation of solvency has been made to the particular seller in writing within three months before delivery the ten day limitation does not apply. Except as provided in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.

(3) The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403). Successful reclamation of goods excludes all other remedies with respect to them.

The timing of the misrepresentation of solvency under subsection (2) relates to receipt of the misinformation, rather than to demand for reclamation upon discovery of insolvency.

114. *See Gilmore, supra* note 60, at 1061-62 (discussing commercial limitations on cash sale doctrine at common law).

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through section 1-103 to be less tolerant about the time within which ABC must assert its reclamation rights when it is dealing with Family Furniture's creditors than when it is dealing with Family Furniture itself. At some point, acquiescence in Family Furniture's possession, no matter how induced, could be thought to convert "unlawful" into "lawful" possession.¹¹⁵ Although ten days may be too short a time for all purposes, courts should be willing to determine, upon examination of the circumstances and of commercial custom and usage, how soon a reasonably diligent seller could have alerted himself to the facts of his buyer's financial life.¹¹⁶ Whatever the outcome of this inquiry, it bears noting that the flexible methodology of Article 2 is and should be a principal resource for informing the language of section 9-113 and for governing, wherever possible, Article 9 security interests arising solely under Article 2.

In bankruptcy a solution in which perfection depends on case-by-case determination of the timeliness of repossession is admittedly short of ideal. Even if such perfection passes muster under the strong-arm clause of section 70(c) of the Bankruptcy Act,¹¹⁷ it may be vulnerable as preferential under section 60.¹¹⁸ On the whole, appellate courts in

115. See, e.g., *Bar Control v. Gifford (In re Colacci's of America, Inc.)*, 490 F.2d 1118 (10th Cir. 1974). Cf. *In re Behring & Behring*, 5 U.C.C. Rep. 600, 606 (N.D. Tex. 1968) (bankruptcy referee), *aff'd*, 445 F.2d 1096 (5th Cir.), *cert. denied*, 404 U.S. 991 (1971) (something more than bare oral demand required to exercise right of reclamation).

116. The idea that a reasonable time to take action may vary with the circumstances is consistent with other provisions in Articles 1 and 2 of the Code. Section 1-204 is extremely open-ended:

Time; Reasonable Time; "Seasonably"

(1) Whenever this Act requires any action to be taken within a reasonable time, any time which is not manifestly unreasonable may be fixed by agreement.

(2) What is a reasonable time for taking any action depends on the nature, purpose and circumstances of such action.

(3) An action is taken "seasonably" when it is taken at or within the time agreed or if no time is agreed at or within a reasonable time.

The remedies provisions of Article 2 demonstrate similar flexibility. The buyer who is tendered nonconforming goods has different time periods in which to act, depending on whether or not the defect is patent and on the remedy that the buyer chooses to pursue. See §§ 2-601, 2-602, 2-607, 2-608. The buyer's delay in notification of dissatisfaction is most likely to be excused when the claim is limited to damages and is brought by "a retail consumer." See § 2-607, Comment 4.

117. The case law under § 70(c) has, at least since *Lewis v. Manufacturers Nat'l Bank*, 364 U.S. 603 (1961), resisted speculation that elevates the bankruptcy trustee over other creditors. For a recent example, see *In re Federal's Inc.*, 553 F.2d 509 (6th Cir. 1977).

118. Extensive revision of the Bankruptcy Act has been pending in Congress for several years. The final shape and destiny of the various proposals for reform are as yet unclear. Each of the various proposals has suggested major substantive alterations of the powers of the trustee in bankruptcy to upset pre-bankruptcy transfers of the debtor's property, powers currently contained in Bankruptcy Act §§ 60, 67, 70, 11 U.S.C. §§ 96, 107, 110 (1970). See HOUSE COMM. ON JUDICIARY, BANKRUPTCY LAW REVISION, H. REP. NO. 595, 95th Cong., 1st Sess. 177-80 (1977) [hereinafter cited as 1977 REPORT]; 1 REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, 93d Cong., 1st Sess. 200-12 (1973) [hereinafter cited as 1973 REPORT]. H.R. 8200, the bill passed by the House

recent years have proven remarkably receptive to arguments that protect open-ended commercial transactions against attack in bankruptcy.¹¹⁹ It should be added that our analysis, which reads expansively the category of security interests arising solely under Article 2, should not increase their vulnerability to the statutory lien provision of the Bankruptcy Act, section 67, which invalidates liens arising "solely by force of statute." Relationships arising under Article 2 are statutory in the sense that a codification is an act of a state legislature. But the relationships thus codified have their origins in common law commercial principles that depend on contract, not on statute. As the Sixth Circuit recently observed in rejecting the application of section 67 to defeat the reclamation right of a defrauded seller, "[t]he Code is far more than a spurious state law created by special interests for their own special protection."¹²⁰ None of the Code's rules for perfection of seller's liens is designed to operate specially in bankruptcy. Only when they operate to protect liens that are essentially secret over prolonged periods should they be read narrowly.

III. Enforcement of the Unpaid Seller's Proprietary Claim to Sold Goods

The unpaid seller who has succeeded in retaining, reclaiming, or reacquiring contract goods has come a long way toward effective protection of his proprietary claim. The fact of his possession validates and perfects his claim to the goods. The question now to be considered is

in early 1978, contains, in addition to sections giving the trustee upset powers (§§ 544, 547, and 548), another section, § 546, that limits the trustee's power to avoid. H.R. 8200, 95th Cong., 1st Sess., 123 CONG. REC. H11746 (daily ed. Oct. 28, 1977). In H.R. 8200, § 546(b) would protect from the trustee in bankruptcy the right of a seller of goods to reclaim sold goods from an insolvent buyer who received goods on credit, so long as such a seller demanded reclamation within 10 days of the debtor's receipt of the goods. If enacted, § 546(b) would solve admirably the problem of § 2-702(3) of the U.C.C.; it would not directly protect the cash seller's right to reclaim under § 2-507(2).

119. It was widely feared that the provisions of Article 9 that protect security interests covering after-acquired property and future advances, often referred to as floating liens, would be deemed to be preferences for the purposes of the Bankruptcy Act. See 2 G. GILMORE, *supra* note 29, at 1309-25. In fact, the case law has accepted the Code plan so uncritically, see, e.g., *DuBay v. Williams*, 417 F.2d 1277 (9th Cir. 1969), that the various proposed new Bankruptcy Acts would revise the law of preference to achieve an intermediate position that would look to the question whether there had been an improvement of the creditor's position at the expense of the debtor's estate. 1977 REPORT, *supra* note 118; 1 1973 REPORT, *supra* note 118, at 201-11. The Reports incorporate the criticism of *DuBay v. Williams* by the Committee on Coordination of the Bankruptcy Act and the Uniform Commercial Code, chaired by Professor Grant Gilmore. 1977 REPORT, *supra* note 118, at 177-79; 1 1973 REPORT, *supra* note 118, at 206-10.

120. *In re Federal's Inc.*, 553 F.2d 509, 517 (6th Cir. 1977). See also Smith, *Title and Right to Possession Under the Uniform Commercial Code*, 10 B.C. INDUS. & COM. L. REV. 39, 53-56 (1968).

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whether, as an Article 2 seller or an Article 9 secured party, ABC in possession may do what it pleases with the contract goods or must account for their proceeds to Family Furniture or takers under Family Furniture. To what extent does Family Furniture's default (or its consent to ABC's possession or retaking) allow ABC to decide whether to retain or to resell the contract sofas? Is ABC or Family Furniture entitled to profit if ABC should happen upon a resale buyer who is willing to pay more for the sofas than the ABC-Family Furniture contract price?

On first reading, the rights of an unpaid seller and a secured creditor after default appear remarkably similar. The provisions on resale under section 2-706¹²¹ and disposition under section 9-504¹²² include require-

121. Section 2-706 provides:

Seller's Resale Including Contract for Resale

(1) Under the conditions stated in Section 2-703 on seller's remedies, the seller may resell the goods concerned or the undelivered balance thereof. Where the resale is made in good faith and in a commercially reasonable manner the seller may recover the difference between the resale price and the contract price together with any incidental damages allowed under the provisions of this Article (Section 2-701), but less expenses saved in consequence of the buyer's breach.

(2) Except as otherwise provided in subsection (3) or unless otherwise agreed resale may be at public or private sale including sale by way of one or more contracts to sell or of identification to an existing contract of the seller. Sale may be as a unit or in parcels and at any time and place and on any terms but every aspect of the sale including the method, manner, time, place and terms must be commercially reasonable. The resale must be reasonably identified as referring to the broken contract, but it is not necessary that the goods be in existence or that any or all of them have been identified to the contract before the breach.

(3) Where the resale is at private sale the seller must give the buyer reasonable notification of his intention to resell.

(4) Where the resale is at public sale

(a) only identified goods can be sold except where there is a recognized market for a public sale of futures in goods of the kind; and

(b) it must be made at a usual place or market for public sale if one is reasonably available and except in the case of goods which are perishable or threaten to decline in value speedily the seller must give the buyer reasonable notice of the time and place of the resale; and

(c) if the goods are not to be within the view of those attending the sale the notification of sale must state the place where the goods are located and provide for their reasonable inspection by prospective bidders; and

(d) the seller may buy.

(5) A purchaser who buys in good faith at a resale takes the goods free of any rights of the original buyer even though the seller fails to comply with one or more of the requirements of this section.

(6) The seller is not accountable to the buyer for any profit made on any resale. A person in the position of a seller (Section 2-707) or a buyer who has rightfully rejected or justifiably revoked acceptance must account for any excess over the amount of his security interest, as hereinafter defined (subsection (3) of Section 2-711).

122. Section 9-504 provides:

Secured Party's Right to Dispose of Collateral After Default; Effect of Disposition

(1) A secured party after default may sell, lease or otherwise dispose of any or all of the collateral in its then condition or following any commercially reasonable preparation or processing. Any sale of goods is subject to the Article on Sales (Article 2).

ments of notice and commercial reasonableness and protect good faith purchasers at a liquidation sale. But closer examination discloses that the Article 2 seller enjoys degrees of freedom that the Article 9 secured party does not share. After default, the Article 2 seller need not permit

The proceeds of disposition shall be applied in the order following to

- (a) the reasonable expenses of retaking, holding, preparing for sale or lease, selling, leasing and the like and, to the extent provided for in the agreement and not prohibited by law, the reasonable attorneys' fees and legal expenses incurred by the secured party;
- (b) the satisfaction of indebtedness secured by the security interest under which the disposition is made;
- (c) the satisfaction of indebtedness secured by any subordinate security interest in the collateral if written notification of demand therefor is received before distribution of the proceeds is completed. If requested by the secured party, the holder of a subordinate security interest must seasonably furnish reasonable proof of his interest, and unless he does so, the secured party need not comply with his demand.

(2) If the security interest secures an indebtedness, the secured party must account to the debtor for any surplus, and, unless otherwise agreed, the debtor is liable for any deficiency. But if the underlying transaction was a sale of accounts or chattel paper, the debtor is entitled to any surplus or is liable for any deficiency only if the security agreement so provides.

(3) Disposition of the collateral may be by public or private proceedings and may be made by way of one or more contracts. Sale or other disposition may be as a unit or in parcels and at any time and place and on any terms but every aspect of the disposition including the method, manner, time, place and terms must be commercially reasonable. Unless collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market, reasonable notification of the time and place of any public sale or reasonable notification of the time after which any private sale or other intended disposition is to be made shall be sent by the secured party to the debtor, if he has not signed after default a statement renouncing or modifying his right to notification of sale. In the case of consumer goods no other notification need be sent. In other cases notification shall be sent to any other secured party from whom the secured party has received (before sending his notification to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. The secured party may buy at any public sale and if the collateral is of a type customarily sold in a recognized market or is of a type which is the subject of widely distributed standard price quotations he may buy at private sale.

(4) When collateral is disposed of by a secured party after default, the disposition transfers to a purchaser for value all of the debtor's rights therein, discharges the security interest under which it is made and any security interest or lien subordinate thereto. The purchaser takes free of all such rights and interests even though the secured party fails to comply with the requirements of this Part or of any judicial proceedings

- (a) in the case of a public sale, if the purchaser has no knowledge of any defects in the sale and if he does not buy in collusion with the secured party, other bidders or the person conducting the sale; or
- (b) in any other case, if the purchaser acts in good faith.

(5) A person who is liable to a secured party under a guaranty, indorsement, repurchase agreement or the like and who receives a transfer of collateral from the secured party or is subrogated to his rights has thereafter the rights and duties of the secured party. Such a transfer of collateral is not a sale or disposition of the collateral under this Article.

The effect of the 1972 amendment is to make it less burdensome for the senior secured lender to deal with junior secured lenders, because notification to them is now required only if they have given the senior secured lender written notice of a claim of interest in the collateral.

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redemption,¹²³ need not resell,¹²⁴ need not account for resale profits.¹²⁵ Under Article 2, the seller, proudly revested with title,¹²⁶ has full authority to dispose of his goods. The Article 9 secured party, by contrast, is a kind of trustee for the benefit of those who have a stake in the secured collateral, the debtor and junior secured parties. Repossession does not definitively terminate the secured transaction and does not extinguish other secured claims, junior or senior. The debtor and junior secured parties are entitled to notification of the repossessing secured party's plans for the secured collateral,¹²⁷ to participation in decisions about the collateral,¹²⁸ and to an accounting of the proceeds generated by the sale of the collateral.¹²⁹ In either article, ABC is entitled first to be made whole and then to have the first say on how to proceed. But the road to correct liquidation under Article 9 is filled with potholes.¹³⁰

It is possible to argue that, because they better protect a wide range of important commercial interests, Article 9 principles should always apply whenever lien creditors or junior secured parties have a stake in liquidation after default. The permissive rules of Article 2, which seem to provide the seller many options and only limited constraints, should perhaps be restricted, as are other Article 2 rules,¹³¹ to situations in

123. Although upon default sellers have a general right to cure, *see* § 2-508, buyers do not. Section 2-511(2) allows a buyer who tenders payment by check additional time to tender cash when the seller so insists; no other provision in Article 2 alters the time or manner of the buyer's contract performance. Even the sections that govern anticipatory repudiation, which encourage retraction of repudiation, do not require the aggrieved seller to permit reinstatement of the contract. *See* §§ 2-610, 2-611, and especially 2-610(b). These provisions are discussed in Peters, *supra* note 8, at 263-67.

124. The seller who does not resell is entitled to damages for nonacceptance measured by the difference between the market and contract prices at the time and place for tender. *See* § 2-708(1). The sections of Part 7 of Article 2, and their drafting history, strongly suggest that the seller can elect this measurement of damages whether or not he actually resells the contract goods. *See* Peters, *supra* note 8, at 260-61. *Contra*, J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE 223-24 (1972).

125. *See* § 2-706(6). If profits result not from changes in the market, but rather from retention of the buyer's down payment, § 2-718(2) and (3) may require accounting for these moneys. The relationship of § 2-718(2) and (3) to resale by a repossessing seller, rather than by a withholding seller, is unclear.

126. *See* § 2-401(4).

127. *See* § 9-504(3).

128. *See* §§ 9-505(2) (junior lienor may require resale of collateral), 9-506 (junior lienor may redeem collateral).

129. *See* § 9-504(1)(c).

130. A secured party who fails to comply with the default rules of Article 9 is liable in damages, under § 9-507(1), to "the debtor or any person entitled to notification or whose security interest has been made known to the secured party" for "any loss caused by a failure to comply." In addition, noncompliance jeopardizes the secured party's claim to a deficiency under § 9-504(2).

131. *See, e.g.*, § 2-507(2) (describing right of cash sale buyer to retain goods as "his right as against the seller" (emphasis added)). In its entirety, § 2-507(2) provides:

Where payment is due and demanded on the delivery to the buyer of goods or

which there are no interests other than those of the immediate buyer and seller. There is support for this argument in section 2-403, which, as one of a variety of provisions subordinating immediate-party claims to third-party intervenors, refers to Article 9 as the source of "rights" for lien creditors and other purchasers.¹³² The provisions of Article 9 on repossession and liquidation do afford affirmative rights to junior lienors who are purchasers¹³³ in the nomenclature of the Code, although lien creditors must look to local process to enforce their rights.¹³⁴ On the other hand, to the extent that Article 9 is more solicitous of Family Furniture as a debtor than is Article 2 of Family Furniture as a buyer, it is somewhat odd to allow access to these provisions to turn on the happenstance of third-party claims under Family Furniture. Furthermore, Article 9 itself, in section 9-113 on security interests arising under the Article on Sales, relegates possessory hybrid security interests to Article 2 rules on default. Thus section 2-403(4) points to Article 9, and section 9-113(c) points to Article 2.

A concrete example may illuminate the dilemma that these sections create. Assume that Family Furniture is indebted to a lender with a

documents of title, his right as against the seller to retain or dispose of them is conditional upon his making the payment due.

The third-party implications of the cash sale are dealt with in § 2-403(1):

A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

- (a) the transferor was deceived as to the identity of the purchaser, or
- (b) the delivery was in exchange for a check which is later dishonored, or
- (c) it was agreed that the transaction was to be a "cash sale", or
- (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

132. Section 2-403(4) provides:

The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9), Bulk Transfers (Article 6) and Documents of Title (Article 7).

133. The definition of "purchaser" in § 1-201(33) informatively provides:

"Purchaser" means a person who takes by purchase.

"Purchase" in § 1-201(32) has affirmative content:

"Purchase" includes taking by sale, discount, negotiation, mortgage, pledge, lien, issue or re-issue, gift or any other voluntary transaction creating an interest in property.

Junior lienors who notify unpaid sellers of their claims therefore have a toehold in both Article 2 and Article 9.

134. Lien creditors are not within the class of beneficial intervenors in Part V of Article 9. Their claims, preserved through § 9-311, must be exercised through whatever rights local law makes available. Section 9-311 provides:

Alienability of Debtor's Rights: Judicial Process

The debtor's rights in collateral may be voluntarily or involuntarily transferred (by way of sale, creation of a security interest, attachment, levy, garnishment or other judicial process) notwithstanding a provision in the security agreement prohibiting any transfer or making the transfer constitute a default.

valid and perfected security interest in all of Family Furniture's sofas, including sofas subsequently to be acquired from such as ABC. Once ABC so designates the sofas in its contract with Family Furniture that they become identified, Family Furniture acquires rights in this collateral, and the interest of its secured lender attaches. So long as ABC remains in possession, it is likely to have priority over the lender's after-acquired property interest.¹³⁵ Should ABC be required to consult with this lender if it intends simply to retain the sofas without a statutory resale? Should the lender be entitled to excess proceeds if the sofas can be resold above contract price?

Here again the method of choice appears to be to avoid categorical resolution of all cases as if they were all part of a unitary whole. The seller who has never relinquished possession should not be burdened by his buyer's other creditors.¹³⁶ Once the seller has delivered the contract goods, unconditionally or under a merely contractual reservation of title, on the other hand, his reacquisition should not divest rights that vested fully during the buyer's possessory interlude.¹³⁷ As usual, delivery on special condition, under a cash sale or a sale induced by misrepresentation of solvency, creates the most difficulty. In these transactions, for which Article 2 provides reclamation as an exclusive remedy, accountability after reclamation seems at violence with the language of section 2-702(3)¹³⁸ and yet totally consistent with the equitable nature of the reclaiming seller's underlying claim. In the absence of firm guidance from the Code or from prior common law, perhaps all of these conflicts should be resolved on the basis of the particular equities of the particular parties in the particular circumstances in which they find themselves.

IV. The Priority of the Unpaid Seller's Rights against Other Takers from the Buyer

The seller's proprietary claim to contract goods, even if valid, perfected, and enforceable, may nonetheless be subordinated to the claims

135. Problems of priority are explored at pp. 947-83 *infra*.

136. From a practical point of view, the 1972 Code, which requires junior lienors first to locate and notify the seller *qua* secured creditor, diminishes the risk that withholding sellers will become enmeshed in junior liens.

137. See pp. 953, 963 *infra*.

138. Section 2-702(3) provides, for the defrauded seller:

The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403).

Successful reclamation of goods excludes all other remedies with respect to them.

There is no parallel textual limitation on reclamation pursuant to a cash sale under § 2-507(2).

of competing third parties who take through Family Furniture. This, the question of priorities, is the last and most difficult inquiry concerning the security implications of the sales transaction. The concept of priorities is, of course, primarily associated with Article 9. Significantly, section 9-113 appears to preserve Article 9 priority rules in their entirety even for possessory security interests "arising solely under the Article on Sales."¹³⁹ Although section 9-113 incorporates the governing provisions of Article 2 for some cases, as in the determination of "the rights of the secured party on default," there is no comparable cross-reference to Article 2 provisions on priority. While it is true that Article 2 has no section denominated "priorities," section 2-403 contains a form of ordering for the cases within its bounds that is indistinguishable from the ordering scheme we customarily consider a priorities framework.¹⁴⁰

The sales contract between Family Furniture and ABC creates opportunities for a variety of competing claimants under Family Furniture, any or all of whom may contest ABC's rights to the contract sofas. This array of claimants to priority is worth cataloguing. Family Furniture, upon entry into the contract with ABC, may enter into resale contracts with its customers, who will certainly qualify as buyers¹⁴¹ and perhaps as buyers in the ordinary course of business.¹⁴² ABC may also be confronted by any one of several types of financiers of Family Furniture. The first is a secured lender to Family Furniture with an after-acquired property interest in inventory. At some point in the preceding five years, Family Furniture may have entered into a secured transaction whose collateral encompassed present and after-acquired furniture, adequately described to include ABC's forthcoming shipment.¹⁴³ If this secured transaction is valid and perfected, it will automatically attach and bring the ABC sofas within its ambit as soon as

139. Section 9-113. See J. WHITE & R. SUMMERS, *supra* note 124, at 781; Hogan, *The Marriage of Sales to Chattel Security in the Uniform Commercial Code: Massachusetts Variety*, 38 B.U.L. REV. 571, 583-84 (1958).

140. The Code nowhere defines a "priority." Taking it, however, to refer to the result that is achieved upon the subordination of one interest to another, it is clear that § 2-403 provides rules for determining which out of several delimited interests is superior to the other interests in the same collateral. As such, it seems appropriate to refer to the rules of § 2-403 as "priority" rules.

141. Section 2-103(1)(a) provides:

In this Article unless the context otherwise requires. . . . "Buyer" means a person who buys or contracts to buy goods.

142. Section 1-201(9) provides in part that:

"Buyer in ordinary course of business" means 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 but does not include a pawnbroker.

143. Sections 9-204(1), 9-403(2).

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Family Furniture acquires rights therein.¹⁴⁴ The second financier is an enabling lender, that is, a lender who finances this very acquisition of sofas, for which a security agreement is negotiated, a financing statement filed, and value given. Once again, as soon as Family Furniture acquires rights in the sofas, this security interest is fully perfected.¹⁴⁵ Moreover, if this enabling lender ensured through adequate tracing that his funds were actually used to acquire rights in the new collateral coming from ABC, he would qualify as a purchase money lender.¹⁴⁶ Finally, ABC may also be confronted with the claims of other lenders who have neither an after-acquired property interest nor an enabling interest, and who are therefore not technically direct financiers, but who have taken and perhaps perfected a security interest in the sofas at or after the time when Family Furniture acquires rights in those sofas.

All of these competitors except the buyer are Article 9 secured creditors¹⁴⁷ as well as Article 2 purchasers.¹⁴⁸ The similarities between them suggest that they be examined together, after an inquiry into the status of the historically favored buyer in ordinary course.

A. *Buyer in the Ordinary Course of Business*

Resale customers of Family Furniture are significant primarily when they qualify as buyers in the ordinary course of business. The buyer in the ordinary course of business is, according to section 1-201(9),

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 but does not include a pawnbroker.

Both pre-Code law and the Code itself extend significant protection to such buyers against the claims of competing third parties.¹⁴⁹

144. Section 9-203.

145. *Id.*

146. Section 9-107(b). On the subject of tracing, see 2 G. GILMORE, *supra* note 29, at 781-82; Jackson & Kronman, *supra* note 100, at 27-31.

147. Sections 1-201(37), 9-102, 9-105(1).

148. Section 1-201(32).

149. 2 G. GILMORE, *supra* note 29, at 678-79:

A general proposition, which is as true as any general proposition can be, is that the good faith buyer in ordinary course of business will take free of any inventory security interest, no matter how cunningly the security agreement may have been drafted. All modern statutes which authorize inventory financing arrangements—such as the Uniform Trust Receipts Act, the Factor's Lien Acts and Article 9 of the Code—expressly provide that such buyers take free of the security interest. The older chattel

1. *ABC in Possession Before Delivery*

Even while ABC remains in possession of the sofas—during the period after identification of the sofas to the contract and before their delivery to Family Furniture—resale claimants may arise. Family Furniture, certainly a person in the business of selling goods of that kind, may well enter into resale contracts before it takes delivery of the sofas and may even arrange for direct delivery from ABC to its customers. Family Furniture's customers are likely to know little and care less about the contractual arrangement between ABC and Family Furniture. There is nothing explicit in the Code's definition of buyer in ordinary course that would require that such a buyer take delivery of the goods.¹⁵⁰ Early drafts of the Code seemed to couple the definition of a buyer in ordinary course with delivery. Section 2-403(4) of the 1950 draft defined such a buyer as one "to whom goods are shipped pursuant to a pre-existing contract or one to whom they are delivered on credit."¹⁵¹ But this language was dropped when the definition was moved to Article 1.¹⁵² Delivery to Family Furniture's resale customers could now be made a prerequisite only by implication. But that implication cannot universally be correct, since the same Article 1 definition is expressly coupled in the priority scheme of Article 7 with an explicit requirement that the buyer also take delivery.¹⁵³ Although the implication might be drawn on a case-by-case basis from the open-ended criteria of buying "in ordinary course" and "in good faith," even this reading is inconsistent with Article 7. Family Furniture's resale customers can be buyers in the ordinary course of business *in absentia*.¹⁵⁴

The question of possession by a buyer in ordinary course is not dispositive on the priority between ABC and Family Furniture's customers. The issue of priority must also take into account whether

mortgage acts (in states where they were construed to allow inventory financing) typically contained no such express provision; indeed, most of these statutes proceeded on the assumption that a properly filed mortgage was "good against the world." Nevertheless, even under such chattel mortgage acts the courts regularly and with remarkably few deviations protected the buyer and held against the mortgagee.

150. See note 142 *supra*.

151. U.C.C. § 2-403(4) (Spring 1950 draft). No definition of "buyer in ordinary course of business" exists in the May 1949 draft of the U.C.C.

152. The definition "with revisions" was moved to Article 1 in the September 1950 revisions to the U.C.C. and appeared in its present form as § 1-201(9) in the 1951 Proposed Final Draft.

153. Section 7-504(2)(b).

154. 2 G. GILMORE, *supra* note 29, at 696; Skilton, *Buyer in Ordinary Course of Business Under Article 9 of the Uniform Commercial Code (and Related Matters)*, 1974 Wis. L. REV. 1, 20. But see Smith, *supra* note 120, at 61.

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Family Furniture must be in possession of the sofas before it can convey them to a buyer in ordinary course. Unfortunately, this issue of priority appears on first glance to be dramatically different under Articles 2 and 9. Under section 2-403, the professional status of the dealer and the innocence of the buyer will defeat the prior rights only of a person who has delivered goods to the dealer or acquiesced in the dealer's continued possession.¹⁵⁵ If Family Furniture never received the sofas from ABC, section 2-403 gives it no power to transfer ABC's rights to them. The parallel section in Article 9, section 9-307, has no such requirement of delivery.¹⁵⁶ Moreover, if ABC's seller's lien is an Article 9 security interest for priority purposes, as section 9-113 seems to require,¹⁵⁷ then a buyer in ordinary course apparently prevails despite perfection and despite his knowledge of the existence of the security interest. Although the Code does not take up the question of whether a security interest "arising solely under" Article 2 for purposes of section 9-113 is to be considered a security interest "created by his seller" for purposes of section 9-307, the thrust of section 9-307's limitation seems directed not at the hybrid security interest brought into Article 9 through section 9-113, but rather at the question of the parties between whom the security interest arose.¹⁵⁸

This literal approach to section 9-307, however, may not be dispositive. Comment 1 to section 9-307 hints that section 2-403, not section 9-307, should control.¹⁵⁹ Moreover, although "delivery" may not be an

155. Section 2-403(2). The definition of "entrusting" "includes any delivery and any acquiescence in retention." Section 2-403(3). There is no reason to think that it is possible to have entrusting without possession. See *DePaulo v. Williams Chevrolet-Cadillac, Inc.*, 10 LEBANON COUNTY [PA.] LEGAL J. 465 (1965). See also UNIFORM SALES ACT § 25. Although the definition of "purchaser" in § 1-201(33) is broad enough to include a buyer in ordinary course, there are sufficient reasons not to read the rights of a buyer in ordinary course under § 2-403(1) as broader than the rights accorded such a buyer under § 2-403(2). See note 178 *infra*.

156. Since § 9-307 states only that "[a] buyer in ordinary course of business . . . takes free of a security interest created by his seller," there is nothing that would expressly limit the applicability of that section to situations in which the seller already had possession. See 2 G. GILMORE, *supra* note 29, at 696.

157. See pp. 916-17 *supra*.

158. Skilton, *supra* note 154, at 7-8; cf. R. HENSON, *supra* note 29, at 109 n.91.

159. The last paragraph of Comment 1 to § 9-307 observes that "Article 2 (Sales) states general rules on purchase of goods from a seller with defective or voidable title (Section 2-403)." The Code, however, is replete with unclear references on this topic. For example, Comment 2 to § 2-403 observes that:

As to entrusting by a secured party, subsection (2) is limited by the more specific provisions of Section 9-307(1), which deny protection to a person buying farm products from a person engaged in farming operations.

And Comment 4 to § 9-306 suggests that the distinction is one of technical application. See generally J. WHITE & R. SUMMERS, *supra* note 124, at 945-46. Compare *National Shawmut Bank v. Jones*, 108 N.H. 386, 236 A.2d 484 (1967) with *Charles S. Martin Distrib. Co. v. Banks*, 111 Ga. App. 538, 142 S.E.2d 309 (1965) and *Sterling Acceptance Co. v. Grimes*, 194 Pa. Super. 503, 168 A.2d 600 (1961).

aspect of buying in ordinary course, passage of title—a generally discredited indicium under the Code—arguably is.¹⁶⁰ Section 1-201(9) defines a “[b]uyer in ordinary course of business” as one who takes by way of “sale,”¹⁶¹ which section 2-106(1) defines in turn as “the passing of title from the seller to the buyer for a price (Section 2-401).”¹⁶² Both section 2-106(1) and section 2-401 are Article 2 definitions, applicable to Article 9 by analogy rather than by fiat; indeed, the use of the term “buyer in ordinary course” in section 2-403(2) suggests that actual passage of title is not necessary before such a buyer can emerge even in Article 2.¹⁶³ In any case, this definitional ambiguity can be used so as to take into account a variety of equitable factors. With ABC still in possession, the battleground will unmistakably be section 9-307(1),¹⁶⁴ and it appears that this definitional flexibility is available to reach an appropriate result.¹⁶⁵ Alternatively, concepts like good faith or ordinary course of business are sufficiently flexible that a court can accommodate

160. See *Chrysler Corp. v. Adamatic, Inc.*, 59 Wis. 2d 219, 238-39, 208 N.W.2d 97, 106 (1973); *Jackson & Kromman*, *supra* note 100, at 23; *Skilton* *supra* note 154, at 17-19.

161. Section 1-201(9) states:

“Buyer in ordinary course of business” means 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 but does not include a pawnbroker. All persons who sell minerals or the like (including oil and gas) at wellhead or minehead shall be deemed to be persons in the business of selling goods of that kind. “Buying” may be for cash or by exchange of other property or on secured or unsecured credit and includes receiving goods or documents of title under a pre-existing contract for sale but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt.

Although not entirely clear, the language of “sale” and “buys” would not seem to cover a “contract to sell.” Cf. *Chrysler Corp. v. Adamatic, Inc.*, 59 Wis. 2d 219, 238-39, 208 N.W.2d 97, 106 (1973) (discussing whether one can become buyer in ordinary course merely by entering into contract to buy or sell).

162. Perhaps contrary to this is § 2-103(1), which states that “[i]n this Article unless the context otherwise requires (a) ‘Buyer’ means a person who buys or contracts to buy goods.” It is not an easy jump, however, to conclude that the definition of the term “buyer” should influence the definition of the separate term “buyer in ordinary course.”

163. Since an “entrusting” includes retention of possession without title, it would be impossible for such an entrustee to pass title. That is, if title were indeed crucial, no buyer in the ordinary course of business could ever arise until *after* § 2-403(2) had operated, which it could not do for lack of a buyer in the ordinary course of business. Such an absurdity, which would reduce § 2-403(2) to a nullity, suggests that, at least here, title cannot be decisive.

164. As we have suggested, *see* pp. 950-51 *supra*, § 2-403(2) will be inoperative until Family Furniture acquires possession.

165. Cf. *Chrysler Corp. v. Adamatic, Inc.*, 59 Wis. 2d 219, 240, 208 N.W.2d 97, 107 (1973):

While the Commercial Code, as pointed out above, does not require that in all cases the buyer actually take delivery in order to have a buyer in ordinary course of business status, sound policy considerations in the instant situation would seem to dictate that the rights of a secured creditor ought not be impaired in the absence of a physical transfer or assignment of the goods.

See Kripke, *Should Section 9-307(1) of the Uniform Commercial Code Apply Against a Secured Party in Possession?*, 33 BUS. LAW. 153 (1977).

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a variety of outcomes that turn on a comparison of equities, rather than on absolute priorities. Still, however limited ABC's risk may be, from time to time, and case by case, that risk is unmistakably larger under Article 9 than it is under Article 2.

2. *ABC Delivers Goods Unconditionally or on Special Condition*

Delivery of the sofas to Family Furniture makes all the difference to the position of a buyer in ordinary course. After delivery, both section 2-403(2) and section 9-307(1) provide that the buyer in ordinary course prevails.¹⁶⁶ Neither games with title¹⁶⁷ nor a transaction that is a cash sale or fraudulent sale¹⁶⁸ makes any difference. Family Furniture has been entrusted with possession through "any delivery" and is thereby able "to transfer all rights . . . to a buyer in ordinary course of business."

3. *ABC Reacquires Goods from Family Furniture*

If ABC reacquires the sofas from Family Furniture at a time when Family Furniture has entered into contracts with would-be buyers in the ordinary course of business, the apparent priority given a buyer in ordinary course under sections 2-403(2) and 9-307(1) cannot be considered apart from the question of the buyer's remedies. Whether or not, as Professor Corbin often reminded us, "possession is nine points in law," it is significant that ABC, and not Family Furniture, has possession. It is helpful to recall that the contract rights of buyers are rarely proprietary. Even a buyer with title cannot ordinarily replevy goods or specifically require their delivery unless they are unique.¹⁶⁹

166. The buyer in the ordinary course of business prevails both under § 2-403(2), because Family Furniture has been entrusted with possession and is entitled to "transfer all rights of the entruster," and under § 9-307(1), because he "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." Although, as we noted, *see pp. 951-52 supra*, the fact that title has not yet passed might be used to suggest that § 9-307(1) is not triggered, such a literal reading should be rejected here, where there is clearly ample reason to have § 9-307(1) reach a result harmonious with § 2-403(2).

167. Section 2-403(3) makes clear that subsection (2) applies "regardless of any condition expressed between the parties to the delivery or acquiescence," and § 2-401(1) itself limits retention of title after delivery to the "reservation of a security interest."

168. Section 2-403(3) makes clear that subsection (2) applies "regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be larcenous under the criminal law." Comment 2 notes that "[t]he principle is extended in subsection (3) to fit with the abolition of the old law of 'cash sale' by subsection (1)(c)."

169. Section 2-711(2) states:

Where the seller fails to deliver or repudiates the buyer may also

- (a) if the goods have been identified recover them as provided in this Article (Section 2-502); or
- (b) in a proper case obtain specific performance or replevy the goods as provided in this Article (Section 2-716).

Thus unless something extraordinary distinguishes ABC's sofas, Family Furniture's failure to execute the sales contract relegates its customer to a claim for monetary damages;¹⁷⁰ neither prepayment by the customer nor the insolvency of Family Furniture automatically creates proprietary rights in the customer. If ABC has no notice of the claims of Family Furniture's customers, its good faith dealings with Family Furniture should therefore be protected. Even though its reacquisition is technically not a sale,¹⁷¹ ABC should have no greater duty of inquiry than would be imposed on any other party dealing with a seller in possession of sold goods. If ABC has actual notice or if its retaking otherwise does not comport with the requirements of good faith, then principles of estoppel would override ABC's normal claim to priority.¹⁷² In the majority of cases, however, latent claims of ownership should

Section 2-716 states:

Buyer's Right to Specific Performance or Replevin

(1) Specific performance may be decreed where the goods are unique or in other proper circumstances.

(2) The decree for specific performance may include such terms and conditions as to payment of the price, damages, or other relief as the court may deem just.

(3) The buyer has a right of replevin for goods identified to the contract if after reasonable effort he is unable to effect cover for such goods or the circumstances reasonably indicate that such effort will be unavailing or if the goods have been shipped under reservation and satisfaction of the security interest in them has been made or tendered.

Section 2-502, the other provision referred to in § 2-711(2), is a very narrow provision, effective only "if the seller becomes insolvent within ten days after receipt of the first installment on their price." It reads, in full:

Buyer's Right to Goods on Seller's Insolvency

(1) Subject to subsection (2) and even though the goods have not been shipped a buyer who has paid a part or all of the price of goods in which he has a special property under the provisions of the immediately preceding section may on making and keeping good a tender of any unpaid portion of their price recover them from the seller if the seller becomes insolvent within ten days after receipt of the first installment on their price.

(2) If the identification creating his special property has been made by the buyer he acquires the right to recover the goods only if they conform to the contract for sale.

Even if a buyer could meet the stringent 10-day precondition, § 2-502(2) applies only where the buyer has "a special property under" § 2-501, thus further limiting the proprietary hopes of a buyer.

170. Assuming that the buyer cannot utilize § 2-502 or § 2-716, his remedies are those specified in § 2-711(1):

Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (Section 2-612), the buyer may cancel and whether or not he has done so may in addition to recovering so much of the price as has been paid

(a) "cover" and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or

(b) recover damages for non-delivery as provided in this Article (Section 2-713).

171. Section 2-401(4).

172. Section 1-103 explicitly preserves "principles of law and equity, including . . . the law relative to . . . estoppel."

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not stand in the way of the reasonable implementation or modification of the contract between ABC and Family Furniture.¹⁷³

In sum, it would appear that delivery is the decisive fact for the priority status of a buyer in ordinary course. When Family Furniture is in possession, a buyer in ordinary course is a sure winner. When ABC is in possession, either before delivery or after reacquisition, it should prevail, unless equitable notions of estoppel and good faith persuade a court otherwise.

B. *Purchasers*

Analysis of the priority rights of other purchasers from Family Furniture tends to proceed from the assumption of a baseline established by the priority rights of a buyer in ordinary course. Both under pre-Code law and the Code itself, the status of a buyer in ordinary course is as favorable as that accorded to any third-party claimant.¹⁷⁴ As one moves beyond that baseline to a more detailed inquiry, however, the answers are not so easy. Purchasers, even secured parties, come in a variety of hues, a situation that is reflected in the elaborate scheme of priority rules enunciated in Article 9. Not surprisingly, then, while delivery should remain a key variable, other significant factors will affect the resolution of priority conflicts when Family Furniture is in possession.

1. *ABC in Possession Before Delivery*

From what has been said, ABC should, before delivery, have priority over the secured parties claiming through Family Furniture. Such purchasers should not prevail when buyers in ordinary course do not.¹⁷⁵ Here it is the language of Article 2 that creates the initial difficulty. The opening sentences of section 2-403(1), by contrast with the later sentences and subsections, do not require that a good faith purchaser for value have purchased from a person in possession.¹⁷⁶ This omission

173. Cf. § 2-402(2) (continuation of state "ostensible ownership" laws, reflecting continuing mistrust of latent ownership claims). See Jackson & Kronman, *supra* note 100, at 9-10. See also pp. 972-73 *infra*.

174. As for the Code, see Skilton, *supra* note 154, at 2. As for pre-Code law, see UNIFORM CONDITIONAL SALES ACT § 9; UNIFORM SALES ACT §§ 24-25; UNIFORM TRUST RECEIPTS ACT § 9(2). See also note 149 *supra*.

175. See pp. 950-53 *supra*.

176. Section 2-403(1) reads:

A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

(a) the transferor was deceived as to the identity of the purchaser, or

cannot be read to impair ABC's rights. On one level, it is possible to avoid the issue by manipulation of title: despite identification, Family Furniture probably has neither partial nor voidable title, and purchasers from Family Furniture are thus disqualified from protection against ABC.¹⁷⁷ On another level, it is sensible to read section 2-403 as part of a unitary whole, with trade-offs that respond to a variety of equitable claims. There is no discernible reason of policy to put ABC at risk against mere purchasers and ordinary buyers when even buyers in the ordinary course of business must prove delivery in order to defeat ABC.¹⁷⁸ Furthermore, the drafting style of the early part of

- (b) the delivery was in exchange for a check which is later dishonored, or
- (c) it was agreed that the transaction was to be a "cash sale", or
- (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

177. See *Toyomenka, Inc. v. Mount Hope Finishing Co.*, 432 F.2d 722, 728 (4th Cir. 1970).

178. As we have seen, a buyer in ordinary course cannot prevail before his seller acquires possession under § 2-403(2). See pp. 950-51 *supra*; cf. Kripke, *supra* note 165, at 157 (arguing that, in context of more than one isolated section, apparent ownership through possession should be read into § 9-307(1) to harmonize it with 2-403(2)).

A review of the drafting history of § 2-403(1) suggests that the requirement of delivery to a person with "voidable title," expressly set forth in that subsection's third sentence, should likewise be read into the preceding sentence. The predecessor to §§ 2-403(2) and (3) first made its appearance in the 1950 draft of the Code. No provision, however, dealt with "voidable title" at that time, and a comment observed that "[s]ince the great bulk of claims of 'prior owners' are those of secured lenders, the rights of purchasers other than buyers in ordinary course are left to the Article regulating the relations between secured lenders and third parties (Article 9)." Section 2-403, Comment 4 (1950 draft).

The voidable title concept was inserted in the 1952 draft of the Code, reading, as it does today, "[a] person with voidable title has power to transfer a good title to a good faith purchaser for value." Section 2-403(1) (1952 draft). There is no indication, however, that this insertion was intended to broaden the protection accorded either to buyers in ordinary course under § 2-403(2) or to purchasers in general. McDonnell, *The Floating Lienor as Good Faith Purchaser*, 50 S. CAL. L. REV. 429, 449 (1977) ("it is more likely that the drafters of the Code, having decided to emphasize the entrustment concept and having encountered difficulties in reducing the nuances of bona fide purchase to statutory form, had decided to leave the latter doctrine where it stood in the case law"); cf. 1 NEW YORK LAW REVISION COMMISSION FOR 1955, STUDY OF THE UNIFORM COMMERCIAL CODE 227 (1955) (discussing the protection given to a "buyer in ordinary course of business" in Article 2; refers only to § 2-403). The New York Law Revision Commission apparently read § 2-403(1) in this manner, for it suggested adding the following provision to that subsection:

When a transferor has a right to recover goods from a transferee, *the transferee's title shall be deemed to be voidable rather than void if the transferor delivered the goods to the transferee pursuant to a transaction intended by the transferor to transfer ownership in the goods. This rule includes but is not limited to cases where*

- (a) the transferor is deceived as to the identity of the transferee, or
- (b) the transferor delivers the goods in exchange for a check which is not collected because of insufficient funds;
- (c) the delivery of the goods is procured through fraud punishable as larcenous under the criminal law.

NEW YORK LAW REVISION COMMISSION FOR 1956, REPORT RELATING TO THE UNIFORM COMMERCIAL CODE 383 (1956) (emphasis added). This proposal clearly viewed the issue of voidable title as depending on delivery of the goods to the transferee. Far from repudiating this reading, the Permanent Editorial Board, in revising § 2-403(1) in 1956 for what be-

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section 2-403(1) is precisely what one would expect for an open-ended rule that directs courts to inquire into comparative equities. The drafters' views about the indeterminacy of title are well matched by their description of the good faith purchaser. Good faith, under Article 2, has a range of meaning that depends on the commercial competence of the actor whose conduct is under scrutiny.¹⁷⁹ The relationship of good faith to notice of claims of ownership is normally articulated as a holy trinity of good faith, lack of notice, and value.¹⁸⁰ Section 2-403(1) speaks only of good faith and value.¹⁸¹ But there is no reason not to consider notice an aspect of good faith¹⁸² and considerable advantage in thus avoiding hard-line distinctions between knowledge, notice, and duty to inquire.¹⁸³

came the 1957 Official Text of the Code, acknowledged that its changes were made "[f]ollowing suggestions of the New York Commission . . ." 1956 RECOMMENDATIONS OF THE EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE 53 (1957).

179. Section 1-201(19) is an open-ended definition in which "[g]ood faith' means honesty in fact in the conduct or transaction concerned." Section 2-103(1)(b) adds an extra requirement for a merchant: "'Good faith' in the case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." See *Sherrock v. Commercial Credit Corp.*, 277 A.2d 708 (Del. Super. Ct. 1971), *rev'd on other grounds*, 290 A.2d 648 (Del. 1972).

180. The definition of a "buyer in ordinary course of business," for example, requires that the party be "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." Section 1-201(9). For other examples, see §§ 2-403(2), 3-302, 6-110, 8-301, 8-302, 9-301(1), 9-307(2), 9-308(a).

181. Section 2-403(1) states only:

A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

- (a) the transferor was deceived as to the identity of the purchaser, or
- (b) the delivery was in exchange for a check which is later dishonored, or
- (c) it was agreed that the transaction was to be a "cash sale", or
- (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

A "purchaser" is defined in § 1-201(33) only as "a person who takes by purchase"; while § 1-201(32) states that "'[p]urchase' includes taking by sale, discount, negotiation, mortgage, pledge, lien, issue or re-issue, gift or any other voluntary transaction creating an interest in property." See *Stowers v. Mahon (In re Samuels & Co.)*, 526 F.2d 1238, 1243-44 (5th Cir.) (en banc), *cert. denied*, 429 U.S. 834 (1976).

182. See, e.g., *Ranchers & Farmers Livestock Auction Co. v. Honey*, 552 P.2d 313 (Colo. Ct. App.), *cert. dismissed*, 553 P.2d 799 (1976) (en banc); Farnsworth, *Good Faith Performance and Commercial Reasonableness Under the Uniform Commercial Code*, 30 U. CHI. L. REV. 666, 668 (1963).

183. Section 1-201(25) states:

A person has "notice" of a fact when

- (a) he has actual knowledge of it; or
- (b) he has received a notice or notification of it; or
- (c) from all the facts and circumstances known to him at the time in question he has reason to know that it exists.

See, e.g., *National Car Rental v. Fox*, 18 Ariz. App. 160, 500 P.2d 1148 (1972); *Greater Louisville Auto Auction, Inc. v. Ogle Buick, Inc.*, 387 S.W.2d 17 (Ky. 1965); *Jordan v.*

Do the priority provisions of Article 9 upset ABC's largely favorable, although open-ended, solution under Article 2? Here it is necessary to separate the categories of purchasers. Article 9 provides that "conflicting security interest[s]," including interests that arise through an after-acquired property clause, are to be subordinated to a perfected purchase money security interest in the same collateral.¹⁸⁴ ABC is probably protected by this priority scheme. Its hybrid security interest either is, or is enough like, an Article 9 purchase money security interest to entitle it to such status.¹⁸⁵ Its continued possession qualifies as perfection,¹⁸⁶ and section 9-113 explicitly negates the requirement of a filed financing statement.¹⁸⁷ Since the sofas are inventory from Family Furniture's point of view, however, ABC's priority might also depend on

Butler, 182 Neb. 626, 634, 637, 156 N.W.2d 778, 783, 785 (1968); Landrum v. Armbruster, 28 N.C. App. 250, 254, 220 S.E.2d 842, 844 (1976); McDonnell, *supra* note 178, at 457. Lack of knowledge (or of reason to know) of outstanding claims was necessary to the common law bona fide purchaser. See Stowers v. Mahon (*In re Samuels & Co.*), 526 F.2d 1238, 1243 (5th Cir.) (en banc), *cert. denied*, 429 U.S. 834 (1976); Johnson v. Robinson, 203 F.2d 135, 136 (5th Cir. 1953); UNIFORM SALES ACT § 24; F. TIFFANY, HANDBOOK OF THE LAW OF SALES 188-97 (2d ed. 1908); Note, *What Constitutes a Bona Fide Purchaser for Value Without Notice?*, 36 COLUM. L. REV. 638 (1936).

184. Sections 9-312(3) and (4) read:

(3) A perfected purchase money security interest in inventory has priority over a conflicting security interest in the same inventory and also has priority in identifiable cash proceeds received on or before the delivery of the inventory to a buyer if

- (a) the purchase money security interest is perfected at the time the debtor receives possession of the inventory; and
- (b) the purchase money secured party gives notification in writing to the holder of the conflicting security interest if the holder had filed a financing statement covering the same types of inventory (i) before the date of the filing made by the purchase money secured party, or (ii) before the beginning of the 21 day period where the purchase money security interest is temporarily perfected without filing or possession (subsection (5) of Section 9-304); and
- (c) the holder of the conflicting security interest receives the notification within five years before the debtor receives possession of the inventory; and
- (d) the notification states that the person giving the notice has or expects to acquire a purchase money security interest in inventory of the debtor, describing such inventory by item or type.

(4) A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral or its proceeds if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter.

185. Section 9-107(a) states:

A security interest is a "purchase money security interest" to the extent that it is

- (a) taken or retained by the seller of the collateral to secure all or part of its price

We have concluded, *see pp. 916-17 supra*, that the seller in possession prior to delivery is the typical Article 2 security interest holder. As such, his interest clearly meets the definition of a purchase money security interest in § 9-107(a). *Cf. 2 G. GILMORE, supra* note 29, at 780-84 (general discussion of requirements of purchase money security interests). *But see* Shanker, *supra* note 79, at 104.

186. *See p. 917 supra*.

187. *See p. 938 supra*.

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compliance with the notification requirement of section 9-312(3).¹⁸⁸ But the requirement of subsection (3) that an earlier secured party be informed of the intentions of the purchase money secured party does not make sense with respect to a seller's possessory lien.¹⁸⁹ Notification is designed to alert an earlier secured lender to the possible impairment of his collateral.¹⁹⁰ If Family Furniture makes prepayment for the ABC sofas with proceeds of the sale of earlier collateral, then there is no diversion, since prepayment is likely to ensure delivery and ABC thereby loses its status as a purchase money seller.¹⁹¹ Without prepayment,

188. Section 9-312(3) states:

A perfected purchase money security interest in inventory has priority over a conflicting security interest in the same inventory and also has priority in identifiable cash proceeds received on or before the delivery of the inventory to a buyer if

- (a) the purchase money security interest is perfected at the time the debtor receives possession of the inventory; and
- (b) the purchase money secured party gives notification in writing to the holder of the conflicting security interest if the holder had filed a financing statement covering the same types of inventory (i) before the date of the filing made by the purchase money secured party, or (ii) before the beginning of the 21 day period where the purchase money security interest is temporarily perfected without filing or possession (subsection (5) of Section 9-304); and
- (c) the holder of the conflicting security interest receives the notification within five years before the debtor receives possession of the inventory; and
- (d) the notification states that the person giving the notice has or expects to acquire a purchase money security interest in inventory of the debtor, describing such inventory by item or type.

189. It is plausible to read § 9-312(3)(c) as validating the priority of a purchase money security interest over conflicting security interests, without notice, so long as the debtor has not received possession of the inventory, since the notification period of that subsection expires only on receipt of possession of the collateral by the debtor. Professor Gilmore notes that "[r]eceiving possession" is evidently meant to refer to the moment when the goods are physically delivered at the debtor's place of business." 2 G. GILMORE, *supra* note 29, at 787. *But cf.* § 9-312, Comment 3 (indicating that § 9-312(3) contains "the additional requirement that the purchase money secured party give notification, as stated in subsection (3), to any other secured party who filed earlier for the same item or type of inventory").

190. Comment 3 to § 9-312 observes:

The reason for the additional requirement of notification is that typically the arrangement between an inventory secured party and his debtor will require the secured party to make periodic advances against incoming inventory or periodic releases of old inventory as new inventory is received. A fraudulent debtor may apply to the secured party for advances even though he has already given a security interest in the inventory to another secured party. The notification requirement protects the inventory financier in such a situation: if he has received notification, he will presumably not make an advance; if he has not received notification (or if the other interest does not qualify as a purchase money interest), any advance he may make will have priority.

See 2 G. GILMORE, *supra* note 29, at 789-90.

191. A purchase money security interest exists only "to the extent" that a security interest is "taken or retained by the seller of the collateral to secure all or part of its price." Section 9-107(a). To the extent that Family Furniture has prepaid for the sofas, ABC is disabled from taking or retaining a security interest that secures that part of the price. *Cf.* 2 G. GILMORE, *supra* note 29, at 784 n.9, 787 n.4 (fractional purchase money interests cannot total more than purchase price).

on the other hand, the collateral of the earlier secured creditor has not yet been impaired. Moreover, the requirement of notification is tied in time to filing or automatic perfection without filing, neither of which describes ABC's perfection status.¹⁹² Section 9-312(3) should therefore be read to postpone the obligation of notification until the debtor receives possession of the secured inventory, a reading that it is possible to extract out of subsection (3)(c).¹⁹³

The use or misuse of proceeds suggests an alternate route to priority that Family Furniture's earlier secured creditor may pursue. Article 9 allows a security interest to continue despite transfer or other disposition of the secured collateral and to encompass the proceeds of disposition and the proceeds of proceeds.¹⁹⁴ Read literally, section 9-306 brings ABC's sofas within the umbrella of the earlier security interest if the sofas are acquired in part by moneys traceably derived from earlier sales of secured furniture. A court may assist ABC by requiring meticulous accounting to trace cash proceeds.¹⁹⁵ But more fundamentally, ABC should be able to persuade a court that, despite identification, no section 9-306 disposition has yet occurred.¹⁹⁶

It is important to be clear about the position of ABC in these confrontations. If no payments are made before delivery or if the buyer otherwise repudiates, ABC should not be accountable to Family Furniture's pre-existing secured creditors before it exercises its Article 2 rights on default, which section 9-113 expressly preserves. Although the priority provisions of Article 9, which section 9-113 does not exclude, leave ABC's rights in jeopardy to some indeterminate extent, mere indeterminacy should not demote ABC's rights against old-value

192. Section 9-312(3)(b) identifies conflicting security interests that are entitled to notification by comparing the dates of their filings with the date of the filing or automatic perfection of the purchase money secured party.

193. See note 189 *supra*.

194. Section 9-306(1) defines "proceeds" as including "whatever is received upon the sale, exchange, collection or other disposition of collateral or proceeds." Section 9-306(2) states:

Except where this Article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof unless the disposition was authorized by the secured party in the security agreement or otherwise, and also continues in any identifiable proceeds including collections received by the debtor.

195. Cf. 2 G. GILMORE, *supra* note 29, at 735-36 (discussing "tracing" of deposits in bank accounts).

196. Section 9-306(1) defines "proceeds" as "whatever is received upon the sale, exchange, collection or other disposition of collateral or proceeds." As we have seen, it appears that a "sale" covers only the actual passing of title, see pp. 951-52 *supra*. Assuming that a similar limiting construction could be placed on the terms "exchange, collection or other disposition," then ABC should be able to persuade a court that Family Furniture has not yet "received" anything.

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secured creditors. There is no reason to treat this indeterminacy as abrogating the established rights of sellers to withhold delivery under pre-Code law. Even if ABC is itself in default in refusing to deliver, Article 2's policy of protecting those who deal with sellers in possession of sold goods¹⁹⁷ should take priority over the claims of the pre-existing secured creditors of Family Furniture.

Family Furniture may, however, have entered into a financial arrangement that may prove more troublesome to ABC: one involving an enabling lender.¹⁹⁸ Since this interest attaches as soon as Family Furniture acquires rights in the sofas,¹⁹⁹ it would appear that the enabling lender's security interest attaches and is perfected simultaneously with ABC's possessory seller's interest. The enabling lender and ABC are both new value parties in their relationship to Family Furniture, although the sum of their new value interests cannot exceed the purchase

197. Section 2-403 states:

Power to Transfer; Good Faith Purchase of Goods; "Entrusting"

(1) A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

- (a) the transferor was deceived as to the identity of the purchaser, or
- (b) the delivery was in exchange for a check which is later dishonored, or
- (c) it was agreed that the transaction was to be a "cash sale", or
- (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

(2) Any 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.

(3) "Entrusting" includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be larcenous under the criminal law.

(4) The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9), Bulk Transfers (Article 6) and Documents of Title (Article 7).

See generally Peters, *supra* note 8, at 235-38.

Section 2-402 is also applicable to protect "creditors" of a seller who have retained possession of sold goods for more than a commercially reasonable time. See Jackson & Kronman, *supra* note 100, at 19-20. However, § 2-402 is not available to subsequent creditors. See McGann v. Capital Sav. Bank & Trust Co., 117 Vt. 179, 89 A.2d 123 (1952); Peters, *supra* note 8, at 239.

198. The term "enabling lender" refers to the holder of a purchase money security interest acquired under § 9-107(b):

A security interest is a "purchase money security interest" to the extent that it is

....

- (b) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.

199. Section 9-203(1)(c).

price of the sofas.²⁰⁰ But unless the lender's funds are actually used to acquire rights in the new collateral, he does not qualify as a purchase money secured party and therefore falls back into the prior secured lender category discussed above.²⁰¹ That demotion reflects the enabling lender's ready access to commercial devices such as joint payee checks that can minimize awkward confrontations. The lender financing a particular acquisition has a greater opportunity to identify his debtor's seller than does the seller to discover his buyer's financier. If the enabling lender's funds have actually been used to pay, in whole or in part, for the sofas that Family Furniture has contracted to buy, that lender would be a purchase money lender (and ABC, to that extent, not). Such an enabling lender has a compelling claim,²⁰² but the question remains whether the lender can insist that ABC deliver if Family Furniture repudiates or if ABC wrongfully withholds the sofas. There is no statutory answer, although Family Furniture is not necessarily in default against the enabling lender. Manipulation of what constitutes the necessary identification will avoid the issue and will likely protect ABC and takers under ABC even in ABC's weakest case, its own default.

By way of summary, the Code's unpaid seller, despite his possessory stance, is exposed to a number of serious competitors. Under both Articles 2 and 9, identification of goods creates rights in the buyer to which third parties may assert claims. Identification is the linchpin around which the seller's vulnerability turns. Default in the sales contract is not crucial in and of itself. A seller's default in selecting non-conforming goods does not prevent identification, although his delivery to another buyer might do so. But purchasers from the seller in possession derive protection under Article 2 without regard to identification, at least so long as their sellers are merchants.²⁰³ A buyer's default, in failing to pay or in otherwise repudiating, does not reverse the acquisition of rights in the sold goods and therefore does not divest security in-

200. 2 G. GILMORE, *supra* note 29, at 784 n.9, 787 n.4. Professor Gilmore correctly notes that "if the collateral depreciates in value or is sold in foreclosure proceedings for less than the original purchase price, the purchase-money interest (or interests) could be more than 100 per cent of present value or of the proceeds realized on disposition." *Id.* at 784 n.9.

201. This follows from the "in fact so used" language of § 9-107(b). For a discussion of the tracing requirement, see J. WHITE & R. SUMMERS, *supra* note 124, at 915-16; Jackson & Kronman, *supra* note 100, at 28.

202. To the extent that the enabling lender has advanced money to ABC (virtually a prerequisite to the status of enabling lender under § 9-107(b)), ABC has both the sofas and the money. Such a situation would be a classic restitutionary case.

203. Section 2-403(1), (2); see Peters, *supra* note 8, at 235-39.

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terests or other claims that attach under Article 9.²⁰⁴ But the prescriptive tendencies of Article 9 should not be used to force a rigid solution. There is no reason why Williston's unpaid seller becomes undeserving once goods have become identified. The Code should be read to protect such a seller unless the particular facts of a case suggest something akin to estoppel, as, for example, when entrusting has been manifested by conduct, or acquiescence in conduct, short of physical transfer. But such examples should be viewed as exceptional and should in each case require evaluation of commercial setting, purpose, and effect. In other words, security interests arising solely under Article 2 are entitled to be adjudicated, even for priority purposes, by the flexible methodology of Article 2.

2. *ABC Delivers Goods Unconditionally*

After unconditional delivery to Family Furniture, the unremarkable status of ABC as a seller out of possession leaves it subordinated to other secured creditors.²⁰⁵ It matters little whether ABC is deemed to be an unsecured creditor or a secured creditor not accorded automatic perfection by section 9-113 and not otherwise protected, and it matters little whether the focus is placed on Article 9 alone or on sections 2-403(1) and (4) in addition. ABC's "right" to "cancel" and to have the goods returned is, after delivery, subject to the superior rights of all other secured creditors of Family Furniture claiming an interest in the sofas.

3. *ABC Delivers Goods on Special Condition*

The priority posture of competing purchasers after a delivery on special condition is more complex. At common law, the cash seller prevailed over competing parties who claimed through the buyer since no title was thought to pass until payment was made.²⁰⁶ The common law treatment of the credit sale induced by fraud, which gave the buyer voidable title that the seller could regain by appropriate means, allowed

204. Section 2-401(4) deals only with the revesting of title; it is silent on the divesting of acquired rights that are not dependent on title.

205. See pp. 912, 917-18 *supra*; R. NORDSTROM, *supra* note 41, at 498-500; Peters, *supra* note 8, at 218-23. As such, this simply continues pre-Code law. See, e.g., Southern Lumber Co. v. Colvin, 104 Ark. 130, 148 S.W. 495 (1912); Gilmore, *supra* note 60, at 1060.

206. This, at least, was the theory. See, e.g., Sprague Canning Mach. Co. v. Fuller, 153 F. 588 (5th Cir. 1908); Kirk v. Madsen, 240 Iowa 532, 36 N.W.2d 757 (1949); McAuliffe & Burke Co. v. Gallagher, 258 Mass. 215, 154 N.E. 755 (1927); Weyerhaeuser Timber Co. v. First Nat'l Bank, 150 Or. 172, 38 P.2d 48 (1934), *aff'd on rehearing*, 150 Or. 172, 203, 43 P.2d 1078 (1935); L. VOLB, *supra* note 61, at 161; Corman, *supra* note 60, at 56-59. Professor Gilmore, however, noted that the cash sale theory was "almost never applied against good faith purchasers in a commercial setting." Gilmore, *supra* note 60, at 1061; see note 62 *supra*.

the buyer to defeat the retaking by resale to a good faith purchaser, which generally required new consideration or detrimental reliance.²⁰⁷ Absent such infusions of new value, creditors had to stand in the unenviable shoes of the defrauding buyer.²⁰⁸

Under the Code the cash sale is no longer treated more favorably than the fraudulent sale, if in fact it ever was. Not only has the Code expressly demoted the importance of title,²⁰⁹ but, as we have already noted, it has also assimilated the cash sale doctrine to the fraudulent sale doctrine.²¹⁰

It is less clear, however, how much the Code has changed the law with respect to the fraudulent sales transaction. Section 2-702(3) directs us to section 2-403 to determine the rights of a "good faith purchaser."²¹¹ That section, in turn, deals with the rights of a "good faith purchaser for value," leaving to Article 9 the rights of "other purchasers."²¹² (Despite the implicit directive of section 9-113 that Article 2 security interests are subject to Article 9 for priority purposes, this express treatment of priorities in section 2-403 should control.)

Section 2-403(1) implicitly abolishes the reclamation right of a seller caught in a fraudulent sales transaction when faced with the competing claim of a party who qualifies as a good faith purchaser for value and

207. See, e.g., *Oswego Starch Factory v. Lendrum*, 57 Iowa 573, 10 N.W. 900 (1881); *Gilbert v. Hudson*, 4 Me. 345 (1826); 3 S. WILLISTON, *supra* note 35, at 448-57; *Gilmore*, *supra* note 60, at 1060; *Peters*, *supra* note 8, at 222 n.71; Note, *supra* note 79, at 758; cf. *Braucher*, *supra* note 60, at 1283-84 (discussing pre-Code law).

208. See, e.g., *Oswego Starch Factory v. Lendrum*, 57 Iowa 573, 578-79, 10 N.W. 900, 903 (1881); *McAuliffe & Burke Co. v. Gallagher*, 258 Mass. 215, 154 N.E. 755 (1927); *Goodwin v. Mass. Loan & Trust Co.*, 152 Mass. 189, 25 N.E. 100 (1890); *Schwartz v. McCloskey*, 156 Pa. 258, 27 A. 300 (1893); 3 S. WILLISTON, *supra* note 35, at 396-401. But see *Kranert v. Simon*, 65 Ill. 344 (1872).

209. Sections 2-401, 9-202. See p. 912 *supra*.

210. See pp. 924-25 *supra*.

211. Section 2-702(3) reads:

The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403). Successful reclamation of goods excludes all other remedies with respect to them.

212. Subsections 2-403(1) and (4) read:

(1) A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though

(a) the transferor was deceived as to the identity of the purchaser, or
 (b) the delivery was in exchange for a check which is later dishonored, or
 (c) it was agreed that the transaction was to be a "cash sale", or
 (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

....

(4) The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9), Bulk Transfers (Article 6) and Documents of Title (Article 7).

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explicitly abolishes the reclamation right of a cash seller in such a situation.²¹³ The extent to which pre-Code law has been changed, then, rests on the scope to be given the phrase "good faith purchaser for value."²¹⁴ Section 2-403(1), as it has been interpreted in *In re Samuels & Co.*,²¹⁵ gives priority to any purchaser who meets the apparently literal requirements of a good faith purchaser for value, including a prior secured lender with an after-acquired property interest.²¹⁶

As interpreted in *In re Samuels & Co.*, the change from common law, and from section 24 of the Uniform Sales Act, is enormous. The group of protected takers is expanded not only from buyers to purchasers, but also from a group that gave new money to a group that may have done nothing since the delivery of the goods to the buyer—or, indeed, may

213. Section 2-403(1) establishes that "[a] person with voidable title has power to transfer a good title to a good faith purchaser for value." It explicitly declares that the purchaser has such power even though, *inter alia*:

- (b) the delivery was in exchange for a check which is later dishonored, or
- (c) it was agreed that the transaction was to be a "cash sale", or
- (d) the delivery was procured through fraud punishable as larcenous under the criminal law.

Section 2-702(3) expressly subjects the reclamation right of a seller caught in a fraudulent sales transaction to "the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403)." See generally Peters, *supra* note 8, at 221-22.

214. See pp. 963-64 *supra*.

215. *Stowers v. Mahon (In re Samuels & Co.)*, 526 F.2d 1238 (5th Cir.) (en banc), *cert. denied*, 429 U.S. 834 (1976).

216. *Id.* at 1241, 1242-44. *In re Samuels & Co.* is perhaps the most famous of these cases; it is by no means the only one, and its result conforms with the majority of cases. See *United States v. Wyoming Nat'l Bank*, 505 F.2d 1064, 1067 (10th Cir. 1974) (apparently leaving open, however, what would have happened if demand for reclamation had been made within 10 days, *id.* at 1068); *In re Daley, Inc.*, 17 U.C.C. Rep. 433 (D. Mass. 1975) (bankruptcy judge); *In re Hayward Woolen Co.*, 3 U.C.C. Rep. 1107 (D. Mass. 1967) (bankruptcy referee); *Stratton Sale Barn, Inc. v. Reed*, 6 U.C.C. Rep. 922 (U.S.D.A. 1969); *General Elec. Credit Corp. v. Tidwell Indus., Inc.*, 565 P.2d 868 (Ariz. 1977); *First Nat'l Bank v. Smoker*, 153 Ind. App. 71, 286 N.E.2d 203 (1972); *Swets Motor Sales, Inc. v. Pruisner*, 236 N.W.2d 299, 304 (Iowa 1975); *First Citizens Bank & Trust Co. v. Academic Archives, Inc.*, 10 N.C. App. 619, 622-24, 179 S.E.2d 850, 853 (Ct. App.), *cert. denied*, 278 N.C. 703, 181 S.E.2d 601 (1971); *Stumbo v. Paul B. Hult Lumber Co.*, 251 Or. 20, 35 n.10, 444 P.2d 564, 571 n.10 (1968) (dictum).

Apparently, two cases have gone the other way. The first, *In re American Food Purveyors, Inc.*, 17 U.C.C. Rep. 436 (N.D. Ga. 1974) (bankruptcy judge), has to be read to be believed. The other is *Zions First Nat'l Bank v. First Sec. Bank, N.A.*, 534 P.2d 900 (Utah 1975), which relied, without discussion of § 2-401(1), on "an agreement that title would pass only upon payment." *Id.* at 902.

Academic commentators early reached precisely the same result as did Judge Godbold in *In re Samuels & Co.* See W. HAWKLAND, A TRANSACTIONAL GUIDE TO THE UCC 304 (1964); Hogan, *supra* note 139, at 580-81; Kennedy, *supra* note 79, at 838; Note, *supra* note 79, at 757-58; cf. R. NORDSTROM, *supra* note 41, at 515 (discussing when, in terms of Code definitions, subsequent purchaser will "terminate" seller's reclamation right). This result had earlier been urged by L. VOLD, *supra* note 61, at 402-05. A cogent criticism of the *Samuels* result exists, however. See McDonnell, *supra* note 178. Legislative dissatisfaction has resulted in a statutory reversal of *Samuels* with respect to livestock sales to meat-packers. See, e.g., Act of Sept. 13, 1976, Pub. L. No. 94-410, § 8, 7 U.S.C.A. § 196 (1976); COLO. REV. STAT. §§ 4-2-401(5), 4-2-403(1.5), 4-2-511(4) (Supp. 1976).

not even have known of the delivery. Although the pre-Code law apparently protected good faith purchasers who injected new money,²¹⁷ the interpretation given section 2-403(1) in *In re Samuels & Co.* extends such protection to prior secured lenders with an after-acquired property interest regardless of whether or not there was detrimental reliance.²¹⁸ The Code never explicitly stated such a design in section 2-403.²¹⁹ A comment to that section suggests, to the contrary, that the drafters intended no expansion, observing that the "older loose concept of good faith and wide definition of value combined to create apparent good faith purchasers in many situations in which the result outraged common sense."²²⁰ This comment, an ill-fitting holdover from earlier drafts,²²¹ may be a poor foothold, but there is nothing in the later draft-

217. See pp. 963-64 *supra*.

218. C.I.T. Corporation, the inventory financier of Samuels & Co., may well have detrimentally relied on the incoming cattle, in that it was counting on the incoming cattle to keep the collateral pool at nearly the same level—a substitution of collateral in which the financier releases proceeds of accounts in return for the new additions to inventory and makes weekly credit decisions on that basis. See generally Note, *After-Acquired Property Security Interests in Bankruptcy: A Substitution of Collateral Defense of the U.C.C.*, 77 YALE L.J. 139 (1967). Cf. *Manchester Nat'l Bank v. Roche*, 186 F.2d 827, 831 (1st Cir. 1951) (discussing "entity theory"—"a 'floating mass', the component elements of which may be constantly changing without affecting the identity of the *res*"). Assuming, as seems probable, that C.I.T. Corporation was adequately monitoring the weekly status of Samuels & Co., see note 226 *infra*, and was making credit decisions based on that status, C.I.T. probably could have shown sufficient detrimental reliance to entitle it to prevail as a good faith purchaser for new value. See McDonnell, *supra* note 178, at 455 ("If, in fact, the financier is making credit decisions on the basis of the new assets, reliance would not be difficult to document.") *In re Samuels & Co.*, however, consistent with other case law, did not examine the question of detrimental reliance, but stopped simply with the observation that C.I.T. Corporation met the literal definition of good faith purchaser for value. *Stowers v. Mahon (In re Samuels & Co.)*, 526 F.2d 1238, 1242-43 (5th Cir.) (en banc), *cert. denied*, 429 U.S. 834 (1976).

219. See McDonnell, *supra* note 178, at 443-60. Two comments to the 1949 draft of what now is § 2-403 suggest, instead, that the original purpose behind that section was to balance the competing equities between the reclaiming seller and competing purchasers. One comment observed that "[t]his Article flatly rejects the general concept of the 'cash sale', offering instead protection to the seller by its specific requirements for 'good faith purchase.'" Section 2-405, Comment 3 (May 1949 draft). The second comment, through its emphasis on "appearances," carried the implication of necessary reliance on the part of the competing purchaser. "The problem underlying this entire section is one of good faith purchase based on grounds which are a combination of reasonable appearances and such action or acquiescence by an original claimant as will justify holding him to answer for those appearances." *Id.*, Comment 5. There is no express indication in later drafts of the Code that the drafters ever repudiated these sentiments.

220. Section 2-403, Comment 3.

221. The comment was attached to § 2-403 when that section read as follows:

Purchase of Limited Interest; Good Faith Purchase; "Entrusting"; "Buyer in Ordinary Course of Business".

(1) A purchaser of goods acquires all title which his transferor has or has power to transfer but a purchaser of a limited interest acquires rights only to the extent of the interest purchased and as between the parties any purchase is subject to its own terms.

(2) Any entrusting of possession of goods to a person who deals in goods of that

ing history of the Code to indicate its repudiation by the drafters.²²²

The drafting style of Article 2 and the generally open-ended definition of the good faith purchaser for value suggest that section 2-403(1) should be read to protect purchasers only if they, like buyers in the ordinary course of business (to whose status delivery is a prerequisite), extend new value to Family Furniture in reliance on the delivery of the sofas.²²³ We earlier observed that, before delivery, ABC should usually prevail over third-party claimants whose interests attach by

kind gives that person power to transfer all rights of the entruster to a buyer in ordinary course of business.

(3) "Entrusting" includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be larcenous under the criminal law.

(4) "Buyer in ordinary course of business" includes a person to whom goods are shipped pursuant to a pre-existing contract or one to whom they are delivered on credit, but does not include a pawnbroker or a person taking from one not dealing in goods of that kind or a person taking an interest in inventory in bulk or as security or a person taking at an hour or under other circumstances which negate good faith or a person purchasing from a farmer.

(5) The extent to which other purchasers take free of the rights of a secured lender is governed by the Article on Secured Commercial Transactions (Article 9).

U.C.C. § 2-403 (Spring 1950 draft). Comment 4 to that section suggested that "the rights of purchasers other than buyers in ordinary course are left to [the article on secured transactions]."

222. Indeed, Justice Braucher has suggested that a "true reading" of § 2-403 would exclude an "unconscious purchaser" from the status of a bona fide purchaser for value. Countryman, *supra* note 109, at 458 n.119 (1971). This appears to accord with what we know of Karl Llewellyn's view. See UNIFORM REVISED SALES ACT § 58, Comment, at 196-97 (proposed final draft No. 1, 1944) (argues for abolition of cash sale doctrine, suggesting "[t]he results really needed can be better and more predictably reached by delimiting the field of the purchase which will be protected"); REVISED UNIFORM SALES ACT § 25, Comment, at 157-58 (2d draft 1941); McDonnell, *supra* note 178, at 435-60.

223. Professor McDonnell concludes:

Since explicit language of exclusion is not present, a requirement that the purchaser in some practical way rely on the assets he is receiving must be inferred in order to exclude "unconscious purchasers" from protection. This construction is permissible since the Code's definition of "purchaser" is applicable "unless the context otherwise requires." Previously, a concrete subsequent transfer to the BFP [bona fide purchaser] after the true owner had parted with his goods was evidence of such reliance. The history of the Code's drafting shows no intent to eliminate the reliance element. If, in fact, no such reliance is present, then based on the history and function of the BFP principle, the lienor ought to lose.

McDonnell, *supra* note 178, at 452-53.

We are aware of the contrary arguments of Professor Vold, *see* L. VOLD, *supra* note 61, at 403-04, but we prefer a case-by-case determination of whether the creditor has detrimentally relied on the new collateral to a flat rule protecting the creditor with an after-acquired property interest, who may not even have known of the new collateral. Where two innocent people are involved, a flexible approach seems preferable to a flat rule. *Cf.* Jordan v. Butler, 182 Neb. 626, 637, 156 N.W.2d 778, 785 (1968) (relying on "a rule of long standing that where one of two innocent persons must suffer by the acts of a third, the one whose conduct, act, or omission enables such third person to occasion the loss must sustain it if the other party acted in good faith without knowledge of the facts and altered his position to his detriment").

way of Family Furniture's acquisition of rights in the sofas.²²⁴ The fact of delivery changes none of the equities, except that it becomes possible for purchasers to extend new value in reliance on the fact that Family Furniture is in possession of the sofas (much as it becomes possible for buyers in ordinary course so to buy).²²⁵ These are the only purchasers who could have changed their position as a result of delivery to Family Furniture, and who could be hurt in a way in which they could not have been hurt before delivery, by ABC's exercise of its reclamation rights. There is no reason of policy to read section 2-403(1) more broadly;²²⁶ a narrow reading makes the class of protected purchasers no broader than the class of protected buyers and so harmonizes the various subsections of section 2-403.²²⁷ The language is open-ended enough to justify relying on the more flexible approach that the pervasive weighing of equities in Article 2 encourages.

Such a construction of "good faith purchasers for value" within the scope of section 2-403(1), requiring some form of new value in reliance on the delivery of the sofas, still leaves room for "other purchasers"

224. See pp. 962-63 *supra*.

225. Cf. *General Elec. Credit Corp. v. Tidwell Indus., Inc.*, 565 P.2d 868, 871-72 (Ariz. 1977): "By allowing the mobile homes to remain on Parkwood's lot without filing notice of its claim of security interest, Tidwell could well have misled G.E.C.C. as well as other creditors of Parkwood into believing that Parkwood possessed greater assets than was the case."

226. A reading of § 2-403(1) such as we have proposed would also seem to facilitate the implementation of another Code policy, that of encouraging inventory financiers to monitor their debtors. Although the Code in § 9-205 repeals the rule of *Benedict v. Ratner*, 268 U.S. 353 (1925), which voided as fraudulent a chattel security interest in inventory where the debtor was given unfettered dominion or control over the collateral, it nonetheless approves of *Benedict's* underlying concept of monitoring as beneficial not only to the inventory financier, but also to his debtor and to other creditors of the debtor. See § 9-205, Comment 3. Thus, § 9-306(4) places commingled proceeds received more than 10 days before the institution of insolvency proceedings beyond the reach of a floating lienor. Professor Gilmore opined that

the Code draftsmen recognized as sound the idea that a secured lender, particularly if he takes as security the inventory and receivables which are the most liquid assets of any enterprise, should, not only in his own interest but in the interest of other creditors, be under compulsion to pay close attention to the course of the debtor's affairs. . . . If self-interest does not do the job, §9-306(4)(d) supplies the incentive.

2 G. GILMORE, *supra* note 29, at 1340; see also 1 *id.* at 361-62. Professor Gilmore suggests that such impetus to policing may, however, not be sufficient. *Id.* at 364.

A reading of § 2-403(1) that would protect floating lienors only if they detrimentally relied on the existence of the incoming collateral would, like § 9-306(4), provide an added impetus to police. If the floating lienor remains an "unconscious purchaser," he will lose his § 2-403(1) priority; if, however, he polices, he should be able to demonstrate without much difficulty that he has detrimentally relied, and thus is entitled to § 2-403(1) priority. Cf. McDonnell, *supra* note 178, at 451-56 (discussion of when detrimental reliance shown). The reading we propose of § 2-403(1), in contrast to a broad application of the literal definition of "value" in § 1-201(44), would therefore facilitate the implementation of the Code's policy of encouraging monitoring by the floating lienor.

227. See pp. 950-51 and note 178 *supra*.

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under section 2-403(4) and even other “good faith purchasers” under section 2-702(3), whose priority status is controlled by Article 9. Significant among these would be the secured creditor with an after-acquired property interest.²²⁸ Since we have considered the reclamation right to be sufficiently like an “interest . . . which secures payment or performance of an obligation” to treat it as a security interest,²²⁹ it would seem to follow that it is also sufficiently like a security interest “taken or retained by the seller of the collateral to secure all or part of its price” to qualify as a purchase money security interest.²³⁰ So long as the security interest exists (which is so long as ABC is given its ostensible power of reclamation), the interest is perfected without filing by virtue of section 9-113,²³¹ and ABC should prevail as a purchase money security interest over competing good faith purchasers, including the secured lender with an after-acquired property interest. Although the phrasing of section 9-312(3)(b) fits this situation awkwardly,²³² it should be read to assure such priority. Even though section 9-312(3) does not allow purchase money security interests in inventory a grace period during which perfection is maintained after delivery, which subsection (4) does allow noninventory collateral,²³³ the reasons for that difference have no application here. Comment 3 to section 9-312 observes:

The reason for the additional requirement of notification is that typically the arrangement between an inventory secured party and his debtor will require the secured party to make periodic advances against incoming inventory or periodic releases of old inventory as new inventory is received. A fraudulent debtor may apply to the

228. Without some extra showing, such a creditor will not be able to establish the extension of new value in reliance on the delivery of the new collateral.

229. Section 1-201(37); see pp. 926-28 *supra*.

230. Section 9-107(a); see pp. 958-60 *supra*.

231. See p. 916 *supra*.

232. Section 9-312(3)(b) states:

A perfected purchase money security interest in inventory has priority over a conflicting security interest in the same inventory and also has priority in identifiable cash proceeds received on or before the delivery of the inventory to a buyer if

....

(b) the purchase money secured party gives notification in writing to the holder of the conflicting security interest if the holder had filed a financing statement covering the same types of inventory (i) before the date of the filing made by the purchase money secured party, or (ii) before the beginning of the 21 day period where the purchase money security interest is temporarily perfected without filing or possession (subsection (5) of Section 9-304)

233. Section 9-312(4) reads:

A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral or its proceeds if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter.

secured party for advances even though he has already given a security interest in the inventory to another secured party. The notification requirement protects the inventory financier in such a situation: if he has received notification, he will presumably not make an advance; if he has not received notification . . . , any advance he may make will have priority.

In this instance, the inventory financier can achieve the same priority with respect to the incoming collateral by monitoring that collateral or otherwise relying on its presence. In such a situation, the inventory financier should be indifferent as to the payment status of the seller of the collateral, for in all instances he will have priority as a good faith purchaser for value under section 2-403(1), and the priority conflict will never reach section 9-312(3).²³⁴ If he does not so rely during the relevant time, when it may be presumed that he knows that recently acquired collateral may be subject to this reclamation right, it would appear that he has not been hurt by the absence of notification. Because the priority accorded on reliance under section 2-403(1) serves a protective function equivalent to notification, there is no reason to require further notification as a prerequisite to ABC's priority under section 9-312(3).²³⁵

The status of an enabling lender is a bit more complicated. Just as in the case of the seller-in-possession,²³⁶ there is no reason why an enabling lender should prevail if he has not taken precautions to ensure that the seller actually receives the enabling advance. This is reflected in Article 9's demotion of such an enabling lender to the status of an ordinary secured party;²³⁷ the seller, logically, would appear to remain in such circumstances "like" a purchase money seller, since he, and not the enabling lender, is actually "financing" the transaction. The same result should be reached under Article 2, either by considering the enabling lender as a "prior" purchaser unable to avail himself of the status of "good faith purchaser for value" within section 2-403(1) or, perhaps more easily, by considering such carelessness on the part of the enabling lender as an equitable factor that impugns his "good faith" under section 2-103(1)(b).²³⁸

234. See pp. 964, 967-68 *supra*.

235. A similar rationale appears to underlie the absence of a notification provision in § 9-312(4). Comment 3 to that section continues by observing that "[s]ince an arrangement for periodic advances against incoming property is unusual outside the inventory field, no notification requirement is included in subsection (4)."

236. See pp. 961-62 *supra*.

237. See p. 962 *supra*.

238. The result of this is to suggest that any third party who wishes to prevail even though his new value is extended prior to physical delivery—and thus prior to the time a buyer in the ordinary course of business would be able to prevail under § 2-403(2)—can do so only by complying with the enabling lender provisions of Article 9.

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If, on the other hand, the enabling lender has prepaid ABC directly, then ABC is not a seller on credit and is unable to avail itself of section 2-702(2) at all. Likewise, the situation of ABC as a cash seller is far different if the check is that of the enabling lender instead of Family Furniture. To trigger any right of reclamation under section 2-507(2), the check of the enabling lender would have to be dishonored, since it is now the financial status of the enabling lender and not that of Family Furniture that is on the line. In the unlikely event that the enabling lender's check is dishonored (and Family Furniture does not step into the breach and pay), there is no reason to accord the enabling lender any rights against ABC at all. Indeed, there is no reason to treat him as an enabling lender; with the dishonoring of the check, he should be disqualified even from the status of a lender.

A transaction involving an enabling lender engages a third possibility. The enabling lender may have paid ABC in part for the sofas, thereby becoming, *pro tanto*, a true enabling lender.²³⁹ Family Furniture, however, may fail to pay the remainder of the contract price for any of the reasons that would ordinarily trigger ABC's reclamation right. If the enabling lender, having qualified under Article 9, is considered a "good faith purchaser for value" within the meaning of section 2-403(1) because of the enabling nature of his money—money clearly advanced in reliance on the delivery of the goods—then the enabling lender should achieve "priority" under this Article 2 provision to the extent of his enabling advance.

4. *ABC Reacquires Goods From Family Furniture*

The priority rights of secured creditors in the situation in which ABC has repossessed the sofas are even more intractable than in the situations discussed thus far. With respect to buyers in ordinary course, as we observed above, resolution of priorities continues to turn on specific rights to the contract goods,²⁴⁰ rights that may presuppose delivery to the buyer as well as to Family Furniture. Other competitors are not so limited. The secured lender whose financing of Family Furniture's inventory includes as collateral the sofas from ABC does have, in contrast with a buyer, a specific right to goods as well as a claim to money.²⁴¹ If ABC's reacquisition relates back to no prior lien

239. See p. 962 *supra*.

240. See pp. 953-54 *supra*.

241. Section 9-503 provides:

Secured Party's Right to Take Possession After Default

Unless otherwise agreed a secured party has on default the right to take possession of the collateral. In taking possession a secured party may proceed without judicial process if this can be done without breach of the peace or may proceed by action. If

other than the seller's automatic possessory lien, Family Furniture had unlimited power to encumber its assets while it had title and possession. Reacquisition by ABC is then a disposition of collateral in which the secured party's interest continues,²⁴² unless ABC can find shelter somewhere in Article 9.

If the security interest was unperfected when ABC took the sofas back, then ABC should be protected against this secret lien. The provisions of section 9-301 enumerate those who prevail over an unperfected security interest and include

in the case of goods . . . a person who is not a secured party and who is a transferee in bulk or other buyer not in ordinary course of business . . . to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected.

This language admittedly does not fit like a glove. ABC is neither a transferee in bulk nor a buyer, because of section 2-401(4); and ABC, although hardly a donee, may not have given value in connection with the redelivery of the collateral, especially if the retaking was occasioned by a dispute about the quality of ABC's original tender. But both history and commercial sense support a reading of section 9-301 that encompasses ABC. At common law, courts regularly cast an equally suspicious eye on creditors who left their chattel mortgagors in possession without recordation as on buyers who left their sellers in possession. In both cases, the secrecy of the latent claim of ownership was held to create an aura of fraud from which innocent parties deserved to be protected.²⁴³ Similarly, in modern law in general and the Code in

the security agreement so provides the secured party may require the debtor to assemble the collateral and make it available to the secured party at a place to be designated by the secured party which is reasonably convenient to both parties. Without removal a secured party may render equipment unusable, and may dispose of collateral on the debtor's premises under Section 9-504.

The right to retain the goods, however, may be limited. *See* § 9-505. This section also provides the mechanism whereby the secured party may "propose to retain the collateral in satisfaction of the obligation." Section 9-505(2).

242. Section 9-306(2) provides:

Except where this Article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof unless the disposition was authorized by the secured party in the security agreement or otherwise, and also continues in any identifiable proceeds including collections received by the debtor.

Since reacquisition is not a "sale," § 2-401(4), ABC cannot rely on § 9-307(1). Although reacquisition is not a "sale" for purposes of § 9-306(2) either, it appears to fit easily in the phrase "other disposition." Section 2-326(2) provides a special rule for goods sold "on approval," but that does not appear to fit ABC's status either.

243. For creditors leaving their chattel mortgagors in possession, see, e.g., *Twyne's Case*, 76 Eng. Rep. 809 (Star Chamber 1601); *Clow v. Woods*, 5 Serg. & Rawl 275, 9 Am. Dec. 346 (Pa. 1819); 1 G. GILMORE, *supra* note 29, at 24, 438-39. For buyers leaving their

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particular, a commercial party should not escape standard commercial responsibilities for perfection at the expense of another party acting in good faith whose injury the commercial lender might easily have avoided.²⁴⁴ Section 9-301(1)(c) should sensibly be taken to include transferees such as reacquiring sellers and transactions instinct with value, so long as reacquisition is made in commercial good faith.

Family Furniture's secured lenders who have perfected stand in a different position. After perfection, such lenders can lose their security interests in the ABC reacquisition only if ABC is a buyer in the ordinary course of business or if the secured lender is deemed in some way to have authorized this disposition.²⁴⁵ ABC's reacquisition does not and should not qualify as ordinary course buying; "ordinary course" must mean something more than ordinary good faith,²⁴⁶ and "buying," under section 1-201, contemplates new value rather than ordinary value.²⁴⁷ And, at least where the reacquisition occurred because of Family Furniture's rejection or justified revocation, section 2-401(4) all but explicitly precludes ABC from the status of a buyer.²⁴⁸

sellers in possession, see, *e.g.*, *Southern Cal. Collection Co. v. Napkie*, 106 Cal. App. 2d 565, 235 P.2d 434 (1951); *McGann v. Capital Sav. Bank & Trust Co.*, 117 Vt. 179, 89 A.2d 123 (1952); *Coburn v. Drown*, 114 Vt. 158, 40 A.2d 528 (1945); an Act against fraudulent Deeds, Alienations, &c., 113 Eliz. 1 c.5 (1570); UNIFORM SALES ACT §§ 25-26 (1950); 2 S. WILLISTON, *supra* note 35, at 351-502; *Jackson & Kronman, supra* note 100, at 9-10.

244. See, *e.g.*, *Wabasso State Bank v. Caldwell Packing Co.*, 251 N.W.2d 321 (Minn. 1976); *Tumber v. Automation Design & Mfg. Corp.*, 130 N.J. Super. 5, 11-13, 324 A.2d 602, 606 (1974); *cf. Sherrock v. Commercial Credit Corp.*, 277 A.2d 708, 710 (Del. Super. Ct. 1971), *rev'd on other grounds*, 290 A.2d 648 (Del. 1972) (policy of Code should be to protect party who does not, or should not be expected to, foresee and guard against given risk).

245. Section 9-306(2) states:

Except where this Article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof unless the disposition was authorized by the secured party in the security agreement or otherwise, and also continues in any identifiable proceeds including collections received by the debtor.

Section 9-307(1) states:

A buyer in ordinary course of business (subsection (9) of Section 1-201) other than a person buying farm products from a person engaged in farming operations 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.

246. Section 1-201(9) requires that a person be in "good faith" and that he buy "in ordinary course." See *Makransky v. Long Island Reo Truck Co.*, 58 Misc. 2d 338, 295 N.Y.S.2d 240 (Sup. Ct. 1968).

247. Section 1-201(9) concludes that

"Buying" may be for cash or by exchange of other property or on secured or unsecured credit and includes receiving goods or documents of title under a pre-existing contract for sale but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt.

248. Section 2-401(4) states:

A rejection or other refusal by the buyer to receive or retain the goods, whether or not justified, or a justified revocation of acceptance reverts title to the goods in the seller. Such reversion occurs by operation of law and is not a "sale".

The issue of the lender's authorization of ABC's reacquisition is not so clearcut; the concept of authority lends itself to a case-by-case comparison of equities.²⁴⁹ Consider the following variations in the interests of the secured lender and the circumstances of the reacquisition. The secured lender may be an earlier lender with an after-acquired property clause or an enabling lender financing this particular shipment of sofas. The reacquisition may involve an exchange of goods for money or goods for goods that leaves Family Furniture's net assets unchanged, or it may involve a repossession threatening the forfeiture of moneys paid as well as further claims for monetary damages. It is not possible to predict, by statutory fiat or academic introspection, the variety of interactions that may occur. Nor is it possible to foresee in whose hands the goods will be when the claim of the secured lender surfaces. When the goods can be located with ABC, perhaps it is appropriate to require ABC to make some concrete showing of authority to dispose before its seller's lien revives; such authorization might be found not only in the terms of the security agreement between Family Furniture and its lender but also in the conduct of the parties and the usage of the trade.²⁵⁰ It is reasonable to condition ABC's seller's lien in this way because ABC, as a commercial seller, can be held to a duty to discover and understand the consequences of his buyer's financial arrangements.²⁵¹

It is not quite so reasonable to apply this rationale if ABC resells, as is the custom of sellers. Buyers from ABC ordinarily have no way of tracing the rights of takers under Family Furniture, perfected or not, since they ordinarily have no way of identifying Family Furniture as a

249. See, e.g., *Universal C.I.T. Credit Corp. v. Middlesboro Motor Sales*, 424 S.W.2d 409, 413 (Ky. 1968); cf. *United States v. Central Livestock Ass'n, Inc.*, 349 F. Supp. 1033, 1034 (D.N.D. 1972) (reliance on particular facts in deciding that sale was "authorized"); *Lisbon Bank & Trust Co. v. Murray*, 206 N.W.2d 96, 97 (Iowa 1973) (question of authority to sell collateral is for trier of fact); *Hempstead Bank v. Andy's Car Rental System, Inc.*, 35 App. Div. 2d 35, 312 N.Y.S.2d 317 (1970) (issue of fact on question of implied authority).

250. See, e.g., *Planters Prod. Credit Ass'n v. Bowles*, 256 Ark. 1063, 1066-68, 511 S.W.2d 645, 647 (1974); *Lisbon Bank & Trust Co. v. Murray*, 206 N.W.2d 96 (Iowa 1973); *Hempstead Bank v. Andy's Car Rental System, Inc.*, 35 App. Div. 2d 35, 312 N.Y.S.2d 317 (1970). But cf. *Vermilion County Prod. Credit Ass'n v. Izzard*, 111 Ill. App. 2d 190, 249 N.E.2d 352 (1969) (clause referring to proceeds cannot be used to establish consent to sale; discussing limited use of course of dealing or trade usage in establishing authority); *Wabasso State Bank v. Caldwell Packing Co.*, 251 N.W.2d 321, 325 (Minn. 1976) (relying on § 1-205(4) to conclude that "when the security agreement requires prior written authorization, it cannot be proved by a course of dealing").

251. See, e.g., *Sherrock v. Commercial Credit Corp.*, 277 A.2d 708 (Del. Super. Ct. 1971), *rev'd on other grounds*, 290 A.2d 648 (Del. 1972); *Mattek v. Malofsky*, 42 Wis. 2d 16, 165 N.W.2d 406 (1969); cf. *National Car Rental v. Fox*, 18 Ariz. App. 160, 500 P.2d 1148 (1972) (reliance on familiarity with business to deny status of good faith purchaser for value).

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prior owner.²⁵² Article 9's section on proceeds teaches that a security interest, once properly effected, survives unauthorized transfers without number.²⁵³ Logically, that teaching is impeccable: neither theft nor unauthorized disposition can be cured by the passage of time or distance. In practice, however, the survival of the security interest conflicts with the policy against secret liens.²⁵⁴ The 1972 revision of the proceeds section strikes a suggestive balance among these competing claims by requiring a secured creditor to reperfect when collateral in the form of proceeds changes identity or location.²⁵⁵ That solution does not apply, in terms, to the problems of priority raised by reacquisition, but it does suggest that a court can read "authority" so as to do commercial justice without doing violence to the basic principles²⁵⁶ of Article 9.

If third-party claims survive ABC's reacquisition of the contract goods from Family Furniture, resale by ABC that is unauthorized by Family Furniture's creditors means that ABC's buyers, even if they are buyers in the ordinary course of business, take subject to security in-

252. Examination of the files for recorded security interests will avail a buyer for ABC only if he knows to check under Family Furniture, an unlikely eventuality.

253. Section 9-306(2) states:

Except where this Article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof unless the disposition was authorized by the secured party in the security agreement or otherwise, and also continues in any identifiable proceeds including collections received by the debtor.

Section 9-307(1) is no longer of any possible use, since the security interests we are concerned with—those held by creditors of Family Furniture—are not "created" by ABC. *See, e.g., National Shawmut Bank v. Jones*, 108 N.H. 386, 236 A.2d 484 (1967); *Skilton*, *supra* note 154, at 7-9.

254. *See, e.g., In re Automated Bookbinding Servs., Inc.*, 471 F.2d 546, 553 (4th Cir. 1972); *Dunham, Inventory and Accounts Receivable Financing*, 62 HARV. L. REV. 588, 610-11 (1949).

255. Section 9-306(3), in the 1972 version, reads:

The security interest in proceeds is a continuously perfected security interest if the interest in the original collateral was perfected but it ceases to be a perfected security interest and becomes unperfected ten days after receipt of the proceeds by the debtor unless

- (a) a filed financing statement covers the original collateral and the proceeds are collateral in which a security interest may be perfected by filing in the office or offices where the financing statement has been filed and, if the proceeds are acquired with cash proceeds, the description of collateral in the financing statement indicates the types of property constituting the proceeds; or
- (b) a filed financing statement covers the original collateral and the proceeds are identifiable cash proceeds; or
- (c) the security interest in the proceeds is perfected before the expiration of the ten day period.

Except as provided in this section, a security interest in proceeds can be perfected only by the methods or under the circumstances permitted in this Article for original collateral of the same type.

256. Compare the suggestion of the ultimate dissent in *Stowers v. Mahon* (*In re Samuels & Co.*), 526 F.2d 1238, 1249 (5th Cir.) (en banc), *cert. denied*, 429 U.S. 834 (1976).

terests under Family Furniture. Resale after reacquisition thus involves a serious risk of liability for breach of warranty of title.²⁵⁷ The magnitude of this risk depends in large measure on the fungibility of the contract goods and on the volume of the seller's business, since a reclaiming third-party lienholder must always carry the burden of identifying goods as collateral. It depends as well on Family Furniture's financial responsibility, since only default by Family Furniture will send its creditors in hot pursuit of remote collateral.

The foregoing discussion has focused only on the possible continuing interests of secured parties vis-à-vis ABC as a repossessing seller. We observed earlier that the reacquiring seller who repossesses because of nonpayment might also be assimilated to the status of an unpaid secured party and thus be subject to Article 9 via section 9-113.²⁵⁸ As a secured party with a security interest belatedly perfected by possession, ABC encounters the same array of takers under Family Furniture as it did as a seller. But since ABC is now an Article 9 party, dealing with customers and lenders under Article 9, its priority position is not necessarily the same.

Article 9 unfortunately has few words of wisdom to enlighten secured parties about the consequences of transactions that move backwards, rather than forwards. There are, however, some clues. On the one hand, the proceeds section, as previously observed, makes security interests more difficult to detach than to attach.²⁵⁹ On the other hand, the assignment section, section 9-318, supports exercise of considerable commercial discretion.²⁶⁰ Clearly, that section does not apply in terms

257. Sections 2-312(1) and (2) state:

(1) Subject to subsection (2) there is in a contract for sale a warranty by the seller that

(a) the title conveyed shall be good, and its transfer rightful; and
 (b) the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.

(2) A warranty under subsection (1) will be excluded or modified only by specific language or by circumstances which give the buyer reason to know that the person selling does not claim title in himself or that he is purporting to sell only such right or title as he or a third person may have.

258. See pp. 933-34 *supra*.

259. See p. 975 *supra*.

260. Sections 9-318(1) and (2) read:

(1) Unless an account debtor has made an enforceable agreement not to assert defenses or claims arising out of a sale as provided in Section 9-206 the rights of an assignee are subject to

(a) all the terms of the contract between the account debtor and assignor and any defense or claim arising therefrom; and
 (b) any other defense or claim of the account debtor against the assignor which accrues before the account debtor receives notification of the assignment.

(2) So far as the right to payment or a part thereof under an assigned contract has not been fully earned by performance, and notwithstanding notification of the assign-

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to reacquisition by a seller of goods; it deals specifically only with assignment of accounts. Its guidelines are nonetheless instructive because they are unusually flexible for Article 9. In subsection (2), neither assignment of an account nor notification of the account debtor of the assignment defeats the continuing right of the parties to the underlying contract to make "any modification of or substitution for the contract . . . in good faith and in accordance with reasonable commercial standards." Even a provision in the security agreement interdicting such a modification or substitution and calling it an event of breach does not make a good faith modification or substitution ineffective against the assignee. At the very least, section 9-318 establishes that subsequent secured transactions do not necessarily lock the original parties into a contract that they decide in good faith to alter. If modification is a tolerable form of alteration, presumably abandonment would be, too; and then default cannot be far behind.²⁶¹ What good faith requires and what is commercially reasonable of course need elucidation.²⁶² But the message of section 9-318 lends itself to the comparison of equities and thus furnishes a useful counterweight to the more rigid instructions of the proceeds section.

Finally, priority rules about one recurrent type of reacquisition are codified in Article 9. If a seller of goods has transferred to a secured party either an account or chattel paper generated by his sale, and if the goods are reacquired by the seller or by the secured party, section 9-306(5) applies.²⁶³ In the ABC-Family Furniture transaction, one situa-

ment, any modification of or substitution for the contract made in good faith and in accordance with reasonable commercial standards is effective against an assignee unless the account debtor has otherwise agreed but the assignee acquires corresponding rights under the modified or substituted contract. The assignment may provide that such modification or substitution is a breach by the assignor.

261. See, e.g., 2 G. GILMORE, *supra* note 29, at 1117-21.

262. See *id.* at 1107-10, 1120-21; *cf.* *Brice v. Bannister*, 3 Q.B.D. 569, 579-80 (1878) (dissenting opinion of Brett, L.J.) (favoring facilitating good faith modification by "parties to an unfilled contract," even when confronted by claim of equitable assignee).

263. Section 9-306(5) reads:

If a sale of goods results in an account or chattel paper which is transferred by the seller to a secured party, and if the goods are returned to or are repossessed by the seller or the secured party, the following rules determine priorities:

- (a) If the goods were collateral at the time of sale, for an indebtedness of the seller which is still unpaid, the original security interest attaches again to the goods and continues as a perfected security interest if it was perfected at the time when the goods were sold. If the security interest was originally perfected by a filing which is still effective, nothing further is required to continue the perfected status; in any other case, the secured party must take possession of the returned or repossessed goods or must file.
- (b) An unpaid transferee of the chattel paper has a security interest in the goods against the transferor. Such security interest is prior to a security interest

tion that section 9-306(5) contemplates is a sale by Family Furniture to one of its customers, on time, which creates either an account or chattel paper. If Family Furniture transfers the account or chattel paper to another secured party and then reacquires the sofa from its customer, section 9-306(5) describes the rights of ABC as inventory financier against the transferee secured party.

Because the rules of section 9-306(5) are complex or downright mysterious, they warrant some explication.²⁶⁴ At the moment *before* reacquisition by Family Furniture, the section contemplates the simultaneous existence of two or three security interests. Family Furniture is a secured debtor on its inventory collateral to ABC, the inventory secured party (here we assume that ABC has taken or is deemed under section 9-113 to have an Article 9 security interest); Family Furniture is also a secured debtor on its transfer of accounts or chattel paper to the transferee secured party.²⁶⁵ Family Furniture is a secured debtor in both of these transactions, but the collateral is not the same, since ABC's basic collateral is sofas, while the transferee's basic collateral is the monetary claim to collect from Family Furniture's customer. If ABC's customer received the sofa on open credit and without further ado, then there are no other security interests. The customer's obligation to pay is an account, which is transferable and which has been transferred. ABC would have an interest in this account as proceeds but would lose to the transferee if the assignment of accounts were the first to be perfected.²⁶⁶ If, on the other hand, the customer signed a

asserted under paragraph (a) to the extent that the transferee of the chattel paper was entitled to priority under Section 9-308.

- (c) An unpaid transferee of the account has a security interest in the goods against the transferor. Such security interest is subordinate to a security interest asserted under paragraph (a).
- (d) A security interest of an unpaid transferee asserted under paragraph (b) or (c) must be perfected for protection against creditors of the transferor and purchasers of the returned or repossessed goods.

264. See generally 2 G. GILMORE, *supra* note 29, at 736-42; Lord, *Rights of Secured Creditors in Returned and Repossessed Goods under the Uniform Commercial Code: A Study of Section 9-306(5)*, 15 DUQ. L. REV. 165 (1976-77).

265. Section 9-106 states that an "[a]ccount" means any right to payment for goods sold or leased or for services rendered which is not evidenced by an instrument or chattel paper, whether or not it has been earned by performance." Section 9-105(1)(b) states that "Chattel paper" means a writing or writings which evidence both a monetary obligation and a security interest in or a lease of specific goods, but a charter or other contract involving the use or hire of a vessel is not chattel paper. When a transaction is evidenced both by such a security agreement or a lease and by an instrument or a series of instruments, the group of writings taken together constitutes chattel paper

266. Section 9-312(5) provides:

In all cases not governed by other rules stated in this section (including cases of purchase money security interests which do not qualify for the special priorities set forth in subsections (3) and (4) of this section), priority between conflicting security

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security agreement, then there is a third security interest. In this third secured transaction, Family Furniture occupies the position of secured creditor, the customer is the debtor, and the sofa is the collateral. In the hands of Family Furniture, this security interest, which is chattel paper, is once again an asset to which ABC has a claim as proceeds. Transfer of the chattel paper establishes and perfects the secured transaction between Family Furniture and the transferee, and assigns to the transferee Family Furniture's rights against the customer. The transferee for new value who takes possession has a perfected security interest in the chattel paper prior to the inventory financier's proceeds interest,²⁶⁷ but he does not automatically have a perfected security interest in the sofa. If the sofa was bought not for personal purposes but to furnish, say, an office, perfection requires filing.²⁶⁸

At the moment *after* reacquisition of the sofa by Family Furniture or its transferee, section 9-306(5) contemplates the simultaneous existence of all of the above, plus more. ABC's security interest in the sofa, which in all probability had been divested by the earlier sale to the customer,²⁶⁹ reattaches.²⁷⁰ Significantly, ABC's lien revives without apparent regard to the customer's status or to the reason for the customer's loss of the sofa. Although retaking by Family Furniture thus appears

interests in the same collateral shall be determined according to the following rules:

- (a) Conflicting security interests rank according to priority in time of filing or perfection. Priority dates from the time a filing is first made covering the collateral or the time the security interest is first perfected, whichever is earlier, provided that there is no period thereafter when there is neither filing nor perfection.
- (b) So long as conflicting security interests are unperfected, the first to attach has priority.

See 2 G. GILMORE, *supra* note 29, at 735.

267. Section 9-308 provides:

Purchase of Chattel Paper and Instruments

A purchaser of chattel paper or an instrument who gives new value and takes possession of it in the ordinary course of his business has priority over a security interest in the chattel paper or instrument

- (a) which is perfected under Section 9-304 (permissive filing and temporary perfection) or under Section 9-306 (perfection as to proceeds) if he acts without knowledge that the specific paper or instrument is subject to a security interest; or
- (b) which is claimed merely as proceeds of inventory subject to a security interest (Section 9-306) even though he knows that the specific paper or instrument is subject to the security interest.

268. The holder of chattel paper has an interest not only in the paper, but also in the goods, § 9-105(1)(b); Lord, *supra* note 264, at 170; cf. Levic, *Security Interests in Chattel Paper*, 78 YALE L.J. 935, 939, 953 (1969) (security interest in chattel paper includes "by definition an interest in the rights of [a dealer] to the collateral which secures the first level transaction"). Section 9-302(1)(d) excepts from the filing requirement "a purchase money security interest in consumer goods." See § 9-302(2); 2 G. GILMORE, *supra* note 29, at 737-38.

269. See §§ 9-306(2); 9-307(1).

270. Section 9-306(5)(a).

to improve ABC's priority against customers and to support the notion that the status of buyer-in-due-course requires possession, retaking does not otherwise do much to improve ABC's position. In particular, section 9-306(5)(b) makes clear that the unpaid transferee of chattel paper, holding a perfected prior interest in the chattel paper while the customer had the sofa, now has a prior interest in the returned sofa as well.²⁷¹ Reacquisition by Family Furniture is only helpful to ABC in that it may facilitate ABC's own reacquisition and thereby allow ABC belatedly to perfect its security interest and possibly (though just barely possibly) to take priority over a transferee of accounts who has been even slower to perfect.²⁷²

These priority rules established by section 9-306(5) appear plausible when read quickly. After all, customers do ordinarily take free of their seller's security interests by virtue of section 9-307, and transfers of chattel paper do ordinarily generate further proceeds that should amply satisfy an inventory financier. In other words, ABC is made whole by Family Furniture's receipt of new value from the transfer of the chattel paper, since Family Furniture can be compelled to deliver to ABC the moneys generated thereby. If ABC allows Family Furniture to squander this money elsewhere, ABC cannot be heard to complain of its own foolishness.

Section 9-306(5), however, is neither so simple nor so satisfactory. It is odd that it covers the chattel paper financier who is a transferee from the seller but is silent about the lender who directly finances the customer and thus generates the chattel paper.²⁷³ It is even odder that the mechanism for protecting the chattel paper transferee depends on the creation by statutory fiat of new secured collateral. Before the section 9-306(5) retaking, the transferee could not have exercised a possessory right to the sofa upon the default of Family Furniture, its debtor, since the sofa was not collateral between Family Furniture and

271. Section 9-306(5)(b) states:

An unpaid transferee of the chattel paper has a security interest in the goods against the transferor. Such security interest is prior to a security interest asserted under paragraph (a) to the extent that the transferee of the chattel paper was entitled to priority under Section 9-308.

See generally 2 G. GILMORE, *supra* note 29, at 737-39.

272. Under § 9-306(5)(c), a transferee of an account gets a security interest in the returned goods. Although this security interest is subordinated to ABC's perfected security interest, this does not aid ABC, for, if it were perfected, it already had priority over the holder of the account prior to this time. See 2 G. GILMORE, *supra* note 29, at 735, 741.

273. Professor Gilmore writes that the policy reasons remain the same, and that "there is no discernable reason why the rule of subsection (a) should not apply in favor of a secured party who had an interest in the goods even when there has not been a subsequent transfer of the resulting receivables." 2 G. GILMORE, *supra* note 29, at 736. He suggests that § 9-306(5) should be read to cover both situations. *Id.* at 737.

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the transferee.²⁷⁴ After the section 9-306(5) retaking, without amendment of the security agreement, the sofa becomes collateral. What has happened to the customer's rights to the sofa? Has the customer's security interest been extinguished by the retaking? Surely not, according to Part 5 of Article 9.²⁷⁵ The sofa has become a commercial football, and any number can play. If Family Furniture defaults to ABC, ABC can claim the sofa as security for the indebtedness of Family Furniture; if Family Furniture defaults to the chattel paper transferee, the transferee can claim the sofa as security for the indebtedness of Family Furniture; if the customer defaults to Family Furniture or its assignee, the chattel paper transferee, the chattel paper transferee can claim the sofa as security for the indebtedness of the customer.

The rules of section 9-306(5) order the rights of claimants against Family Furniture; they do not order, but arguably confuse, the rights of the customer. If, for example, repossession from the customer was improper, subsequent default by Family Furniture should not give rights in the sofa to either ABC or the chattel paper transferee. If the repossession was proper, in that it was consented to by the customer, it may have been accomplished by the seller even though the seller is no longer the effective secured party because of the assignment of the chattel paper. Section 9-306(5) states that the statutory lien it creates will require perfection for protection against purchasers of the returned or repossessed goods.²⁷⁶ Thus the seller in possession can proceed to resell (or to return the goods to ABC?) until the transferee files to give notice of his claim to the sofa against Family Furniture as debtor. This will be an unusual filing, to say the least, and, unless the transferee was exceptionally clairvoyant, an unlikely event until after the retaking by Family Furniture.²⁷⁷ For the earlier chattel paper transaction was perfected as to the sofa, if there was a filing, by filing against the cus-

274. The transferee received the rights of Family Furniture as against the customer, but, in that transaction, Family Furniture occupied the role of creditor, not debtor. In the transaction that transfers the chattel paper to the transferee, Family Furniture is a debtor, to be sure, but the sofa is not collateral securing *that* debt.

275. As a debtor, despite default, the customer has rights of redemption and rights concerning liquidation. As a secured lender, the transferee of chattel paper, despite the customer's default, has rights at least as a junior lienor, if he does not have priority.

276. Section 9-306(5)(d) requires that:

A security interest of an unpaid transferee asserted under paragraph (b) or (c) must be perfected for protection against creditors of the transferor and purchasers of the returned or repossessed goods.

277. Cf. Skilton, *supra* note 154, at 9 (noting that § 9-306(5)(d) "contemplates a filing as to the goods naming the dealer as debtor"). But see 2 G. GILMORE, *supra* note 29, at 738 ("There is no reason, however, why the financing statement cannot be drafted so as to cover both the chattel paper and the underlying goods in case of returns and repossessions.")

tomers, a different debtor, and as to the monetary claim, not by filing but by taking the papers.²⁷⁸ Even if this unusual event can be brought to pass, its payoff can hardly be clear. Resale purchasers at liquidation sales, as after repossession, are protected by section 9-504 from other junior liens if they buy in good faith;²⁷⁹ should they suddenly be vulnerable to these odd liens, perfected or not? Buyers in ordinary course are notoriously immune to perfection, particularly when their sellers have created the disputed security interest; should they then be forced to distinguish between security interests "created" consensually and those "created" by statute?²⁸⁰ Section 9-306(5) is a maze of blind alleys, a misguided venture into overly specific solutions for intractably complex problems.²⁸¹

Perhaps the best approach to section 9-306(5) is to treat it, with respect, less as a set of binding directives than as a suggestive approach to complex realities. What, then, could one take from the section? Re-acquisition by sellers is commercially reasonable in a great variety of circumstances, despite many competing interests. In sorting out these competing claims, commercial law should facilitate modification and substitution of collateral when collectibility is impaired.²⁸² But the process of substitution should take into account the obligation to give

278. Section 9-305 provides that "[a] security interest in . . . chattel paper may be perfected by the secured party's taking possession of the collateral," a point that is re-emphasized in § 9-302(1)(a). See 2 G. GILMORE, *supra* note 29, at 737 ("If the secured party had perfected his interest by taking possession of the chattel paper, he would have to reperfect his interest in the goods either by filing or by taking possession [of the goods].")

279. Section 9-504(4) provides that:

When collateral is disposed of by a secured party after default, the disposition transfers to a purchaser for value all of the debtor's rights therein, discharges the security interest under which it is made and any security interest or lien subordinate thereto. The purchaser takes free of all such rights and interests even though the secured party fails to comply with the requirements of this Part or of any judicial proceedings

(a) in the case of a public sale, if the purchaser has no knowledge of any defects in the sale and if he does not buy in collusion with the secured party, other bidders or the person conducting the sale; or

(b) in any other case, if the purchaser acts in good faith.

280. We suggested earlier that the answer was no, see p. 951 *supra*. Comment 4 to § 9-306 appears to agree:

If the dealer thereafter sells the chattel to a buyer in ordinary course of business in any of the foregoing cases [discussing § 9-306(5)], the buyer is fully protected under Section 2-403(2) as well as under Section 9-307(1), whichever is technically applicable. See also Skilton, *supra* note 154, at 8-9.

281. In a slightly different vein, Professor Gilmore has suggested that § 9-306(5) should be used, by analogy, to cover transactions resulting in accounts or chattel paper, even if there is no transfer, 2 G. GILMORE, *supra* note 29, at 736, and that "the same rules should apply, by analogy," to a sale that gives rise to negotiable instruments, *id.* at 741.

282. This is clearly the rationale underlying § 9-306(5). See 2 G. GILMORE, *supra* note 29, at 738, 741.

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notice of changes to innocent third parties.²⁸³ On this admittedly oversimplified level, section 9-306(5) becomes spiritually a first cousin of the assignment section, section 9-318. Issues of priority that cannot be resolved categorically have to be managed by choosing among irreconcilables as best we can.

This reading brings the rights of ABC as a hybrid secured party into close alignment with its rights as an ordinary reacquiring seller. Other things being equal, ABC's priority against other secured parties should be governed by the first-to-file rule, so that ABC, perfected by repossession, should not be burdened by competing claims that remain unperfected at the time of its reacquisition. ABC, however, cannot avoid the claims of those who have a perfected interest against Family Furniture or Family Furniture's customers. Again, it is the latent claims of the secured creditors of Family Furniture's customers that are most troublesome. Although repossession by Family Furniture cannot extinguish such claims, courts have a special obligation to inquire into possible arguments of estoppel in such cases. If repossession is triggered by the customer's inability to pay, for example, a secured lender might well be deemed to be on notice that default frequently leads to repossession and repossession frequently leads to resale. For the protection of others more innocent, a secured lender's failure to intervene should be deemed an acquiescence in the seller's repossession and an entrusting of the collateral to the repossessing seller.²⁸⁴

Revival of claims of ownership by a reacquiring seller of goods is necessarily a perilous undertaking. So long as Article 9 is read with sensitivity to commercial realities, it probably matters little whether the original seller is thought to have or to regain a security interest. Either way, reasonable commercial expectations will stand a reasonable chance of protection. If Article 9 is read literally and applied peremptorily, on the other hand, no seller can safely reacquire goods without an assurance of indemnity from a willing and solvent buyer. Such indemnities are likely to be awkward to acquire.

Conclusion

The world of the Uniform Commercial Code is a more complicated world than the one for which Williston wrote the Uniform Sales Act

283. Cf. § 9-306(5)(d) (requirement of perfection of unpaid transferee's § 9-306(5)(b) or (c) security interest "for protection against creditors of the transferor and purchasers of the returned or repossessed goods").

284. Cf. § 9-306(2) (providing for continuation of security interests in collateral unless disposition authorized). This, of course, would be true whether the lenders are those of Family Furniture itself, or those of customers of Family Furniture.

and the *Treatise on Sales*. The world of Article 9 on first reading—and second and third—is, in turn, more intricate than the world of Article 2. This is due in part to the more resounding accomplishment, when compared with prior law, that is Article 9. Yet it is due also to the fact that Karl Llewellyn's original vision of Article 2 survived the process of drafting and enactment largely intact, whereas the vision of Llewellyn, Grant Gilmore, and Allison Dunham for Article 9 met resistance from those who felt more secure in precision.²⁸⁵ Professor Gilmore has reminded, gently but repeatedly, that the inevitability of change will render functionless a commercial statute too inflexible to adapt.²⁸⁶ The structural simplicity of Article 2 enhances its capacity to respond to the complexities of the real world, to the large and evolving variety of "commercial" transactions. The capacity of Article 9 to adapt to changing commercial realities depends on accommodating demands for rigor in the short run and for transactional sense and adjustment to new problems in the long run.

Just as rights under Article 2 must take into account competing claims under Article 9, so too must those claims be read with an Article 2 understanding of the underlying obligation. So viewed, Article 9, like Article 2, can provide commercial parties with a framework for achieving reasonable commercial ends with reasonable certainty. Commercial statutes work better and live longer when they dispense organizing principles that reasonably guide rather than detailed rules that insistently bind.

In *The Death of Contract*, Professor Gilmore suggests that in the development of law, as in literature and the arts, there are brief classical periods in which "everything is neat, tidy and logical."²⁸⁷ The drafting of codes is one manifestation of the classical aspiration to a formal, highly structured legal system. The reactions to the classical periods, Professor Gilmore suggests, are romantic periods characterized by a preference for an open-ended, improvisational approach to society. In law, the romanticism of some legal realists urged the transformation of all issues into questions of fact for resolution by juries. Neither or-

285. See Gilmore, *On Statutory Obsolescence*, 39 U. COLO. L. REV. 461, 472-73 (1967); cf. G. GILMORE, *THE AGES OF AMERICAN LAW* 85 (1977) (discussing influence of practicing lawyers on drafting of Code).

286. See, e.g., G. GILMORE, *supra* note 285, at 85; Gilmore, *supra* note 3, at 461; Gilmore, *supra* note 285, at 472-77; Gilmore, *In Memoriam: Karl Llewellyn*, 71 YALE L.J. 813, 814-15 (1962); Gilmore, *supra* note 60, at 1121-22.

287. G. GILMORE, *THE DEATH OF CONTRACT* 102 (1974).

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ganizing principles nor detailed rules were thought necessary or useful.²⁸⁸

Commercial law is not well suited to either the classical or the romantic models at their extremes. The learning from all of the great commercial lawyers—Mansfield, Cardozo, Llewellyn, and Gilmore—has always been that the legal system must draw on the commercial sense of the transaction and the parties, in a process that must have boundaries while retaining elasticity as well. Over twenty years ago, Professor Gilmore noted that

[t]he only legal certainty is the certainty of legal change. But if we keep our categories broad and flexible, we can, as lawyers, do a good deal to see that the change which will come in any case is helped into being, is integrated into the body of the law as part of an ordered pattern and not left to come lurching and banging destructively into the vulnerable framework of a too rigidly conceived structure of doctrine, principles and rules.²⁸⁹

A commercial code that is too ambitious, that purports alone to impose order on the commercial world, will destroy itself.²⁹⁰ It will invite avoidance and amendment and will fuel litigation.²⁹¹ Yet reasonably construed, with a sense of history as well as of the present, a code can also aid the growth of the commercial world by a combination of guidance and flexibility.²⁹² This, we believe, is the lesson that an examination of transactions that straddle Articles 2 and 9 brings home with particular clarity. Read literally and peremptorily, the Code solutions vacillate in an almost schizophrenic manner, resulting from the apparent inattention to the relation of Article 9 to Article 2. Yet read sensibly, with an understanding not only of the scheme of Article

288. *Id.*

289. Gilmore, *supra* note 60, at 1121-22.

290. Professor Gilmore has quoted, with approval, the observation of Justice Story: We ought not to permit ourselves to indulge in the theoretical extravagances of some well-meaning philosophical jurists, who believe that all human concerns for the future can be provided for in a code, speaking a definite language. Sufficient for us will be the achievement, to reduce the past to order and certainty; and that this is within our reach cannot be a matter of doubtful speculation.

J. STORY, *On the Progress of Jurisprudence* (Address to the Suffolk Bar Association, 1821), in MISCELLANEOUS WRITINGS OF JOSEPH STORY 198, 238 (1852), *quoted in* Gilmore, *supra* note 285, at 476 n.30.

291. *See* Gilmore, *supra* note 3, at 461.

292. A preference for contextual decisionmaking on a case-by-case basis need not depend on exaggerated expectations of judicial infallibility. True, legal implications are more likely to be perceived accurately in the actual circumstances of litigated cases than in the hypothetical speculation that necessarily attends legislative drafting. But even if courts and legislators err with equal frequency, the zone of exposure created by judicial error is clearly narrower and more readily correctable than that created by legislative error.

9 but also of the nature of the underlying Article 2 transaction, the structure adapts. The Uniform Commercial Code, even in Article 9, is sufficiently open-textured that it can be interpreted, in the common law tradition, as a "case-law Code" of vital importance to a continuously changing world.²⁹³

293. The term "case-law Code" is Professor Gilmore's, which he used to describe what he perceived to be the ideal of Karl Llewellyn in drafting the Uniform Commercial Code. Gilmore, *supra* note 286, at 814-15:

It was, I believe, Karl's non-systematic, particularizing cast of mind and his case-law orientation which gave to the statutes he drafted, and particularly to the Code, their profound originality. . . . His instinct appeared to be to draft in a loose, open-ended style; his preferred solutions turned on questions of fact (reasonableness, good faith, usage of trade) rather than on rules of law. He had clearly in mind the idea of a case-law Code: one that would furnish guide-lines for a fresh start, would accommodate itself to changing circumstances, would not so much contain the law as free it for a new growth. . . . I have come to feel that Karl saw more clearly than his critics and that the Code as he initially conceived it might better have served the purposes of the next fifty years.

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