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The Intersections of Articles 2 and 9: Recommendations for Clarification and Revisions

Richard E. Speidel

Northwestern University School of Law

James J. White

University of Michigan Law School, jjwhite@umich.edu

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The Intersections of Articles 2 and 9: Recommendations for
Clarification and Revisions

By

Richard E. Speidel
Northwestern University School of Law
Chicago, Illinois

and

James J. White
University of Michigan Law School
Ann Arbor, Michigan

**The Intersections of Articles 2 and 9: Recommendations for
Clarification and Revisions**

Richard E. Speidel
Northwestern University School of Law

James J. White
University of Michigan Law School

1. Introduction

Both Article 2, Sales and Article 9, Secured Transactions are under revision. The process of coordination is underway, but there is still much work to do. The following materials identify the major issues at the intersections and some tentative solutions.

All references are to the 1990 Official Text of the Uniform Commercial Code unless otherwise stated. When stated, references are to the October, 1995 Draft of Article 2 and the July, 1995 Draft of Article 9.

2. Scope in General

A. Article 2.

Article 2, deals with "transactions in goods" which, in most cases, are contracts for the sale of goods. §2-102. See §2-103(a) (Oct. 1995). "Goods" are defined in §2-105(1) as "all things...that a movable at the time of identification to the contract for sale," with certain specific inclusions and exclusions. See § 2-102(a)(25) (Oct. 1995).

B. Article 9.

Article 9 applies to "any transaction (regardless of form) which is intended to create a security interest in personal property or fixtures including goods...." §9-102(1). "Security interest" is defined in §1-201(37) as an "interest in personal property or fixtures which secures payment or performance of an obligation." "Goods" for Article 9 are defined in §9-105(1)(h) and classified for purposes of perfection and priority in §9-109. See §§9-105(a)(18) & 9-109 (July 1995).

C. Overlaps.

Obvious overlaps between Article 2 and Article 9 arise when either the seller or the buyer has a security interest in goods that are the subject of a contract for sale. Article 9 may also be involved where a creditor of or purchaser from the seller or buyer claims the goods. The definition of "security interest" helps to draw lines here.

Title retention. For example, the seller has a security interest if it retains or reserves title to the goods

"notwithstanding shipment or delivery to the buyer." §§1-201(37) & 2-401(2). See §2-401(b)(2) (Oct. 1995). This security interest, however, is unperfected unless the seller complies with the perfection requirements of §§9-302 through 9-306 of Article 9. The risk of failing to perfect is clear: The security interest is subordinate to the creditors and purchasers stated in §9-301(1) and is vulnerable to the trustee in bankruptcy as a "lien" creditor under Section 544(a) of the Bankruptcy Code. See §9-301(1)(c) & (3).

Special property interest. On the other hand, the "special property interest of a buyer of goods on identification of those 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." See §§2-401(1) & 2-501(1). Thus, a buyer who replevies identified goods under §2-716(3) is enforcing an Article 2 special property interest rather than an Article 9 security interest. See §2-707(c) (Oct. 1995). A financing or pre-paying buyer, however, could perfect a security interest in goods still in the seller's possession under Article 9.

Scope provisions. The scope provision of the current Article 2 does not deal with the case where a sale and a security interest are involved in the same transaction. Section 2-102 provides that Article 2 "does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate only as a security transaction." Although §2-102 is silent in the mixed transaction, Article 9 seems to overstate its scope: Section 9-102(1)(a) states that Article 9 applies to "any transaction (regardless of form) which is intended to create a security interest in personal property." Presumably, Article 9 only applies to that part of the sales transaction where the creation, perfection, priority and enforcement of a security interest are at stake.

Section 2-103(c) (Oct. 1995) tries to help by providing that if Article 2 "conflicts with Article 2A or 9, those articles govern." This is another way of saying that if the seller or buyer has a security interest as defined in §1-201(37), Article 9 applies to the perfection, priority and enforcement of that interest and preempts Article 2 in cases of conflict.

Can we do better than this?

D. Other transactions.

The interest of a lessor, a consignor or a bailor in goods entrusted to another may or may not be a security interest. If it is not, Article 9 does not apply. For leases of goods, Article 2A applies.

Leases of goods. Whether a transaction creates a lease or a security interest is determined by the complex and elaborate test

in §1-201(37). The focus is upon the economics of the transaction rather than the intention of the parties. See *In re Allen*, 174 B.R. 1156 (D. Ore. 1994) (purported lease a true lease and not a disguised installment sale). If a "true" lease is created, neither Article 2 nor Article 9 apply. Thus, the lessor's interest in leased goods, see §2A-103(1)(m) & (q), is enforceable by repossession upon the lessee's default without complying with the filing or any other requirements of Article 9. See §2A-525. As a precaution, the lessor may file a financing statement covering leased goods under Article 9. §9-408. See §9-408 (July 1995)(same).

Consignments. Section 1-201(37) provides that reservation of title in a "consignment" does not create a security interest unless the consignment is "intended as security." But a consignment in "any event is subject to the provisions on consignment sales (Section 2-326)." The consignment problem will be discussed, infra.

Bailments. Although §1-201(37) does not say, the ownership interest of a bailor of goods is not without more a security interest. The bailor can recover goods upon default by the bailee without regard to Article 9. Nevertheless, a bailment intended as security does create a security interest subject to Article 9. Whether a purported bailment actually creates a security interest is a complex question for which the UCC provides no answer. See *In re Sitkin Smelting and Refining, Inc.*, 639 F.2d 1213 (5th Cir. 1981); R. Speidel, R. Summers and J. White, *Sales and Secured Transactions: Teaching Materials* 371-381 (5th ed. 1993).

3. Interest of the Seller.

A. The problem.

In a contract for sale, the buyer may be obligated to pay the price before, at or after delivery of the goods. Exactly when the buyer must pay depends upon the agreement of the parties or the "default rules" of Article 2. See §§2-507, 2-511 and 2-310.

Upon default in payment, the seller may wish to retain or regain possession of the goods and pursue appropriate remedies. Assuming that the seller does not have a perfected security interest in the goods created by agreement with the buyer, to what extent can the seller retain or regain possession of the goods under Article 2 without preemption by Article 9? More importantly, what is the effect of any right to possession as against the buyer against creditors of or purchasers from the buyer? The answer depends upon whether the goods have been delivered to the buyer at the time of default.

Although A sale "consists in the passing of title from the seller to the buyer for a price (Section 2-401)," see §2-106(1), and elaborate rules for when title passes are provided, §2-401, title is irrelevant to defining the seller's rights or drawing

the lines between Articles 2 and 9. See §9-202, in accord. From the seller's perspective, possession or the right to possession is and should be the key.

B. Seller has possession or right to possession of goods

In the following examples, assume that the buyer has agreed to pay the price at or before delivery and the buyer does not yet have possession or the right to possession of the goods. The goods are in the possession of either the seller, the seller's bailee or a carrier en route to the buyer.

If the buyer is insolvent or defaults in payment, at least three questions must be answered:

(1) Does the seller have the right to retain or regain possession under Article 2;

(2) If so, is that right a security interest "arising under" Article 2 as conceived by §9-113; and

(3) If the seller has a right to possession against the buyer, (a) what are the seller's remedies and (b) to what extent are they limited by the rights of creditors of or purchasers from the buyer? Neither the current UCC nor the caselaw provide satisfactory answers to this last question. See James J. White & Robert S. Summers, Uniform Commercial Code § 21-9 (4th ed. 1995).

1. Seller in possession, Buyer insolvent or defaults.

(a) Insolvency.

Insolvency is defined in §1-201(23). Unless otherwise agreement, insolvency alone is neither a repudiation nor a default by the buyer.

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..." Section 2-705. §2-702(1). See §2-718(a) (Oct. 1995)(same). In effect, insolvency of the buyer converts a credit transaction to a cash transaction.

Section 2-705(1) provides that 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)..." See §2-718(b) (Oct. 1995)(same). Assuming that timely notice is given to the carrier, subsection (3), the right to stop against the buyer continues until the buyer receives the goods, see *In re Bill's Dollar Stores, Inc.*, 164 B.R. 471 (D. Del. 1994) (when buyer received possession under §2-705 and §546(c) of the Bankruptcy Code), or has a right to goods in the possession of a bailee or carrier, subsection (2). See *Siderpali, S.P.A. v. Judal Industries, Inc.*, 833 F.

Supp. 1023 (S.D.N.Y. 1993) (carrier issues bill of lading to buyer).

Is the seller's right to withhold delivery or stop in transit because of the buyer's insolvency a "security interest arising solely under the Article on Sales?" See §9-113. Since the buyer is not yet in default (the stoppage is conditional), the answer appears to be no. See §9-113, comment 1, which omits references to insolvency. But since the rights are similar to those of a secured party, there should be a clear answer to this question and the preferable answer is yes.

If insolvency rights are security interests arising solely under Article 2, §9-113, these legal consequences follow "so long as the debtor does not have or does not lawfully obtain possession of the goods":

1. No security agreement is necessary to make the security interest enforceable;
2. No filing is required to perfect the security interest;
3. The rights and remedies of the seller as a secured party on default by the buyer are governed by Article 2 rather than by Article 9; and
4. Priorities and related problems are presumably governed by Article 9.

The seller's rights against creditors of and purchasers from the buyer are discussed, infra.

(b) Default in payment before delivery.

Buyer's failure to make a payment due "on or before delivery" is a breach of contract. §2-703. See §2-601(b) (Oct. 1995). It also provides clear grounds for demanding adequate assurance of due performance under §2-609.

A seller in possession may "with respect to any goods directly affected...withhold delivery of such goods." §2-703(a). See §2-715(1) Oct. 1995) (same).

In an installment contract, if the breach is of the "whole" contract the seller may "with respect to the whole undelivered balance...withhold delivery of such goods" and cancel the contract. §2-703. See §2-611 (Oct. 1995), where defaults in payment by the buyer are now specifically covered.

If the goods are in the possession of a bailee or a carrier when the buyer defaults, the seller's right to stop delivery, as with insolvency, is determined under §2-

705. Unlike insolvency, however, if the buyer fails to make a payment due before delivery the seller can stop delivery of only a "carload, truckload, planeload or larger shipment of express or freight." §2-705(1). This limitation has been removed in §2-718(b) (Oct. 1995).

The right to stop or withhold delivery is clearly a security interest arising "solely under Article 2." §9-113. It is enforceable against the buyer and effective against creditors of and purchasers from the buyer under Article 9.

(c) Rights and remedies after effective stoppage or withholding delivery

What are seller's remedies under Article 2?

Assuming that the buyer has breached and the seller has a security interest arising under Article 2, the seller's remedies are determined by Article 2 rather than Article 9. The seller's remedial options are stated in §2-703. See §2-715 (Oct. 1995).

If the seller is in possession or control of identified goods, an action for the price may be available if the seller is unable to resell them under §2-709(1)(b). See §2-722(a)(3) (Oct. 1995) (same).

If an action for the price is not available, the seller may resell the goods under §2-706. See §2-719 (Oct. 1995). If the resale is made in good faith and a commercially reasonable manner, the seller may recover the "difference between the resale price and the contract price" plus incidental damages. §2-706(1). But the seller is not accountable to the buyer for any profit made on the resale. §2-706(6).

Section 2-719 (Oct. 1995) deletes the requirement in §2-706(3) that the seller must give the buyer notice before a private resale. Notice is required when collateral is disposed of by sale under Article 9. See §9-504(g) (July 1995).

Under the October, 1995 Draft of Article 2, a seller may, in appropriate cases, have specific performance against the buyer, §2-707 (Oct. 1995), and recover consequential damages, §2-706 (Oct. 1995).

What about creditors of and purchasers from the buyer?

It is possible that a buyer will have title to or a special property interest in identified goods before taking delivery. It is also possible that a creditor of or a purchaser from the buyer² will claim the goods after the buyer's insolvency or default while they are

still in the seller's possession or control. How should priority disputes like this be resolved?

Although the buyer may have some rights in the goods, those rights are conditional against the seller upon performing the contract as agreed. A secured party whose security interests attaches to or a good faith purchaser of those rights, therefore, should be subject to the condition. In short, the seller should have a defense based upon the theory that the buyer is insolvent or has breached and the purchaser gets only the rights of the buyer and no more. See §2-403(1). See also, *In re Morrison Industries, L.P.*, 175 B.R. 5 (W.D.N.Y. 1994) (seller's justified refusal to deliver to insolvent buyer defense in bankruptcy).

The same result occurs under Article 9. In most cases, the seller's possessory security interest under §9-113 will predate the time when the interest of other secured parties or lien creditors attach or contract with good faith purchasers are made. The seller should have priority in these cases without resort to the conditional rights theory. See §§ 9-305 & 9-312 (July 1995).

What about the unusual case of a buyer who qualifies as a buyer in the ordinary course of business (BIOCB) under §1-201(37) even though the goods are not in its seller's possession? First, it cannot claim "all rights" of the original seller because that seller has not entrusted the goods to a merchant as required by §2-403(2) & (3). See §2-404 (Oct. 1995) (same). The seller has or controls possession at all times. Second, it is possible that the BIOCB might take free of the seller's security interest under §9-307(1). There is no explicit requirement that the seller have possession of the goods before a BIOCB can be created and some courts have so ruled. See, e.g., *Daniel v. Bank of Hayward*, 425 N.W.2d 416 (Wis. 1988). Even so, the BIOCB simply takes free of the seller's possessory security interest in whatever rights are purchased. Since those rights are conditional and there is no entrusting, the seller should prevail over the BIOCB under §2-403(1).

The best solution is to say clearly in § 9-113 or Article 2 that if the seller has a perfected security interest arising under Article 2 and the buyer is in default, third party claims to the goods where possession or control remains with the seller have no legal effect. The seller is free to pursue Article 2 remedies without fear from creditors of or purchasers from the buyer.

2. **Buyer has possession or control of the goods.**

The seller's right to reclaim goods from the buyer or to assert priority over secured parties or purchasers from the buyer becomes more tenuous when the buyer has possession or control of the goods before insolvency or default. For purposes of this discussion, possession means physical possession and "control" means that the buyer is the party entitled under a negotiable document of title or a seller may not longer stop delivery under §2-705(2) or a bailee has acknowledged to the buyer that it is entitled to possession. See §2-503(4).

(a) Seller perfects security interest in goods.

In these cases, §9-113 does not apply because the seller no longer has possession. The creation, perfection, priority and enforcement of the security interest is governed solely by Article 9.

For a discussion of the effect of retaining title after delivery, see supra at §2(C).

(b) Reclamation of goods.

At common law, the seller had a limited right to reclaim goods delivered to the buyer (1) in a credit transaction to an insolvent buyer, see §2-702(2), and (2) in a cash sale where payment was "due and demanded" upon delivery and payment, usually by check, failed when the check was dishonored, see §2-507(2). See also, §2-511(3). The reclamation right, when available, was not a security interest and did not depend upon any public notice or filing.

Under §2-716 (Oct. 1995), the seller's two reclamation rights are integrated into one section and are exercisable only as follows:

Section 2-716(a)(1) (Oct. 1995) provides: "A seller who discovers that the buyer has received goods while insolvent may reclaim the goods upon a demand made within 10 days after receipt. If a recorded [written] misrepresentation of solvency was made to the reclaiming seller less than three months before delivery, the demand is timely if made within a reasonable time after delivery."

Section 2-716(a)(2) (Oct. 1995) provides: "If payment is due and demanded on delivery to a buyer, a seller may reclaim the goods delivered upon a demand made within a reasonable time after the seller discovers or should have discovered that payment was not made." In most cases, this would involve a check or draft that "bounced."

Note that the different grounds for reclamation justify a different time period for making the demand. The

demand, however, is limited to the goods not the proceeds, but see *United States v. Westside Bank*, 732 F.2d 1258 (5th Cir. 1984), and §2-716 (Oct. 1995) does not specify how the reclamation should be made. Would "self help" work here?

What about creditors or purchasers from the buyer? Section 2-716(b) (Oct. 1995) provides: "A seller's right to reclaim under subsection (a) is subject to the rights under this article of a buyer in the ordinary course of business or other good-faith purchaser under this Article arising before the seller takes possession under a timely demand for reclamation." Thus, if the demand was timely but the purchaser's right arose before actual reclamation, the seller would be "subject to" that right. The priority contest between a seller entitled to reclaim under §2-716 (Oct. 1995) and a lien creditor is left to other state law.

In this setting, "good faith purchaser" includes a secured party whose after-acquired security interest attaches upon delivery to the buyer. See *In re Blinn Wholesale Drug Co., Inc.*, 164 B.R. 440 (E.D.N.Y. 1994) (extensive discussion of reclamation in bankruptcy).

Unlike §2-702(2) and (3), §2-716(a) and (b) (Oct. 1995) no longer provide that §2-716 is the exclusive ground for reclamation for the "buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay" and that "successful reclamation of goods excludes all other remedies with respect to them."

As with §2-702(2), the right to reclaim for insolvency is somewhat broader under §2-716(a)(1) (Oct. 1995) than under §546(c) of the Bankruptcy Code. See *In re Julien Co.*, 44 F.3d 426 (6th Cir. 1995) (no reclamation under §546(c) where buyer not insolvent under Bankruptcy Code and reclamation demand not in writing); *In re Adventist Living Centers, Inc.*, 52 F.3d 159 (7th Cir. 1995) (goods reclaimed must be in debtor's possession at time of reclamation demand). The right to reclaim in a cash sale is not treated in §546(c).

(c) Sale on Approval or Return; Consignments.

If goods are delivered under a contract that provides for their return upon specified events, the right to reclaim between the parties is clear. But what about creditors of the transferee? To what extent do they prevail over the transferor? See, generally, James J. White & Robert S. Summers, *Uniform Commercial Code* §21-4 (4th ed. 1995).

In a sale on approval, where the goods are delivered primarily for use, §2-326(1)(a), see 2-406(a)(1) (Oct.

1995) (same), the goods are not subject to claims of the buyer's creditors "until acceptance," unless §2-326(3), now §2-407, applies.

In a "sale or return," where the goods are delivered "primarily for resale," §2-326(1)(b), see §2-406(a)(1) (Oct. 1995) (same), goods are subject to the claims of the buyer's creditors while in the buyer's possession. §2-326(3), see §2-406(e) (Oct. 1995) (same), and are subject to §2-407 (Oct. 1995). See *In re Joy*, 169 B.R. 931 (D. Neb. 1994) (seller on sale or return fails to satisfy §2-326(2)).

In non-sale transactions, such as consignments not intended as security [where Article 9 clearly applies, see § 1-201(37)], the goods are subject to the claims of the consignee's creditors to the extent that §2-326(3), now §2-407 (Oct. 1995), applies.

Revised Section 2-407(a) (Oct. 1995) applies if goods (1) valued at more than \$1,000 are (2) delivered to a person other than an auctioneer (3) who deals in goods of that kind under a name other than the name of the person making delivery (4) for the purpose of sale." If these requirements are satisfied, the transaction is treated as a "consignment" even though other traditional requirements are not met.

If §2-407(a) applies, the "goods are subject to claims of creditors while in the possession of that person unless the requirements of subsection (b) are satisfied." The broad definition of "creditor" in §1-201(12) includes the Internal Revenue Service, see *Knight v. United States*, 838 F. Supp. 1243 (M.D. Tenn. 1993), and the lien of a landlord, *Lynch Austin Realty, Inc. v. Engler*, 647 So.2d 988 (Fla. App. 1994). The rights of purchasers from the person to whom the goods are delivered are determined under §2-403, now §2-404 (Oct. 1995). See also, *ITT Commercial Finance Corp. v. Unlimited Automotive, Inc.*, 166 B.R. 637 (N.D. Ill. 1994), where the requirements were not satisfied.

If the requirements of subsection (b) are satisfied, the person making delivery "has priority in the goods and any proceeds of sale over creditors of the person to whom the goods were delivered." §2-407(b) (Oct. 1995).

The requirements of subsection (b) are satisfied in two situations:

The person making delivery "establishes that the person to whom the goods were delivered is generally known by its creditors to be substantially engaged in selling the goods of others." This provision was in

§2-326(3). In light of the proof difficulties, should it be retained? See *In re Creative Goldsmith of Washington, D.C.*, 178 B.R. 87 (D. Md. 1995) (proof of general knowledge fails).

The person making delivery "complies with Section 9-114(a) or complies with the requirements for perfecting a security interest in the goods, to the extent provided in Section 9-114(a) or otherwise in Article 9."

The "sign law" exception in §2-326(3)(a) has been deleted.

If the consignment is not intended as security or the "consignor" does not create and perfect a security interest under Article 9, §9-114 states the effect of a consignment filing under §9-408. In essence, if the "consignor" makes what amounts to a "purchase money" filing, see §9-312(3), it has "priority over a secured party who is or becomes a creditor of the consignee and who would have a perfected security interest in the goods if they were the property of the consignee, and also has priority with respect to identifiable cash proceeds received on or before delivery of the goods to a buyer." § 9-114(1), see §9-114(a) (July 1995) (same). If the filing requirements are not met, "a person who delivers goods to another is subordinate to a person who would have a perfected security interest in the goods if they were the property of the debtor." §9-114(2).

4. Interests of Buyer

Suppose the seller becomes insolvent, repudiates or fails to deliver and, at the time of the insolvency or breach has goods identified to the contract in its possession. The buyer, who has a special property interest [but not a security interest, see §1-201(37)] in the goods, may have paid nothing or may have advanced all or part of the price. The buyer wants those goods from the seller free and clear of claims to them by creditors of or purchasers from the seller. The buyer, however, has not perfected a security interest in the goods under Article 9. Does Article 2 provide any help?

A. Recovery from the Seller.

(1) Specific Performance

Under §2-716(1), specific performance "may be decreed where the goods are unique or in other proper circumstances." Revised §2-707(a) (Oct. 1995) also authorizes specific performance "if the parties have expressly agreed to that remedy in their contract." See *Bandeer v. Brossman*, 611 N.Y.S.2d 985 (N.Y. Sup. Ct.).

1994) (reviewing grounds for specific performance). See also, White & Summers, supra at §6-6(c), favoring more specific performance.

Specific performance may be granted even though the goods have not been identified or the price paid. In essence, the seller is ordered to perform the contract and the buyer must pay the price as agreed. The court has control over the transaction through terms and conditions in the decree. §2-716(2), §2-707(b) (Oct. 1995).

2. Replevin

Under §2-716(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." This right is preserved in §2-707(c) (Oct. 1995), although the replevin language has been dropped.

Replevin may be available even though there is no specific performance decree and the buyer has not paid any of the price. It is in addition to the "buyer's right to recover identified goods on the seller's insolvency." Comment 3.

3. Seller's Insolvency

Section 2-502 provides limited grounds for a buyer of identified goods who has paid "part or all of the price" to "recover them" from an insolvent seller, even though the goods have not been shipped. These grounds are:

The buyer must make and keep good a tender of "any unpaid portion of the price;

The seller becomes insolvent "within ten days after receipt of the first installment on their price;" and

If identification is made by the buyer the goods must "conform to the contract for sale."

Revised §2-724 (Oct. 1995) provides: "A buyer who pays all or a part of the price of goods identified to the contract, whether or not they have been shipped, on making and keeping good a tender of full performance, may recover them from the seller if the seller repudiates or fails to deliver as required by the contract." This revision, which eliminates the insolvency requirement, provides increased protection under Article 2 to the "prepaying" or "financing" buyer.

B. Creditors of or Buyers from the seller.

Assume that as between the seller and the buyer, the buyer is entitled to specific performance or may recover identified goods under either §2-716(3), now §2-707(c) (Oct. 1995), or §2-502, now §2-724 (Oct. 1995). Assume also that the buyer does not have a security interest in the goods. To what extent is the buyer's right to recover subject to creditors of or purchasers from the seller?

(1) Creditors

Section 2-402 deals with rights of the seller's "unsecured creditors...with respect to goods which have been identified to a contract for sale" and presumably retained by the seller.

Rights of an "unsecured creditor" are "subject to the buyer's rights to recover the goods" under §§2-502 and 2-716 of the 1990 Official Text, except as provided in subsections (2) and (3). §2-402(1).

Subsection (2) states when a "creditor of the seller may treat a sale or an identification of goods to a contract as void" for fraud under other state law, except that "retention of possession in good faith and current course of trade by a merchant-seller for a commercially reasonable time after sale or identification is not fraudulent.

Subsection (3)(a) provides that "Nothing in this Article shall be deemed to impair the rights of creditors of the seller...under the provisions of the Article on Secured Transactions (Article 9)."

In sum, if the buyer has a right to replevin identified goods under §2-716(3), an unsecured creditor is subject to that right unless the seller's retention of possession was fraudulent under subsection (2). Article 9 would not apply.

There are two important changes in the October, 1995 revision of Article 2:

First, the prepaying or financing buyer's right to recover identified goods is broader in §2-724 (Oct. 1995) than it was in §2-502. The requirement that the seller be insolvent is deleted.

Second, in §2-405(a) (Oct. 1995), formerly §2-402, the phrase "unsecured creditors" is changed to "creditors," which includes "a general creditor, a secured creditor, a lien creditor...etc." §1-201(12). Thus, a secured creditor of the seller might be subject to the rights of a buyer with a special property interest under §2-724 unless the secured creditor's rights under Article 9, are impaired. §2-405(c)(1) (Oct. 1995).

Are those Article 9 rights impaired? Unless the buyer is a BIOCB under §9-307(1), the security interest would continue in the goods and the proceeds even though the buyer is entitled to possession. Thus, the buyer might win the possession battle under Article 2 but lose the priority war under Article 9, unless the buyer becomes a BIOCB at the time of identification.

There has been no litigation of significance under §2-402. In fact, it is not even cited in White and Summers.

(b) Buyers

Suppose that the buyer leaves goods identified under the contract for sale in the seller's possession and the seller, without authority, sells them to a good faith purchaser or a BIOCB. The parties' rights are determined by §2-403, now §2-404 (Oct. 1995), and security interests would normally not be involved.

Suppose a prepaying buyer creates and perfects a security interest in identified goods in the seller's possession. Suppose, also, that the seller, a merchant, sells those goods to a BIOCB. The BIOCB would take free of the security interest under §9-307(1).

C. Security Interest of Buyer after Rightful Rejection or Justifiable Revocation of Acceptance.

Section 2-711(3), now §2-723(c) (Oct. 1995), provides that the buyer has a security interest in goods in its possession after a rightful rejection or justifiable revocation of acceptance. The interest secures "payments made on their price and any expenses reasonably incurred in their inspection, receipt, transportation, care and custody."

Section 2-723(c) (Oct. 1995) clarifies that the buyer holds the goods subject to the duties of care imposed by §§2-605 and 2-606. In addition, the buyer with a security interest arising under this section must give the seller reasonable notification of any intended resale under §2-719 (Oct. 1995). Presumably, the buyer must account to the seller for any proceeds in excess of the amounts secured.

5. Conclusion

The following conclusions are suggested:

First, where either the seller or the buyer are in possession or control of identified goods and the other defaults, Article 2 should define the rights between the parties and, with Article 9, clarify the rights of other creditors of and purchasers from the party not in possession. In general, those creditors and purchasers should have no rights to the goods.

Second, where the goods are in the possession of the defaulting party and the other party seeks to recover them by asserting an Article 2 interest, as between the parties that right to possession should be honored. There are both historical and practical reasons for preserving and, in some cases, expanding these Article 2 reclamation or recovery interests.

Third, the rights of creditors of and purchasers from the party in possession, however, must be considered, especially where the creditor is a secured party. There is no public notice that goods in the possession of a seller or buyer are subject to an Article 2 interest held by the other party. Unlike consignment filings, however, there is no easy way for notice to be given of the Article 2 interest.

Fourth, if public notice is the key objective, a solution between the extremes of "all Article 2" or "all Article 9" is to expand §9-408, dealing with leases and consignment filings, to include the Article 2 interests and to clarify the priorities and remedies that follow a proper filing.