

December 14, 1995

**To: Article 2 Drafting Committee**

**From: Richard E. Speidel, Reporter**

**Re: Meeting with Article 9 Drafting Committee**

At the request of Reporters Harris and Mooney and the Chair, Bill Burke, I attended a meeting with the Article 9 Drafting Committee on Saturday, December 2, 1995 in Miami. In preparation for this first coordination meeting, I drafted a memo entitled "The Intersections of Articles 2 and 9: Recommendations for Clarification and Revisions", a copy of which is attached.

Here is a brief summary of what transpired:

1. The "scope" provision, 2-103(c) (Oct. 1995), was discussed. (Memo at 2). There was no objection to the general approach, but some illustrations of conflicts between Articles 2 and 9 are needed for the comments.

2. Attention was paid to the rights of a seller in possession of goods upon default or insolvency of the buyer. (Memo 4-7). The consensus was that the seller should be able to retain possession free of claims of the buyer and creditors of and purchasers from the buyer and enforce the contract under Article 2. The result can be justified either under 9-113 or on the ground that the interest of the buyer and creditors of and purchasers from are conditional upon the buyer obtaining possession without a default. Clarification of the justification is needed.

My preference would be to reduce the dependence upon 9-113 and Article 9 to justify the result.

Questions raised:

1. Suppose the buyer obtains unlawful possession (i.e., gives a check that bounces). Clarify whether that possession must be lawful before the seller loses.

2. Suppose possession is lawful, a security interest attaches and the buyer innocently returns the goods to the seller's inventory. Is the security interest cut off? (Not unless there is a BIOCB transaction.)

3. Suppose the seller has a security interest in the goods perfected by filing. The buyer defaults and the seller in possession elects to rely on 9-113 and resell the goods under 2-719(a) (Oct. 1995). Can the buyer force the seller to dispose of the goods under Article 9? Presumably the answer is no, especially if the buyer has not advanced any of the price and no third party interests are involved.

3. There was little discussion about seller reclamation of goods delivered to the buyer. (Memo 8-9.) Steve Harris questioned the proposed deletion of the language that "successful reclamation of goods excludes all other remedies with respect to them." The original purpose was to limit the

number of fact specific fraud claims. Also, Harris noted that the deletion of "lien creditor" from 2-702(3) in 1966 was intended to increase the reclaiming seller's protection.

4. On the issues of Sale on Approval or Return and Consignments, (Memo 9-11), several points were made by the Drafting Committee:

Greater clarity is needed on the status of a sale or return or a sale on approval with reference to the creditor's rights under new 2-407. Should both types of sales be subject to 2-407?

Objections were made to deleting the consignor's ability to prove that the person to whom delivery was made was "generally known" by creditors to be engaged in the business of selling the goods to others, such as "consignment shops." Also, it was suggested that the \$1,000 exclusion was too low. We need to review these consumer protection problems. See Note, The UCC and Consignment: Making the Code Safe for Artists and Other "Little Fellows", 12 Cardozo Arts & Ent. L.J. 579 (1994).

We should review the "proceeds" problem, in that several cases protect the proceeds of goods delivered in a reclamation.

5. The final discussion topic was the continuing problem of "pre-paying" or "financing" buyers. (Memo 12-14.) The Drafting Committee recognized and was concerned about the change from "unsecured" creditors to "creditors" in new 2-405(a) and the expansion of the pre-paying buyer's rights under new 2-724. These changes posed a potential threat to security interests in the seller's inventory.

On balance, however, the Drafting Committee agreed that if the conditions of 1-201(9) are satisfied, the pre-paying buyer should be treated as a BIOCB from the time of identification, even if the seller still has possession of the goods. Moreover, the agreed price should be ratably adjusted to the condition of the goods in the seller's possession. More than one asset-based lender observer agreed with this approach.

The challenge to a financing buyer who prefers to perfect a security interest in goods the seller's possession under Article 9 rather than rely on new 2-724 was discussed but no conclusions were reached. It was noted that in a case where a buyer who needs the goods enforces a security interest in them, Article 9 is not very helpful: The secured buyer must dispose of the goods to enforce the security interest and has only a limited right to keep them through strict foreclosure under 9-505.