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The Intersection of Articles 2 and 9

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THE INTERSECTION OF ARTICLES 2 AND 9

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I. Standard Form Contracts.

Draft § 2-206(b) excludes certain terms in standard form contracts to which a consumer is a party. To what extent, if any, does Draft § 2-206(b) apply to the provisions of a conditional sale contract that relate to the security interest? The November 1996 draft reads as follows:

(b) Where a consumer has manifested assent to a standard form, a term contained in the form which the consumer could not have reasonably expected is not part of the contract unless the consumer expressly agrees to it.

II. Buyer in Ordinary Course; Prepaying Buyer.

A. A buyer in ordinary course of business takes free of a security interest created by the seller. Draft § 9-316(b). At what stage in the transaction--e.g., identification of the goods, passage of title--does a person become a buyer in ordinary course? Does it matter whether the buyer has paid some or all of the price? See Draft §§ 1-201(9); 2-405; 2-707; 2-724.

B. Which practices are relevant to a determination of whether the buyer buys "in ordinary course"? See Draft § 1-201(9).

C. Can a person become a buyer in ordinary course if the secured party is in possession of the collateral? See Draft § 9-316.

D. If a secured party entrusts collateral to a merchant (other than the debtor) who deals in goods of the kind, does a buyer in ordinary course from the merchant take free of the security interest? See Draft § 2-404(d).

III. Consignments.

A. A consignment is a bailment. Nevertheless, current law provides that a consignor (owner) may lose its interest in the goods to creditors of the consignee (bailee) under certain conditions. See § 2-326.

B. Under Draft Article 9, a "consignment" (as defined) is called a "security interest," see Draft § 1-201(37), and Article 9 would determine the rights of the consignee's creditors as against the consignor. See Draft § 9-112(a)(4). However,

non-UCC law would determine the rights of the consignor and consignee between themselves. See Draft § 9-601(d); Notes to Draft § 2-407.

C. The range of consignments covered by Draft Article 9 differs somewhat from the range covered by current law. See Draft § [2-102].

D. Consignment

Consider the following case under existing and revised Articles 2 and 9. Assume that Debtor operates a large aluminum smelter. Bank has lent several millions of dollars to Debtor and has taken and perfected a security interest in all of the raw materials and in the processed aluminum of Debtor. Manufacturer later makes a contract with Debtor under which Manufacturer will provide the raw materials for processing into aluminum. This material is commingled with other material on hand at Debtor and under the terms of the contract between Manufacturer and Debtor, Manufacturer pays a "tolling fee." The base fee is a fixed dollar amount per pound, but it rises and falls with the price of aluminum. Half of the aluminum produced by Debtor from the raw material provided by Manufacturer is to be delivered directly to Manufacturer's buyer, Toy Co., who uses the raw aluminum to manufacture toys. The other half of the aluminum attributed to raw material provided by Manufacturer is returned to Manufacturer. Assume that one can identify the raw material and finished aluminum that "belongs" to the Manufacturer only by calculating a percentage of the output from the percentage of input. If the Debtor defaults at a time when it had \$1.5 million of material and aluminum on hand that had been provided by or was attributed to Manufacturer, who gets the raw materials and the aluminum, Bank or Manufacturer?

IV. Seller's Right to Reclaim Delivered Goods.

A. Under certain narrowly defined circumstances, a seller may enjoy a right to reclaim goods delivered to a buyer. The goods may, however, become subject to a security interest in favor of the buyer's secured party. If so, who has priority? Compare Draft § 2-716(b) with Draft § 2-404(b).

B. A similar situation may arise when the buyer acquires goods subject to a security interest created by the seller in favor of the seller's secured party. If a security interest in favor of the buyer's secured party attaches to the goods, which secured party (buyer's or seller's) has priority? See Draft § 9-323.

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