Comments

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The Article 9 Buyer's Seller Rule & the Justification for Its Harsh Effects

I

All fifty states and the District of Columbia adopted Revised Article 9 of the Uniform Commercial Code (Code) in July of 2001.[1] However, Old Article 9 continues to govern the majority of Article 9 disputes because the security agreements were created under Old Article 9. As a result, an examination of Old Article 9 is not only relevant but the best place to begin in order for one to understand its successor.

When one attempts to ascertain the meaning and purpose for any particular section in Article 9 of the Code in isolation from the remaining sections in Article 9, and the other Articles, especially Article 1, it is not apparent how the liberal construction and application of any single section achieves the Code's primary purpose of simplifying, clarifying, and modernizing the law in order to facilitate commercial transactions.[2] This is especially apparent when one analyzes the limitations set forth in section 9-320(a),[3] the successor statute to the old version at section 9-

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[1] UNIF. COMMERCIAL CODE, Adoption of Revised Article 9 (2000), 3 U.L.A. 14-18 (2003).

[2] U.C.C. § 1-102.

[3] U.C.C. § 9-320(a) states:

> Except as otherwise provided in subsection (e), a buyer in ordinary course of business, other than a person buying farm products from a person engaged in farming operations, takes free of a security interest created by the

307(1).[4] This Comment examines the meaning and effect of the Buyers of Goods Rule, in particular the "Buyer's Seller" sub-element within it, and attempts to excavate its elusive policy.

In this Comment, Part II serves as an introduction to section 9-320(a) where I analyze its sub-elements to show the related problems that result from its application. Part III outlines the policy behind section 9-320(a) using related case law and interpreting this section in the context of the entire Code. Commentators frequently criticize section 9-320(a)'s harsh effects because they cannot identify a tenable policy to support it. Despite the criticism, the section stands virtually unchanged since the Code's inception in September 1951. It seems unlikely that the drafters of such a "mature and developed" statute would continue to overlook such a simple and obvious effect. From its inception, the Code "was put forward as the grandest achievement of all time in the history of private statute law making."[5] Through the analysis of the rich factual background of the case law, along with the related law review articles on this issue, this Comment will provide the elusive justification for section 9-320(a)'s harsh results. Part IV examines how courts have attempted to circumvent the section 9-320(a) harsh results. In this part, this Comment discusses how the authorization exception in section 9-315(a)(1) functions in relation to 9-320(a) and how an analysis of section 9-315(a)(1) helps one understand the limited effect section 2-403(2) should have upon purchased goods encumbered by a perfected security interest. Part IV concludes with an analysis of a creative, but incorrect, decision handed down by the Oregon Supreme Court which bends the Code's rules far from where they should be. Part V provides a brief explanation of the priority rules associated with proceeds and shows how the burden im-

> buyer's seller, even if the security interest is perfected and the buyer knows of its existence.

The Farm Products exception reference in subsection (e) is not relevant for the purposes of this Comment.

4 The old version of this rule differs slightly from § 9-320(a) but only in form, not substance. It states:

> A buyer in the 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.

U.C.C. § 9-307(1) (revised 2001).

5 JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE: SECURED TRANSACTIONS § 7 (5th ed. 2000).

posed on innocent buyers in the ordinary course of business can be shifted so that the priority battle is only between secured parties, both of which are better suited to bear the loss than the innocent purchaser.

II

Construction and Application of section 9-320(a)

A. Introduction to the Problem

Section 9-320(a) states the necessary conditions a buyer in the ordinary course must satisfy in order for her to purchase goods and take free from any perfected security interest in those goods. Since its inception, courts and legal scholars have criticized this rule because it fails to extend the protections normally associated with buyers in the ordinary course of business to *all* similarly situated buyers in the ordinary course of business. Before isolating the problematic transaction leading to these harsh consequences, it is best to first understand the rule in the context where the discontinuation of the security interest is without dispute.

Whether consumers realize it or not, they rely upon section 9-320(a) whenever purchasing goods from a retail establishment because the more specific provision, section 9-315(a)(1), states that a perfected security interest continues in the collateral upon *any disposition*, unless some other exception in Article 9 applies.[6] It is common for persons who are in the business of selling goods of a kind, like watches, appliances, sports equipment, or automobiles, to seek a loan in order to purchase inventory to sell to the public. Before a lender—usually a bank—will extend credit, it normally requires the dealer, or debtor, to give the lender a security interest in the inventory. If the dealer defaults, normally the security agreement allows the lender to foreclose upon the collateral and sell it so that it can satisfy any remaining debt. However, section 9-320(a) is an exception to section 9-315(a)(1) because it automatically discontinues the security interest so that the goods purchased are no longer encumbered by the lender's security interest. Section 9-320(a)'s effect ensures that

[6] Old § 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." U.C.C. § 9-306(2) (revised 2001).

the buyer acquires the goods with "clear title."[7]

For example, suppose Smith, a buyer in the ordinary course of business,[8] purchases goods from a dealer's inventory. Smith takes free, or assumes ownership free and clear of the existing security interest in the goods purchased, because section 9-320(a) states that buyers in the ordinary course of business assume title to the goods free of the security interest if the security interest was created by the *buyer's seller*. In this case, the dealer is the buyer's seller, the dealer selling the goods, and the buyer is Smith. Without this rule, buyers would likely hesitate before purchasing goods from a dealer because the buyer could not be certain it would acquire clear title, which section 9-320(a) ensures. The alternative would be cumbersome. That is, without this statute, before purchasing goods, the buyer would need to check the filing system in order to determine if the goods are encumbered or verify if the dealer is authorized to sell the goods free of the security interest. This rule frees consumers from the task of checking the filing office or verifying the dealer has the authority to sell the goods. In effect, section 9-320(a) encourages consumers to purchase freely.[9] In this context it is clear how section 9-320(a) facilitates commercial transactions.

The general application of section 9-320(a) does not always yield such favorable results. For example, suppose Jones purchases an automobile from a person who is in the business of

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[7] A title free from any encumbrances, burdens, or other limitations. BLACK'S LAW DICTIONARY 1493 (7th ed. 1999).

[8] U.C.C. § 1-201(b)(9) defines "Buyer in ordinary course of business" as:

> [A] person that buys goods in good faith, without knowledge that the sale violates the rights of another person in the goods, and in the ordinary course from a person, other than a pawnbroker, in the business of selling goods of that kind. A person buys goods in the ordinary course if the sale to the person comports with the usual or customary practices in the kind of business in which the seller is engaged or with the seller's own usual or customary practices. A person that sells oil, gas, or other minerals at the wellhead or minehead is a person in the business of selling goods of that kind. A buyer in ordinary course of business may buy for cash, by exchange of other property, or on secured or unsecured credit, and may acquire goods or documents of title under a preexisting contract for sale. Only a buyer that takes possession of the goods or has a right to recover the goods from the seller under Article 2 may be a buyer in ordinary course of business. Buyer in ordinary course of business does not include a person that acquires goods in a transfer in bulk or as security for or in total or partial satisfaction of a money debt.

[9] RUSSELL A. HAKES, THE ABC'S OF THE UCC. REVISED ARTICLE 9 SECURED TRANSACTIONS 89 (2000).

selling goods of the kind. Like most consumers, assume that Jones cannot pay for the automobile outright, so a bank, or even the car dealer itself, enables Jones to purchase the automobile on credit, and in exchange, Jones gives the lender a security interest in the automobile. After the purchase, but before Jones is finished paying back the debt to the secured party, she either sells the automobile, or trades it in as a partial exchange for a new automobile to a third party who is in the business of selling automobiles. In this situation, although the seller, Jones, created the security interest, the third-party dealer will not take free of the existing security interest because the dealer is not a buyer in the ordinary course. Jones' status as a mere consumer, and not a dealer of cars, prohibits the third-party dealer from becoming a buyer in the ordinary course of business.[10] Nevertheless, the third-party dealer subsequently places the used automobile in her inventory for sale to the public. This new buyer, Edwards, purchases the automobile subject to the original security interest because her seller, the third-party dealer, did not create the security interest; rather, Jones did.

In this situation, Edwards, a buyer in the ordinary course of business, purchases the used automobile from the third-party dealer, but it is subject to the existing security interest because Edwards's seller, the third-party dealer who purchased the used automobile from Jones, did not create the security interest. After Jones sells the automobile to the third-party dealer, she discontinues making payments to her secured party because the third-party dealer assures her that it will satisfy the remaining debt. At this juncture, a textbook-scenario section 9-320(a) priority dispute begins between Edwards and her lender and the secured party that enabled Jones to initially purchase the car. The third-party dealer either fails to use the proceeds to pay Jones' secured party, or it will file for bankruptcy.[11] As a result, Jones' secured party forecloses on the collateral so that it can sell and satisfy the amount it was due.

Courts and legal scholars have questioned section 9-320(a)'s narrow scope and the anomalous consequences that befall some buyers in the ordinary course. Professors White and Summers note that

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[10] *See* U.C.C. § 1-209(9).

[11] Ocean County Nat'l Bank v. Palmer, 457 A.2d 1225, 1227 (N.J. Super. Ct. App. Div. 1983).

> the difficulty is that the policy of 9-320 would seem to cover [the innocent purchaser, Edwards, in the second example above]. [Edwards] is neither more nor less than a garden variety purchaser who pays cash and buys out of the inventory of a dealer [just as Smith did in the first example above].[12]

Barkley Clark also recognizes this anomaly. He states that if the purposes behind "[t]he Article 9 priority rules [are aimed toward] encourag[ing] the flow of commerce not only by protecting buyers out of inventory under section 9-307(1), but also by giving special privileges to other kinds of good faith purchasers, such as purchasers of chattel paper,"[13] it seems odd that section 9-320(a) does not also protect purchasers like Edwards because most people recognize that the rule's primary purpose is to protect good-faith innocent purchasers like her. In an effort to avoid this harsh effect, one might assume that courts would exercise their authority to liberally construe and apply the Code when resolving priority disputes of this kind so that both Smith and Edwards are treated similarly. Courts rarely use this language to protect buyers such as Edwards,[14] and this Comment will later show why

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[12] WHITE & SUMMERS, *supra* note 5, at § 24-8(b).

[13] BARKLEY CLARK & BARBARA CLARK, THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE, ¶ 3.01[2][d] (rev. ed. 2002).

[14] In *Gordon v. Hamm*, the court struggled with factual circumstances similar to my example above "because the four parties to this lawsuit are not morally blameworthy, yet someone must suffer the loss occasioned by the absent thief. Legally, however, the case is simple." 74 Cal. Rptr. 2d 631, 635 (Cal. Ct. App. 1998). In *Milledgeville Cmty. Credit Union v. Corn*, the trial court was:

> particularly troubled by this situation because of the apparent innocence of [defendant] who is a buyer in the ordinary course of business, and therefore tried to evaluate the public policy considerations. In doing so, I look to any wrongdoing or apparent wrongdoing on the part of either party. Plaintiff . . . also appears to be entirely innocent of any wrong doing. They have loaned money and done precisely what the statute required in order to perfect their security interest in that . . . . The question becomes, should the law put the onus on the owner of the secured interest to follow the security interest and insure that it not be sold off improperly, or should the onus instead be placed on the purchaser of a vehicle to insure that he purchases clear title.

716 N.E. 2d 864, 866-67 (Ill. Ct. App. 1999) (quoting trial court) (alterations in original).

In *Martin Bros. Implement Co. v. Diepholz*, the court recognized that

> the result which flows from this construction of the statute may seem unjust. The buyer who purchases goods from a seller who has created the security interest takes free of that interest even though the buyer could conceivably discover the existence of a security interest by a title search. When a security interest exists in favor of a remote seller, however, that same buyer will not take the goods free and clear of the security interest, even though the burden of locating the remote party's interest is much

such a construction is wrong.

Despite the years of painstaking drafting, most law students will attest that after studying Article 9, the Code's "rules of priority are exquisitely complicated."[15] In order to comprehend the correct meaning of these rules and how they operate, it is recommended that one first attempt to "understand the policy behind each rule."[16] However, this solution is not very helpful because it is so difficult to interpret or articulate any reasonable policy underlying the limited scope of section 9-320(a) because the Drafters did not provide any explanation for it.[17] Finally, the Official Comments for Old section 9-307(1), and its revised counterpart, section 9-320(a), are unhelpful in providing the needed clarification of this facially simple but anomalous section.

> greater. However, this is consistent with the general rule set forth in the Code that a security interest continues in collateral despite a sale or other disposition of that collateral.

440 N.E.2d 320, 325 (Ill. App. Ct. 1982).

In *Exchange Bank of Osceola v. Jarrett*, the court also recognized that

> this is a harsh result, since the purchaser . . . had no means to learn . . . that the property he purchased was subject to a security interest. It may be that legislative action is necessary to prevent such results in the future. Since we are bound by the enacted laws, and must give full faith and credit to the laws of our sister states, no other course is open to us here.

588 P.2d 1006, 1009 (Mont. 1979).

Finally, in *General Motors Acceptance Corp. v. Troville*, the court showed that its hands were tied and "if a hardship results from our interpretation, it is for the Legislature to remove it." 6 U.C.C. Rep. Serv. 409, 413 (Mass. App. Ct. 1969).

[15] WHITE & SUMMERS, *supra* note 5, at § 24-1.

[16] *Id*.

[17] Richard Nowka, *Section 9-320(a) of Revised Article 9 and the Buyer in Ordinary Course of Pre-Encumbered Goods: Something Old and Something New*, 38 BRANDEIS L.J. 9, 11 (1999-2000) (Section 9-320(a)'s "Comment includes no statement of the policy behind the requirement. The continuance of the BIOC Rule without comment on the purpose for its inclusion is disappointing in view of the previous lack of explanation and the literature commenting on the issue."). Robert Dugan, *Buyer-Secured Party Conflicts Under Section 9-307(1) of the Uniform Commercial Code*, 46 U. COLO. L. REV. 333, 347 (1975) (The author concludes that "it is difficult to perceive any compelling justification for the prevailing interpretation of the created-by-his-seller language . . . ."); Charles L. Knapp, *Protecting the Buyer of Previously Encumbered Goods: Another Plea for Revision of UCC Section 9-307(1)*, 15 ARIZ. L. REV. 861, 864 (1973) (stating that the results are "wrong because it ignores economic and social realities, wrong because it misallocates an unavoidable risk inherent in the financing of goods, and wrong because it fails to follow the logic of the Code itself"); *Special Project, The Priority Rules of Article 9*, 62 CORNELL L. REV. 834, 963 (1977) (hereinafter "Special Project") (arguing that there is no valid distinction between two different buyers in the ordinary course of business who purchase goods out of a dealer's inventory that justifies the harsh treatment to the particular buyer who unknowingly purchased preencumbered goods).

B. Statutory Contraction

Before a reader attempts to wrap her mind around the meaning and operation of any Article 9 priority rule, she should first think of these rules as serial competitions pitting the secured creditor against a series of opponents. In each case one competitor is a secured creditor, while the other competitor changes with each section. Thus section 9-317 covers a secured creditor versus a lien creditor; section 9-322 covers the case of a secured creditor versus secured creditor.[18] In a buyers of goods context, section 9-320(a) covers the case of a secured creditor against the buyer in the ordinary course.[19]

Consequently, the starting point for any discussion about Article 9's priority rules begins with section 9-201(a),[20] the section where the security agreement acquires its power. If the terms of the "security agreement"[21] so provide, then upon the debtor's default the secured party always wins because its rights to the collateral "are superior to anyone, anywhere, anyhow" unless an exception to this rule exists elsewhere in the Code.[22] The strength of this section cannot be over-emphasized. The section

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[18] WHITE & SUMMERS, *supra* note 5, at § 24-1.

[19] When the security interest is not perfected, § 9-317(b) allows certain buyers of goods to take free under circumstances different than what § 9-307(1) and § 9-320(a) require. Section 9-317 states: "Except as otherwise provided in subsection (e), a buyer . . . of . . . goods . . . takes free of a security interest . . . if the buyer gives value and receives delivery of the collateral without knowledge of the security interest . . . and before it is perfected." U.C.C. § 9-317(b). I do not discuss this exception because it is rare for a secured party to not perfect. Most of the cases I examine involve sophisticated secured parties who are familiar with the requirements of Article 9 and the benefits perfection provides.

[20] U.C.C. § 9-201(a) states: "Except as otherwise provided in [the Uniform Commercial Code], a security agreement is effective according to its terms between the parties, against purchasers of collateral, and against creditors." However, old U.C.C. § 9-201 states:

> Except as otherwise provided by this Act a security agreement is effective according to its terms between the parties, against purchasers of the collateral, and against creditors. Nothing in this Article validates any charge or practice illegal under any statute or regulation thereunder governing usury, small loans, retail installment sales, or the like, or extends the application of any such statute or regulation to any transaction not otherwise subject thereto.

U.C.C. § 9-201 (revised 2001).

[21] "'Security Agreement' means an agreement that creates or provides for a security interest." U.C.C. § 9-102(a)(73).

[22] Special Project, *supra* note 17, at 842; CLARK & CLARK, *supra* note 13, at ¶ 3.02.

"means what it says,"[23] and it does not give the secured party's competitors much, if any, latitude to get out from under it. Provided there are no exceptions, the secured party generally wins most competitions.

Just as quickly as this section confers broad power upon secured parties, it immediately qualifies itself by stating that there are exceptions to this rule found throughout the entire Code.[24] The importance of the first seven words of section 9-201, "except as otherwise provided in this Act", cannot be over-emphasized because they bring in all of the Article 9 priority exceptions along with any others found throughout the Code.[25] "Thus the starting point for any analysis about the rights of a buyer vis-à-vis a prior secured creditor is the security agreement itself."[26]

The general rule under section 9-201(a) is confirmed by the more specific provision at section 9-306(2),[27] which states that the security interest continues upon the sale or any other disposition unless the secured party authorizes the disposition.[28] Normally, an inventory lender gives its debtor express permission to sell because the lender expects the debtor-dealer to sell her inventory and amortize the loan with the sale proceeds.[29] In addition, the secured party's protection continues after the sale because it also has a security interest in the proceeds.[30]

This Comment does not focus on authorized transactions; it focuses on transactions where the dealer had no opportunity to authorize the sale. Normally, the secured party is operating under the assumption that its debtor continues to possess the collateral and will continue to make payments in accordance with the security agreement. However, if the debtor either sells or trades the collateral in exchange for a new purchase without informing the secured party, then the secured party is not in position to authorize the sale because it is under the assumption its debtor is still in possession. Almost without exception, the debtor's security agreement expressly forbids any disposition without the written consent of the secured party. If a subsequent

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23 White & Summers, *supra* note 5, at § 24-2.
24 U.C.C. § 9-201(a).
25 Special Project, *supra* note 17, at 842.
26 White & Summers, *supra* note 5, at § 24-8.
27 *See supra* note 6.
28 White & Summers, *supra* note 5, at § 24-8
29 Clark & Clark, *supra* note 13, at ¶ 3.02[3][b].
30 U.C.C. § 9-315(a)(2).

buyer purchases these goods after the initial debtor sold or exchanged them with a dealer, and they are encumbered by a preexisting security interest that was not created by the buyer's seller, the subsequent buyer's primary course of action will come under section 9-307(1) or section 9-320(a), because these sections are devoted to unauthorized dispositions,[31] or cases where the parties are silent about authorization.

C. Buyers in the Ordinary Course

Section 9-320(a), and its older counterpart section 9-307(1), have two primary elements. First, the buyer must be a buyer in the ordinary course. Second, the buyer's seller must have created the security interest in order for the security interest to be discontinued. I will examine the buyer's seller element in Part III below. In regard to the buyer in the ordinary course element, it is composed of five sub-elements. Below I discuss each subelement and the problems commonly associated with these provisions. In the end, I intend to show the proper meaning, operation, and application of each sub-element so that upon the synthesis of these sub-elements one can determine with certainty when a buyer acquires the goods free of the security interest.

Article 9 does not define buyers in the ordinary course; rather, Article 1 defines it.[32] The term is almost exclusively limited to buyers out of inventory;[33] however, exceptions apply if the seller's business comports with ordinary business practices.[34] This section breaks down the five sub-elements, most of which

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[31] U.C.C. § 9-320(a), Comment 6 states:

> The limitations that subsections (a) and (b) impose on the persons who may take free of a security interest apply of course only to unauthorized sales by the debtor. If the secured party authorized the sale in an express agreement or otherwise, the buyer takes free under Section 9-315(a) without regard to the limitations of this section. (That section also states the right of a secured party to the proceeds of a sale, authorized or unauthorized.). Moreover, the buyer also takes free if the secured party waived or otherwise is precluded from asserting its security interest against the buyer.

[32] *See supra* note 8.

[33] CLARK & CLARK, *supra* note 13, ¶ 3.04[1].

[34] *Id.* at 3-47. *See also* Rhode Island Hosp. Trust Co. v. Leo's Used Car Exch., Inc., 314 F. Supp. 254, 255-56 (D. Mass. 1970) (holding that the sale of a car at a location at which neither buyer nor seller was doing business was not a transaction in the ordinary course of business); Bank of Ill. v. Dye, 517 N.E. 2d 38, 40 (Ill. App. Ct. 1987) (holding that the test for "buyer in the ordinary course of business" is satisfied if the sale comported with customary business practices and the buyer was in fact a typical buyer of the seller).

are understandable without much explanation or analysis, while others require reference to other Code definitions and case law to interpret and determine their effect.

First, in order to be a buyer in the ordinary course, the buyer must purchase the goods in "good faith."[35] The buyer's actual knowledge is probative when determining good faith, rather than what a reasonable person in similar circumstances should have known.[36] The contracting parties' conduct determines good faith in regard to their obligations. Good faith is troublesome because no two instances of it are the same despite the fact that the Code provides a standard definition for it.

Hodges Wholesale Cars v. Auto Dealer's Exchange of Birmingham helps flesh out the meaning.[37] In this case, Alexander sold to a person whose identity was not disclosed, and the court referred to this person as the "initial buyer."[38] At the time of the sale, Alexander endorsed the title to the bearer of the title and gave it to the initial buyer.[39] The initial buyer gave Alexander a check in exchange for the car and the title.[40] Subsequently, the initial buyer resold the car to Express, but the initial buyer held himself out to be Alexander.[41] Express issued a check payable to "Doyle Alexander" and took possession of the car and its title.[42] Because the initial buyer passed a bad check to Alexander, the court had to determine whether the initial buyer could transfer good title when it only possessed voidable title.[43] The court held that

> Express did not know, and had no reason to know, that the initial buyer's representations were false. The initial buyer held himself out to be Doyle Alexander, and the certificate of

35 The definition for "good faith" in Article 1 is subjective: "[H]onesty in fact in the conduct or the transaction concerned." U.C.C. § 1-201(19). However, the definition in Article 9 has both subjective and objective elements: "[H]onesty in fact and the observance of reasonable commercial standards of fair dealing." U.C.C. § 9-102(a)(43). If the buyer is a dealer in the business of selling goods of the kind or merchant, then the two-prong definition is used.

36 Louis & Diederich, Inc. v. Cambridge European Imports, Inc., 234 Cal. Rptr. 889, 896 (Cal. Ct. App. 1987).

37 Hodges Wholesale Cars v. Auto Dealer's Exch. of Birmingham, 628 So. 2d 608 (Ala. 1993).

38 *Id*. at 609.

39 *Id*.

40 *Id*.

41 *Id*.

42 *Id*.

43 *Id*. at 610.

> title to the car showed that Alexander was the owner. The certificate of title bore Alexander's unforged signature as seller. Express gave the initial buyer a check made payable to Doyle Alexander. There was no evidence presented to show that, in negotiating and consummating the purchase of the car, Express had been less than honest or had failed to observe reasonable commercial standards of fair dealing.[44]

Consequently, the court held that Express acted in good faith because it subjectively did not know the initial buyer was not Alexander, nor would a reasonable person have known.[45]

Second, the buyer must be without knowledge that the sale violates the rights of a third party. That is, it must not know the sale violates some term in the seller's security agreement. As stated above, most security agreements do not allow disposition without the secured party's written authorization. If the buyer knows that the sale violates a term such as this, then the buyer knows the sale violates the rights of a third party. Mere knowledge that the goods are subject to a security interest does not show that the buyer knew the sale violated the rights of a third party.[46] In the unproblematic transactions described above,[47] third-party rights are not at stake since the dealer's lender anticipates that she will sell the goods in order to pay off the loan. If the third party is a dealer of used cars, who later turns around and sells to a buyer in the ordinary course, the new buyer is subject to the "without knowledge" requirement. This sub-element is not difficult to overcome in the multiple-sales context because buyers typically do not suspect a dealer's inventory is subject to a security agreement that prohibits the sale to the public.[48]

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[44] *Id*. at 611.

[45] The drafts for revised Article 1 do away with the subjective formulation and adopt the definition found in the other revised articles. Revised Article 1, *in* SELECTED COMMERCIAL STATUTES, at 1084 (William H. Henning ed. 2001).

[46] Rome Bank & Trust Co. v. Bradshaw, 237 S.E.2d 612, 615 (Ga. Ct. App. 1977).

[47] *Supra* Part II.A.

[48] The "good faith" and "without knowledge" requirements have left some to ask what the latter adds to the former since a person cannot buy in good faith if he knows the sale violates the rights of a third party. WHITE & SUMMERS, *supra* note 5, at § 24-8(b). Professor James Steven Rogers reasons that the confusion might be caused by a quirk in language. James Steven Rogers, *Policy Perspectives On Revised U.C.C. Article 8*, 43 U.C.L.A. L. REV. 1431, 1470 (1996). Well before the UCC, in the eighteenth and nineteenth century, a person who took free of adverse claims was not described as a "good faith purchaser" but a "bona fide purchaser for value and without notice." *Id.* Since "bona fide" only refers to "value" and "without notice," confusion developed in the twentieth century when the words "good faith" were used in exchange which Rogers surmises was due to a desire to substitute all-English phrases for Latin terms. *Id.* This shift in use can sometimes cloud the issue since

The sale of used automobiles brings a different problem to light for both the "good faith" and "without knowledge" sub-elements. The perfection of a security interest in an automobile is not governed by the traditional filing method in section 9-310(a).[49] In a Florida Court of Appeals case, Caron purchased a new motorhome and Green Tree enabled Caron to make the purchase. In exchange, Caron gave Green Tree a security interest in the motorhome.[50] Green Tree noted its security interest on the title.[51] Two years after the sale, but before Caron paid his debt to Green Tree, and without its authorization, Caron traded the motorhome to Wildcat, who later sold the motorhome from its inventory to Zimerman.[52] The court held that Zimerman was not a buyer in the ordinary course of business because he failed to investigate the condition of the title.[53] The court recognized that the notation of a lien on a certificate of title is constructive notice,[54] and any such buyer assumed the existing "defects and liens on the title."[55] However, jurisdictions are split on this issue.[56]

In *Franklin v. First National Bank of Morrill, Nebraska*,

good faith does not always show that value was given. *Id.* In addition to Professor Rogers' observations, the 1956 Recommendations of the Editorial Board for the Uniform Commercial Code shed some light on the issue. It noted that "[t]he reference to 'Good Faith' was added on the recommendation of the New York Commission to make it clear that one who buys dishonestly is not within the definition. The 'without knowledge' addition spells out one important type of dishonesty." 1956 Recommendations of the Editorial Board of the Uniform Commercial Code, *in* XVIII UNIFORM COMMERCIAL CODE DRAFTS, 37 (Elizabeth Slusser Kelly ed. 1984).

49 The perfection of a security interest to goods subject to a statute in § 9-311(a) does not require the filing of a financing statement. U.C.C. § 9-310(b)(3). A person perfects a security interest in an automobile by complying with the applicable certificate of title statute. U.C.C. 9-311(a)(2).

50 Green Tree Acceptance, Inc. v. Zimerman, 611 So. 2d 608, 609 (Fla. Dist. Ct. App. 1993).

51 *Id*.

52 *Id*.

53 *Id*. at 610.

54 *Id*.

55 *Id*.

56 *See, e.g.*, Thorn v. Adams, 865 P.2d 417, 419-20 (Or. Ct. App. 1993) (holding that nothing in the motor vehicle statutes required plaintiff to take possession of the certificate of title at the moment she purchased the car in order to acquire legal title. Absent such a requirement, plaintiff's "failure" to obtain the certificate of title at the moment that she purchased the car is not unreasonable and does not put plaintiff on notice that the transaction was "unusual."); Franklin v. First Nat'l Bank of Morrill, Neb., 848 P.2d 775, 780 (Wyo. 1993) (holding that mere knowledge that the goods to be purchased are secured does not show the person knew the sale violated the security agreement); Ellsworth v. Worthey, 612 S.W.2d 396, 400 (Mo. Ct. App. 1981)

Franklin purchased a used automobile from a dealer whose lender had a perfected security interest by noting its lien on the title.[57] After the dealer filed for bankruptcy, the dealer's lender argued it was entitled to possession of the automobile.[58] The lower court reasoned that there would be little or no effect when one notes its lien on the title if it is only going to be voided by a subsequent sale in the ordinary course.[59] In its decision, the lower court relied on the Motor Vehicle Registration Act rather than the Uniform Commercial Code in determining the priority issue.[60] The *Franklin* court reversed the lower court's decision because the Uniform Commercial Code determines the outcome in priority disputes, not registration acts.[61]

The "good faith" and "without knowledge" sub-elements tie in well with the third sub-element, which requires the buyer to make her purchase for cash, by exchange for other property, or on secured or unsecured credit. However, she may not acquire goods in bulk or in partial or complete satisfaction of a pre-existing debt.

Fourth, the buyer must purchase the goods from a person who is in the business of selling goods of the kind. This is usually not difficult to determine since a watch dealer sells watches, a dealer in automobiles sells automobiles, and an appliance dealer sells appliances.[62] However, there are limits. In *Hempstead Bank v. Andy's Car Rental System, Inc.*, the court held a person who rents cars is not a dealer even when he subsequently sells them.[63] As a result, this precluded the buyer from acquiring the protections that go along with a buyer in the ordinary course of business.[64] In any event, the determination of this sub-element usually boils down to a question of fact, in which case the courts' decisions vary.[65]

In addition, it is important to note that it is not necessary for

(holding sale of a used vehicle without delivery of a duly assigned certificate of title at the time possession to the vehicle is given is ordinarily fraudulent and void).

57 *Franklin*, 848 P.2d at 778.

58 *Id*. at 777.

59 *Id*. at 778.

60 *Id*.

61 *Id*. at 779.

62 WHITE & SUMMERS, *supra* note 5, at § 24-8(b).

63 Hempstead Bank v. Andy's Car Rental Sys. Inc., 312 N.Y.S.2d 317, 320-22 (N.Y. 1970).

64 *Id*.

65 Foy v. First Nat'l Bank of Elkhart, 868 F.2d 251, 254 (7th Cir. 1989).

the dealer to be a dealer when she initially obtains the goods in order for her to turn around and sell the goods to a consumer without violating the buyer in the ordinary course of business provision. That is, the person making the sale must be a dealer only at the time of the sale, not at the time the person acquires the goods. The Supreme Court of Maine decided a case where a husband and wife jointly purchased a boat from a boat dealer.[66] They gave their lender a security interest in the boat and the lender took all the necessary steps to perfect this security interest.[67] After this purchase, but before satisfying the debt, the husband purchased a boat dealership and subsequently put the boat in its inventory for sale to the public.[68] Later, the husband sold the boat to Estes, who gave Barco a security interest in the boat which Barco perfected.[69] After the sale, the husband failed to use the proceeds to pay off the secured creditor and consequently the creditor attempted to foreclose on the collateral.[70] A priority battle ensued between the initial lender and Estes, and the court held Estes was a buyer in the ordinary course because at the time of the sale the husband was a boat dealer.[71] The fact that the wife was not a dealer did not taint Estes' buyer in the ordinary course status because she had the power to authorize such a disposition.[72]

Fifth, a person is a buyer in the ordinary course only if she takes possession of the goods or has right to possession under Article 2.[73] After satisfying the requirements of section 1-201(9),

[66] Key Bank of Maine v. Estes, 669 A.2d 162 (Me. 1995).
[67] *Id*.
[68] *Id*.
[69] *Id*.
[70] *Id*. at 163.
[71] *Id*.
[72] *Id*.
[73] Carey Aviation, Inc. v. Giles World Marketing, Inc., 46 B.R. 458, 461-62 (Bankr. D. Mass. 1985). The court held that where

> the goods have been identified to the contract of sale as determined under § 2-501 . . . the buyer obtains a special property right in them which, even though he has not yet accepted the goods, gives him a right of action under § 2-722 against a secured party who causes him actionable injury in dealing with the goods.

Id. at 461-62. Despite the fact that the goods were not in a deliverable state, they were still identifiable because the seller noted its place on the assembly line and gave it an identification number. *Id.* The adversary proceeding of *In re Doughty's Appliance, Inc.*, 236 B.R. 407, 410 (Bankr. D. Or. 1999), held that buyers who took possession but had not paid were still buyers in the ordinary course but would have to make full payment if they expected to keep the goods.

the buyer in the ordinary course of business

> takes his place beside the holder in due course of negotiable instruments, the bona fide purchaser of negotiable documents, the bona fide purchaser of investment securities, the bona fide purchaser of chattel paper, and others in a select circle of bona fide purchasers of certain kinds of property who are privileged characters. Buyer in ordinary course of business is the goods-purchasing counterpart. While no two characters in the group are quite the same, they have in common the fact that they all acquire rights better than the rights of some kinds of claimants who did not authorize the transfer.[74]

On its face, it appears that if a person is a buyer in the ordinary course, she will take the goods free of any pre-existing claim, just as the Code protects other kinds of good faith purchasers.

D. The Limitations of Buyer's Seller Rule

The buyer's seller element, in either the old or the revised version, is the more interesting element not only because of the adverse effects it imposes upon some buyers in the ordinary course of business, but also for the countless and creative means buyers, secured creditors, and judges use when attempting to avoid the harsh results. Consequently, it is no surprise that most of the case law decided under either section 9-307(1) or section 9-320(a) involves this single issue.[75]

In short, if a person buying goods is a buyer in the ordinary course and the security interest was created by the buyer's seller, then the buyer takes the goods free of the security interest despite the language in section 9-306(2) or Revised section 9-315(a)(1), and even the language in section 9-201(a), all of which more or less state that the security interest withstands disposition. Before discussing the limitations of the buyer's seller rule, and whether there are ways around it, it is important to determine which party created the security interest: the debtor buyer or the secured party extending credit.

Section 9-203 outlines which party is the creator of the security interest. This section states that a security interest does not attach to the collateral until it becomes enforceable against the debtor.[76] Enforceability is determined by three elements. First,

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[74] Robert H. Skilton, *Buyer in Ordinary Course of Business Under Article 9 of the Uniform Commercial Code (and Related Matters)*, 1974 WIS. L. REV. 1, 2 (1974).

[75] WHITE & SUMMERS, *supra* note 5, at § 24-8(b).

[76] U.C.C. § 9-203(a).

"value" must be exchanged.[77] Second, the debtor must have rights in the collateral or have the power to transfer those rights in the collateral to a secured party.[78] Third, the debtor executes a security agreement that provides a description of the collateral.[79] It is important to recognize that the security interest does not become enforceable until the debtor, not the secured party, authenticates a security agreement. That is, the security interest is not transferred to the lender without the debtor's signature on the security agreement. This is also shown by sketching the relationship between the debtor and secured party and noting that the secured party is not in the position to create the security interest.

For example, Smith buys an appliance from a dealer. The dealer's inventory is subject to its lender's security interest. If the sales are unauthorized, Smith, a buyer in the ordinary course of business, takes free because her seller, the dealer, created the security interest. This section is meant to function in the context of inventory sales that are subject to a security interest.[80] It would be strange to suppose the lender or the secured party was the party that created the security interest because the secured party would never be in the position where it could sell the goods. Its business is extending credit, not selling goods. As a result, when the litigation only involves the secured party, or where the dealer that made the initial sale is the secured party, and the debtor is no longer involved in the priority dispute, Old section 9-306(2) or Revised section 9-315(a)(l) will be the applicable rule because the issue in those cases turns on whether the secured party authorized the disposition.

The issue normally involved in this context evolves where the

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[77] U.C.C. § 9-203(b)(1). The definition for "value" is found in § 1-201(44) which states:

> [a] person gives 'value' for rights if he acquires them (a) in return for a binding commitment to extend credit or for the extension of immediately available credit whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; or (b) as security for or in total or partial satisfaction of a pre-existing claim; or (c) by accepting delivery pursuant to a preexisting contract for purchase; or (d) generally, in return for any consideration sufficient to support a simple contract.

[78] *Id*. § 9-203(b)(2).

[79] *Id.* § 9-203(b)(3)(A). There are three other ways a debtor can meet this final condition. See U.C.C. § 9-203(b)(3)(B)-(D). However, I do not discuss them because the cases I used for this analysis do not use these methods for attachment.

[80] WHITE & SUMMERS, *supra* note 5, at § 24-8(b).

encumbered goods were subject to at least one sale after the initial sale in which the security interest was created.[81] Here is a brief example of a typical multiple-sales transaction:

> Jones . . . purchases a new automobile and gives a security interest to Rao Bank; then . . . Jones trades the automobile in (without revealing the security interest) to Purkayastha Motors, an automobile dealer who in turn sells the automobile to Szot . . . . Ultimately, Rao Bank attempts to recover the automobile from Szot. Because the security interest was not created by Szot's seller (Purkayastha Motors), but by Jones, Szot does not qualify for coverage under 9-320(a), and his interest will be subordinate to the security interest of Rao Bank.[82]

In most instances, courts apply the buyer's seller rule in accordance with a plain reading of the statute. *In re Sunrise R.V., Inc.* is an excellent example.[83] In *Sunrise*, Ede purchased a Lindy Motorhome ("Lindy") from All Seasons.[84] Ede gave All Seasons a security interest in the Lindy but All Seasons later sold the sales contract and security agreement to Yegen.[85] Over a year later, Ede traded the Lindy to Sunrise for credit; Sunrise was in the business of selling motorhomes.[86] At no point after the initial sale to Ede was Yegen notified of the trade-in.[87] Subsequently, Sunrise put the Lindy in its inventory and sold it to Carr.[88] After Carr paid the debt owed to Sunrise for the Lindy, he demanded that Yegen deliver the certificate of title, but Yegen refused because the proceeds Sunrise received from the sale were not used to satisfy the debt owed to him.[89] At this point, a priority battled ensued.

In *Sunrise*, there was no dispute whether Yegen properly perfected his security interest but only whether the sale to Carr was subject to or free from Yegen's security interest.[90] After the court briefly summarized Old section 9-306(2), noting that secur-

[81] I refer to this type of scenario as a multiple-sales transaction.

[82] WHITE & SUMMERS, *supra* note 5, at § 24-8(b). The case recognized as being the leading authority on this issue is *National Shawmut Bank of Boston v. Jones*, 236 A.2d 484 (N.H. 1967). However, I do not recommend this case for insight on the operation of the buyer's seller element because the opinion is written with little if any factual background and it is unclear who actually made the subsequent sale.

[83] *In re* Sunrise R.V., Inc. 105 B.R. 587, 587 (Bankr. E.D. Cal. 1989).

[84] *Id*. at 589.

[85] *Id*.

[86] *Id*.

[87] *Id*.

[88] *Id*.

[89] *Id*.

[90] *Id*. at 590.

ity interests survive disposition,[91] it went on to state that the only exception remotely applicable to this transaction was section 9-307(1) and it correctly held that despite Carr's buyer in the ordinary course status, he could not take free because his seller, Sunrise, did not create the security interest.[92] Rather, Ede created it when he first purchased the Lindy from All Seasons.[93]

This example clearly shows the limitations imposed on all buyers. In addition to Carr's inability to shake the security interest, also note that even if Ede had been the seller, Carr would not have been able to invoke the protections of section 9-307(1) because Ede was not a dealer of automobiles.

III

The Justification for the Buyer's Seller Rule's Harsh Consequences

The difficulty most people struggle with while attempting to understand section 9-320(a) is why the buyer's seller element precludes a buyer from gaining the protections of a buyer in the ordinary course of business when this person purchases inventory that is subject to a security interest not created by her dealer/seller. That is, the buyer is innocent and buying in good faith, and it seems unreasonable to penalize someone in this context. In the situation where buyers purchase goods from a dealer's inventory, and the dealer created the security interest, there is no question that the Buyers of Goods Rule has the proper effect. It ensures that good-faith purchasers can assume that the security interest in the dealer's inventory is discontinued, and as a result, the buyer does not have to stop to consider whether this transaction will end up in litigation.[94]

Since our economy is driven by commercial transactions initiated by consumers, it is easy to overlook the Code's purpose. That is, it not only ensures that good-faith purchasers are protected but it also protects secured parties that follow the letter of the law by filing a financing statement so that their security interests are perfected. Unfortunately, courts too frequently only focus on the protection of good-faith purchasers when considering the factors that are traditionally recognized or understood to fa-

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91 *Id*.

92 *Id*.

93 *Id*. at 591.

94 Clark & Clark, *supra* note 13, at ¶ 3.04[3].

cilitate or hasten commercial transactions.[95] White and Summers also get caught up in this by noting that

> the policy of . . . [section 9-320] would seem to cover . . . [buyers in the ordinary course of business purchasing goods from a person that did not create the security interest because these persons are] . . . neither more nor less than a garden variety purchaser who pays cash and buys out of the inventory of a dealer.[96]

That is, there should be no difference in treatment between buyers in the ordinary course of business merely because one happened to purchase goods encumbered by a remote party, not the buyer's seller, when on the face the dealer appeared to be selling goods it was authorized to sell.

Despite the Drafter's lack of formal commentary on the rule's elusive policy, the preservation of the rule through the initial drafting process and two actual revisions should be a strong indication that there was a reasonable rationale in their minds. In the early stages of Article 9, the 1951 draft of section 9-307 did not contain the buyer's seller language.[97] It is unclear whether the absence of the buyer's seller language in the earlier drafts meant that the Drafters did not intend for this limitation to apply. However, after its addition, the Drafters comment that the change was only to clear up the rule's ambiguity.[98] After the Code's adoption, the Drafters continued to seek out recommendations in order to clarify this new but rich Act. In particular, Donald Raspon's observation is the most enlightening because the Drafters failed to change the rule after he addressed the apparent anomaly. Rapson stated:

> However, 9-307(1) provides only that he "takes free of a security interest created by *his* seller." Here the security interest was created not by his seller (Dealer Y) but by Dealer X. Hence, on this plain-meaning interpretation, it would appear that Buyer 1 does not take the item free of Bank A's security

[95] McFadden v. Mercantile-Safe Deposit & Trust Co., 273 A.2d 198, 209 (Md. 1971) (explaining that it is generally recognized that the purpose of section 9-307(1) is to protect the buying public where the secured party finances inventory that is sold to the public by the debtor in the regular course of the debtor's business).

[96] WHITE & SUMMERS, *supra* note 5, at § 24-8(b).

[97] March 21, 1951 Draft of Article 9, Secured Transactions, *in* VI UNIFORM COMMERCIAL CODE CONFIDENTIAL DRAFTS 67 (Elizabeth Slusser Kelly & Ann Puckett eds. 1995).

[98] 1956 Recommendations of the Editorial Board of the Uniform Commercial Code, *in* XVIII UNIFORM COMMERCIAL CODE DRAFTS 310 (Elizabeth Slusser Kelly ed. 1984).

interest. Is this a defect in the statute?[99]

The Drafters' failure to change the provision is evidence that they intended for it to operate as such but also that they must have had good reasons for this result because the drafting process was undertaken with painstaking detail over the course of many years. The fact that the rule has withstood the revision process (in fact, three to date) is not conclusive, but it is a good indication that the Drafters did not overlook this effect.

Sometimes court opinions help uncover the policy. A notable case from Georgia was able to put its finger upon this elusive policy when it recognized that the rule not only served to protect buyers in the ordinary course of business but also secured parties.[100] In *Commercial Credit Equipment Corp. v. Bates*,[101] Bates purchased a tractor from a dealer and gave CCEC a security interest in the collateral.[102] Bates had no immediate use for the tractor, so he leased it to Anderson so that he could use it in his pond-digging business.[103] While the tractor was in Anderson's possession, he lent it to the dealer who originally made the sale to Bates as a favor but never recovered it from him.[104] While the tractor was stored on the dealer's premises, it was subsequently sold by an employee to McKinnon.[105]

The court reasoned that the rules in Article 9, in addition to the rest of the Code, served to protect secured parties as well as good-faith innocent purchasers like buyers in the ordinary course of business.[106] That is, if secured parties could not rely on the protections section 9-306(2) offered, then too few lenders would be willing to lend at all.[107] Without this provision there would be a chilling effect upon the Code's primary purpose of facilitating commercial transactions.[108] Whether one views the problem

[99] Donald J. Raspon, BUYERS IN THE ORDINARY COURSE OF BUSINESS AND PURCHASERS OF THE RESULTING PAPER: PROBLEMS CONCERNING THE INTERRELATIONSHIP OF U.C.C. SECTIONS 9-307 AND 9-308, *in* VI UNIFORM COMMERCIAL CODE CONFIDENTIAL DRAFTS 197 (Elizabeth Slusser Kelly & Ann Puckett eds. 1995).

[100] Commercial Credit Equip. Corp. v. Bates, 285 S.E.2d 560 (Ga. Ct. App. 1981).

[101] The facts for this case are summarized in a related but separate opinion, *Commercial Credit Equip. Corp. v. Bates*, 267 S.E.2d 469, 470 (Ga. Ct. App. 1980).

[102] *Id*.

[103] *Id*.

[104] *Id*.

[105] *Id*. at 470-71.

[106] Commercial Credit Equip. Corp. v. Bates, 285 S.E.2d 560, 561 (Ga. Ct. App. 1981).

[107] *Id*.

[108] *Id*.

from the secured party's perspective or the debtor's, in the end, the protection of secured parties also protects consumers and dealers. The mere fact that this rule fails to protect every single buyer in the ordinary course of business is not a failure to facilitate commercial transactions because a strict application would hamper the facilitation to a greater degree by making credit transactions more dangerous.

Furthermore, the Code has other remedies for remote buyers in the ordinary course. Article 2 protects buyers in the ordinary course who purchase goods from dealers that did not create the security interest. For example, an innocent purchaser who buys goods encumbered by a security interest not created by its seller has a cause of action for breach of the implied warranty of title under section 2-312(1)(b) which provides that the goods purchased are free from any security interest.[109] Of course, if the wrongful seller is insolvent or bankrupt, then the buyer obtains nothing more than a mere judgment. Nevertheless, it is not as if those who cannot invoke the protections of section 9-307(1) or section 9-320(a) are left with nothing.

In addition, it is not as if section 9-320(a) is the only section of the Code that imposes harsh consequences upon innocent parties. For instance, section 2-403(2) gives a person who is in the business of selling goods of the kind the power to transfer the rights of the entruster. In the case where a person brings her heirloom watch to a watch dealer for repair, and the dealer sells it, the justification for protecting the purchaser is that the true owner should have been more careful in selecting where to take her watch for repair. Section 9-320(a) is justified with a similar rationale. In the majority of cases discussing the priority dispute in the context of automobile sales, where perfection is regulated by statute, not by the filing of a financing statement, the secured party's only means to perfect is by noting the lien on the certificate of title. Some critics of section 9-320(a) incorrectly state

[109] The relevant subsections state that there is in a contract for sale a warranty by the seller that the title conveyed shall be good and the goods shall be delivered free from any security interest unless otherwise agreed; a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like, but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications. U.C.C. § 2-312(1), (3).

that the buyers in these transactions are not in a position to protect themselves. For instance, Professor Lipson states:

> [T]he secured party is usually in the better position to protect itself; the buyer is never going to be able to learn of the security interest of a person so far back in the chain; it is economically inefficient and perhaps morally repugnant to place the loss with the bona fide purchaser, and so on. Given the reluctance of courts to enforce what they often characterize as a harsh result, it is not surprising that the rule has few cheerleaders.[110]

This is incorrect. If the buyer is purchasing an automobile, then the title should adequately inform the buyer whether the automobile is subject to a security interest, not a financing statement. In these situations, section 9-320(a)'s harsh effects are justified because the buyer could have easily requested to see the title, just as the person could have taken his watch to a more trustworthy repair person. If most of the troublesome cases litigated under section 9-320(a) involve automobiles, then the rule's harsh effects are in order because it is not burdensome for a buyer to look at the title, which one would expect a seller to possess if it were really intending to make a sale. There are very few, if any, reasonable explanations a consumer could give for not noticing or asking to see the title before making the purchase. If the dealer does not have the title, then this should immediately put the buyer on notice that either there is something wrong with the title or that this purchase might violate the rights of a third party.[111] In the end, the harsh effects are justified because it is not too much to require a buyer to beware in this context.[112]

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110 Jonathon C. Lipson, *Remote Control: Revised Article 9 and the Negotiability of Information*, 63 OHIO ST. L.J. 1327, 1384-85 (2002).

111 Superior Bank, FSB v. Human Serv. Employees Credit Union, 556 S.E.2d 155, 159 (Ga. Ct. App. 2001) (holding that whenever a security interest is noted on the certificate of title for a vehicle, the title is deemed to provide constructive notice to future creditors and buyers that the vehicle is encumbered by a security interest. As a result, a subsequent purchaser or creditor is deemed to have constructive knowledge of the prior perfected security interest thereby making his claim subordinate to or ineffective in taking advantage of the buyer's seller rule.).

112 Milledgeville Cmty. Credit Union v. Corn, 716 N.E.2d 864, 867 (Ill. App. Ct. 1999).

IV

WHAT ARE THE COURTS DOING? THE LIMITATIONS OF AUTHORIZATION, ENTRUSTMENT, AND THE PLAIN MEANING OF THE BUYER'S SELLER RULE

There are a handful of decisions where courts have allowed buyers in the ordinary course to take free even when they failed to satisfy the Buyers of Goods Rule. In these cases, the courts discontinue the security interest by allowing the buyers to fall back upon either section 9-306(2), section 2-403(2), or on a suspect interpretation of section 9-307(1). Buyers prevailing under one of these alternatives are faced with other obstacles. First, in regard to section 9-306(2), buyers must show an authorization occurred. Second, if buyers are attempting to use section 2-403(2), then they must show that entrustment applies in the context of security interests not solely in the context of title transfers. Third, when courts are not relying on the Code's other sections to extricate a remote buyer in the ordinary course from the purported harsh results, courts have struggled to construe section 9-307(1) differently from its widely recognized meaning so that they could arrive at the "correct" result.

A. Authorization Under Section 9-306(2)

In *Central California Equipment Co. v. Dolk Tractor Co.*,[113] the court does not treat authorization lightly. In *Dolk*, Progressive purchased a corn harvester and Central secured the sale by obtaining a security interest in the harvester.[114] The security agreement expressly prohibited the debtor from selling the collateral unless the secured party gave written permission.[115] After it could no longer continue making payments, Progressive requested help from Central to find a buyer so that the new buyer could take over the payments.[116] In response, Central's president mentioned to Dolk that the harvester was for sale.[117] Later, a salesperson from Central brought together Progressive, Dolk, and McCormack to discuss the possibility of selling the harvester

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[113] Cent. Cal. Equip. Co. v. Dolk Tractor Co., 144 Cal. Rptr. 367 (Cal. Ct. App. 1978).

[114] *Id*. at 368.

[115] *Id*.

[116] *Id*.

[117] *Id*.

to Dolk.[118] Although both Dolk and McCormack claimed Central authorized the sale, its president denied knowing a sale ever took place, but more importantly, Central never gave permission in written form.[119] The court held the required authorization could have only been satisfied by a written release; mere *acquiescence* was insufficient to show that the sale was authorized.[120] The court explained that the authorization exception in section 9-306(2) "should be found with extreme hesitancy and should generally be limited to the situation of a prior course of dealing" where the parties did not require written authorization.[121]

This opinion shows that authorization is not easy to come by in the case where written authorization is required to discontinue a security interest under section 9-306(2). The effect *Dolk* has upon authorization requirements becomes apparent in the context where the goods are subject to the entrustment section in Article 2. This connection is developed more thoroughly in the subsection below.

B. Section 2-403(2) and its Effects upon Security Interests

As a preface to this discussion, White and Summers state that the cases holding that buyers can fall back on section 2-403(2) when they cannot properly invoke section 9-307(1) are all in error.[122] Unfortunately, the authors do not elaborate on why they believe these decisions are in error. They merely refer to the apparent equivocation between the two examples in section 9-320(a)'s Comment 3.[123]

A notable case breaking ranks from section 9-307(1)'s clear guidelines is *Executive Financial Services, Inc. v. Pagel*.[124] In yet another factually complicated transaction, Executive Financial Services (EFS) purchased three tractors from Tri-County, which was owned by Mohr and Loyd.[125] EFS then leased the tractors

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118 *Id*.

119 *Id*. at 369.

120 *Id*. at 371.

121 *Id*.

122 WHITE & SUMMERS, *supra* note 5, at § 24-8(c).

123 *Id*. The two examples in Comment 3 that White & Summers refer to only occur in Revised Article 9, not Old Article 9. Whatever equivocation one might find within these examples, and what this might have invited courts to do in cases decided under Old Article 9-307(1), is unclear and is no explanation for the opinions decided under the rules of Old Article 9.

124 Executive Fin. Serv., Inc. v. Pagel, 715 P.2d 381 (Kan. 1986).

125 *Id*. at 383.

to Mohr-Loyd Leasing, which was an entity distinct from Tri-County but owned and operated by Mohr and Loyd.[126] On behalf of Tri-County, Loyd sold all three tractors to third parties.[127] It is important to note that when EFS purchased the tractors it never took possession of them. Rather, they remained on Tri-County's premises at all times; furthermore, the owners never segregated or marked the tractors from the remainder of its inventory to show that EFS or Mohr-Loyd claimed an interest in them.[128] The issue before the court was whether the third-party buyers purchased the tractors free of the security interest.

In its discussion, the court correctly held that section 9-307(1) was not applicable because the seller, Tri-County, did not create the security interest; rather, Mohr-Loyd Leasing did.[129] This prohibited the buyers from taking free under section 9-307(1), so in turn, they attempted to invoke section 2-403(2) in an effort to discontinue the perfected security.[130] This case presented a unique set of facts because typically the party entrusting the goods to a dealer is the debtor that originally purchased the goods and gave its secured party a superior security interest in the goods. However in *Pagel*, EFS, the secured party, entrusted the goods, not the debtor, Mohr-Loyd Leasing.[131]

The Code's entrustment provision, section 2-403, states:

> "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.[132]

In this case, the court chose to apply the passive definition of entrusting, acquiescence in retention, when it held that EFS's failure to remove the tractors from Tri-County's lot had the effect of entrusting the goods to Tri-County.[133] In the proper application, this provision states that an entrustment "of possession of goods to a merchant who deals in goods of that kind gives him

126 *Id*.
127 *Id*.
128 *Id*.
129 *Id*. at 385.
130 *Id*.
131 *Id*. at 387.
132 U.C.C. § 2-403(3) (emphasis added).
133 *Pagel*, 715 P.2d at 387.

power to transfer all rights of the entruster to a buyer in ordinary course."[134] In this case, EFS, the secured party, entrusted the goods to Tri-County, thereby empowering it to transfer all the rights EFS had in the collateral. As a secured party, EFS has the right to authorize the collateral's disposition free of the security interest. In effect, the entrustment to Tri-County put it in the shoes of the secured party, and consequently the court held that it could sell the goods under whatever terms it desired.

This interpretation is consistent with a plain reading of section 2-403(2), but the meaning of any statute, especially one in the Code, should be determined in light of the statute's intended purpose. It is clear that section 2-403(2)'s language tends to indicate that entrustment may discontinue a perfected security interest if the secured party is the entruster, but this is a tenable interpretation only when section 2-403(2) is read in isolation from the other sections in Part 4 of Article 2 and Article 9.

The entrustment provision's more familiar application is where a true owner of a watch entrusts it to a watch dealer for repair. Before the watch dealer returns the watch to the true owner, the watch dealer sells the watch to a buyer in the ordinary course of business. In this context the buyer takes title to the watch in virtue of the broad power conveyed to the dealer by the language in section 2-403(2) because the statute gives the dealer the "power to transfer all rights of the entruster to a buyer in ordinary course of business."[135] In this example, there is no doubt that the buyer in the ordinary course takes title to the watch, but this does not mean that the powers an entruster gains for purposes of transferring title also extend to the powers controlling a security interest. In *Pagel*, the court went too far.

When attempting to reconcile the co-existence of two statutes that yield different results, courts have the duty to reconcile them and give effect to both; however, where a court cannot, then "a specific statute will not be controlled or nullified by a general one."[136] In considering whether to apply section 2-403(2) in the context of security interests, a court should first determine if there are more specific statutes on point. In the *Pagel* case there were. Section 9-306(2) states that "a security interest continues in collateral notwithstanding sale, exchange or other disposition

[134] U.C.C. § 2-403(2).
[135] *Id*.
[136] Morton v. Mancari, 417 U.S. 535, 550-51 (1974).

thereof unless the disposition was *authorized by the secured party in the security agreement*."[137] Unfortunately, the Code does not provide a definition for "disposition." As a result, this Comment relies upon Black's Law Dictionary's definition, which defines it as the "act of transferring something to another's care or possession."[138] If this definition is put side-by-side with the Code's definition of "entrusting" in section 2-403(3), then any delivery in retention of possession of goods clearly falls within the meaning or class of acts recognized as a disposition. Section 9-306(2) operates in the specific context where goods subject to a security interest are disposed. One might interpret section 9-306(2) to operate in the general context of any disposition just as section 2-403(2)'s general treatment of entrustment. However, there is a difference between them because section 9-306(2) specifically refers to dispositions where the collateral is encumbered by a security interest, and in this specific context, the security interest continues.

When a person has the power to transfer all rights of the entruster, as section 2-403(2) provides, it certainly seems to establish that this person also has the power to discontinue the security interest because secured parties have this power. However, section 2-403(2) makes no reference to the situation where the goods disposed are subject to a security interest. It treats all dispositions alike, unlike section 9-306(2) which operates in the specific context where the goods are encumbered. Section 9-306(2)'s specificity should urge a court to use it if it conflicts with section 2-403(2) because in the context of security interests authorization is not achieved by mere acquiescence.

As discussed above, the court in *Central California Equipment Co. v. Dolk Tractor Co.* held that mere acquiescence cannot pass as authorization.[139] Consequently, if a secured party entrusts goods to a person who is in the business of selling goods of the kind, but the entrustment is achieved via acquiescence, not delivery, then the entrustment provision cannot be used in the context of multiple-sales transactions because entrustment's dual definition conflicts with the more specific language in Article 9, which does not allow mere acquiescence to suffice as authorization. In

[137] U.C.C. § 9-306(2) (emphasis added).

[138] BLACK'S LAW DICTIONARY 484 (7th ed. 1999).

[139] Cent. Cal. Equip. Co. v. Dolk Tractor Co., 144 Cal. Rptr. 367, 371 (Cal. Ct. App. 1978).

addition to this argument, section 9-306(2)'s lead-in language clearly states that the effect of other Articles is of no consequence.[140]

Just as section 9-201(a) has an exception clause built into it,[141] so does section 9-306(2). The first few words specifically limit any exceptions to those found in Article 9, not Article 2. As discussed above, the broad power a secured party gains from section 9-201(a) is also limited by any exception found throughout the entire Code.[142] If one reads section 9-201(a) in isolation, it appears that section 2-403(2) should have been available to the buyers in *Pagel* because the entrustment language appears to confer this power and section 9-201(a) does not limit the exceptions to Article 9 but instead the whole Code. This is true, but not after section 9-306(2) reconfirms the superiority of secured parties in this more specific context.[143] Section 9-306(2)'s specific language controls over section 9-201's general language, and more importantly, since authorization is not equated with acquiescence, as *Dolk* held, entrustment should not provide the sought-after substitute when entrustment amounts to nothing more than acquiescence.

C. Article 2, Part 4 Was Not Meant to Operate in the Context of Security Interests

When viewed in its entirety, the Code has two recurring characteristics. First, in format, each Article is a smaller version of the entire Code. That is, if viewed from above, one sees that the format of the whole Code is duplicated in each Article, its parts, and ultimately the sections that hold everything together. For instance, the rules and definitions in Article 1 are applied throughout the entire Code. In some respects, Article 1 is the first part of the remaining Articles in their treatment of commercial law just as the definitions in section 9-102(a) are the first part of Article 9 that apply to the remaining parts in that Article's treatment of secured transactions. In both cases, the latter portions have less or sometimes no effect without the former infusing meaning into them. That is, without the former parts, especially the definition sections, the words in the latter parts

140 *See supra* note 6 for the lead language of § 9-306(2).
141 U.C.C. § 9-201(a).
142 *See supra* note 22 and accompanying text.
143 WHITE & SUMMERS, *supra* note 5, § 24-8.

would be empty or open to interpretation and ambiguity. Fortunately, they are not and this format clears up most of the ambiguity with clear definitions and sections that build upon the preceding sections.

Second, each Article tends to begin with very broad, general, and absolute rules that are tempered by exceptions in subsequent sections. For instance, section 9-201(a) states that the secured party always wins, unless there are exceptions elsewhere in the Code.[144] Section 3-306 states that a "person having rights of a holder in due course takes free of the claim to the instrument."[145] However, section 3-302 limits the broad right a holder in due course acquires from section 3-306. When a person interprets the Code in the context of these two themes, it undoubtedly has an effect upon the meaning and operation of any section in the Code.

While considering the effect of entrusting under section 2-403(2) in regard to secured transactions, the court in *Pagel* should have first considered the purpose and meaning of the sections and sub-sections preceding section 2-403(2) before it interpreted what it understood this section to mean in isolation. That is, before one attempts to understand any sub-section of section 2-403, she should first consider whether the preceding sections have any effect upon that section's interpretation.

One of the changes the Code had upon commercial law was to move away from the age-old doctrine wherein transfer of ownership was dependent upon the delivery of title from one party to the next. For instance, the lead-in language in Part 4 of Article 2 states:

> 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.[146]

In addition to the lead-in language, section 2-401's subsections make this more clear by stating that the title to goods is deemed to have passed at the time the goods have been identified by con-

[144] *See supra* note 20.
[145] U.C.C. § 3-306.
[146] U.C.C. § 2-401.

tract,[147] or when the buyer takes possession of the goods, even if the buyer has not yet obtained the actual documents.[148] If one reads all of Article 2's Part 4 in this context, the interpretation of subsequent sections would be different than if it were read in isolation.

For instance, after section 2-401 discusses the requirements for transfer of ownership, section 2-403(1) starts with a broad rule that one cannot transfer more than one has legal right to.[149] Section 2-403(1)'s first sentence more or less restates the old property principle, *nemo dat qui non habet*.[150] After the Drafters cast this broad and powerful rule, they immediately limit its effect in section 2-403(1)'s second sentence by stating that in certain contexts one may transfer more than one has legal right to.[151] Section 2-403(1) should serve as a warning to those attempting to transfer ownership. Not only is transfer of title unnecessary, as section 2-401 provides, but in some cases ownership may be transferred when the transferor fails to have the required legal rights. It is not possible to interpret section 2-403 to operate in the context of transferring security interests if it is read along with section 2-401. Section 2-403 was created for the transfer of *ownership* in a context where title and normal bargains are absent. That is, section 2-403(1) begins by limiting a transferor's rights to no more than it possesses, but then it makes an exception for the purpose of facilitating commercial transactions.

For example, the second sentence of section 2-403(1) outlines the conditions for when a person with voidable title can pass *good* title to a good faith purchaser for value.[152] That is, it out-

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147 U.C.C. § 2-401(1).

148 *Id*. § 2-401(2).

149 The first sentence of § 2-403(1) states "[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."

150 No one can give that which he does not have. BLACK'S LAW DICTIONARY 1660 (7th ed. 1999).

151 The second sentence of § 2-403(1) states:

> 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 that was 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.

152 Voidable title is transferred when the transferor was deceived as to the identity of the purchaser, the delivery was in exhange for a check which is later dishonored,

lines when a person is able to give more than she has legal right to. After reading the earlier sections in Part 4 of Article 2, the reader should interpret the entrustment sub-section in the context of Part 4 as a whole. If this is done, then it is apparent that the Drafters' purpose for these sections was to preserve *good* title, not to ensure *clear* title.[153] In addition, Professor Hawkland states:

> In a broad sense, section 2-403(2) exemplifies one effort to "modernize the law governing commercial transactions" in keeping with the underlying philosophy of the UCC. Accordingly, when a housewife takes her vacuum cleaner for repairs to a merchant who also is in the business of selling vacuum cleaners new and old, the sale by him to a buyer in the ordinary course of business passes a *good* title to the latter.[154]

After one looks at the Act as a whole and considers its direct language and the relevant commentary, it is clear that Article 2's Part 4 focuses on the conditions under which *good* title passes. If the Drafters intended for entrustment to discontinue a security interest, then they would have been more careful and used the words "clear title" which means "[a] title free from any encumbrances, burdens, or other limitations."[155] At least facially, there is nothing inconsistent with interpreting section 2-403(2) as the court did in *Pagel*, but it is only consistent if section 2-403(2) is read or interpreted in isolation. As noted in Section II, the exceedingly challenging task of applying Article 9 is for one to construe and apply all the operable and relevant Code sections in a *consistent* manner.

There are two more factors that give this interpretation more weight. First, Old section 9-306(2) states "[e]xcept 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 iden-

it was agreed that the transaction was to be a "cash sale," or the delivery was procured through fraud punishable as larcenous under the criminal law. U.C.C. § 2-403(1). Good title is "[a] title that is legally valid or effective." BLACK'S LAW DICTIONARY 1493 (7th ed. 1999).

[153] A title free from *any* encumbrances, burdens, or other limitations. BLACK'S LAW DICTIONARY 1493 (7th ed. 1999) (emphasis added).

[154] WILLIAM D. HAWKLAND, UNIFORM COMMERCIAL CODE SERIES, § 2-403:7, at 612 (emphasis added) (quoting U.C.C. § 1-102(2)(a)).

[155] *See supra* note 153.

tifiable proceeds including collections received by the debtor."[156] If one intends to find an exception to this rule, then it must be found in Article 9, *not* Article 2.[157]

Second, Article 2 also imposes similar restrictions. For example, in section 2-402(3)(a), the section *preceding* section 2-403, the drafters state that nothing in Article 2, which naturally includes entrusting, shall impair the rights of creditors of the seller that are governed under the provisions of Article 9.[158] If the Drafters did intend for Part 4, or all of Article 2, to have an effect upon secured transactions, then why did they not put a conflict provision in Part 1 of Article 2 just as they did with Articles 3 and 4?[159] The Drafters put this provision into Part 4 because they meant for Part 4 to only affect transfer of ownership, *not security interests*.

Of course it is difficult to interpret what the phrase "creditors of the seller" means in addition to determining if it is applicable to transactions like the one in *Pagel.* However, in *Matteson v. Harper*,[160] the Oregon Supreme court invoked this section to prohibit the discontinuation of the security interest upon the sale of collateral that was subject to limited resale authorization. In *Matteson*, the debtor transferred the collateral to an auctioneer for sale when he could no longer make payments.[161] After the secured party was notified, he authorized the auctioneer to make a sale but only at a specific price.[162] The auctioneer sold the collateral for an amount less than the secured party specified.[163] The buyer argued that the agreement between the secured creditor and the auctioneer had no effect because entrustment gives the entrustee all powers of the entruster *regardless of any condition expressed between them*.[164] The court held that the entire issue of entrustment was not relevant because section 2-402(3)(a) states that nothing in Article 2 can impair the rights of creditors of the seller.[165]

More recently the Arizona Court of Appeals held that only the

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156 U.C.C. § 9-306(2) (revised 2001) (emphasis added).
157 White & Summers, *supra* note 5, at § 24-8(c).
158 U.C.C. § 2-403(3)(a).
159 *See* U.C.C. § 3-102(2) and § 4-102(1).
160 Matteson v. Harper, 682 P.2d 766, 769 (Or. 1984).
161 *Id*. at 767.
162 *Id*. at 768.
163 *Id*.
164 *Id*. at 769.
165 *Id*. The court held that the auctioneer was one of the seller's creditors despite

person granting the security interest to the secured party is a creditor of the seller, even if the secured party itself entrusts goods to this party.[166] If one considers *Matteson*, then it is not clear why the court in *Pagel* did not recognize Tri-County as one of EFS's sellers. Yes, it was true that EFS extended credit to Mohr-Loyd Leasing, but Tri-County sold the goods; however, the same individuals that owned Mohr-Loyd Leasing owned Tri-County. In this context, if there is any problem with applying section 2-402(3)(a), then it is a formal problem, not one of substance. Nevertheless, if one considers section 2-402(3)(a) in light of Article 9's priority rules, the only consistent interpretation is that the entrustment power in section 2-403(2) applies only to transactions that involve equipment, not inventory or consumer goods, because section 9-307(1) already determines the result when inventory is the subject matter. This is the rationale adopted in the Second Circuit.[167]

D. Bending the Buyer's Seller Rule Beyond Recognition

The fairly recent Oregon Supreme Court case, *Schultz v. Bank of the West*,[168] turns the Buyers of Goods Rule on its head, especially the buyer's seller element. In *Schultz*, the Muirs purchased a motorhome from a dealer and gave its lender, Bank of the West (the Bank) a security interest in the vehicle.[169] The Bank perfected by noting the lien on the title.[170] A few years after purchasing the motorhome, the Muirs brought it to Gateleys, a motorhome dealer, and had it sell the motorhome and apply the purchase price to a new motorhome that the Muirs purchased from Gateleys.[171] Gateleys eventually sold the Muirs' old motorhome to the Schultzes, who were allegedly unaware that the motorhome was being sold for the Muirs.[172] After the sale, Gateleys failed to satisfy the outstanding debt to the bank and it

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there being no formal relationship between them because the auctioneer was acting as an agent for the debtor who was one of the seller's creditors. *Id.* at 769 n.7.

166 Sears Consumer Fin. Corp. v. Thunderbird Prods., 802 P.2d 1032, 1037 (Ariz. Ct. App. 1990).

167 Aircraft Trading & Servs., Inc. v. Braniff, Inc., 819 F.2d 1227, 1235 (2d Cir. 1987).

168 Schultz v. Bank of the West, 934 P.2d 421 (Or. 1997).

169 *Id*. at 422.

170 *Id*.

171 *Id*.

172 *Id*.

later filed for bankruptcy.[173] After learning that the Bank had a security interest in the motorhome, the Schultzes brought an action seeking a declaration that they owned the motorhome free of the Bank's security interest.[174] The trial court granted summary judgment for the Schultzes but the court of appeals reversed, holding that the Bank's security interest remained in effect because Gateleys did not create the security interest and only had the power to transfer title.[175] The Oregon Supreme Court reversed, but in order for it to arrive at this result, it bent the meaning and operation of section 9-307(1) far beyond any liberal construction section 1-102 should allow.

The court's discussion began by stating that the court of appeals erred when it defined "buyer in the ordinary course of business" only in regard to section 9-307(1), and not section 1-201(9).[176] The court's interpretation of "buyers in the ordinary course" focused upon whom the buyer makes its purchase from in order to invoke the protections of a buyer in the ordinary course of business.[177]

The court stressed that section 1-201(9) requires that the buyer purchase goods "from a *person* in the business of selling goods of that kind," not that this person must also have title to the goods.[178] This is the crucial step in the court's determination of who the *seller* really was, the Muirs or Gateleys. In its discussion the court looked to section 2-106(1), which defines "sale" as "the passing of title from the *seller* to the buyer for a price."[179] Since the Muirs are the party that actually passed title, the court held no other party could be regarded as seller in the context of this definition. Consequently, the Schultzes were able to satisfy section 1-201(9)'s sub-element, purchasing from *a person* who is in the business of selling goods of the kind, because they bought from Gateleys, a person in the business of selling motorhomes. The Schultzes were also able to take the motorhome free of the security interest because the court held that section 2-106(1) deems the Muirs as the seller, and as such, they created the se-

173 *Id*.
174 *Id*.
175 *Id*.
176 *Id*. at 424.
177 *Id*. at 423.
178 *Id.* (quoting OR. REV. STAT. § 71.2010(a) (1997)) (alteration in original).
179 U.C.C. § 2-106(1) (emphasis added).

curity interest.[180] In effect, the Oregon court bifurcates the term "seller" under section 9-307(1) by letting it refer to Gateleys insofar as the buyer in the ordinary course element is concerned, but then quickly flips the term around by allowing it to stand for the Muirs for purposes of the buyer's seller element.

I applaud the Oregon Supreme Court's recommendation to read the Code's sections together and not in isolation.[181] Yet, the court fails to follow its own recommendation. For instance, in *Schultz*, when the court relies on the definition of "sale" in section 2-106(1) in order for it to apply the term "seller" to the Muirs instead of Gateleys, it fails to recognize that Article 2 already provides a definition for "seller": "[A] person who sells or contracts to sell goods."[182] The court clearly said that the contracting parties were the Schultzes and Gateleys, and in light of the definition of "seller" in section 2-103(1)(d), only Gateleys fit this definition, not the Muirs. To do otherwise, the *Schultz* court would not only have to apply the word "seller" to two different entities, the Muirs and Gateleys, but also ascribe two different meanings to the word "seller." This is far from ordinary.

Furthermore, the court violates the rule of statutory construction discussed above.[183] If two statutes conflict, then the one that is more specific controls over the general. In this case, section 2-103(1)(d) gives a specific definition of "seller." Nothing is more specific than a definition and it makes no sense for the court to not use it, especially when the court conveniently borrows the term "seller" from a definition for "sale" in order to arrive at what it regarded as the best solution. The rationale behind the *Schultz* opinion relies upon an interpretation that the Drafters recognized. That is, not all sellers would have title to the goods sold. Consequently, the court states that the Drafters made a "conscious choice" to use the word "person" instead of the word "seller," but the court gives no authority for this interpretation other than its "equitable" construction of section 1-201(9).[184]

Instead of inserting its own definition for "seller," the *Schultz* court should have looked to the Code for other reasons to explain why the Drafters chose "person" instead of "seller" when

[180] *Schultz*, 934 P.2d at 423-25.
[181] *Id*. at 424.
[182] U.C.C. § 2-103(1)(d).
[183] *See supra* note 136 and related text.
[184] *Schultz*, 934 P.2d at 423.

drafting section 1-201(9). On its face, the format of section 1-201(9) does not lend itself to use of the word "seller" because stylistically it does not fit well in the place of "person." For instance, "a seller in the business of selling goods of the kind" would have been a poor wording choice due to the redundancy. The most natural word choice would have been "merchant," not "person." However, the Drafters could not use the word "merchant" because it is a term of art that has a technical definition in section 2-104(1). This section defines "merchant" not only as "a person who deals in goods of the kind," but also one who by his "occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction."[185] Had the drafters used "merchant" instead of "person" in section 1-201(9), the result would have widened the scope beyond the class of persons they intended to protect.

Nevertheless, the Oregon Supreme Court attempted to reinforce its interpretation of section 1-201(9)'s without knowledge sub-element by mistakenly inserting the word "ownership" into the section and then interpreting this section to be primarily concerned with ownership rights. The court stated

> the text of [section 1-201(9)] recognizes that a sale to a buyer in ordinary course may be "in violation of the *ownership* rights . . . of a third party." Any ownership rights in a third party would mean that the "person in the business" did not have title to the goods. Thus, the text of [section 1-201(9)] indicates that "person" does not mean "seller."[186]

The court could not have arrived at this interpretation unless it inserted the word "ownership" into its strained and inaccurate quotation of the without knowledge sub-element. The without knowledge sub-element actually states, "[a] person that buys goods in good faith, without knowledge that the sale violates the rights of another person in the goods . . . ."[187] The court's interpretation stands up only if this statute were concerned about harming an owner's rights.[188] The purpose of the without knowledge sub-element not only referred to "true owners" but to any party that might have an interest in the goods sold, like a security interest!

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185 U.C.C. § 2-104(1).

186 *Schultz*, 934 P.2d at 423 (quoting OR. REV. STAT. § 71.2010(9) (1997)) (omission in original).

187 U.C.C. § 1-201(9).

188 *Id*.

The Code contains other indications showing that the Oregon Supreme Court's interpretation was not correct. For instance, the Drafters chose to use the term "person" instead of "seller" because they provide a technical definition for "person" just as they do for "seller." Article 1 defines "person" as "an individual or an organization."[189] The drafters choose to use "person" because using "seller" would not indicate that they intended for it to include entities such as a "corporation . . . or any other legal or commercial entity."[190]

Other jurisdictions appear to be in agreement with this interpretation. In a more recent decision by the Appellate Court of Illinois, the court used *Black's Law Dictionary*'s definition of seller: "A person who sells or contracts to sell goods."[191] This definition references section 2-103(1)(d) as its source.[192] The court held that the seller is not the person who transfers title but the person who does the actual contracting.[193] Consequently, the Appellate Court of Illinois' treatment of sellers would have deemed Gateleys to be the seller, not the Muirs.[194]

In addition, earlier editions of *Black's Law Dictionary* show that the Oregon Supreme Court departed from the well established meaning of "seller." In the 1910 edition of *Black's Law Dictionary*, the word "seller" is defined as "the party who transfers property in the contract of sale. The correlative is 'buyer' or 'purchaser.'"[195] According to these definitions the Schultzes were "buyers," and the correlative "seller" should have been Gateleys, thereby preventing the court's bifurcation of "seller." Of course, there is nothing that requires courts to follow the meanings used in a particular dictionary, but it is not as if *Black's Law Dictionary* is arbitrarily or carelessly defining words. If one looks into its earlier editions, the definitions were taken from court opinions and the subsequent editions track the Code for

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189 U.C.C. § 1-201(30).

190 U.C.C. § 1-201(28).

191 BLACK'S LAW DICTIONARY 1365 (7th ed. 1999).

192 *Id.*

193 Milledgeville Cmty. Credit Union v. Corn, 716 N.E.2d 864, 867-68 (Ill. App. Ct. 1999).

194 *Id.*

195 BLACK'S LAW DICTIONARY 1069 (2d ed. 1910). The 1933 edition uses the same definition. BLACK'S LAW DICTIONARY 1599 (3d ed. 1933). The 1968 edition uses the same definition. BLACK'S LAW DICTIONARY 1525 (4th ed. 1968). The 1979 edition is the point where the definition falls in step with the U.C.C.'s definition in § 2-103(d). BLACK'S LAW DICTIONARY 1220 (5th ed. 1979).

the definition of "seller." In addition to this etymological argument, one respected commentator stated that the court's interpretation of section 9-307(1) and section 1-201(9) was not warranted.[196]

When *Schultz* is read under the rules of Revised Article 9, the court's opinion appears to be even less compelling. That is, if *Schultz* had been decided under Revised Article 9, the court would have had a much more difficult time recognizing the Muirs as "sellers." In Revised Article 9, the Drafters add a new section called "Rights and Title of Consignee With Respect to Creditors and Purchasers."[197] Subsection (a) states in part that "the consignee is deemed to have rights and title to the goods identical to those the consignor had or had power to transfer."[198] This provision would have had a strong effect upon the court's treatment of the meaning of the word "seller." That is, section 9-319 would have prohibited the court from treating the Muirs as a seller, especially if the interpretation of one section should be consistent with the others around it. If the court intended to be consistent, which is a virtue in most contexts, it would have refrained from using the definition of "sale" in section 2-106(1) so that it could call the Muirs "sellers" because section 9-319(a) states that Gateleys would have been the party that actually transferred title.[199] Unfortunately, section 9-319(a) would not have been dispositive in *Schultz*.

According to Revised Article 9, the *Schultz* transaction would not have been subject to this section because a true "consignment" does not involve goods that were "consumer goods" immediately before delivery to the consignee.[200] Even though

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[196] Steven O. Weise, a member of the Permanent Editorial Board for the Uniform Commercial Code, former Chair of the Subcommittee on Secured Transactions of the American Bar Association Section of Business Law, and the American Bar Association's Advisor to the Article 9 Drafting Committee, held that the definitions of buyer and seller should be correlated when interpreting § 9-307(1). Steven O. Weise, *U.C.C. Article 9: Personal Property Secured Transactions*, 54 BUS. LAW. 307, 331 (1998).

[197] U.C.C. § 9-319.

[198] *Id*. § 9-319(a).

[199] *Id*.

[200] U.C.C. § 9-102(a)(20) states:

> "Consignment" means a transaction, regardless of its form, in which a person delivers goods to a merchant for the purpose of sale and: (A) the merchant: (i) deals in goods of that kind under a name other than the name of the person making delivery; (ii) is not an auctioneer; and (iii) is not generally known by its creditors to be substantially engaged in selling the

section 9-319(a) would not have directly affected the result in *Schultz*, that does not mean this section would not have influenced the court and kept it from recognizing the Muirs as the seller so that it would preserve some level of consistency when such a situation did arise.

Had the motorhome merely been used for non-consumer purposes, such as a piece of equipment for a business the Muirs owned, the statute would have been applicable and, as a result, would have required the court to recognize Gateleys as title holders for purposes of protecting secured lenders like Gateleys.

V

REDIRECTING THE HARSH CONSEQUENCES

The Code provides other ways to avoid the harsh results attributed to the Buyers of Goods Rule by redirecting the burden to those who are better suited to bear the loss. For example, section 9-315(c) states that "a security interest in proceeds is a perfected security interest if the security interest in the original collateral was perfected."[201] The secured party's perfected status is automatic but only lasts for twenty days unless one of three conditions occurs,[202] in which case the security continues until it lapses under section 9-515.[203]

If this rule had been applied to any of the troublesome multiple-sales transactions discussed above, other than *Schultz*, then it would have redirected the priority battle to the secured parties, not the secured party and the subsequent buyer in the ordinary course of business. That is, section 9-315(d) provides that if the secured party had obtained a perfected security interest in the proceeds of the collateral, in addition to the collateral alone, then it would have been deemed to have held a security interest with a higher priority in the subsequently purchased collateral, even when the second secured party properly filed its financing

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> goods of others; (B) with respect to each delivery, the aggregate value of the goods is $1,000 or more at the time of delivery; (C) the goods are not consumer goods immediately before delivery; and (D) the transaction does not create a security interest that secures an obligation.

"'Consumer goods' means goods that are used or bought for use primarily for personal, family, or household purposes." U.C.C. § 9-102(a)(23).

[201] U.C.C. § 9-315(c).

[202] U.C.C. § 9-315(d).

[203] U.C.C. § 9-315(e)(1).

statement.[204]

Section 9-315(d) would not have helped the injured buyers in the ordinary course of business in *Schultz* because this section does not provide for automatic continuation of perfection in proceeds when the original collateral was an automobile. If the method for perfecting a security interest in an automobile permitted the secured party to perfect in proceeds too, then this would have allowed the original secured party in *Schultz* to foreclose on the motorhome the Muirs subsequently acquired with their trade-in. Again, an innocent party would have to bear the loss but it would have been a bank which is insured to protect it from such losses.

Conclusion

Pre-Code law had for quite some time protected buyers in the ordinary course without many exceptions, because the concept was originally defined only in regard to the buyer, not both the buyer and seller.[205] However, upon the emergence of the Code, the Drafters concluded that the favorable status of the buyer in the ordinary course does not always facilitate commercial transactions, especially in situations where the secured party's rights are not protected. The effects of the buyer's seller rule might be harsh at times, but the bottom line is that the serial competitions taking place between secured creditors and buyers in the ordinary course of business require that the secured creditor win. Without this level of assurance, the facilitation of commercial transactions would be undermined and this would have a far greater impact on this purpose than the injuries to a handful of remote buyers.

In order to understand the meaning and effect of the buyer's seller rule, one must see that it was meant to protect secured parties as well as consumers. Since more of us tend to fall in the consumer's shoes, it is hard to understand why the Drafters prohibit remote buyers from obtaining the same protections other buyers in the ordinary course of business possess. In the end, without secured creditors, dealers would be unable to finance their inventory.

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[204] U.C.C. § 9-322(b).

[205] *Uniform Trust Receipts Law*, *in* The Law of Chattel Mortgages and Conditional Sales and Trust Receipts, § 635, at 825 (Samuel W. Eager ed. 1941).

In order to better understand the buyer's seller rule, one must read it in conjunction with Article 1, and any other relevant provision from the Code, because the meaning of a single section does not become completely clear until the section can be put side-by-side with every other relevant section and read in a manner that is not only facially consistent, but also consistent with its intended and underlying purpose.