

2003-2004

Rules of Contract Law

SELECTIONS FROM THE UNIFORM
COMMERCIAL CODE, THE CISG, THE
RESTATEMENT (SECOND) OF CONTRACTS,
AND THE UNIDROIT PRINCIPLES, WITH
MATERIAL ON CONTRACT DRAFTING

Charles L. Knapp
Nathan M. Crystal
Harry G. Prince

ASPEN
PUBLISHERS

RULES OF CONTRACT LAW
Selections from the Uniform
Commercial Code, the CISG, the
Restatement (Second) of Contracts,
and the UNIDROIT Principles
with Material on Contract Drafting
2003–2004 Statutory Supplement

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ASPEN
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1185 Avenue of the Americas, New York, NY 10036
www.aspenpublishers.com

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Aspen Publishers
1185 Avenue of the Americas
New York, NY 10036

Printed in the United States of America.

1 2 3 4 5 6 7 8 9 0

ISBN 0-7355-2812-8



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2003–2004**

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Contents

Uniform Commercial Code	1
Editors' Note	1
Table of Sections	4
Sections	7
Revised Uniform Commercial Code — Article 1 — General Provisions (2001 Official Text)	98
Editors' Note	98
Table of Sections	98
Sections	99
Proposed Revisions to Uniform Commercial Code — Article 2 — Sales (2002 Draft)	109
Editors' Note	109
Table of Sections	110
Sections	111
Convention on Contracts for the International Sale of Goods	141
Editors' Note	141
Table of Articles	143
Articles	146
Restatement (Second) of Contracts	167
Editors' Note	167
Table of Sections	169
Sections	174
Principles of International Commercial Contracts	213
Editors' Note	213
Table of Articles	214
Articles	217
Materials on Electronic Contracts	239
Comment: Uniform Computer Information Transactions Act	239

Uniform Computer Information Transactions Act	
Section 112: Manifesting Assent	245
Section 113: Opportunity to Review	248
Electronic Signatures in Global and National Commerce Act,	
Editors' Note	249
Electronic Signatures in Global and National Commerce Act	251
Contract Drafting: A Sample Problem	263
The Problem	263
The Lawyer's Role and Ethical Obligations in Contract Drafting	264
The Drafting Process	265
Model Contract with Comments	266
Counseling the Client	269
Bibliography	270
Sample Examination Questions with Model Answers	271
Editors' Note	271
Contract Formation, Defenses, and Remedies	271
Justifications for Nonperformance and Remedies	280
Conditions and Justifications for Nonperformance	288
Sample Examination Questions without Model Answers	305
Mutual Assent and the Statute of Frauds	305
Battle of the Forms: UCC §2-207	306
Interpretation	307
Breach and Remedies	308

Uniform Commercial Code

*EDITORS' NOTE*¹

As the United States developed a national market economy during the nineteenth century, the number of business transactions across state lines increased dramatically. Many of these transactions were cumbersome, however, because of differences among the states on commercial subjects, such as negotiable instruments, sales, and warehousing. Recognizing these problems, a number of business lawyers suggested the need for greater uniformity among the states in commercial law.

In 1889 the legislature of New York, the leading commercial state at that time, passed a statute providing for the appointment of commissioners who were authorized to solicit the appointment of commissioners from other states for the purpose of preparing uniform state laws. In 1892 the first meeting of the National Conference of Commissioners on Uniform State Laws (NCCUSL) was held in connection with the annual meeting of the American Bar Association. At first the Commissioners concentrated on technical questions, such as standardized forms for acknowledgement of instruments, but they soon ventured into more substantive areas. By the early part of the twentieth century, the Commissioners had prepared uniform acts on a number of commercial subjects: negotiable instruments, sales, warehouse receipts, bills of lading, and trust receipts, to name just a few.

Adopted in many states, the uniform acts did foster the cause of uniformity to some extent. A number of factors, however, limited the success of the National Conference. Professor and later Judge Robert Braucher summarized the problems as follows:

[The history of the uniform acts] provides an illustration of four major difficulties which have afflicted uniform legislation: (1) difficulty in obtaining original enactment, (2) a tendency toward deviation from the official text at the time of the original adoption, (3) nonuniform judicial interpretation, and (4) difficulty in promulgating and obtaining enactment of uniform amendments.

1. Matters covered in this Note are explored more fully in the following works: R. Braucher & Robert R. Riegert, *Introduction to Commercial Transactions* 19-31 (1977); J. White & R. Summers, *Uniform Commercial Code Handbook* 1-7 (5th ed. 2000); and Nathan M. Crystal, *Codification and the Rise of the Restatement Movement*, 54 *Wash. L. Rev.* 239 (1979).

Robert Braucher & Robert Riegert, Introduction to Commercial Transactions 21-22 (1977).

By 1940 it was apparent that many of the uniform acts adopted early in the century required revision. At the fiftieth annual meeting of the National Conference of Commissioners, William A. Schnader, the president of the Conference, called for the creation of a uniform commercial code. The Conference quickly adopted his suggestion, subject to obtaining funding. In 1944 the Conference combined forces with the American Law Institute (ALI) to sponsor the project, with Professor Karl Llewellyn of Columbia Law School as Chief Reporter.

After a lengthy process, involving circulation of drafts among advisors, business groups, and others, The National Conference and the ALI issued an official text of the proposed Code in 1951. Pennsylvania became the first state to adopt the Code, in 1953. The project received a major setback in 1956, however, when the New York Law Revision Commission, after a three-year study, advised the New York Legislature that the Code "is not satisfactory in its present form." The New York Law Revision Commission's study has been published in a six-volume set and remains an important source of information about the Code.

The New York study caused the ALI and the National Conference to reexamine the Code. In 1958 the sponsoring organizations issued a revised Official Text. New York adopted this new version of the Code in 1962, and other states quickly followed suit. By 1968 the Code was in force in all jurisdictions except Louisiana, where only certain articles have been enacted. Even to this day, however, the process of revision goes on. In 1961 the ALI and the National Conference created a Permanent Editorial Board for the Uniform Commercial Code to monitor developments in commercial law and propose revisions of the Code.

Although titled a commercial code, the name is somewhat of a misnomer because the Code fails to cover a number of important commercial subjects. Transactions involving real estate and personal services are generally outside the scope of the Code. In addition, even for transactions subject to the Code, many aspects are regulated by other bodies of law. For example, Article 8 of the Code deals with title and transfer of investment securities, such as common stock. Most of the law governing transactions in securities, however, lies outside the Code. Moreover, common law principles continue to govern transactions to which the Code is applicable unless specifically displaced by Code provision. UCC §1-103.

Rather than a comprehensive code of commercial law, the UCC instead consists of a loosely related collection of revised versions of the most significant uniform acts adopted earlier this century by the National Conference of Commissioners. Article 1 covers a number of general matters; it includes a section containing definitions that apply throughout the Code. UCC §1-201. A substantial revision of Article 1 was completed in 2001 but it had been enacted only in the U.S. Virgin Islands as of March 1, 2003. Thus, the version of Article 1 contained in this part of the Supplement continues to be the applicable law in almost every jurisdiction. Many sections from Revised Article 1 are included in a later part of this Supplement.

Article 2, which is the principal part of the Code addressed in most contracts courses, deals with transactions involving the sale of goods. A major revision of Article 2 was nearing completion at the time this Supplement was written and many sections from Proposed Article 2 are included in a subsequent part. Article 2A deals with various aspects of leases of personal property, including formation of lease contracts, performance, and default. For several years the ALI and National Conference worked on

a proposed Article 2B, dealing with computer information transactions. After much controversy over the provisions, the ALI and the National Conference decided that such rules should not be proposed as part of the UCC but would be incorporated instead into a separate Uniform Computer Information Transactions Act (UCITA). The Act was adopted by the National Conference in 1999, but not by the ALI. A more detailed discussion of UCITA is included in the Materials on Electronic Contracts later in this Supplement.

“Commercial paper” — checks, notes, and drafts — is the focus of Article 3; the processing of such instruments through the banking system is the subject of Article 4; fund transfers are the topic of Article 4A. Article 5 deals with the rights and liabilities of parties to “letters of credit.” Article 6 establishes rules for “bulk sales,” transactions in which the owner of a certain type of business sells substantially all of the assets of that business. On recommendation of the NCCUSL, a majority of states have now repealed Article 6. Article 7 governs “documents of title,” such as bills of lading issued by carriers of goods, or warehouse receipts issued by companies that are involved in the storage of goods. Article 8 regulates the ownership and transfer of investment securities. Finally, Article 9 provides for the creation and protection of security interests in personal property.

Unlike the Restatements, which have only persuasive weight, the UCC is a statute, having the force of law. It is important to remember, however, that in each state the “law” is not the official text of the Code promulgated by the ALI and the National Conference of Commissioners, but that state’s own enacted version of the Official Code. Most states have made nonuniform changes in certain provisions of the Official Text. See U.C.C. Rep. Serv., State U.C.C. Variations.

Each section of the Official Text of the Code is followed by an Official Comment, which includes reference to prior law, discussion of the purposes of the section, and definitional cross references. What weight should be given to the discussion in the official comments? Since the state legislatures have not enacted the comments, they do not have the force of law. Do they have at least the persuasive status of “legislative history”? Two well-known commentators on the Code have made the following observations:

Certainly the comments are not entitled to as much weight as ordinary legislative history. In some states the comments were not placed before the enacting body prior to adoption of the Code. Indeed, some of the present comments were not even in existence at the time the section to which they are now appended was adopted. Furthermore, much of the Code is highly technical “lawyer’s” law. If the average legislator who voted to enact the Code in a given state did not understand the intricacies of Article Four or Article Nine at the time of enactment, it is likely that he did not grasp the relevant comments either.

James J. White & Robert S. Summers, *Uniform Commercial Code* 14 (5th ed. 2000). Nonetheless, court opinions frequently have given the comments substantial weight. Indeed, White and Summers suggest that the courts have taken to use of the comments “like ducks to water.” *Id.* at 13. See, e.g., *Carlund Corp. v. Crown Center Redevelopment*, 849 S.W.2d 647, 650 (Mo. Ct. App. 1993); *B & W Glass, Inc. v. Weather Shield Mfg., Inc.*, 829 P.2d 809, 816 (Wyo. 1992) (comments treated as persuasive authority).

This part of the Supplement includes the text of a number of sections from Article 2 of the Code, along with a few provisions from Articles 1, 3, and 9. Official Comments for the most significant sections are included as well. The editors are grateful to

the Permanent Editorial Board for the Uniform Commercial Code for permission to reprint this material. — Copyright various dates by the American Law Institute and the National Conference of Commissioners on Uniform State Laws.

ARTICLE 1. GENERAL PROVISIONS

Part 1. Short Title, Construction, Application and Subject Matter of the Act

- §1-102. Purposes; Rules of Construction; Variation by Agreement
- §1-103. Supplementary General Principles of Law Applicable
- §1-105. Territorial Application of the Act; Parties' Power to Choose Applicable Law
- §1-106. Remedies to Be Liberally Administered
- §1-107. Waiver or Renunciation of Claim or Right After Breach

Part 2. General Definitions and Principles of Interpretation

- §1-201. General Definitions
- §1-203. Obligation of Good Faith
- §1-204. Time; Reasonable Time; "Seasonably"
- §1-205. Course of Dealing and Usage of Trade
- §1-206. Statute of Frauds for Kinds of Personal Property Not Otherwise Covered
- §1-207. Performance or Acceptance Under Reservation of Rights
- §1-208. Option to Accelerate at Will

ARTICLE 2. SALES

Part 1. Short Title, General Construction and Subject Matter

- §2-102. Scope; Certain Security and Other Transactions Excluded from this Article
- §2-103. Definitions and Index of Definitions
- §2-104. Definitions: "Merchant"; "Between Merchants"; "Financing Agency"
- §2-105. Definitions: Transferability; "Goods"; "Future" Goods; "Lot"; "Commercial Unit"
- §2-106. Definitions: "Contract"; "Agreement"; "Contract for Sale"; "Sale"; "Present Sale"; "Conforming" to Contract; "Termination"; "Cancellation"

Part 2. Form, Formation and Readjustment of Contract

- §2-201. Formal Requirements; Statute of Frauds
- §2-202. Final Written Expression: Parol or Extrinsic Evidence
- §2-203. Seals Inoperative
- §2-204. Formation in General
- §2-205. Firm Offers
- §2-206. Offer and Acceptance in Formation of Contract
- §2-207. Additional Terms in Acceptance or Confirmation
- §2-208. Course of Performance or Practical Construction
- §2-209. Modification, Rescission and Waiver
- §2-210. Delegation of Performance; Assignment of Rights

Part 3. General Obligation and Construction of Contract

- §2-301. General Obligations of Parties
- §2-302. Unconscionable Contract or Clause
- §2-305. Open Price Term
- §2-306. Output, Requirements and Exclusive Dealings

Uniform Commercial Code

- §2-307. Delivery in Single Lot or Several Lots
- §2-308. Absence of Specific Place for Delivery
- §2-309. Absence of Specific Time Provisions; Notice of Termination
- §2-311. Options and Cooperation Respecting Performance
- §2-312. Warranty of Title and Against Infringement; Buyer's Obligation Against Infringement
- §2-313. Express Warranties by Affirmation, Promise, Description, Sample
- §2-314. Implied Warranty: Merchantability; Usage of Trade
- §2-315. Implied Warranty: Fitness for Particular Purpose
- §2-316. Exclusion or Modification of Warranties
- §2-317. Cumulation and Conflict of Warranties Express or Implied
- §2-318. Third Party Beneficiaries of Warranties Express or Implied
- §2-319. F.O.B. and F.A.S. Terms
- §2-320. C.I.F. and C. & F. Terms
- §2-326. Sale on Approval and Sale or Return; Rights of Creditors
- §2-327. Special Incidents of Sale on Approval and Sale or Return
- §2-328. Sale by Auction

Part 4. Title, Creditors and Good Faith Purchasers

- §2-401. Passing of Title; Reservation for Security; Limited Application of This Section
- §2-402. Rights of Seller's Creditors Against Sold Goods
- §2-403. Power to Transfer; Good Faith Purchase of Goods; "Entrusting"

Part 5. Performance

- §2-501. Insurable Interest in Goods; Manner of Identification of Goods
- §2-502. Buyer's Right to Goods on Seller's Repudiation, Failure to Deliver, or Insolvency
- §2-503. Manner of Seller's Tender of Delivery
- §2-504. Shipment by Seller
- §2-507. Effect of Seller's Tender; Delivery on Condition
- §2-508. Cure by Seller of Improper Tender or Delivery; Replacement
- §2-509. Risk of Loss in the Absence of Breach
- §2-510. Effect of Breach on Risk of Loss
- §2-511. Tender of Payment by Buyer; Payment by Check
- §2-512. Payment by Buyer Before Inspection
- §2-513. Buyer's Right to Inspection of Goods

Part 6. Breach, Repudiation and Excuse

- §2-601. Buyer's Rights on Improper Delivery
- §2-602. Manner and Effect of Rightful Rejection
- §2-603. Merchant Buyer's Duties as to Rightfully Rejected Goods
- §2-604. Buyer's Options as to Salvage of Rightfully Rejected Goods
- §2-605. Waiver of Buyer's Objections by Failure to Particularize
- §2-606. What Constitutes Acceptance of Goods
- §2-607. Effect of Acceptance; Notice of Breach; Burden of Establishing Breach After Acceptance; Notice of Claim or Litigation to Person Answerable Over
- §2-608. Revocation of Acceptance in Whole or in Part
- §2-609. Right to Adequate Assurance of Performance
- §2-610. Anticipatory Repudiation
- §2-611. Retraction of Anticipatory Repudiation
- §2-612. "Installment Contract"; Breach
- §2-613. Casualty to Identified Goods
- §2-614. Substituted Performance

- §2-615. Excuse by Failure of Presupposed Conditions
- §2-616. Procedure on Notice Claiming Excuse

Part 7. Remedies

- §2-702. Seller's Remedies on Discovery of Buyer's Insolvency
- §2-703. Seller's Remedies in General
- §2-704. Seller's Right to Identify Goods to the Contract Notwithstanding Breach or to Salvage Unfinished Goods
- §2-705. Seller's Stoppage of Delivery in Transit or Otherwise
- §2-706. Seller's Resale Including Contract for Resale
- §2-708. Seller's Damages for Non-acceptance or Repudiation
- §2-709. Action for the Price
- §2-710. Seller's Incidental Damages
- §2-711. Buyer's Remedies in General; Buyer's Security Interest in Rejected Goods
- §2-712. "Cover"; Buyer's Procurement of Substitute Goods
- §2-713. Buyer's Damages for Non-Delivery or Repudiation
- §2-714. Buyer's Damages for Breach in Regard to Accepted Goods
- §2-715. Buyer's Incidental and Consequential Damages
- §2-716. Buyer's Right to Specific Performance or Replevin
- §2-717. Deduction of Damages from the Price
- §2-718. Liquidation or Limitation of Damages; Deposits
- §2-719. Contractual Modification or Limitation of Remedy
- §2-721. Remedies for Fraud
- §2-723. Proof of Market Price: Time and Place
- §2-725. Statute of Limitations in Contracts for Sale

ARTICLE 3. NEGOTIABLE INSTRUMENTS

Part 1. General Provisions and Definitions

- §3-104. Negotiable Instrument

Part 3. Enforcement of Instruments

- §3-302. Holder in Due Course
- §3-305. Defenses and Claims in Recoupment
- §3-306. Claims to an Instrument
- §3-311. Accord and Satisfaction by Use of Instrument

ARTICLE 9. SECURED TRANSACTIONS

Part 1. Short Title, Applicability and Definitions

- §9-102. Policy and Subject Matter of Article
- §9-104. Transactions Excluded From Article

Part 2. Validity of Security Agreement and Rights of Parties Thereto

- §9-206. Agreement Not to Assert Defenses Against Assignee; Modification of Sales Warranties Where Security Agreement Exists

Part 3. Rights of Third Parties; Perfected and Unperfected Security Interests; Rules of Priority

- §9-318. Defenses Against Assignee; Modification of Contract After Notification of Assignment; Term Prohibiting Assignment Ineffective; Identification and Proof of Assignment

ARTICLE 1. GENERAL PROVISIONS***Part 1. Short Title, Construction, Application and Subject Matter of the Act*****§1-102. Purposes; Rules of Construction; Variation by Agreement**

(1) This Act shall be liberally construed and applied to promote its underlying purposes and policies.

(2) Underlying purposes and policies of this Act are

(a) to simplify, clarify and modernize the law governing commercial transactions;

(b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;

(c) to make uniform the law among the various jurisdictions.

(3) The effect of provisions of this Act may be varied by agreement, except as otherwise provided in this Act and except that the obligations of good faith, diligence, reasonableness and care prescribed by this Act may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.

(4) The presence in certain provisions of this Act of the words “unless otherwise agreed” or words of similar import does not imply that the effect of other provisions may not be varied by agreement under subsection (3).

(5) In this Act unless the context otherwise requires

(a) words in the singular number include the plural, and in the plural include the singular;

(b) words of the masculine gender include the feminine and the neuter, and when the sense so indicates words of the neuter gender may refer to any gender.

§1-103. Supplementary General Principles of Law Applicable

Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.

§1-105. Territorial Application of the Act; Parties’ Power to Choose Applicable Law

(1) Except as provided hereafter in this section, when a transaction bears a reasonable relation to this state and also to another state or nation the parties may agree that the law either of this state or of such other state or nation shall govern their rights and duties. Failing such agreement this Act applies to transactions bearing an appropriate relation to this state.

(2) . . .

§1-106. Remedies to Be Liberally Administered

(1) The remedies provided by this Act shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed but neither consequential or special nor penal damages may be had except as specifically provided in this Act or by other rule of law.

(2) Any right or obligation declared by this Act is enforceable by action unless the provision declaring it specifies a different and limited effect.

**§1-107. Waiver or Renunciation of Claim or Right
After Breach**

Any claim or right arising out of an alleged breach can be discharged in whole or in part without consideration by a written waiver or renunciation signed and delivered by the aggrieved party.

***Part 2. General Definitions and Principles of
Interpretation*****§1-201. General Definitions**

Subject to additional definitions contained in the subsequent Articles of this Act which are applicable to specific Articles or Parts thereof, and unless the context otherwise requires, in this Act:

(1) “Action” in the sense of a judicial proceeding includes recoupment, counterclaim, set-off, suit in equity and any other proceedings in which rights are determined.

(2) “Aggrieved party” means a party entitled to resort to a remedy.

(3) “Agreement” means the bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance as provided in this Act (Sections 1-205 and 2-208). Whether an agreement has legal consequences is determined by the provisions of this Act, if applicable; otherwise by the law of contracts (Section 1-103). (Compare “Contract.”)

(4) “Bank” means any person engaged in the business of banking.

(5) “Bearer” means the person in possession of an instrument, document of title, or certificated security payable to bearer or indorsed in blank.

(6) “Bill of lading” means a document evidencing the receipt of goods for shipment issued by a person engaged in the business of transporting or forwarding goods, and includes an airbill. “Airbill” means a document serving for air transportation as a bill of lading does for marine or rail transportation, and includes an air consignment note or air waybill.

(7) “Branch” includes a separately incorporated foreign branch of a bank.

(8) “Burden of establishing” a fact means the burden of persuading the triers of fact that the existence of the fact is more probable than its non-existence.

(9) “Buyer in ordinary course of business” means 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