

## Official Comment

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10. "Good faith." ~~Good faith is defined in Article 8 for purposes of the application to Article 8 of Section 1-203, which provides that "Every contract or duty within this Act [the Uniform Commercial Code] imposes an obligation of good faith in its performance or enforcement." Section 1-201(b)(20) defines "good faith" as "honesty in fact and the observance of reasonable commercial standards of fair dealing."~~ The sole function of the good faith definition in Revised Article 8 is to give content to the Section 1-203 obligation as it applies to contracts and duties that are governed by Article 8. The standard is one of "reasonable commercial standards of fair dealing." The reference to commercial standards makes clear that assessments of conduct are to be made in light of the commercial setting. The substantive rules of Article 8 have been drafted to take account of the commercial circumstances of the securities holding and processing system. For example, Section 8-115 provides that a securities intermediary acting on an effective entitlement order, or a broker or other agent acting as a conduit in a securities transaction, is not liable to an adverse claimant, unless the claimant obtained legal process or the intermediary acted in collusion with the wrongdoer. This, and other similar provisions, see Sections 8-404 and 8-503(e), do not depend on notice of adverse claims, because it would impair rather than advance the interest of investors in having a sound and efficient securities clearance and settlement system to require intermediaries to investigate the propriety of the transactions they are processing. The good faith obligation does not supplant the standards of conduct established in provisions of this kind.

In Revised Article 8, the definition of good faith is not germane to the question whether a purchaser takes free from adverse claims. The rules on such questions as whether a purchaser who takes in suspicious circumstances is disqualified from protected purchaser status are treated not as an aspect of good faith but directly in the rules of Section 8-105 on notice of adverse claims.

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### Definitional Cross References:

- "Agreement". Section 1-201(b)(3).
- "Bank". Section 1-201(b)(4).
- "Person". Section 1-201(30)(b)(27).
- "Send". Section 1-201(38)(b)(36).
- "Signed". Section 1-201(39)(b)(37).
- "Writing". Section 1-201(46)(b)(43).

**Section 9\_102. DEFINITIONS AND INDEX OF DEFINITIONS.**

(a) [Article 9 definitions.] In this article:

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(43) [reserved] ~~“Good faith” means honesty in fact and the observance of reasonable commercial standards of fair dealing.~~

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**3. Definitions Relating to Creation of a Security Interest.**

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b. **“Security Agreement.”** The definition of “security agreement” is substantially the same as under former Section 9\_105—an agreement that creates or provides for a security interest. However, the term frequently was used colloquially in former Article 9 to refer to the document or writing that contained a debtor’s security agreement. This Article eliminates that usage, reserving the term for the more precise meaning specified in the definition.

Whether an agreement creates a security interest depends not on whether the parties intend that the law *characterize* the transaction as a security interest but rather on whether the transaction falls within the definition of “security interest” in Section 1\_201. Thus, an agreement that the parties characterize as a “lease” of goods may be a “security agreement,” notwithstanding the parties’ stated intention that the law treat the transaction as a lease and not as a secured transaction. See Section 1-203.

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**14. Consignment-Related Definitions: “Consignee”; “Consignment”; “Consignor.”** The definition of “consignment” excludes, in subparagraphs (B) and (C), transactions for which filing would be inappropriate or of insufficient benefit to justify the costs. A consignment excluded from the application of this Article by one of those subparagraphs may still be a true consignment; however, it is governed by non-Article 9 law. The definition also excludes, in subparagraph (D),

what have been called "consignments intended for security." These "consignments" are not bailments but secured transactions. Accordingly, all of Article 9 applies to them. See Sections 1-201~~(37)~~(b)(35), 9-109(a)(1). The "consignor" is the person who delivers goods to the "consignee" in a consignment.

The definition of "consignment" requires that the goods be delivered "to a merchant for the purpose of sale." If the goods are delivered for another purpose as well, such as milling or processing, the transaction is a consignment nonetheless because a purpose of the delivery is "sale." On the other hand, if a merchant-processor-bailee will not be selling the goods itself but will be delivering to buyers to which the owner-bailor agreed to sell the goods, the transaction would not be a consignment.

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16. "**Document.**" The definition of "document" is unchanged in substance from the corresponding definitions in former Section 9\_105. See Section 1-201~~(15)~~(b)(16) and Comment ~~15~~16.

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19. "**Good Faith.**" This Article expands the definition of "good faith" to include "the observance of reasonable commercial standards of fair dealing." The definition in this section applies when the term is used in this Article, and the same concept applies in the context of this Article for purposes of the obligation of good faith imposed by Section 1\_203. See subsection (c).