Welcome to this podcast on the Right of Reclamation brought to you by CALI. I am Professor Scott J. Burnham.

We learned in the CALI Lesson on Anticipatory Repudiation that when either party has reasonable grounds for insecurity—that is, they have reasonable grounds to believe the other party may not perform—they may demand adequate assurance of future performance and withhold their performance until they get assurances.

If a buyer has already performed by paying for the goods before delivery, and then they become insecure about getting the goods, it is too late to do anything about it.

But if the seller has already performed by shipping the goods, and then they become insecure about getting paid, the seller may be entitled to some relief. This is the remedy of reclamation, by which the seller reclaims the goods from the shipper or the buyer. In this podcast you will learn when and how a seller can exercise this right and what its limitations are.

The right of reclamation is found in UCC § 2-702. This remedy is available only if the seller can satisfy certain requirements.

The first requirement is that the seller discovers that the buyer is insolvent. *Insolvent* is a term of art that is defined in § 1-201(b)(23):

"**Insolvent**" means: (A) having generally ceased to pay debts in the ordinary course of business other than as a result of bona fide dispute; (B) being unable to pay debts as they become due; or (C) being insolvent within the meaning of federal bankruptcy law.

This is a broad definition of insolvency, incorporating two common measures of insolvency. The first, called Cash Flow Insolvency, means that the party is unable to pay its debts as they become due. This is a forward-looking test, for the party must be incapable of paying both current and prospective obligations. The second measure, called Balance Sheet Insolvency, means that the party’s liabilities exceed their assets. That is, if all the assets were sold for their fair value, the amount raised would not pay the debts.

After discovering that the buyer is insolvent under either of these tests, the next requirement is timely notification. The seller must make the demand for reclamation within 10 days after the buyer receives the goods. There is one exception to this rule: if within three months before delivery, the buyer misrepresented its solvency to the seller in writing, then the 10 day limitation does not apply.

If the seller complies with these requirements, then it may reclaim the goods. Of course, as a practical matter, the buyer does not usually hand over the goods, so the seller may have to go to court to get them back, and the goods might not be worth the time and expense of doing so.

And there is a significant legal restriction on the seller’s right to reclaim the goods. Subsection (3) of § 2-702 provides that “The seller’s right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article.” So if the buyer has already committed to sell the goods to good faith purchasers such as buyers from inventory, those third parties will have priority over the seller.

Most importantly, the Code definition of *purchaser* in §§ 1-201(b)(29) and (30) includes secured creditors. As you will learn in the course on Article 9 Secured Transactions if you haven’t already had the pleasure of taking it, a secured creditor is a party that has a security interest in the personal property of a debtor and has the right to repossess that property on the debtor’s default.

Many commercial buyers have loans secured by all or substantially all of their existing and future goods. The moment a buyer who has granted a security interest purchases goods, the lender’s security interest attaches to the goods. In such a situation, the secured lender’s rights to the goods in the hands of the buyer take priority over the seller’s right of reclamation, and the seller has essentially made a gift of the goods to the secured creditor. The seller would still have a right to payment from the buyer, but that might not be collectible.

Moreover, many insolvent buyers end up in bankruptcy. While the Bankruptcy Code also has a provision on reclamation, most courts have found that the Article 2 rules apply in bankruptcy as well, so the seller will still lose out to secured creditors.

You have learned in this podcast that the right of reclamation is a very limited right. You should be able to enumerate the conditions that a seller must satisfy in order to exercise it and explain how other parties may have priority over the seller who exercises it.

I hope you have enjoyed this podcast on the Right of Reclamation.

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