CHAPTER TWO

THE BAILOR AND BAILEE RELATIONSHIP

A. BAILMENT

A bailment is usually defined as delivery of possession of specified goods to a bailee who acknowledges receipt of the goods and contracts to deliver them. While the common law may distinguish between various types of bailments depending upon the purpose of the bailment, Article 7 does not do so. Rather, Article 7 treats bailment as a unitary topic, concentrating on carriers that contract to transport the goods and warehouses that contract to store the goods. Nothing in Article 7 requires a bailee to issue a document of title when it receives the goods.

Even though bailments usually involve the bailor depositing the goods with the bailee, Article 7 addresses the idea that the bailee may claim ownership in the goods. The fact that the bailee may claim an ownership interest in the goods does not preclude the application of the provisions of Article 7 to the issuer of a document of title. UCC 7-401. UCC 7-201(b) recognizes that a bonded warehouse may issue documents purporting to be a warehouse receipt even though the warehouse owns the goods described. UCC 7-202(b) requires the warehouse to state on the warehouse receipt whether it is claiming any ownership interest in the goods described in the receipt.

Why might a warehouse issue a warehouse receipt for goods owned by the warehouse and not by a bailor? Because warehouse receipts are used to transfer rights in goods, a warehouse may issue a warehouse receipt for goods it owns as a mechanism to transfer rights in the goods described in the receipt to a buyer or a lender. This use of warehouse receipts may result in a situation in which a warehouse "over issues" receipts. That is, the warehouse issues more warehouse receipts covering the goods than the goods it has on hand. This is particularly likely when the goods are fungible goods such as grain. The warehouse then transfers those warehouse receipts to buyers or lenders. When the buyers or lenders come to collect the goods there are not enough goods to satisfy all claims made under the warehouse receipts. The rights of third parties to goods when the bailee issues a document of title will be addressed in Chapter 3.

B. LIABILITY FOR NON-RECEIPT OR MISDESCRIPTION

If a bailee issues a document of title, the document of title will describe the goods that have been deposited with the bailee. Two problems may arise from that description. First, the document of title may indicate that goods have been received when in fact the bailee has not received the goods. Second, the description in the document of title may fail to accurately describe the goods that have been received. The general rule is that the issuer of a document of title is liable for damage caused by reliance on the description of the goods in the document of title. UCC 7-203 and 7-301. An issuer includes someone who did not receive the goods purportedly covered by the document of title. UCC 7-102(a)(8).

Under UCC 7-203, which applies to all documents of title other than bills of lading, the issuer will not be liable for harm caused by an inaccurate description if the document conspicuously indicates that the issuer does not know whether all the goods described were received or whether the goods conformed to the description. The issuer may do so by using standard phrases such as "contents, condition, and quantity unknown" or "said to contain" or other words of similar meaning. According to the comment to UCC 7-203, this relief from liability is intended to operate where the description is furnished by the depositor but does not relieve the issuer from liability if it knowingly issues a document of title when the goods have not been received. The issuer's liability for the inaccurate description runs to a party to the document of title or to a good faith purchaser for value of the document who relies on that inaccurate description and is damaged by that reliance. This would include the bailor or a transferee of the document of title. The issuer will not be liable to a party to the document or a purchaser that had notice of the non-receipt or misdescription. Notice, defined in UCC 1-202, means not only knowledge of the fact but also reason to know of the fact.

> EXAMPLE 1: Bridget delivered to Ace Warehouse, Inc. several cartons that Bridget did not want the warehouse to open. Bridget furnished to Ace a description of the goods contained in the cartons. Ace put in the warehouse receipt a conspicuous notation "said to contain" followed by Bridget's furnished description of the goods. Ace will not have liability to a purchaser who relies on that description if that description is inaccurate. Even if Ace did not place the conspicuous notation "said to contain" on the warehouse receipt, Ace will not be liable to Bridget as she furnished the description and will, in most instances, have notice that the description was inaccurate.

Under UCC 7-301, the issuer of a bill of lading may preclude recovery based upon non-receipt or misdescription of the goods if the bill of lading indicates that the issuer does not know whether any or all of the goods were received or conform to the description. The issuer may do so by using standard phrases such as "contents or condition of contents of packages unknown" or "shipper's weight, load and count" or words of similar meaning. The issuer cannot preclude recovery for the inaccurate description if the issuer loaded the goods unless the goods are concealed in packages. Even then, the issuer has an obligation to count the packages loaded. UCC 7-301(b). A shipper who furnishes a description to the issuer guarantees to the issuer the accuracy of the shipper's description and must indemnify the issuer against damages caused by the inaccurate description. UCC 7-301(e). Comment 3 to UCC 7-301 indicates that this section does not relieve the issuer from its obligation to actually receive the goods in situations where the shipper does not make the description. An issuer may also indicate in the bill of lading that the shipper loaded the goods and if that is in fact true, the issuer is not liable for damages caused by improper loading. UCC 7-301(d). Nothing in Article 7, other than the carrier's duty of care discussed below, would impose liability for improper loading. Liability for improper loading may be imposed based upon other law such as federal law or state regulatory law. The issuer's liability for non-receipt or misdescription, if it arises, is to the consignee on the bill of lading or a holder to which a negotiable bill of lading has been duly negotiated. The liability is not to the consignor or shipper who deposited the goods with the issuer.

EXAMPLE 2: Bridal Goods, Inc. loaded a semi-truck container with packages and delivered the container to Great Plains Shipping Inc. for the carrier to transport to Chicago. Great Plains issued a bill of lading stating "shipper's weight, load and count" followed by a description of the goods furnished by Bridal Goods. Under UCC 7-301(a), Great Plains would not be liable for misdescription or non-receipt of the described goods. Under 7-301(d), Great Plains would not be liable for damage to the goods based upon improper loading because Bridal Goods loaded the goods in the container.

C. CARING FOR THE GOODS WHILE IN THE BAILEE'S POSSESSION

The general obligation of a bailee under Article 7 is to take reasonable care of the goods. UCC 7-204(a), 7-309(a). A bailee may agree by contract to a higher standard of care. A common carrier, under other law, may be liable for damages to goods in its care not caused by the carrier's negligence. A common carrier's liability has traditionally been to insure the safety of the goods except for limited exceptions such as acts of God, acts of the public enemy or the fault of the owner. Article 7 does not prevent that imposition of higher liability under that other law. UCC 7-309(a).

A warehouse and a carrier may not disclaim its obligation to take reasonable care of the goods. UCC 1-302. A warehouse may, either in the warehouse receipt or a storage agreement, limit its liability for damages caused by lack of reasonable care. If the bailor requests that the warehouse increase its limit on liability, the warehouse may charge an increased rate. UCC 7-204(b). Former law required that the limitation of liability be stated per article stored or by weight. This requirement was deleted in the 2003 revisions as out of step with industry practice. UCC 7-204, comment 2. Thus a warehouse may provide a monetary cap on damages without designating it as per unit stored or per unit of weight. A carrier may, either in the bill of lading or in the transportation agreement, limit its liability for damage to the goods by stating a value that the damages may not exceed if the carrier's rates are dependant on value and the consignor is afforded an opportunity to declare a higher value. UCC 7-309(b). These limitations on liability are not an impermissible attempt to disclaim the obligation to act with reasonable care. UCC 7-204, comment 2. The limitation of liability allowed under either UCC 7-204 or 7-309 is not effective if the bailee converts the goods to the bailee's own use. UCC 7-204(b), 7-309(b). Conversion to the bailee's own use is not shown merely by the failure of the bailee to redeliver the goods. UCC 7-204, comment 4; UCC 7-309, comment 3. The comments also indicate that "conversion to its own use" is a narrower concept than conversion generally. The document of title, storage agreement, or transportation agreement may also contain reasonable provisions as to the time and manner of presenting claims and commencing actions for loss or damage to the goods. UCC 7-204(c), 7-309(c). Federal law or state regulatory law may also govern the issue of when and how claims must be presented.

> EXAMPLE 3: A warehouse receipt, issued by Ace Warehouse Inc., provides "in any event, damages for loss or damage to the goods stored shall be limited to $1,000." When Ace redelivered the goods to the bailor, the goods were damaged due to water leaking on the goods. Even if the damage to the goods was significantly more than the $1,000 limitation and the damage was caused by Ace's lack of reasonable care, Ace's liability is limited to $1,000. The bailor may argue that the limited liability clause is invalid under some other law, such as the contract doctrine of unconscionability, and thus not enforceable. The law of contracts, not Article 7, would determine that issue.

If a bailee is unable to deliver the goods to the bailor because the bailee cannot find the goods, the issue is what presumption is created by that failure to redeliver. Although some courts had held that failure to redeliver the goods when demanded created a presumption that the goods had been converted, the comments to UCC 7-204 and 7-309 disapprove that line of cases. The bailee is liable for a failure to redeliver the goods to the person entitled to them under the document of title, UCC 7-403, so the key question is whether the liability limitation in the document of title or storage or transportation agreement is effective. Under UCC 7-204 and 7-309, the limitation is effective unless the bailee has converted the goods to its own use. The key to this question is often the allocation of the burden of proof. Other than the comment that precludes assuming a conversion took place by the mere failure to redeliver, Article 7 does not address questions of burden of proof. The import of the comment, however, is to place on the person claiming conversion the burden of proving the conversion took place by offering evidence other than the mere failure of the bailee to redeliver. Even having said that, the person claiming the goods must also prove the bailee converted the goods to "its own use," not merely that the goods were converted, in order to avoid the limitation of liability.

Other than the general duty of reasonable care as discussed above, Article 7 addresses two other issues that are relevant to the care of goods. First, UCC 7-207(a) provides that the warehouse shall keep goods covered by a warehouse receipt separate in order to permit identification and delivery of the goods. Having stated that obligation, which may be varied by agreement, UCC 7-207(a) also provides that different lots of fungible goods may be commingled. Fungible goods are defined as "goods of which any unit, by nature or usage of trade, is the equivalent of any other like unit." UCC 1-201(b)(18)(A). If different lots of fungible goods are commingled, then each person with a claim to a lot is treated as an owner in common of the mass of fungible goods. UCC 7-207(b).

Example 4: Ace Warehouse receives truckloads of corn from different bailors. On Monday, Ace received a truckload of No. 2 yellow corn and a different truckload of No. 1 white corn. The corn in those two truckloads may not be fungible.

Example 5: Ace Warehouse received two truckloads of corn from different bailors. All of the corn that was delivered was No. 2 yellow corn. Ace could commingle that corn and store it together in a grain silo. Each bailor would be treated as an owner in common of the entire mass of corn and entitled to a proportionate share of the mass depending upon the quantity they had delivered.

Second, if a carrier issues a through bill of lading, the issuing carrier is liable not only for its actions in respect to the goods but also for actions of the carriers who perform under the through bill of lading. UCC 7-302(a). This liability may be altered in international transportation agreements. The issuer of the through bill of lading who is required to pay due to a performing carrier's breach of its obligation may recover from that performing carrier the amount it was required to pay plus its expenses incurred in defending against the liability. UCC 7-302(c).

Example 6: Creative Designs, Inc. delivered goods to Federal Carrier, located in Chicago, for delivery to Beijing. Federal Carrier issued a through bill of lading for the goods and also contracted with Worldwide Carriers to pick up the goods in California for delivery to Beijing. Federal Carriers transported the goods to California. Under the through bill of lading, Federal Carriers will be liable for the performance of Worldwide Carriers. Because this involves international transportation, under UCC 7-302, Federal Carriers could provide in the bill of lading that it is not responsible for Worldwide's performance. Because this is interstate transportation, federal law will preempt Article 7 if federal law has a contrary provision. UCC 7-103.

D. THE BAILEE'S LIEN

The bailee who has received goods generally has charges for the cost of storage or transportation. The bailee's charges are generally determined by the agreement of the parties, although in the past, charges for some types of transportation were determined through published tariffs. In this era of deregulation, the mandatory tariff structure does not come into play as it did in the past. To the extent there is a mandatory tariff concerning the bailee's charges, that tariff would determine the bailee's charge. UCC 7-103, comment 2.

If the bailee's charges are paid, the bailee does not need to resort to any enforcement process to collect. Article 7 provides for bailee's liens in the event the bailee's charges are not paid. The warehouse lien is provided for in UCC 7-209 and the carrier's lien is provided for in UCC 7-307. Neither section is exclusive in that liens may be allowed under other state or federal law. In addition, either a warehouse or a carrier may decide not to rely on the protection provided by the lien and may obtain a security interest in collateral in order to secure the amounts owed to the warehouse or carrier. See UCC 7-204(b), 7-307 comment 1. Security interests are consensual interests in personal property to secure obligations and are governed by UCC Article 9. UCC 9-109. The bailee's lien in Article 7, on the other hand, arises nonconsensually, that is the person owning the goods deposited with the bailee does not need to agree in order for the lien to arise. The lien arises by operation of the statutory sections.

The warehouse's lien arises whenever goods are deposited with a warehouse and a warehouse receipt or a storage agreement covers the goods deposited. UCC 7-209(a). Prior to the 2003 revisions, the warehouse's lien did not arise if a warehouse receipt covering the goods was not issued. The carrier's lien arises when goods deposited are covered by a bill of lading. UCC 7-307(a). The carrier's lien was not expanded to cover situations where there is a transportation agreement but not a bill of lading issued.

The important issues in considering the bailee's lien as provided for in Article 7 are: (1) for what amounts may the bailee assert a lien; (2) against what property may the bailee assert a lien; (3) how may the lien be enforced; and (4) against whom can the bailee assert a lien. We will consider the first three issues in this chapter and defer consideration of most of the issues involved in the fourth question until Chapter 3.

1. Amount of the Bailee's Lien

The warehouse's lien is for "charges for storage or transportation, including demurrage and terminal charges, insurance, labor, or other charges, present or future, in relation to the goods, and for expenses necessary for preservation of the goods or reasonably incurred in their sale pursuant to law." UCC 7-209(a). The carrier's lien is more limited in amount, covering "charges after the date of the carrier's receipt of the goods for storage or transportation, including demurrage and terminal charges, and for expenses necessary for preservation of the goods incident to their transportation or reasonably incurred in their sale pursuant to law." UCC 7-307(a). The storage agreement or document of title need not state exact amounts or that a lien on the goods covered by the storage agreement or document of title are subject to a lien. The lien arises by operation of law to secure the amounts stated in the statute.

2. Property Subject to the Bailee's Lien

The warehouse has a specific lien against the goods covered by the warehouse receipt or storage agreement or the proceeds of those goods for the charges and expenses related to those described goods. The warehouse may have a general lien against the goods stored or their proceeds for charges and expenses related to other goods stored with the warehouse if the warehouse receipt or storage agreement claims that general lien. UCC 7-209(a). The warehouse need not rely on its statutory lien and may take a security interest in any of the bailor's property in order to secure obligations that the bailor owes to the warehouse. That security interest would be governed by Article 9. UCC 7-209(b).

> Example 7: Creative Design stored goods with Ace Warehouse subject to a storage agreement. Ace will have a lien on the goods stored for the charges and expenses described above even if the storage agreement does not state that a lien is claimed or state the exact amount of the lien. Now assume that Creative Designs stored a second lot of goods with Ace. Ace issued a warehouse receipt for the second lot of goods. The second lot of goods will be subject to a lien for the charges and expenses related to the second lot of goods. However, that second lot of goods will not be subject to a lien for the charges and expenses related to the first lot of goods and the first lot of goods will not be subject to a lien for charges and

expenses related to the second lot of goods. For Ace to encumber the first lot of goods with the statutory warehouse lien related to charges and expenses for the second lot of goods, the storage agreement for the first lot of goods must make clear that the first lot of goods is subject to a lien for charges and expenses for other goods stored by the same bailor in the warehouse. For the second lot of goods to be subject to a lien for the charges and expenses related to the first lot of goods, the warehouse receipt covering the second lot of goods must provide that those goods are subject to a lien for charges and expenses for other goods stored by the same bailor with the warehouse. Of course, Ace may take a security interest in the stored goods or other items of the bailor's property by getting a security agreement with the bailor pursuant to Article 9.

The carrier has a lien on the goods covered by the bill of lading or their proceeds for the charges and expenses related to those goods. UCC 7-307(a). The carrier does not have the ability to claim a statutory lien for charges and expenses related to other goods carried by the carrier. Of course, the carrier may obtain a security interest if the carrier wishes to make goods in its possession subject to a security interest for charges and expenses related to carriage of other goods.

Example 8: Great Plains Shipping, Inc. takes three different lots of goods from Creative Design for shipment covered by three different bills of lading. Great Plains has a lien on the goods covered by each bill of lading only for the charges and expenses related to the goods covered by each bill of lading. If Great Plains wants to cross collateralize the obligation to pay for the transportation charges and other expenses, Great Plains must obtain a security agreement from Creative Design.

The bailee's lien under Article 7 terminates whenever the bailee voluntarily gives up possession of the goods or unjustifiably refuses to deliver the goods. UCC 7-209(e), 7-307(c). Losing the lien provided for in Article 7 does not deprive the bailee of other remedies a creditor has against the debtor, including the right to sue for a judgment and collect money owed. UCC 7-210(g), 7-308(f).

> **Example 9:** Creative Design presented to Ace Warehouse a warehouse receipt covering goods stored with Ace. Ace delivered the goods to Creative Design even though all of the charges related to those goods were not paid. By giving up possession of the goods, Ace lost its right to assert a lien in the goods no longer in Ace's possession but did not lose the ability to sue Creative Design to collect the amounts owed under basic principles of contract law.

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3. Enforcement of the Bailee's Lien

UCC 7-210 governs enforcement of the warehouse's lien and UCC 7-308 governs enforcement of the carrier's lien. Both sections allow the bailee to sell the goods subject to the lien in order to collect the amount of the lien. The sale may be either a private or public sale and must be commercially reasonable in the terms of sale and the manner of conducting the sale. The bailee may only offer the amount of goods for sale that is apparently necessary to satisfy the lien amounts unless the goods are sold in the usual manner in a recognized market for that type of goods, at the current price in the market, or in conformity with commercially reasonable practices of dealers in that type of goods. In those three instances, the sale is also deemed to be commercially reasonable. Establishing that a better price could be obtained if there was a sale in a different manner does not make the sale commercially unreasonable. The concept of commercial reasonableness has a well-developed body of case law under Article 9. Comment 4 to UCC 7-210 indicates that if the bailee's sale under Article 7 would be commercially reasonable under the provisions of Article 9, the sale meets the commercial reasonableness requirement of Article 7.

Prior to sale, the bailee must give notice to all persons known to claim an interest in the goods. The notice must state the amount due, the nature of the proposed sale and the time and place of a public sale. UCC 7-210(a) and 7-308(a).

In the case of a warehouse's lien but not a carrier's lien, if the goods are stored by someone other than a merchant storing goods in the course of its business, additional requirements must be met. UCC 7-210(b). First, the notice to persons known to claim an interest in the goods must: (i) contain an itemized statement of the claim, (ii) describe the goods subject to the lien, (iii) demand payment not less than ten days after the notice was received, and (iv) contain a conspicuous statement of a date by which the claim must be paid or a public auction at a specified date and time will be held. UCC 2-710(b)(2). The 2003 amendments eliminated the former requirement that the notice be sent in person or by certified or registered mail. Notice may be sent by any reasonable means. UCC 1-202. Second, public advertising must take place after the date stated in the notice for payment and for at least two weeks prior to the sale date. That public advertisement must be in a newspaper of general circulation where the sale is to be held and if no such newspaper exists, advertisements of the sale must be posted in no less than six conspicuous places in the neighborhood where the sale is to take place for at least ten days prior to the sale date. UCC 7-210(b)(5). Third, a public sale is the only sale that may be held. UCC 7-210(b)(3). Finally, the sale must take place at the nearest suitable place to where the goods are held or stored. UCC 7-210(b)(4). All of these requirements are in addition to the basic requirement of a commercially reasonable sale.

A warehouse may elect to use the more explicit notice provision even in cases where the bailor is a merchant and is storing its goods in the course of its business. UCC 7-210(h). A carrier may, but is not required to, follow this more extensive notice and public sale process. UCC 7-308(g).

Example 10: Bridget stored some household goods with Ace Warehouse Inc. and did not pay the storage charges. Ace has a lien on the goods for the storage charges and expenses of sale and may sell those goods at a commercially reasonable sale. Because Bridget is not a merchant storing goods in the course of its business, Ace must comply with the more extensive notice process and must sell the goods at a public sale.

Example 11: Bridget shipped household goods with Great Plains Shipping Inc. and did not pay the transportation charges. Great Plains need only conduct a commercially reasonable sale of the goods and must merely give notice to all persons known to claim an interest in the goods. Great Plains could sell the goods at a private sale if that was commercially reasonable.

As to both the warehouse's lien and the carrier's lien, a person claiming rights to the goods may pay the amount of the lien and the bailee's expenses in complying with the sale process. If the person pays those amounts, the bailee may not sell the goods. UCC 7-210(c), UCC 7-308(b). If the bailee sells the goods in the sale authorized by Article 7, the bailee may collect its lien amount out of the proceeds and if there are funds left over, must hold those funds for the person to whom the bailee would have been bound to deliver the goods. UCC 7-210(f), 7-308(e).

A purchaser in good faith at the sale to foreclose the bailee's lien takes the goods free of the claims of any person against whom the lien could be validly asserted even if the bailee fails to comply with the requirements of the provisions governing the sale process. UCC 7-210(e), 7-308(d). If the bailee conducts a public sale, the bailee may be a purchaser at the sale. UCC 7-210(d), 7-308(c). If the bailee conducts a lien foreclosure but fails to follow the process set forth in Article 7, the bailee is liable for damages caused by the failure to comply. If the failure to comply is willful, the bailee is liable for conversion. UCC 7-210(i), 7-308(h).

Example 12: Creative Design Inc. stored its excessive inventory with Ace Warehouse. Creative Design did not pay the storage charges and Ace commenced the foreclosure process. Ace failed to give notice to Creative Design, a person that Ace knew claimed an interest in the goods. Ace sold the goods to Overstock Goods Inc. at a public sale that was otherwise commercially reasonable. Ace would be able to credit against the amounts owed, the amount received from the sale. If there was a surplus of funds, Ace has to turn the surplus over to the person that would have been entitled to the goods. Overstock Goods Inc. bought the goods at the sale free of the claims of Creative Design as long as Overstock Goods acted in good faith. Ace would be liable to Creative Design for damages caused by the insufficient notice and if the court found that Ace had willfully failed to give notice to Creative Design, Ace would be liable for conversion.

The bailee is not limited in its ability to collect the lien amount to the process just described. The bailee may sue to collect amounts owed to it under other law governing creditor's rights. UCC 7-210(g), 7-308(f). This would be particularly important to a bailee who has lost its lien due to the fact that it delivered the goods to the person entitled to them under the document of title. UCC 7-209(e), 7-307(c).

Example 13: Creative Design Inc. shipped goods using Great Plains Shipping Inc. Creative Design did not pay the shipping charges. Great Plains Shipping held a proper foreclosure sale and sold the goods. The sale price did not bring the amount necessary to satisfy the charges and expenses owed. Great Plains would be able to sue Creative Design for the deficiency under basic principles of contract law. If Great Plains did not sell the goods but rather released the goods to the consignee under the bill of lading without getting payment for the shipping charges, Great Plains could sue Creative Design as a matter of contract law even though the carrier would not have a lien on the released goods.

4. Persons Subject to the Bailee's Lien

The bailee's lien is enforceable against the bailor. UCC 7-209(a) (effective against bailor), 7-307(b) (effective against consignor in most cases). Thus if the bailor is seeking to obtain the goods from the bailee, the bailee may refuse to turn over the goods to the bailor unless the bailor satisfies the bailee's lien. See UCC 7-403(b). We will consider the ability of the bailee to assert the bailee's lien against persons other than the bailor in Chapter 3. Consideration of this issue is deferred to Chapter 3 because the enforceability of the lien against third parties depends in some instances on whether the document of title is negotiable and to whom the document of title is negotiated.

E. TERMINATION OF THE CONTRACT FOR STORAGE

A warehouse may terminate the storage of the goods in several situations. The warehouse may want to terminate storage at the end of the stated term for storage. If there is no stated term for storage, the warehouse may terminate the storage by giving thirty days' notice of termination. In both situations, the warehouse must give notice to the person on whose account the goods are stored and to all persons known to claim an interest in the goods. The warehouse may require payment of all charges. If the goods are not removed by the date stated in the notice, the warehouse has the right to sell the goods pursuant to the lien enforcement process provided for in UCC 7-210. UCC 7-206(a).