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### One for All, But None for (All of) One: Revised Article 1 of the Uniform Commercial Code (Part 2 of 2)

Keith A. Rowley

*University of Nevada, Las Vegas – William S. Boyd School of Law*

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## One for All, But None for (All of) One: Revised Article 1 of the Uniform Commercial Code (Part 2 of 2)

Part One of this article examined four major differences between Revised Article 1 of the Uniform Commercial Code and Nevada's current version of Article 1, codified at N.R.S. §§ 104.1101 et seq. Part Two explores how Revised Article 1 has fared thus far in other states and suggests what the Nevada Legislature should consider when deciding in the upcoming legislative session whether to enact Revised Article 1 as written, whether to enact it with revisions, or whether not to enact it at all.

### News from the Front: The Fate of Revised Article 1 in Other States

Virginia was the first state to adopt Revised Article 1. Effective July 1, 2003, Virginia's version of Revised Article 1 embraces the narrowed scope of the uniform version,<sup>1</sup> as well as the extension of course of performance to all transactions governed by the Code.<sup>2</sup> On the other hand, Virginia's version of Revised Article 1 rejects the unitary good faith standard<sup>3</sup> and the uniform version's choice of law provision,<sup>4</sup> opting to retain the essence of former Section 1-105, requiring some reasonable relation between the state whose law the parties choose by agreement and the transaction the parties choose to

#### Written By:

Keith A. Rowley  
Associate Prof. of Law  
Boyd School of Law  
UNLV

subject to that law.<sup>5</sup>

Texas, whose version of Revised Article 1 took effect September 1, 2003, likewise embraces the narrowed scope of the uniform version<sup>6</sup> and the extension of course of performance to all transactions governed by the Code,<sup>7</sup> and rejects the uniform version's choice of law provision,<sup>8</sup> opting to retain the essence of former Section 1-105.<sup>9</sup> However, unlike Virginia's, Texas's version of Revised Article 1 embraces the unitary good faith standard - requiring both merchants and non-merchants to "observ[e] reasonable commercial standards of fair dealing."<sup>10</sup>

Idaho, whose version of Revised Article 1 took effect July 1, 2004, Minnesota, whose version of Revised Article 1 took effect August 1, 2004, Alabama and Delaware, each of whose versions of Revised Article 1 takes effect January 1, 2005, and Hawaii, whose version of Revised Article 1 "take[s] effect upon its approval,"<sup>11</sup> also narrow Article 1's scope,<sup>12</sup> extend the relevance of course of performance to all Code transactions<sup>13</sup> and reject the uniform version's choice of law provision,<sup>14</sup> opting to retain the essence of each state's former Section 1-105.<sup>15</sup> Alabama, Hawaii, and Idaho, like Virginia, reject the unitary good faith standard.<sup>16</sup> Delaware and Minnesota, on the other hand, like Texas, embrace the unitary good faith

standard.<sup>17</sup>

Massachusetts and West Virginia legislative committees are presently considering their own versions of Revised Article 1. Neither has passed either house, much less both houses, of their respective legislatures, and so their content may change between now and when, if ever, they become law. The version currently before the West Virginia Senate Judiciary Committee follows Texas, Minnesota, and Delaware in rejecting only the uniform choice of law provision and otherwise adopting the uniform version of Revised Article 1 in all material aspects, including the unitary good faith standard.<sup>18</sup> The version currently before the Massachusetts House Commerce and Labor Committee conforms in all material respects to the uniform version of Revised Article 1, *including the uniform choice of law provision* that every other state has rejected.<sup>19</sup>

### What's Nevada to Do?

... Article 1 provides rules that govern all transactions covered by the UCC without regard to their nature. It contains general rules of construction for interpreting the provisions of the entire Code, definitions applicable throughout the Code, a choice of law rule that applies to the other articles to the extent they do not contain their own provisions on choice of law, and a few substantive provisions applicable throughout the entire Code. Its provisions are the coordinating mechanism that holds the Code together, providing a level of commonality across the various substantive Articles of the Code.

Because the provisions of Article 1 apply to the entire Code, the impact of decisions regarding what provisions it includes is greater than that for decisions regarding provisions in individual articles...<sup>20</sup>

Everything else being constant, uniformity is good for commercial law and, in turn, for commerce, because the predictability fostered by uniformity reduces transaction costs and "levels the playing field" across jurisdictions. However, everything else rarely is constant, and uniformity may bear costs as well as benefits.

#### 1. Course of Performance

The decision to explicitly import course of performance into Revised Article 1 appears sound and carries with it no apparent cost. A widely-recognized principle of contract law counsels courts to look to the parties' course of performance of a contract —

sometimes referred to as the parties' "practical construction" of the contract — when interpreting or construing that contract.<sup>21</sup> It is not surprising, therefore, that every state that has enacted Revised Article 1 to date has enacted Section R1-303 as drafted. If Nevada enacts Revised Article 1, it should enact Section R1-303 as drafted. Doing so will foster uniformity.

## 2. Choice of Law

The decision to allow parties to choose the law of some jurisdiction wholly unrelated to them or their transaction is contrary to the prevailing rules regarding contractual choice of law<sup>22</sup> and is sufficiently problematic that none of the states that have enacted Revised Article 1 to date have enacted Section R1-301 as drafted. If Nevada enacts Revised Article 1, it should not enact Section R1-301(a)-(e) as drafted. Not enacting Section R1-301(a)-(e) will foster uniformity.

## 3. Scope

The decision to narrow Article 1's scope — notwithstanding the protestations of its drafters that they did not do so<sup>23</sup> — is not costless, although the benefits of uniformity may outweigh those costs. Sales of intangible or immovable personal property not governed by another article of the Code, which are within the scope of Nevada's current Article 1, are excluded from the scope of Revised Article 1; therefore, parties to these sales will, *inter alia*, lose the protection of the Code's duty of good faith and fair dealing and of the default statute of frauds set forth in N.R.S. § 104.1206. Nevada courts recognize an implied duty of good faith and fair dealing in all contracts,<sup>24</sup> so parties to contracts excluded by Revised Article 1 appear to be protected from bad faith and unfair dealing. On the other hand, there is no general statute of frauds that will fill the gap left by the loss of N.R.S. § 104.1206. Some may see that as a good thing. If a majority of the Nevada Legislature does not, it appears to have four options: (1) do not enact Revised Article 1; (2) enact Revised Article 1,

but without the new scope provision, Section R1-102; (3) enact Revised Article 1, but with an expanded scope provision that would encompass all sales of personal property not governed by another Article of the Code; or (4) enact Revised Article 1 and either amend N.R.S. § 111.220<sup>25</sup> to include sales of personal property not governed by the Code as revised or enact a stand-alone statute of frauds covering sales of personal property not governed by the Code in the wake of Revised Article 1.<sup>26</sup> Enacting Section R1-102 as written while retaining a renumbered N.R.S. § 104.1206 is not an option, because, in light of Section R1-102, a statute of frauds in Revised Article 1 would not apply to any transactions.

Thus far, the states that have enacted Revised Article 1 have not addressed the effects of its narrowed scope provision, and nothing I have read or heard suggests that any state has declined to enact Revised Article 1 because of Section R1-102's effects. Enacting Section R1-102 as written will foster uniformity. That said, if the Nevada Legislature enacts Revised Article 1 without Section R1-102, or with an amended Section R1-102 that broadens the scope of Revised Article 1 to include transactions that are within the implied scope of current Article 1, the impact on commerce should be negligible, as the net effect would be to keep the scope of Revised Article 1 the same as that of current Article 1. Enacting or amending a non-UCC statute of frauds to require a signed writing evidencing a contract for the sale of personal property not governed by Article 2 or 8 should, likewise, have a negligible impact on commerce, as the net effect would be to require a signed writing only in cases in which current law already does so.

## 4. Good Faith

The only disagreement among the states that have enacted Revised Article 1 thus far is whether to enact Revised Article 1's unitary good faith standard or retain a bifurcated standard, holding merchants and others assumed to have knowledge of commercial reasonable-

ness to a more expansive definition of good faith than it does non-merchants and others assumed not to have knowledge of commercial reasonableness.<sup>27</sup> At this point in time, the split is so even, it is hard to claim that any act will promote uniformity.

Assuming that N.R.S. § 104.1201(19) affords non-merchants at least as much protection in UCC transactions as Nevada's common law duty of good faith and fair dealing would afford them in a non-UCC transaction, the more interesting question seems to be whether enacting Section R1-201(b)(20) as written would afford non-merchants less protection than Nevada's common law duty of good faith and fair dealing. If so, and assuming further that the Nevada Legislature does not wish to erode the good faith protection currently afforded non-merchants in transactions governed by the Nevada Uniform Commercial Code, then it could follow the slight majority, reject the unitary good faith standard of Section R1-201(b)(20), and leave N.R.S. §§ 104.2103(1)(b) and 104A.2103(3) in place to retain the current merchant / non-merchant distinction.<sup>28</sup> Alternatively, Nevada could alter the language of Section R1-201(b)(20), so that the unitary standard would apply "except as otherwise provided in Articles 2, 2A, and 5," and leave N.R.S. §§ 104.2103(1)(b) and 104A.2103(3) in place to retain the current merchant/non-merchant distinction.

## Endnotes

1. VA. CODE § 8.1A-102 (Supp. 2003).
2. *Id.* § 8.1A-303.
3. Compare *id.* §§ 8.1A-201(b)(20) & 8.2-103(1)(b) with UCC § R1-201(b)(20) (2001).

As in Part One of this article, all citations in the text and notes to Revised Article 1 are in the form of "UCC § R1-..." or "Section R1-...." All citations in the text and notes to pre-Revised Article 1 will be to the relevant provision of the *Nevada Revised Statutes*, where possible; otherwise, they will be in the form of "UCC § 1-..." or "Section 1-...." See *One for All, But None*

*continued on page 30*

## Professor's Corner

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for (All of) One: Revised Article 1 of the Uniform Commercial Code (Part 1 of 2), NEV. LAW., July 2004, at 26, 27 n.1.

4. Compare VA. CODE § 8.1A-301 with UCC § R1-301.

5. See VA. CODE § 8.1-105 (2001).

6. See TEX. BUS. & COM. CODE ANN. § 1.102 (Vernon Supp. 2004).

7. *Id.* § 1.303.

8. Compare *id.* § 1.301 with UCC § R1-301.

9. See TEX. BUS. & COM. CODE ANN. § 1.105 (Vernon 1968).

10. TEX. BUS. & COM. CODE ANN. § 1.201(b)(20) (Vernon Supp. 2004).

11. See 2004 Haw. Sess. Laws 162, § 20. Presumably, this means July 2, 2004, when Hawaii's governor signed the bill into law.

12. 2004 Ala. Acts 2004-524, § 1 (to be codified at ALA. CODE § 7-1-102); S.B. 326, § 1 (to be codified at DEL. CODE ANN. tit. 6, § 1-102); 2004 Haw. Sess. Laws 162, § 1 (to be codified at HAW. REV. STAT. § 490:1-102); IDAHO CODE § 28-1-102 (Supp. 2004); 2004 Minn. Sess. Law Serv. ch. 162, art. 1, § 2 (to be codified at MINN. STAT. ANN. § 336.1-102).

13. 2004 Ala. Acts 2004-524, § 1 (to be codified at ALA. CODE § 7-1-303); S.B. 326, § 1 (to be codified at DEL. CODE ANN. tit. 6, § 1-303); 2004 Haw. Sess. Laws 162, § 1 (to be codified at HAW. REV. STAT. § 490:1-303); IDAHO CODE § 28-1-303; 2004 Minn. Sess. Law Serv. ch. 162, art. 1, § 18 (to be codified at MINN. STAT. ANN. § 336.1-303).

14. 2004 Ala. Acts 2004-524, § 1 (to be codified at ALA. CODE § 7-1-301); S.B. 326, § 1 (to be codified at DEL. CODE ANN. tit. 6, § 1-301); 2004 Haw. Sess. Laws 162, § 1 (to be codified at HAW. REV. STAT. § 490:1-301); IDAHO CODE § 28-1-301; 2004 Minn. Sess. Law Serv. ch. 162, art. 1, § 16 (to be codified at MINN. STAT. ANN. § 336.1-301).

15. See ALA. CODE § 7-1-105 (2002); DEL. CODE ANN. tit. 6, § 1-105 (1999 & Supp. 2002); HAW. REV. STAT. § 490:1-105 (2003); IDAHO CODE § 28-1-105 (Michie 2001); MINN. STAT. ANN. § 336.1-105 (West 2002).

16. 2004 Ala. Acts 2004-524, § 1 (to be codified at ALA. CODE § 7-1-201(b)(20)); 2004 Haw. Sess. Laws 162, § 1 (to be

codified at HAW. REV. STAT. § 490:1-201(b)); IDAHO CODE § 28-1-201(b)(20).

17. S.B. 326, § 1 (to be codified at DEL. CODE ANN. tit. 6, § 1-201(b)(20)); 2004 Minn. Sess. Law Serv. ch. 162, art. 1, § 10 (to be codified at MINN. STAT. ANN. § 336.1-201(b)(20)).

18. See S.B. 254, available at [http://129.71.164.29/Bill\\_Text\\_HTML/2004\\_SESSIONS/RS/Senate/S\\_BILLS/sb254%20intr.htm](http://129.71.164.29/Bill_Text_HTML/2004_SESSIONS/RS/Senate/S_BILLS/sb254%20intr.htm) (last visited July 16, 2004).

19. See H.B. 91, available at <http://www.mass.gov/legis/bills/house/ht00091.htm> (last visited July 16, 2004).

20. Kathleen Patchel & Boris Auerbach, *The Article 1 Revision Process*, 54 SMU L. REV. 603, 603-04 (2001) (footnotes omitted).

21. See, e.g., *Moore v. Prindle*, 394 P.2d 352, 354 (Nev. 1964) ("In determining which contract is in effect the practical construction and interpretation of the parties as evidenced by their conduct is always persuasive, if not conclusive." (citing *Reno Club v. Young Inv. Co.*, 182 P.2d 1011 (Nev. 1947), and *Flyge v. Flynn*, 166 P.2d 539 (Nev. 1946)); accord *Wiley v. Cook*, 583 P.2d 1076, 1078 n.2 (Nev. 1978). See generally RESTATEMENT (SECOND) OF CONTRACTS § 202(4) (1979); Keith A. Rowley, *Contract Construction and Interpretation: From the "Four Corners" to Parol Evidence (and Everything in Between)*, 69 MISS. L.J. 73, 147-49 (1999).

22. See NEV. REV. STAT. § 104.1105(1) (2003) (requiring that the "transaction bear[] a reasonable relation" to the chosen state); *Sievers v. Diversified Mortgage Investors*, 603 P.2d 270, 273 (Nev. 1979) ("Under choice-of-law principles, parties are permitted within broad limits to choose the law that will determine the validity and effect of their contract. The situs fixed by the agreement, however, must have a substantial relation with the transaction, and the agreement must not be contrary to the public policy of the forum." (citations omitted)). See generally *One for All ... (Part 1 of 2)*, *supra* note 3, at 29 nn.21-22; Richard K. Greenstein, *Is the Proposed UCC Choice of Law Provision Unconstitutional?*, 73 TEMP. L. REV. 1159 (2000).

23. See *One for All ... (Part 1 of 2)*, *supra*

note 3, at 29 n.3.

24. See, e.g., *Pemberton v. Farmers Ins. Exch.*, 858 P.2d 380, 382 (Nev. 1993); *Overhead Door Co. of Reno v. Overhead Door Corp.*, 734 P.2d 1233, 1235 (Nev. 1987).

25. NEV. REV. STAT. § 111.220 (requiring a subscribed writing evidencing any agreement not to be fully performed within one year, any promise to answer for another's debt, any promise or agreement made upon consideration of marriage, any promise or commitment by a person engaged in the business of lending money to lend \$100,000 or more, and any promise or commitment to pay a fee of \$1,000 or more for obtaining a loan of money or extension of credit). N.R.S. § 111.220 bears a close resemblance to portions of *Restatement (Second) of Contracts* § 110(1), *supra* note 21, as does N.R.S. § 111.210, requiring a subscribed writing for the sale or lease of any interest in real property for more than one year, NEV. REV. STAT. § 111.220.

26. Cf. ARIZ. REV. STAT. § 44-101(4) (2003) (barring any action "[u]pon a contract to sell or a sale of ... choses in action of the value of five hundred dollars or more" unless "the promise or agreement upon which the action is brought, or some memorandum thereof, is in writing and signed by the party to be charged, or by some person by him thereunto lawfully authorized").

27. Compare NEV. REV. STAT. § 104.1201(19) ("'Good faith' means honesty in fact in the conduct or transaction concerned.") with *id.* § 104.2103(1)(b) ("'Good faith' in the case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.").

28. See 2004 Ala. Acts 2004-524, § 1 (to be codified at ALA. CODE § 7-1-201(b)(20)); 2004 Haw. Sess. Laws 162, § 1 (to be codified at HAW. REV. STAT. § 490:1-201(b)); IDAHO CODE § 28-1-201(b)(20) (Supp. 2004); VA. CODE § 8.1A-201(b)(20) (Supp. 2003).