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

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The 2003 Legislative Session (and subsequent special sessions) having been dominated by Nevada's impending budgetary crisis, revising Nevada's version of the Uniform Commercial Code was not a priority in Carson City. By the time the 2005 Legislative Session begins, the American Law Institute (ALI) and the National Conference of Commissioners on Uniform State Laws (NCCUSL) will have finalized comprehensive revisions of Articles 1 ("General Provisions"), 2 ("Sales"), 2A ("Leases"), and 7 ("Documents of Title"), as well as, conforming amendments to other articles, for the Nevada Legislature's consideration.

The ALI and NCCUSL completed their work on Revised Article 1 after Nevada's 2001 Legislative Session adjourned. As of June 1, 2004, Alabama, Idaho, Minnesota, Texas, and Virginia have enacted their own versions of Revised Article 1, and Hawaii's version awaits only gubernatorial approval. The ALI and NCCUSL completed their work on Revised Article 7 after Nevada's 2003 Legislative Session adjourned. As of June 1, 2004, Alabama, Connecticut, Idaho, Maryland, Minnesota, and Virginia have enacted their own versions of Revised Article 7, and Hawaii's version awaits only gubernatorial approval. As of June 1, 2004, the official comments accompanying Revised Articles 2 and 2A have yet to be finalized. Therefore, it seems a bit premature at present to write about Revised Articles 2 and 2A. And, while documents of title are, no doubt, scintillating subjects to some, this article and its companion focus on the proposed changes to Article 1, which affect every transaction governed by the Code.

As I will discuss in more detail below, there are four essential differences between Revised Article 1 and the version of Article 1 presently codified at N.R.S. §§ 104.1101-.1208. First, Revised Article 1 narrows its own scope, so that it applies only to transactions governed by some other article of the Code. Second, Revised Article 1 applies the same good faith standard to merchants and non-merchants. Third, Revised Article 1 purports to allow the parties in any transaction in which no party is a consumer to choose to have their transaction governed by the law of any state, without regard to any relationship

(or lack thereof) between that state and either the parties to the transaction or to the transaction itself. Fourth, Revised Article 1 extends the relevance of course of performance evidence to all agreements governed by the Code.

Good Fences Make Good Neighbors: The Scope of Revised Article 1

Unlike current Article 1, which contains no explicit scope provision, U.C.C. § R1-102¹ states that Revised Article 1 only "applies to a transaction to the extent that it is governed by another article of [the Code]."² In other words, if a transaction does not fall within the scope of Article 2, 2A, 3, 4, 4A, 5, 7, 8, or 9, it is not subject to Revised Article 1.

This is a departure from current law, notwithstanding the statement by Revised Article 1's drafters that Section R1-102 merely "makes clear what has always been the case — the rules in Article 1 apply [only] to transactions ... governed by one of the other articles of the Uniform Commercial Code."³ N.R.S. § 104.1206 requires a signed writing evidencing a contract (other than a security agreement) for the sale of personal property (other than goods and investment securities) if a party wishes to enforce that contract "beyond \$5,000 in amount or value of remedy."⁴ In so doing, N.R.S. § 104.1206 implicitly recognizes that Article 1 governs sales of personal property that fall outside the scope of Articles 2, 2A, 3, 4, 4A, 5, 7, 8, and 9. If that were not the case, there would be no need for N.R.S. § 104.1206, and one of the fundamental canons of statutory construction is that one should always construe a statute to have meaning and purpose.⁵ What the text of N.R.S. § 104.1206 makes implicit, the official comment to current Section 1-206 makes explicit, stating that its purpose is to "fill the gap" left by statute of frauds provisions elsewhere in the Code — principally "relat[ing] to the sale of general intangibles,"⁶ such as intellectual property rights,⁷ goodwill and other intangibles included in the sale of a going business concern,⁸ franchise rights,⁹ and "choses in action,"¹⁰ as well as to sales of other forms of intangible personal property not covered by another Code provision.¹¹

If It's Good Enough for Sears Roebuck, It's Good Enough for Me: Good Faith Under Revised Article 1

Both current and Revised Article 1 impose on all parties to any agreement governed by the Code a duty of good faith in their performance and enforcement of the agreement.¹² Other than changing "or" to "and," in order to make clear that the duty of good faith applies to both contractual performance and enforcement, and changing the verbiage used to refer to the rest of the Code, the language of the pre-revised and revised sections imposing a duty of good faith are identical. What is not identical is the way the current version of Article 1 and Revised Article 1 define "good faith." N.R.S. § 104.1201 defines good faith as "honesty in fact in the conduct or transaction concerned."¹³ Thus, the question under current Article 1 is whether the person was subjectively truthful and behaved honestly.¹⁴ In addition to this requirement of subjective honesty, under Revised Article 1 the party must also "observ[e] reasonable commercial standards of fair dealing."¹⁵ Thus, Revised Article 1 applies the same standard of good faith to non-merchants that current Articles 2 and 2A apply only to merchants.¹⁶

Suppose I sign a contract to purchase a home spa from Sears and that I further agree to make monthly payments for a fixed term, to maintain the spa for the duration of the payment period, and to promptly notify Sears of any non-routine maintenance needs that arise for the duration of the express warranty that is part of the sales agreement. Under Revised Article 1, not only must Sears (the merchant seller) observe reasonable commercial standards of fair dealing, so must I (the non-merchant buyer) — even though I may have no reason to know what constitutes "reasonable commercial standards of fair dealing" in the sale and servicing of home spas. If reasonable commercial standards of fair dealing in the performance of a contract for the sale and servicing of a home spa require that I inspect the home spa every few days, and I fail to inspect the spa for a

two week period because I am on vacation, when I return home and find the spa not working as warranted, am I breaching my duty of good faith by insisting that Sears make good on its warranty? Revised Article 1's reasonable-person-with-knowledge-of-the-trade standard suggests I am in breach.¹⁷

Where do You Want to Go Today?: Choice of Law Under Revised Article 1

Both current and Revised Article 1 empower the parties to agree on governing law, subject to certain limitations. Where current and Revised Article 1 part ways is that, while current Article 1 requires the parties to choose the law of a jurisdiction that is reasonably related to the transaction,¹⁸ Revised Article 1 requires no such relationship between the transaction and the chosen jurisdiction,¹⁹ unless one or more parties to the agreement at issue is a consumer.²⁰ In so doing, Revised Article 1 ignores the general tendency of states to allow parties to choose only the law of a jurisdiction bearing some relationship to the parties, to the transaction, or both, and then only if the chosen law does not conflict with some fundamental public policy of a state bearing a greater relationship to the dispute than the chosen state.²¹ As one leading commentator puts it, Section R1-301 is "far broader, cover[s] far more contracts, and (by sheer force of numbers of contracts implicated) [is] less deferential to the ordinarily-governing law of other jurisdictions than any widely-known conflict of laws rule[] anywhere."²²

Returning to my earlier hypothetical, if Sears is headquartered in Illinois, I am a Nevada resident, and I purchase the home spa from a Sears store in Las Vegas, then a provision in the sales agreement subjecting all disputes to Maine law would not be binding because I am a consumer. But, if Sears purchased the spa for resale from The Wizard of Spas, located in Kansas, and had the spa shipped directly to the Nevada store, then a provision in the Sears-Wizard of Spas agreement subjecting all disputes to Maine law would be

binding because neither party is a consumer.

Second Verse Same as the First: Course of Performance Under Revised Article 1

The text of current Article 1 refers to course of performance only as one possible element of an "agreement."²³ Otherwise, course of performance is defined and operationalized in Articles 2 and 2A.²⁴ As a result, there has been some uncertainty what effect course of performance has on transactions governed by Articles 3, 4, 4A, 5, 6, 8, or 9; and, assuming it has some effect beyond Articles 2 and 2A, how course of performance fits into the hierarchy set forth in pre-Revised Section 1-205.²⁵ Revised Article 1 resolves any uncertainty by defining course of performance and fixing its position in the hierarchy of express and implied terms of any agreement governed by the Code.²⁶ ■

Part Two of this article, which will appear in next month's Nevada Lawyer, discusses other states' enactments of Revised Article 1 and suggests one or more courses of action for the Nevada Legislature with respect to each of the changes examined here.

Endnotes

1. For ease of reference, from this point forward, all citations in the text and notes to Revised Article 1 are in the form of "U.C.C. § 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 "U.C.C. § 1-..." or "Section 1-...." The pre-2001 uniform version of Article 1 can be found in its entirety, with official comments, in *Uniform Laws Annotated*. 1 U.L.A. §§ 1-101 to 1-208 (1989 & Supp. 2004). The uniform version of Revised Article 1 can be found in its entirety, with official comments, in the 2004 Supplement to *Uniform Laws Annotated*. 1 U.L.A. §§ R1-101 to R1-310 (Supp. 2004).

2. U.C.C. § R1-102 (2001). And, in case you weren't paying attention, Section R1-301 reiterates that *it* — which, of course, is part of

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Revised Article 1, and therefore covered by § R1-102 - "applies to a transaction to the extent that it is governed by another article of [the UCC]." *Id.* § R1-301(b).

3. *Id.* § R1-102 cmt. 1; see also Kathleen Patchel & Boris Auerbach, *The Article 1 Revision Process*, 54 SMU L. REV. 603, 605 (2001) (recognizing that, while current Article 1's scope "implicitly ... has always been that it only governs transactions within the scope of other articles of the UCC ... the lack of an express scope provision occasionally caused courts and commentators to express uncertainty about which transactions are governed by its substantive rules").

4. NEV. REV. STAT. § 101.1206(1)-(2).

5. See Karl N. Llewellyn, *Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes are to be Construed*, 3 VAND. L. REV. 395, 400 (1950) ("If a statute is to make sense, it must be read in the light of some assumed purpose. A statute merely declaring a rule, with no purpose or objective, is nonsense.").

6. U.C.C. § 1-206 cmt. (1995).

7. See, e.g., *Grappo v. Alitalia Linee Aeree Italiane, S.p.A.*, 56 F.3d 427, 431 (2d Cir. 1995); *Mellencamp v. Riva Music Ltd.*, 698 F. Supp. 1154, 1163 (S.D.N.Y. 1988).

8. See, e.g., *Olympic Junior, Inc. v. David Crystal, Inc.*, 463 F.2d 1141, 1143 (3d Cir. 1972); *Beldengreen v. Ashinsky*, 528 N.Y.S.2d 744, 746-47 (N.Y. Civ. Ct. 1987).

9. See, e.g., *American Buick, Inc. v. General Motors Corp.*, 66 S.W.3d 51, 60-61 (Mo. Ct. App. 2001).

10. See, e.g., *Sel-Lab Mktg., Inc. v. Dial Corp.*, 48 UCC Rep. Serv. 2d 482, 485-86 (S.D.N.Y. 2002) (right of first refusal); see also *In re Furst*, 914 F. Supp. 734, 737 (D. Mass. 1996) (royalty rights).

11. See, e.g., *FDIC v. Herald Square Fabrics Corp.*, 439 N.Y.S.2d 944, 951-52 (N.Y. App. Div. 1981) (sale of chattel paper not given as collateral).

12. See NEV. REV. STAT. § 104.1203; U.C.C. § R1-304.

13. NEV. REV. STAT. § 104.1201(19).

14. See Margaret L. Moses, *The New Definition of Good Faith in Revised Article 1*, 35 U.C.C.L.J. 47, 48-49 (2002).

15. U.C.C. § R1-201(b)(20) ("Good faith' ... means honesty in fact and the observance of reasonable commercial standards of fair

dealing.").

16. Compare NEV. REV. STAT. § 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." (emphasis added)) and *id.* § 104A.2103(3) (incorporating N.R.S. § 104.2103's good faith standard by reference) with *id.* § 104.1201(19) ("Good faith' means honesty in fact in the conduct or transaction concerned."). See generally Moses, *supra* note 14, at 51-52.

17. See generally Moses, *supra* note 14, at 50-51 (reaching a similar conclusion juxtaposing the "honesty in fact" test of former U.C.C. Article 3 with the "honesty in fact and ... observance of reasonable commercial standards of fair dealing" test of current U.C.C. § 3-103(1)(d)). If so, my breach will not give Sears independent grounds to recover from me, but it may well give Sears a defense to excuse it from liability for its breach of warranty. See U.C.C. § R1-304 cmt. 1; see also Moses, *supra* note 14, at 48 n.6.

18. See NEV. REV. STAT. § 104.1105(1) ("Except as otherwise provided 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 of this state or of such other state or nation governs their rights and duties.").

19. See U.C.C. § R1-301(c)(1) (allowing the parties to choose a state's law "whether or not the transaction bears a relation to the State designated").

20. See *id.* § R1-301(e)(1).

21. See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2) (1971) (amended 1989); see, e.g., *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)).

22. William J. Woodward, Jr., *Contractual Choice of Law: Legislative Choice in an Era of Party Autonomy*, 54 SMU L. REV. 697, 740 (2001). Professor Woodward elaborates:

The Article 1 provision states a rule for any case subject to the Uniform Commercial Code, unless displaced by a specified provision elsewhere in the UCC. This means that all sales and leases of goods contracts will be covered, as will contracts in all the other areas covered by the Uniform Commercial Code. Thus the provision will be available for a large percentage of the staggeringly large number of commercial contracts formed in our economy every day. There are no size or value limitations. Parties to every commercial contract from the sale to a carpenter of a screwdriver to the large-scale business liquidation sale will be able to choose unrelated law to cover their transaction.

Id. at 740-41 (footnotes omitted).

23. NEV. REV. STAT. § 104.1201(3). The official comments to a few sections of current Article 1 mention course of performance; but, they generally do so in the context of discussing the meaning of "agreement," see U.C.C. §§ 1-102 cmt. 2 & 1-204 cmt. 2; and, like the definition of "agreement," they refer the reader seeking the meaning of "course of performance" to U.C.C. § 2-208, see U.C.C. §§ 1-102 cmt. 2 & 1-205 cmt. 2.

24. See NEV. REV. STAT. §§ 104.2208 & 104A.2207.

25. See *id.* § 104.1205(4); compare, e.g., *National Livestock Credit Corp. v. Schultz*, 653 P.2d 1243 (Okla. Ct. App. 1982) (affirming the trial court's resort to course of performance evidence in resolving a dispute governed by Article 9) with, e.g., *Universal C.I.T. Credit Corp. v. Middlesboro Motor Sales, Inc.*, 424 S.W.2d 409, 411 (Ky. 1968) ("[U.C.C. § 2-208] deals with sales only. As to secured transactions the code apparently does not contain a rule for varying the contract by performance.").

26. U.C.C. § R1-303(a), (d) & (e). See generally Patchel & Auerbach, *supra* note 3, at 610 ("Although the comments to pre-revision Section 1-205 refer to course of performance, the section itself deals with only course of dealing and usage of trade. The Revision remedies this omission by adding course of performance to course of dealing and usage of trade as relevant in ascertaining the meaning of the parties' agreement and supplementing its express terms." (footnote omitted)).