Chapter 2: Article One: General Provisions

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CHAPTER 2

Article One: General Provisions

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§2.1. General. Article 1 consists of two parts and contains general principles governing the application and interpretation of the rest of the Code. It is difficult without examining each of the substantive provisions of the next eight Articles to say how far these general provisions change the law of Massachusetts. But Article 1 cannot be ignored: it sets the tone for the rest of the Code and affects the operation of every portion of the Code. The provisions of greatest breadth are perhaps those on variation by agreement in Section 1-102 and those on territorial application in Section 1-105. The forty-six definitions in Section 1-201 affect the application of nearly every section. Section 1-107 on discharge without consideration, Section 1-203 on the obligation of good faith, and the changes in certain rules of evidence also seem particularly significant.

§2.2. Variation by agreement. Until 1950 the Code included a provision that the rules of the Code which were not qualified by such words as “unless otherwise agreed” could not be modified by agreement.¹ That provision was criticized by a committee of the American Bar Association, and was replaced in later drafts by a provision permitting contrary agreement except as to (a) definitions and formal requirements, (b) rights of third parties, and (c) obligations “such as” good faith and reasonable care. That provision was enacted in Pennsylvania. Supplement No. 1 revised it to place more emphasis on freedom of contract and to delete the unspecified limitation embodied in the words “such as.” The New York Law Revision Commission disapproved the revised provision, and in 1956 the sponsors’ Editorial Board approved the provision now found in Section 1-102 (3) of the Massachusetts act.

The present provision states affirmatively at the outset that freedom


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of contract is a principle of the Code. No exception is stated for definitions or for the rights of third parties; those exceptions were deleted as unnecessary. The remaining exceptions are (a) "as otherwise provided in this chapter" and (b) "the obligations of good faith, diligence, reasonableness and care prescribed by this chapter." Where the Code prescribes such an obligation, the result seems to be to limit the power which the parties would have under prior law to contract for exemption from liability for negligence. In such cases, however, the same subsection expressly permits agreement on standards of performance if the standards "are not manifestly unreasonable."

§2.3. Use of draftsmen's comments. The Code as enacted in Pennsylvania included Section 1-102(3)(f) and (g), expressly authorizing reference to the Comments of the sponsors in the construction and application of the Code. It was also provided that in the event of conflict between text and comment, text controlled, and that prior drafts of text and comments might not be used. The Massachusetts Code does not contain these provisions; they were deleted in the 1956 revision because the old comments were out of date and new ones had not yet been prepared, and because the changes from the text enacted in Pennsylvania seemed to be legitimate legislative history.

Since the enactment of the Code in Massachusetts, the sponsors have been preparing to publish new comments, revised in accordance with the revisions of the text and with the reasons given by the Editorial Board for those revisions. The old comments not only had official status in Pennsylvania; they were also adopted by a special commission in Massachusetts in 1954. It may be, therefore, that where the Massachusetts text follows the Pennsylvania text, the old comments have a status in Massachusetts as extrinsic aids to interpretation not vastly different from their status in Pennsylvania. The Editorial Board's explanation of the 1956 changes, which was available to the legislature when the Massachusetts Code was enacted, may possibly be entitled to similar treatment. But it seems clear that the revised comments, not published until after the enactment of the Code, have no official status. Nonetheless, they may be very helpful to both lawyers and courts, in much the same way that Williston on Sales is a useful guide to the meaning of the Uniform Sales Act, drafted by Professor Williston. Their status may be compared to that of the various Restatements.

2 See 2 Restatement of Contracts §574; Restatement of Contracts, Mass. Annot. §574.

§2.3. 1 Report of the Special Commission to Investigate and Study the Uniform Commercial Code, House No. 2400, (1954), pp. 16-17, 201.


3 Cf. Fairbanks, Morse & Co. v. Consolidated Fisheries Co., 190 F.2d 817, 822n (3d Cir. 1951); Alaska Pacific Salmon Co. v. Reynolds Metals Co., 163 F.2d 643, 657n (2d Cir. 1947).
§2.4. Territorial application. In its original form Section 1-105, providing for choice of law, aroused almost universal opposition among teachers of conflict of laws.1 The New York Law Revision Commission proposed that the section be deleted altogether and the subject left wholly to the common law.2 The Editorial Board chose instead to rewrite the section. Subject to specific choice-of-law rules set forth in other sections, the revised section expressly authorizes parties to agree that the law of a particular state shall govern whenever the transaction bears a "reasonable relation" to the chosen state. Failing such agreement the Code applies to transactions bearing an "appropriate relation" to the enacting state.

As to choice of law by agreement, the Code seems to be consistent with prior Massachusetts law.3 As for the concept of an "appropriate" relation, the Official Comment invites consideration of practical consequences in the manner of recent decisions under New York law.4 Such an approach finds some support in recent Massachusetts cases, although traditionally many contract issues have been decided by Massachusetts courts under the law of the place of contracting.5

§2.5. Release without consideration. Under Section 1-107, "Any claim or right arising out of an alleged breach can be discharged in whole or in part without consideration by a written waiver or renunciation signed and delivered by the aggrieved party." The italicized words appear in the Massachusetts Code but not in the Pennsylvania Code. In its setting this provision seems to be limited to discharge after breach of an obligation arising under the Code. Similar provisions as to sale contracts and negotiable instruments apply before breach as well.1

§2.6. Good faith. The provision for release without consideration, like all other provisions of the Code, must be read in the light of the pervasive obligation of "good faith" established by Section 1-203 in the "performance or enforcement" of "every contract or duty within" the Code. "Good faith" is defined in Section 1-201 (19) to mean "honesty in fact in the conduct or transaction concerned." In Article 2 on Sales, "good faith" in the case of a merchant "includes the observance of reasonable commercial standards of fair dealing in the

4 See Global Commerce Corp. v. Clark-Babbitt Industries, Inc., 239 F.2d 716, 719 (2d Cir. 1956).
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1 (emphasis supplied). The italicized words, not found in the Pennsylvania text, were added on the recommendation of the New York Law Revision Commission; they bring to mind a recent reference by the New York Court of Appeals to "the good old rule that there is in every contract an implied covenant of fair dealing." 2

The standard of "honesty in fact" is traditionally the subjective standard of "the pure heart and the empty head." The absence of any general obligation to follow the objective standard of the "reasonable man" is emphasized by the history of the Code obligation of good faith. In the Spring 1950 edition the general definition of good faith included "observance by a person of the reasonable commercial standards of any business or trade in which he is engaged." The quoted language was criticized by a committee of the American Bar Association, 3 and was deleted by the sponsors from the general definition. But similar language was inserted at strategic points in the text promulgated by the sponsors and adopted in Pennsylvania. 4 Reference to "reasonable commercial standards" in the definition of a holder in due course of a negotiable instrument was the subject of voluminous discussion in the proceedings of the New York Law Revision Commission, where vigorous objection was made on behalf of the Chase National Bank. 5 The Editorial Board deleted the offending language, and the New York Commission approved.

In the Massachusetts Code there remain two references to "good faith including observance of reasonable commercial standards." 6 In two other sections reference to action "in good faith and in accordance with" such standards suggests that good faith may not include their observance. 7 In the Sales Article "good faith" and "fair dealing" have the connotation quoted above. Elsewhere in the Code "good faith" stands as "honesty in fact." This adoption of the subjective standard leaves open the possibility that unreasonable conduct may provide evidence relevant to the issue of good faith. In view of that possibility, the difference between subjective and objective standards, however important to linguistic artistry, may well have no significant effect on the outcome of litigation. A lower court decision in Pennsylvania, applying the "reasonable commercial standards" provision, tends to confirm such a judgment. 8

§2.6. 1 UCC §2-103 (1) (b).
4 UCC §§2-103(1)(b), 3-302(1)(b), 7-501(4) (1952 ed.).
6 UCC §§7-404, 8-318.
7 Id. §§3-406, 3-419 (b).
§2.7. Notice. Like "good faith" and "value," "notice" is a pervasive concept in the Code, especially in the numerous provisions on the effect of a good faith purchase for value without notice of a claim or defense.\(^1\) Section 1-201 (25) through (27) distinguishes four concepts used throughout the Code. First, one person "notifies" or "gives" a notice to another by taking reasonable steps to inform him. Second, a notice or notification is "received" when it is delivered at a place held out by the recipient as the place for receipt of such communications. Third, a person has "notice" of a fact when he knows it, when he has received a notice of it, or when he has "reason to know" that it exists. Fourth, "know," "discover" or "learn" refers to actual knowledge rather than to reason to know.

The 1956 changes in these definitions were "based on a study of all the provisions of the Code relating to knowledge, notice or notification."\(^2\) One of the changes was the addition of the following sentence: "The time and circumstances under which a notice or notification may cease to be effective are not determined by this Act." At the same time there was deleted a provision that a purchaser was charged with notice that securities had been lost or stolen for six months after receipt of notification to that effect.\(^3\) The result seems to be to leave to judicial decision the effect of "forgotten notice."\(^4\)

An important limitation on notice, knowledge, or a notice or notification received by an organization is contained in Section 1-201 (27). The organization is bound by a standard of due diligence in communication to the individual conducting the transaction to which the notice is relevant. The effect seems similar to that of provisions for "reasonable opportunity to act" on a notice.\(^5\)

§2.8. Value. Section 1-201 (44) provides a new definition of "value," consolidating three separate definitions appearing in the Pennsylvania text.\(^1\) Separate definitions remain, however, for negotiable instruments and bank collections.\(^2\) The rule of Swift v. Tyson,\(^3\) that value is given when a negotiable instrument is taken on account of an antecedent debt, is made applicable generally; where a contrary result is intended, it is provided for separately from the element of value, as in the general definition of "buyer in ordinary course of business" and in the definition for documents of title of "duly negotiate."\(^4\)


\(^{\text{2}}\) 1956 Recommendations of the Editorial Board for the Uniform Commercial Code § 1-201, Reason 25.

\(^{\text{3}}\) UCC §§3-303, 4-208, 4-209.

\(^{\text{4}}\) 16 Pet. 1, 10 L. Ed. 865 (U.S. 1842).

\(^{\text{5}}\) UCC §§1-201(9), 7-501(4).

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The principal difference between the negotiable instrument definition in Article 3 and the general definition in Article 1 relates to the status of an executory promise as value. In Article 3 value is given "to the extent that the agreed consideration has been performed," when a negotiable instrument is given, or when an "irrevocable commitment" is made to a third person. The general definition includes "a binding commitment to extend credit" and "the extension of immediately available credit," even though not drawn upon and even though there is a right of charge-back. In Article 4 on bank collections, credit may be value though not drawn upon, but as to "an item deposited in an account" value is given "to the extent to which credit given for the item has been withdrawn or applied" on a "first-in, first-out" basis. As a result of these provisions, value may sometimes be given for goods or documents but not for an accompanying negotiable instrument. And in some cases it may become important whether an item has been "deposited in an account."

§2.9. Acceleration clauses. Section 1-208 provides that a term for acceleration of payment or performance by one party "when he deems himself insecure" shall be construed to permit acceleration only if he "in good faith believes that the prospect of payment or performance is impaired." The burden of establishing lack of good faith is placed on the other party. These provisions should be read in conjunction with the provision of Article 3 that an acceleration clause does not impair the negotiability of commercial paper.1

Section 1-208 has been attacked as an unjustifiable interference with freedom of contract, and defended as a clarifying restatement of prior law; it has also been suggested that the law in some states is less favorable to the lender in that he bears the burden of proving his own good faith and reasonable conduct.2 It seems very likely that there will be continuing efforts to secure legislation protecting retail installment buyers against acceleration "arbitrarily and without reasonable cause."3 The position of the sponsors of the Code has been that such legislation should be enacted separately from the Code.4

§2.10. Miscellaneous. The foregoing are not the only significant provisions of Article 1. Space does not permit further elaboration, but mention should be made of Section 1-202, making certain third-party documents prima facie evidence of the facts stated in them; Section 1-205, defining the role of course of dealing and usage of trade; Section 1-206, providing a novel Statute of Frauds for the sale of certain types of intangibles; and Section 1-207, authorizing performance and acceptance of performance "without prejudice."

§2.9. 1 UCC §§3-109(1)(c), 3-104(1).
3 See N.Y. Personal Property Law §§302(13), 403(3)(b).
4 See Notes to §§9-102, 9-203 (1952 ed.).