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# Downtown Code: A History of the Uniform Commercial Code 1949-1954, 49 Buff. L. Rev. 359 (2001)

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# Downtown Code: A History of the Uniform Commercial Code 1949-1954

ALLEN R. KAMP†

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## INTRODUCTION

My article studies a critical era in the history of the Uniform Commercial Code: the era in which the proposed Code of 1949, a product of the academic drafters, entered into the political world and changed to meet political realities.<sup>1</sup> Marking the end of this era was the start of the New York State Law Revision Commission's (NYLRC)<sup>2</sup> study of the

1. For a general description of the 1949 Code reception, see J. Francis Ireton, *The Commercial Code*, 22 MISS. L.J. 273 (1951). "At that time several affected industries came out with strong pleas against it and publicized their position all over the country." *Id.* at 279.

2. Zipporah Wiseman points out that the conventional analysis of the Code's history starts at the NYLRC's Report of 1954-56, at which time the Code had already gone through significant compromise. Zipporah Batshaw Wiseman, *The*

U.C.C. in 1954. In these few years, the drafters of the U.C.C. made several fundamental decisions about its nature which today form the basis of the nation's and the world's commercial jurisprudence.<sup>3</sup>

*Uptown Act* and *Downtown Code*, the titles of my two articles in the history of the U.C.C., represent my view that the present Code is a product of two conflicting visions of what commercial law should be—one, a regulatory system based on self-regulation by the trade, judicial supervision according to commercial norms, and legislative dictate, as opposed to one based on an autonomous business world operating under a regime of unregulated contract. The history of the Code's drafting during these years can be seen as the triumph of the latter vision. In the words of Soia Mentschikoff, "special interests" won over the drafters' desire to protect small merchants and consumers.<sup>4</sup>

The drafters in the main placated those commercial interests they had to in assuring the Code's passage. There was some rebellion among the drafters, especially concerning the banking provisions of article 4, and some holding the line, as in keeping the unconscionability section,<sup>5</sup> but generally bankers, manufacturers, retailers, and secured financiers got what they wanted.

A metaphor of two colliding tectonic plates serves to describe the collision of the two visions, and a great deal of the problematic sections of the U.C.C. exist along the fault lines formed by that collision. Commercial issues that were the subject of debate, compromise, victory, and defeat in the years 1949 to 1956 constitute the troublesome Code sections today.<sup>6</sup>

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*Limits of Vision: Karl Llewellyn and The Merchant Rules*, 100 HARV. L. REV. 465, 467 (1987).

3. "Judged by its reception in the enacting legislatures, the Code is the most spectacular success story in the history of American law." JAMES F. WHITE & ROBERT S. SUMMERS, *UNIFORM COMMERCIAL CODE* 5 (3d ed. 1988).

4. The title of Gilmore's *Death of Contract* (1974) is ironic in that he witnessed the triumph of contract over regulation in the Code's drafting. See, e.g., Meeting of the Enlarged Editorial Board 284 (Jan. 27-29, 1951) (on file with American Law Institute (A.L.I.) Archives, University of Pennsylvania Law Library and the Buffalo Law Review) [hereinafter Enlarged Editorial Board] (statement of Soia Mentschikoff).

5. See *infra* p. 415.

6. See the following portions of JAMES J. WHITE & ROBERT S. SUMMERS, *UNIFORM COMMERCIAL CODE* (4th ed. 1995): Chapter 4, "Unconscionability"; Chapter 9, "Warranty"; Chapter 11, "Defenses to Warranty Action"; Chapter 12,

This story, which is a political one, differs from the generally accepted history of the Uniform Commercial Code. The Code's drafting "continues to be represented, as a neutral, balanced, expertise-based process."<sup>7</sup> The reality is that the Code is a political document—the product of political realities of the early 1950s on the state level.

Overall, the 1949 Code contained much more regulatory law, much more control over commercial activity than does the modern U.C.C. The earlier code's consumer protection sections, the pervasive good faith provisions, the mandatory application of trade usages, the presumption that Code sections were mandatory, all worked to control merchants' conduct. These sections empowered judges to regulate the reasonableness of contract and to police commercial behavior.

How we got from the primarily academic draft of 1949 to that of 1954 is a complicated story which has to be pieced together from the American Law Institute (ALI) archives, the Llewellyn Papers, the Code drafts, the records of meetings, and the secondary literature. As Professor N.E.H. Hull points out, academic lawyers engage in private as well as public discourse.<sup>8</sup> The private discourse in the correspondence and the private meetings reveals many more drafting conflicts

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"Disclaimers of Warranty Liability and Modification of Buyer's Remedies"; Chapter 17, "The Effect of Regulations J and CC"; Chapters 18, § 18-2, "The Deposit Contract"; and Chapters 22-25.

7. Edward L. Rubin, *The Code, The Consumer, and the Institutional Structure of the Common Law*, 75 WASH. U. L.Q. 11, 13 (1997).

8.

There are two contemporaneous, parallel levels of discourse in academic jurisprudence. There is a public level of discourse—the exchange of arguments in articles, speeches and books—in which great minds reveal their secrets to the world. This is the source material for the student of "schools" and "movements," enabling—indeed forcing—the scholar of public discourse to group these articulations into preconceived categories. The historian who attempts to reconstruct the reality of what the jurisprudents themselves were doing at the time that they created the public discourse, penetrates to a second deeper level of discourse, a private level. This private discourse consists in correspondence and informal discussion among academic jurisprudents. The student of the private discourse reconstructs the reality of these intellectual exchanges, revealing the authors' intended meaning of words used in the public discourse.

N.E.H. Hull, *Networks & Bricolage*, 35 AM. J. LEGAL HIST. 307, 309 (1991). Professor Hull's views on historiography are also set out in her excellent histories of the ALI, *Restatement and Reform: A New Perspective on the Origins of the American Law Institute* and *Back to the "Future of the Institute" in THE AMERICAN LAW INSTITUTE SEVENTY-FIFTH ANNIVERSARY 1923-1998* 49, 105 (1998).

than does the public discourse. Partly due to a desire to have the Code enacted and partly due to pressure not to air their disagreements in public, the Code drafters presented the face of the bland, value-free expert to the world. The reality is much more interesting.<sup>9</sup>

My topic is a complex one and may interest different types of readers. Some may be interested in the general story of the Code, while others may be in how specific Code articles and sections developed. Some may be interested in the history of the Code as a case study on the fortunes of a proposed progressive statute in the post-war era. I have attempted to write this article to serve these groups.

I start with a description of my heretical view of the Code's development, and then discuss the general conditions surrounding its drafting. The drafting was done with little publicity or public awareness. I also describe the main players, many of whom were crucial to the Code's drafting but are forgotten today.<sup>10</sup> The article will describe the 1949 Code, what it was, and how it differed from earlier proposals; the drafters' hopes for their Code, the unfavorable reaction to it by the organized bar and the affected commercial interests, and the realities of the political world that greeted the Code. After discussing the changes in the certain sections which were the main subjects of controversy, the article will describe briefly the Code's entry into the process of review by

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9. Professor Hull points out that the public discourse comes to dominate and the private is lost.

True, seen from a distance over time, the public discourse comes to dominate the private discourse. Aided by intellectual debtors of the great jurists, public exchanges sever themselves from the private discourse and take on a life of their own—an externally defined jurisprudential dialogue. The public discourse becomes the focus of later interpretation and analysis. The private discourse, so vital to the intellectual process—the human social, intimate, interactive context of intellectual history—is lost. While later jurists and legal scholars are entitled to abstract the public discourse from its original informing, nurturing, private dialogue, the historian is not so free. We historians must rediscover the private discourse and use it to reinterpret the public discourse.

Hull, *supra* note 8, at 309-10.

10. An example is Walter Malcolm, the subject of a bitter controversy involving Grant Gilmore, Soia Mentschikoff, and William Schnader. His participation in drafting article 4 is largely ignored. White and Summers list Fairfax Leary, Jr. as the principal drafter of article 4, but it was Malcolm who rewrote that article after the drafters decided to omit it in 1951. WHITE & SUMMERS, *supra* note 3, at 4; Walter Malcolm, *Article 4-A Battle With Complexity*, 1952 WIS. L. REV. 265, n.\*.

the NYLRC. The ultimate fate of the Code provisions we have been studying will be given before we contemplate what this history could mean.

My history and conception of the Uniform Commercial Code differs from the usual perception of its drafting, purposes, and nature. The U.C.C. is generally presented as "legislation which achieves certain goals, such as uniformity, clarity, and technological modernity, while being politically acceptable to all state legislatures."<sup>11</sup> The U.C.C. is seen as a product of an institutionalized drafting system, in which two august, expert institutions, the American Law Institute (ALI) and the National Conference of Commissioners (NCC) on Uniform State Laws, together produced the U.C.C. in consultation with academics, lawyers, and business. The Code is thus seen as a product of an apolitical consensus rather than one formed by the clash of opposing interests.

The drafters themselves promulgated the impression of a neutral, expertise-driven, detail-oriented process, in which no one group or set of interests was favored over another. Karl Llewellyn always characterized sales law as "non-political."<sup>12</sup> Llewellyn's statement to the NYLRC<sup>13</sup> presented his Code as the product of "ten years of expert study and critique" as well as the institutional critique of the ALI and the NCC, and having "the benefit of consultation and criticism by informed representatives of industry after industry and group upon group occupied in various areas of commerce or of commercial

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11. Rubin, *supra* note 7, at 12.

12.

One characteristic of private law, and especially of sales law when regarded as rules governing professional businessmen, is that there is little clash of interests. "[M]ost of the Sales field is uncolored as most other law is not by the clash of class and passion." In a report accompanying an early draft, the Sales statute is referred to as "both non-political, and non-criminal, in character." Defending the Code before the New York Law Revision Commission, Llewellyn again stressed the "non-political" character of commercial law. By his suggestion that article II rules be limited, in many cases, to transactions between merchants, Llewellyn limits the rules to situations where experience shows that all interests are satisfied by the rule.

Peter Winship, *Jurisprudence and the Uniform Commercial Code: A "Commote"*, 31 SW. L.J. 843, 861 (1977) (alteration in original) (citations omitted) (quoting Karl N. Llewellyn, *Across Sales on Horseback*, 52 HARV. L. REV. 725, 726 (1939)).

13. See Statement to the Law Revision Commission by Professor Karl N. Llewellyn, *reprinted in* 1 State of N.Y. Law Revision Comm'n, Report of the Law Revision Comm'n for 1955 (1955).

finance; and the general critique of bar association committees and of an extraordinary number of independent legal experts."<sup>14</sup>

Llewellyn described the drafting process as one of exhaustive attention to detail, with constant criticism and revision.<sup>15</sup> Llewellyn's wife and co-drafter, Soia Mentschikoff, had also previously described the Code as a product of revision upon revision, with consultation every step of the way. She described the process as one in which the individual drafters would submit their proposals to the drafting staff, who would consult with advisors and lay groups and then resubmit the modifications to the initial drafter. The draft would go through at least three such cycles before being submitted to working groups of the ALI, then the tentative draft would go to the ALI, then to specific ALI sections and then back to the Conference.<sup>16</sup>

Standard histories of the Code also present the drafting of the Code as done by experts working in an institutional setting.<sup>17</sup> The story is told again of the ALI and NCC coming together and sponsoring a drafting process in which practitioners and professors acting with advisors come up with draft after draft. Braucher and Riegert do mention the attack on the Code by Emmet Smith, house counsel to the Chase National Bank, as well as academic criticism,<sup>18</sup> but do

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14. *Id.* at 23.

15. *Id.* at 26.

Article by article there was one draftsman, or a team of two, preparing, presenting, revising. The drafter's work was under steady criticism and revision, typically in three-day sessions every six to ten weeks, by a group of advisors which included experts in the field of law concerned, experts in the field of business or finance concerned, and also lawyers or judges of general experience and *no* expertness whose important business was to see that it all made sense and that each part could be understood by men who were *not* experts. Results of any meeting were worked over, tested out, and brought in again for any misguess to be gone over afresh. There was constant correspondence and consultation with any outside experts in the business or law concerned who could be discovered and who would give the time.

*Id.*

16. See Soia Mentschikoff, *The Uniform Commercial Code, An Experiment in Drafting*, 36 A.B.A.J. 419, 420 (1950); see also WILLIAM TWINING, KARL LLEWELLYN AND THE REALIST MOVEMENT 285-86 (1973).

17. See WHITE & SUMMERS, *supra* note 3, at 2-4; William Schnader, *A Short History of the Preparation and Enactment of the Uniform Commercial Code*, 22 U. MIAMI L. REV. 1 (1967); ROBERT BRAUCHER & ROBERT A. RIEGERT, INTRODUCTION TO COMMERCIAL TRANSACTIONS 19-31 (1977).

18. *Id.* at 27.



not mention our specific political controversies. By the 1980s, in symposiums like "Origins and Evolution: Drafters Reflect Upon the Uniform Commercial Code,"<sup>19</sup> the drafters looked back at the drafting of the Code through a rose-colored haze, congratulating themselves for a job well done.

This public description of a neutral drafting process engaged in by expert commercial law specialists is in stark contrast to Mentschikoff's contemporary description of the proposed Code being changed into "a special-interest type of legislation."<sup>20</sup>

The Code itself does two things which effectively hide its history. It explicitly presents itself as value-free, as in its statement of purposes:

(a) to simplify, clarify and modernize the law governing commercial transactions;

(b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;

(c) to make uniform the law among the various jurisdictions.<sup>21</sup>

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19. Soia Mentschikoff et al., *Origins and Evolution: Drafters Reflect Upon the Uniform Commercial Code*, 43 OHIO ST. L.J. 535 (1982).

20.

In the last two years as amendments have been made to the Code, and changes in policy made, the Code has consistently moved onto a special-interest type of legislation and away from a public-interest type of legislation.

I think that Section by Section as the changes have been made they have not been changes which in and of themselves have been dramatic or have meant anything particular, and that each one of them by itself is a change which cannot only be lived with but considerable argument can be made for it as well as against it.

I think there will have to be a line drawn at which that type of change section by section and provision by provision on the Code has got to cease. I don't know whether this Section is the Section on which we have got to say, "This far we move in terms of special interest, and no further." It is certainly a Section which raises the general problem. . . . I think it is something none of us has considered, because I don't think any of us—with the possible exception of the Reportorial Staff—are fully aware of how many of the changes made in the Code in the last two years were special-interest changes.

Enlarged Editorial Board, *supra* note 4, at 284-85.

21. U.C.C. § 1-102 (1991).

The Code also does not refer to any rejected versions. Deleted sections which were the subject of intense debate and prolonged negotiation simply disappear from view. The early consumer protection sections of article 9, for example, are simply not there, and no mention of their disappearance is made in the comments or anywhere else. The comments do not give any indication of the struggles that produced the sections. For example, objective good faith was applicable throughout the Code until the May 1951 draft.<sup>22</sup> Then, due to ABA criticism, the standard of subjective good faith was adopted in article 1, with articles 2 and 3 retaining objective good faith, until it was dropped in article 3 after the NYLRC process. Soia Mentschikoff felt strongly enough on the issue to submit a memorandum to the NYLRC on the issue.<sup>23</sup> In 1990, the phrase "observance of reasonable commercial standards of fair dealing" was added to the article 3 definition (section 3-103(4)).<sup>24</sup> The present section's comment points out the 1990 change, but makes no reference to the controversy in the 1950s. The issue is an important one, involving questions of autonomy and freedom from regulation versus the desirability of regulating commerce by trade norms, which was Llewellyn's prime goal for the Code.<sup>25</sup> The comment, however, ignores any description of conflicting policies or even that the section makes a choice between

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22. U.C.C. § 1-201(19), Proposed Final Draft No. 2 (Spring 1951), *reprinted in* 12 U.C.C. DRAFTS 35 (Elizabeth Slusser Kelly ed., 1984). In commercial law talk, "objective good faith" is defined in terms of objective standards; "subjective good faith" just requires no bad intent.

23. Memorandum from Soia Mentschikoff on Section 3-302(1)(b) (Aug. 16, 1954) (on file with A.L.I. Archives, University of Pennsylvania Law Library and the Buffalo Law Review).

24. See WHITE & SUMMERS, *supra* note 6, at 517-21.

25. The ABA position was that:

Prima facie it is reasonable to require good faith in the performance of contracts. However, it is of interest that this provisions and certain others in the same vein have produced quite a violent reaction on the part of some businessmen and business lawyers. They say: "Why should the Code draftsmen tell us to be good? Businessmen, or at least most of them, carry on business ethically and did so long before the Code was ever conceived. The Code should not try to prescribe morals."

Walter Malcolm, *The Proposed Uniform Commercial Code*, 6 BUS. LAW., 113, 127 (1950). For Llewellyn's emphasis on trade norms see Allen R. Kamp, *Between the Wars Social Thought: Karl Llewellyn, Legal Realism, and the Uniform Commercial Code in Context*, 59 ALB. L. REV. 327 (1995), and *Uptown Act: A History of the Uniform Commercial Code: 1940-1949*, 51 S.M.U. L. REV. 275 (1998).

them.

The student of the Code would then think he or she is faced with a statute of non-controversial, technical provisions, put together by commercial law experts who arrived at a consensus as to what a technical framework for commerce should be through a meticulous and painstaking drafting process.

What are the problems with the standard history of the bureaucratically produced Code? One is that the temporary compromises made to get the Code enacted have become permanent principles of American commercial legislation. These principles include the exclusion from the Code of affirmative consumer protection and the allowance of variation of the Code sections by agreement.<sup>26</sup> An example of the confusion of compromise with tradition is Professor Fred H. Miller's discussion of the "exclusion, consistent with the traditional U.C.C. approach, of affirmative consumer protection provisions from revised articles 3 and 4."<sup>27</sup> He states, "A review of state law also will demonstrate that consumer law in relation to articles 3 and 4 has grown outside of the U.C.C. and as an appendage to it in the area of commercial paper since consumer law represents the later development in this context."<sup>28</sup> He points out that consumer protection sections were "thought to be inappropriate" in part because "the U.C.C. is not a regulatory statute for the most part. Consumer provisions are regulatory in nature, cannot be made a subject to variation by agreement, and require sanctions for violation to insure compliance."<sup>29</sup>

But the original intent of the drafters was that the Code: was to include affirmative consumer protection, was to be mandatory instead of being subject to agreement, and was to have a strong regulatory component. Consumer protection does not represent a later development, but a taking up by individual states and Congress of the Code's consumer protection provisions after they were dropped.

They were dropped because of a lack of political support or even interest. At the time, there was no organized support for consumer protection legislation. As noted by Grant Gilmore, the proposed Code drew little public interest: "It is a

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26. See Fred H. Miller, *U.C.C. Articles 3, 4 and 4A: A Study in Process and Scope*, 42 ALA. L. REV. 405, 410-16 (1991).

27. *Id.* at 412.

28. *Id.* at 413.

29. *Id.*

technical statute for specialists. Unfortunately all the specialists are on the same team and there is no opposition."<sup>30</sup> The organized bar and the affected industries just did not accept any change towards greater regulation and the proponents of such change (with the exception of Llewellyn) judged their prospects of getting such legislation passed as hopeless.<sup>31</sup>

At the meeting of the Enlarged Editorial Board of February, 1951, the participants debated the political support or lack thereof for the proposed consumer protection sections of article 9. These sections provided for disclosures of insurance and interest charges similar to those mandated by Truth-in-Lending in 1964. Mentschikoff argued for such disclosures.<sup>32</sup> Although she saw getting such legislation enacted as "extremely tough sledding,"<sup>33</sup> she thought that groups, especially labor and women's, could be aroused to deliver effective political support.<sup>34</sup>

Ireton observed that he had tried to get consumer protection legislation passed and had received no support

30. Grant Gilmore, *The Secured Transactions Article of the Commercial Code*, 16 L. AND CONTEMP. PROBS. 27, 48 (1951).

31. For a general discussion of the political realities in the Truman years, see PHYLLIS DE LUNA, *PUBLIC VERSUS PRIVATE POWER DURING THE TRUMAN ADMINISTRATION* (1997), and ALONZO L. HAMBY, *HARRY S. TRUMAN IN LEADERSHIP AND THE MODERN PRESIDENCY* 68 (1988).

32.

For this reason, practically speaking, the disclosure provisions separating the two charges have not had much effect as yet. We feel that this is a question of education. And on this I perhaps feel more deeply than Mr. Llewellyn; it is a question of education of women's groups as to what it means when you buy a refrigerator or washing machine or a stove. I am speaking now not only of the automobile field, which of course is the primary interest or one of the primary interests of the secured-lender situation here.

I think that if people realized generally that there was availability of shopping for rates of interest, that that would materially reduce the rates which are now being charged.

Enlarged Editorial Board, *supra* note 4, at 281-82.

33. *Id.* at 284.

34.

We think part of the answer to that again lies in the education of the groups that have not been consulted about the Code, know nothing about the Code (and here I speak of labor union groups and women's groups in particular), and that political power of such groups, if it is subject to arousalment at all, is really in our opinion considerable [sic] more effective than the political power of the groups which have been effectively organized up to this point.

*Id.*

from labor unions.<sup>35</sup> He predicted that the local time sellers (dealers who sold on credit) would provide pervasive opposition while the public would be apathetic:

"Your opposition is going to come from your local time seller who lives at every cross-roads throughout any state you go into, who wields a powerful influence. Your public support would be somewhat apathetic, I think. I don't think you could arouse much support over this thing."<sup>36</sup>

Schnader noted that they could not wait for the labor unions and the women's groups to get involved.<sup>37</sup>

At the conclusion of this discussion, Mentschikoff and Gilmore attempted to make a deal, dropping consumer protection for Ireton's support of the Code:

MISS MENTSCHIKOFF: I don't want to put you on the spot, but I want to ask you one question, Jerry, to illustrate my point. You have been working with this group for a year or two years. Suppose this provision goes out. Will your group support the Code? Are you in position to tell us?

MR. IRETON: Well, Karl asked me that question last fall, and frankly I can't commit anybody to anything.

MISS MENTSCHIKOFF: What is your judgment on it?

MR. IRETON: I think I could get them to support it.

PROFESSOR GILMORE: With this Section out?

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35. "I went to a labor union to enlist their aid, and got nowhere. They just weren't interested." *Id.* at 293. For a biographical description of Francis Ireton, William Schnader, Homer Kripke, and Grant Gilmore see *infra* notes 56-102 and accompanying text.

36. *Id.* at 296.

37.

I might say in response to what Ben said, that if we wait until all the women and the labor unions, and groups like that, go to the legislature and say they want the Commercial Code passed, we might as well adjourn now because we will never get the Code passed in any state, in my opinion.

*Id.* at 293.

MR. IRETON: Yes.<sup>38</sup>

The drafters' exclusion of consumer protection thus was a response to the particular political situation they faced.

Another problem with the standard history is that it leaves out the human drama. The conflicts between "town" and "gown," among William Schnader and Homer Kripke and Grant Gilmore and Soia Mentschikoff, have disappeared. The arduous task of drafting, negotiating, and disseminating the Code is ignored. The petty squabbles and the deep divisions over values have disappeared from the official record. And it is that disappearance of the debate over values which is the problem. The Code is not just a product of expertise—it represents significant choices about significant values. Like all legislation, it helps some people and interests and hurts others. The denial that there are value choices prevents us from thinking about them and re-deciding them again.

## I. BEFORE THE STRUGGLE

As in reviewing the order of battle before a conflict, we need to review the plans for enactment, the personnel of the drafting teams, the limitations of the ALI/NCC drafting process, and the specific and general aspects of the responses to the proposed Code.

### A. *The Two Visions*

The academic reformers, the world of "Uptown," wanted a "business commonwealth," a regulated system of commerce, in which a modern, efficient commercial law based on good business practices and judicial oversight would replace antiquated formal laws and unregulated private agreement. The commercial world, "Downtown," did want the efficiency of a modern statute, but did not want regulation. It wanted autonomy and freedom from oversight by trade groups, statutes, and judges.

1. *The Academic Reformers.* The vision of the reforming drafters was a peculiar combination of a modernistic realism, which imposed order and control with the goal of realizing a regime of efficient high speed production,

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38. *Id.* at 294.

financing, and distribution, and of a humanistic desire for a kinder and gentler commercial world, based on cooperation, reasonableness, and decency.<sup>39</sup>

The Code was to be a practical statute that would make for an efficient commerce by removing impediments to mass production and mass distribution. By 1949, the flexible contract rules of today's Code were largely in place. Article 2 had rejected title and formalistic rules of offer and acceptance.<sup>40</sup> The banking and secured transactions article would also evolve to provide for efficient, flexible frameworks for transactions, unburdened by older, restrictive doctrines.

Still to be decided, however, was just how secured financing interests and banking were to be regulated, and how much consumer and small business protection, judicial oversight, and imposition of trade norms were to be included in the Code. The initial Code proposals would have provided for a nicer commercial world than the enacted version. To be sure, there is a connection between the "efficiency" concerns and the "cooperation" concerns—both were seen by the drafters as necessary for prosperity.<sup>41</sup> But the second set of concerns were a much harder sell politically.

The reformers' vision was manifested in the early Code's

39. Professor James Whitman writes that, although Llewellyn drew on German Romanticism, it was based on American social vision:

To be sure, Llewellyn's 1940-41 conception of the "friendly[,] . . . neighborly" *Volk* was not a German one. The Llewellyn of 1941 was guided as much by the social vision of Frank Capra as by the legal-historical vision of Levin Goldschmidt; behind Llewellyn's theorizing lay a Depression-era longing for small-town cooperation and social normalcy, in which the power of the community would stand by the "little man" in his conflict with the "big man."

James Whitman, *Commercial Law and the American Volk: A Note on Llewellyn's German Sources for the Uniform Commercial Code*, 97 YALE L.J. 156, 173 (1987).

40. As stated by the introductory comment to article 2:

The arrangement of the present Article is in terms of contract for sale and the various steps of its performance. The legal consequences are stated as following directly from the contact and action taken under it without resorting to the idea of when property or title passed or was to pass as being the determining factor. The purpose is to avoid making practical issues between practical men turn upon the location of an intangible something, the passing of which no man can prove by evidence and to substitute for such abstractions proof of words and actions of a tangible character.

U.C.C. § 2-101 Comment (1995).

41. See Kamp, *supra* note 25.

provisions and commentary. For example, the first two sentences of Llewellyn's General Comment emphasize the basic principles of good faith, reasonableness, and commercial standards.<sup>42</sup> Commercial contracts were not to be adversary but cooperative.<sup>43</sup> The secured transactions article required the inventory lienholder to liquidate the collateral for the benefit of all the creditors.<sup>44</sup> The provisions for a direct action against the manufacturer for breach of warranty were to relieve "from actual suit those smaller dealers who might otherwise be put out of business by an injury which they have no adequate means of preventing."<sup>45</sup>

The direct action and the warranty provisions sought to protect the consumer; similarly, the secured transactions article sought to provide for notice before repossession, for non-waiver of consumer defenses, and for disclosures of interest rates and fees for credit buyers. In 1949, Code provisions would apply unless it was specifically stated that they would be subject to agreement. The unconscionability section and others gave the judge the tools to police contracts for reasonableness. The entire Code imposed objective good

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42.

Underlying every sales contract are the basic principles of good faith, the elimination of surprise and technical traps, and the interpretation of all phases of the formation and performance of the contract in the light of reasonable behavior under the existing circumstances. When the parties to a sales contract are commercial men, the reasonable meaning of either language or actions is the commercial meaning in the commercial circumstances, and commercial good faith calls for observance of commercial standards by men of commerce.

General Comment on Parts II and III Formation and Construction 1, Llewellyn Papers, A.A.J.2. (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review). Citations to the "Llewellyn Papers" are to the Llewellyn Archives at the University of Chicago Law Library and are indexed in University of Chicago Law Library, *The Karl Llewellyn Papers: A Guide to the Collection*, in UNIVERSITY OF CHICAGO BIBLIOGRAPHIES AND GUIDES TO RESEARCH 46-67 (1970). This General Comment is discussed *infra* at n.222 and accompanying text.

43. "This Act adopts the principles of those cases which see a commercial contract not as an 'arm's length' adversary venture, but as a venture of material interest, when successful, and as involving due regard for commercial decencies when an expected favorable outcome fails." U.C.C. § 1-203, cmt. 10, Proposed Final Draft (1950), reprinted in 10 U.C.C. DRAFTS 68 (E. Kelly ed., 1984).

44. U.C.C. Article VII, Tentative Draft No. 2 (1948), reprinted in 5 U.C.C. DRAFTS 435 (E. Kelly ed., 1984).

45. U.C.C. § 2-79, cmt., May 1949 Draft (1949), reprinted in 7 U.C.C. DRAFTS 266-67 (E. Kelly ed., 1984).



faith, which meant that all commerce had to be conducted according to commercial norms. Thus, drafters' proposals required merchants to be under the control of trade norms, judicial supervision, and legislative dictate.

2. *The Representatives of Business.* Business rejected the reformist program of the drafters. Business wanted to be autonomous—it did not want its freedom of action regulated by judge, statute, or trade. It did not want to be forced into a reasonable, cooperative mode. It did not want new theories of liability.

Bernard Broeker, who represented Bethlehem Steel, expressed the hard-bargaining mood of business: "I see no reason why I should not be allowed to make an unreasonable contract . . . . Quite often I know each party to a contract thinks there are some unreasonable provisions in it, but it is the best deal he can make."<sup>46</sup> As to the good faith requirement, the American Bar Association's response was "Why should the Code draftsman tell us to be good?"<sup>47</sup> Business did not want any increase in potential liability, created either by an objective good faith requirement or by new warranty actions.

Business expressed its desires positively by positing the goal of freedom of contract. Any proposed regulatory legislation was judged by whether or not it restrict business's freedom to operate.

There is a contradiction in the assumptions of the business representatives. They utterly rejected reform legislation that would reallocate power in society, but they did want legislation that would empower business. They wanted, for example, the unified article 9 security interests that allows a financier to have priority on almost all the debtor's assets but did *not* want *any* provisions for consumer disclosures or limitations of obtaining or realizing on a security interest. They did not see the creation of the article 9 security interest as a reallocation of power to the financier, but they did see consumer and small business protection as

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46. Enlarged Editorial Board, *supra* note 4, at 172 (statement of Bernard Broeker).

47. *Report of Committee on the Proposed Commercial Code/Developments since September 1949 Report* (1950), Llewellyn Papers J.XII.1.g (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review), reprinted in 6 BUS. LAW. 119 (1951) [hereinafter *September 1949 Report Developments*].

unwise paternalism. The representatives of business, then, were willing to accept and support the vision of a modern commercial code, but fought against any regulatory proposals.

The history of the U.C.C. and its present content was created by the struggle between these competing visions.

## B. *The Plans For Enactment*

1. *The Proposed Federal Code.* Of course, the U.C.C. is uniform *state* legislation, and the most widely adopted uniform state law. It has been adopted by every state except Louisiana, as well as the District of Columbia and the Virgin Islands,<sup>48</sup> but never as federal law. It is ironic that it was first proposed as a federal statute and that its adoption on the state level rather than on the federal level was seen by some of its proponents as a second-best solution.

The entire U.C.C. project grew out of a proposed Federal Sales Act, which was introduced in Congress in the late 1930s. Llewellyn contacted the federal act's proponents and involved himself in the project. He "saw a Federal Sales Act as a means of promoting general reform of the law of sales. If Congress acted, it would be difficult for the states not to fall into line."<sup>49</sup> Considering the arduous process of seeking the Code's adoption at the state level, Llewellyn's statement in 1942 predicting quick Congressional enactment seems painfully naive.<sup>50</sup>

The drafts of the Code contained provisions dealing with the Code as a federal statute until the Spring 1951 draft.<sup>51</sup> In

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48. WHITE & SUMMERS, *supra* note 3, at 1.

49. TWINING, *supra* note 16, at 278; *see also* Federal Sales Bill (1937), reprinted in 1 U.C.C. DRAFTS 1 (E. Kelly ed., 1984).

50. Llewellyn wrote in 1942:

The Conference foresaw that a Congressional Act would come close to forcing adoption of a parallel act by the States—and very speedily. It foresaw also that the main work of uniformity, to wit, the ironing out of cross-state transactions, would be done at a single stroke by a Congressional Act.

Letter from Karl Llewellyn to William Draper Lewis (Feb. 27, 1942) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review). Later in the letter, he proposed for the commercial code as a whole, stating, "On the matter of adoption, the procedure should follow that proposed for the Revised Sales Act. The way to get rid of the troubles of the Erie R.R. v. Tompkins, and to offer to international commercial transactions a single, clear and modernized law, is by Congressional action." *Id.*

51. The provisions do not appear in Uniform Commercial Code, Proposed Final

1951, Robert Braucher, a Code drafter, states in his *Federal Enactment of the Uniform Commercial Code* that "[a] state should not enact the Code unless there is a reasonable assurance that it will shortly be enacted by Congress."<sup>52</sup> Braucher felt that only federal enactment could insure uniformity.<sup>53</sup>

Also, Schnader mentioned that the ALI/NCC had made a commitment to the New York Merchants Association (which had sponsored the Federal Sales Act) to seek Congressional enactment.<sup>54</sup> I have found no record of the proponents giving up making the Code federal law, but the federal provisions were dropped in the Spring 1951 draft. It is probable that the proponents never explicitly gave up on federal enactment but that their hopes for it just faded away.

The fact that the U.C.C. is a state, rather than a federal, statute has several important repercussions. It means that the Uniform Commercial Code is not uniform; it varies significantly from state to state.<sup>55</sup> It also means that the Code is subject to federal preemption. The Federal Reserve's Regulation CC on check collection, for example, has invalidated huge portions of article 4.<sup>56</sup> Federal preemption

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Draft, No. 2, Text Edition (Spring 1951), reprinted in 12 U.C.C. DRAFTS 1 (E. Kelly ed., 1984). Compare the provision for the "Federal Version" in U.C.C. § 1-105, Proposed Final Draft (Spring 1950), reprinted in 10 U.C.C. DRAFTS 51 (E. Kelly ed., 1984).

52. Robert Braucher, *Federal Enactment of the Uniform Commercial Code*, 16 LAW & CONTEMP. PROBS. 100, 113 (1951).

53. *Id.* at 104.

54.

Chairman Schnader: I differ with Mr. Llewellyn. I think we are under an obligation to fix up Article 2 so that it can be introduced in Congress, because that was the original understanding between us and the Merchants Association of New York when they delayed their pushing of the Federal Sales Act.

Enlarged Editorial Board, *supra* note 4, at 207. My version of the history of the proposed federal enactment differs from Professor E. Hunter Taylor, Jr., who writes that Schnader reacted strongly against Congressional action and that Llewellyn had induced the backers of the federal bill to hold off until the NCC took action. In any case, Schnader's statement in 1951 shows that he was not against any Congressional enactment but rather wanted the NCC to take part in charting any Congressional legislation. See E. Hunter Taylor, Jr., *Uniformity of Commercial Law and State-by-State Enactment: A Confluence of Contradictions*, 30 HASTINGS L.J. 337, 340-41 (1978).

55. See WHITE & SUMMERS, *supra* note 3, introduction § 3, at 7.

56. See Regulation CC Availability of Funds and Collection of Checks, 12 C.F.R. pt. 229 (2000); Edward L. Rubin, *Thinking Like a Lawyer, Acting Like a Lobbyist: Some Notes on the Process of Revising UCC Articles 3 and 4*, 26 LOY. L.A.

has complicated commercial law, with the interaction between federal law and the U.C.C. creating complex, difficult, and often insolvable legal problems.<sup>57</sup>

For our purpose, the most important repercussion was the forcing of the proponents into the state political arena. No quick Congressional legislation was to occur, rather the Code was to be subject to the slow lobbying process in several state capitals. As stated above, the proponents ran into various roadblocks and were shunted into the New York Law Revision Commission process. Federal adoption of the Revised Sales Act, the 1949 Code, or the 1951 Code would have resulted in a very different commercial law than the one we now have.

2. *The Hopes for Adoption.* The proponents of the Code hoped for adoption by the early 1950s. J. Francis Ireton reports that "the sponsors of the Code had originally intended to approve it finally in September 1949 . . . ."<sup>58</sup> The sponsors originally planned to concentrate "on some of the principal commercial states, especially California, Illinois, New Jersey, New York, Ohio, and Pennsylvania."<sup>59</sup> Although William Schnader was successful in getting the Code adopted in Pennsylvania, the Code elicited too much opposition and hit too many roadblocks for quick adoption.<sup>60</sup> The banking opposition led by Emmet Smith of the Chase National Bank was successful in having the Code referred to the New York Law Revision Commission in late 1952. Then all the states (except Pennsylvania) were willing to wait until the Commission had done its work.<sup>61</sup>

We may infer from the provisions of the 1949 Code that the drafters still wanted a commercial law that regulated commercial behavior through the imposition of trade usages, trade norms, and the Code provisions that were assumed to be mandatory. The Code provisions provided for consumer and small merchant protection, regulated secured lending,

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L. REV. 743, 774-76 (1993).

57. See Allen Kamp, *Increasing Complexity in Commercial Law: The Failure of the Uniform Commercial Code*, 10 CORP. COUNS. REV. 60, 67-73 (1991).

58. Ireton, *supra* note 1, at 279.

59. TWINING, *supra* note 16, at 293.

60. See Ireton, *supra* note 1, at 279 ("At that time [1949] several affected industries came out with strong pleas against it and publicized their position all over the country.").

61. TWINING, *supra* note 16, at 293.

and allowed meaningful consumer law suits by warranty beneficiaries against manufacturers. Provisions such as section 2-302, unconscionability, allowed judicial policing of contracts on the ground of reasonableness.

In 1951, Grant Gilmore felt that the Code proponents were offering the business world a reasonable deal: a statute that would allow efficient secured lending in return for some regulation and consumer protection.

Financing institutions have much more to gain by the enactment of Article 9 than they can possibly lose. Their gain will be in large part the debtor's gain as well. No one should expect something for nothing, and the lenders are being asked to pay a price. The price is stated in the imposition of duties of care on the part of the lender which cannot be contracted out of; in the incorporation of provisions designed to protect the borrower and his other creditors from the undesirable effects of permitting one lender to achieve a monopoly position by tying up all of a debtor's assets; in the requirement of public filing for all non-possessory security interests; and in casting on the lender certain business risks, which arise from the chosen debtor's fraudulent activity. Some of the new provisions are introduced as effective substitutes for outworn protective devices. Others make explicit doctrines which have been implicit in the law, and thus in a position to be conveniently overlooked. The price asked is not unreasonable; the bargain offered allows for a fair profit on the transaction.<sup>62</sup>

As stated by Gilmore, "Article 9 with a liberal hand removes most of the restrictions and limitations on lender's operations which have grown up over a century at common law and under statute."<sup>63</sup> These liberal provisions include the floating lien, the repeal of *Benedict v. Ratner*<sup>64</sup> which required the secured party's monitoring of the debtor's accounts, the assignment of future accounts, the rejection of outmoded formalities, and the abandonment of restrictions on the lender's actions after default.<sup>65</sup>

It was in return for this freeing of the secured party that the financing industry was supposed to accept some consumer protection and disclosures and other regulation which limited the power of financiers. One could generalize from Gilmore's statement to the entire U.C.C.—the proposed

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62. Gilmore, *supra* note 30, at 47 (citations omitted).

63. *Id.* at 34.

64. 268 U.S. 353 (1925).

65. Gilmore, *supra* note 30, at 34-35.

Code would free commerce from outmoded formalism, but in return trade usage, the Code, and judges would police commercial activities. Gilmore felt that the deal offered the financiers was a fair one. "The price asked is not unreasonable; the bargain offered allows for a fair profit on the transaction."<sup>66</sup> Gilmore, however, had an uneasy feeling that the affected groups might not be so reasonable: "In dealing with the special interest groups over the past few years I have, however, at times found it difficult to escape the impression that what was being demanded was a free statutory subsidy . . . ."<sup>67</sup>

Even if, however, the academics were not to be able to get what they wanted, the stage was set for a compromise. The academics were willing to compromise to get *some* of their proposals enacted. An analysis of Llewellyn's letters to Emma Cortsuet (his second wife) about a drafting session in 1941 concludes, "The letters show that Llewellyn's concern for the Code was so great that he was able to put his own ideas aside for the sake of compromise."<sup>68</sup> In my prior article, I argue that Llewellyn's commitment to "realism," his disdain for the impractical intellectual whose "physique mentally turn[s] soft and gooey like a spotted apple,"<sup>69</sup> made him especially want to compromise to achieve something real.<sup>70</sup> Schnader's attitude is expressed in one of his statements: "we are not just working on this Code for mental exercise; we want to see something enacted."<sup>71</sup> The drafter's desire to achieve something was a powerful spur to compromise.

Business also expected to make some compromises and get the Code enacted. In 1951, Ireton stated that the American Bar Association would ultimately approve the Code and that it would be adopted. "Ultimately we are going to approve this Code. Now let us make it as good a code as we

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66. *Id.* at 47.

67. *Id.*

68. Dom Calabrese et al., *Karl Llewellyn's Letters to Emma Cortsuet Llewellyn from the Fall 1941 Meeting of the National Conference of Commissioners on Uniform State Law*, 27 CONN. L. REV. 523, 531 (1994).

69. Karl N. Llewellyn, *Our Present Intellectualism*, Llewellyn Papers, B.V.3.h. (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

70. Kamp, *supra* note 25, at 337-38.

71. Consideration of Proposed Final Draft of the UNIFORM COMMERCIAL CODE 97 (May 18, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) [hereinafter A.L.I./N.C.C. Consideration].

can.”<sup>72</sup> Thus the negotiation process was constrained by two parameters: the drafters needed the approval of the organized bar and the affected industries, and the organized bar and the affected industries (except the bankers) realized that there would be a Code. The two groups had to reach a compromise and thus outside interests were in the main trying to suggest changes that would benefit themselves rather than trying to kill the Code. The strategy of the commercial interests was to work with the ALI/NCC, not to defeat it. Even the Chase National Bank was able only to postpone the Code’s adoption.<sup>73</sup>

### C. *The Players*

1. *The Change in Personnel.* Those working on the Code changed in the late 1940s and early 1950s. We have to have some understanding of the personalities of those who had prepared the initial drafts in order to understand what happened to the UCC during our period. First, two important drafters died in the late forties. Hiram Thomas, the lawyer for the New York Merchants Association, represented the practitioners’ viewpoint in the early Code sections. He wanted the Code to preserve “fundamental contract rules” and was against some of Llewellyn’s more radical ideas, such as the extensive merchant rules and the merchant tribunals.<sup>74</sup> Thomas had chaired the committee which introduced the Federal Sales Act in Congress in 1937, thereby starting the entire U.C.C. drafting process.<sup>75</sup> It is to Thomas, not Llewellyn, that we owe the introduction of the equitable concept of unconscionability into sales law. Thomas suggested, in an off-hand way, the use of

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72. ABA Meeting 24 (Jan. 13, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

73. Ireton stated, “Please come in with suggestions. Ultimately we are going to approve this Code. Now let us make it as good a code as we can. We don’t want to be in a position of criticizing code without having an affirmative position.” *Id.*

74. See TWINING, *supra* note 16, at 284-85. For Thomas’ insistence on contract rules, see Joint Advisory Committee Meeting, May 21 and 22, 1945, at 1, Llewellyn Papers, J.VII.2.a. (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review), and Letter from Hiram Thomas to Herbert Goodrich (Apr. 29, 1948) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review). For Thomas’ role in the rejection of Llewellyn’s merchant rules and juries, see Wiseman, *supra* note 2.

75. Federal Sales Bill (1937), *reprinted in* 1 U.C.C. DRAFTS 1 (E. Kelly ed., 1984); see also TWINING, *supra*, note 16, at 277.

"unconscionable," rather than Llewellyn's term, "unreasonable," in invalidating disclaimers of remedies. "I would suggest 'or oppressively,' some word like that. If you are going to have some standard, let it not be pure reason. You might use 'unconscionable' or something the court can look at and say, this is so arbitrary and oppressive and unconscionable that we won't stand for it."<sup>76</sup> By 1948, however, Thomas was ill and working at home. He soon ceased his involvement in the Code's drafting.<sup>77</sup>

William Draper Lewis, the founder and Director of the ALI, was a patrician figure who created the *Restatements*. He died in 1949.<sup>78</sup> In his place, William Schnader, a former attorney general of Pennsylvania, became the political manager of the Code.<sup>79</sup> It was due to Schnader's efforts that Pennsylvania became the first state (and the only one until 1957) to adopt the Code in 1953.<sup>80</sup> His authoritarian nature was revealed by his sobriquet, "General Schnader."<sup>81</sup> He took Alison Dunham to task for asking for an honorarium and attempted to prevent Grant Gilmore and Soia Mentschikoff from criticizing Walter Malcolm's article 4 as being too probank.<sup>82</sup> He had a low regard for Dunham's and Gilmore's abilities<sup>83</sup> and analogized Gilmore and Mentschikoff's position as drafters to lawyers hired to do a job. He saw the august law professors who drafted the Code as hired help.<sup>84</sup>

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76. NCC, 52nd Annual Conference, Detroit, Michigan 33-34, indexed at J.IV.2.f (August 18-22, 1942) (on file with the Llewellyn Archives, University of Chicago Law Library and the Buffalo Law Review).

77. Letter from Hiram Thomas to Herbert Goodrich (April 29, 1948) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

78. 2 WHO WAS WHO IN AMERICA 1943-1950 322 (1950).

79. "On behalf of the Commissioners he largely directed the campaign for adoption of the UCC by the states." Peter Coogan, *Reflections of a Drafter*, 43 OHIO ST. L.J. 545, 546 n.3 (1982).

80. Braucher, *supra* note 17, at 25.

81. Homer Kripke, *Reflections of a Drafter*, 43 OHIO ST. L.J. 577, 582 (1982).

82. See *infra* note 145 and accompanying text.

83. See *infra* note 144 and accompanying text.

84.

So far as concerns the propriety of a member of the drafting staff attacking any part of the Code, it just seems to me that you and I have different standards of professional ethics. It is not a case of academic freedom about which the teaching staffs of our educational institutions sometimes get themselves excited.

Rather, it is a situation similar to one in which a lawyer employed to do a reorganization job for a corporation, accepted compensation for his work, and then stepped out and attacked the plan with a view to



Llewellyn, although he lived until 1962, withdrew somewhat from the drafting process. The reasons may have included his declining health, due in part to his alcoholism, his disinterest in the minutia of drafting, and his renewed interest in jurisprudence. According to a recent article, Llewellyn experienced a profound crisis in 1945-46. He was suffering from alcoholism, depression, and the trauma of separating from his second wife.<sup>85</sup> Of course, Llewellyn's ideas and participation informed the U.C.C. from beginning to end, as well as profoundly influencing tort law and contract law. He is the most significant figure in twentieth century private law.<sup>86</sup> His role was partially taken by his third wife, Soia Mentschikoff.<sup>87</sup> The Karl Llewellyn Papers reveal that she took charge of such details as arranging transportation and hotel rooms for the drafting conferences, as well as leading the political negotiations, such as those with Frank Dierson over the warranty and direct action provisions.<sup>88</sup>

Two other drafters, William Prosser and Fairfax Leary, ceased having any great involvement with the U.C.C. Prosser, who had no experience in negotiable instruments,

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getting the stockholders to defeat it.

Goodness knows, nobody on the drafting staff was silenced at any time as far as the Editorial Board or the membership of either Conference or Institute was concerned; but after a joint meeting has spoken and placed its approval on the product, it seems to me that it would be the worst of bad taste, to say the least, for any of the paid staff to start a campaign to defeat all or any part of the Code.

Letter from William A. Schnader to Soia Mentschikoff (Nov. 8, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

85. James Connolly, Peggy Pschirrer, & Robert Whitman, *Alcoholism and Angst in the Life and Work of Karl Llewellyn*, 24 OHIO N.U. L. REV. 43, 98 (1998).

86. For a recent description and analysis of Llewellyn's jurisprudence, see N.E.H. HULL, ROSCOE POUND & KARL LLEWELLYN: SEARCHING FOR AN AMERICAN JURISPRUDENCE (1997).

87. TWINING, *supra*, note 16, at 286. Soia Mentschikoff had been Llewellyn's student, research assistant, and associate Chief Reporter of the Code. After marrying Llewellyn, she accepted a joint appointment with him at the University of Chicago Law School in 1951. *Id.* at 112.

88. See Letter from Frank T. Dierson to Herbert F. Goodrich (Mar. 16, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library and the Buffalo Law Review) (describing the negotiation between counsel for the food and drug manufacturing industries and Mentschikoff); see also Connolly, *supra* note 85, at 103 (stating that Mentschikoff provided "the organizing and 'policing' function he [Llewellyn] required to avoid self-destruction.").

had been picked by Llewellyn to draft article 3.<sup>89</sup> In the forties, Prosser was in Minnesota, struggling with the comments to article 3.<sup>90</sup> Article 3 elicited little controversy and Prosser did not participate in political discussions. Prosser's article 3, characterized by Gilmore as "a museum of antiquities—a treasure house crammed full of ancient artifacts whose use and function have long since been forgotten," went on to ultimate enactment.<sup>91</sup>

Fairfax Leary was replaced as the drafter of article 4 by Gilmore, who was then replaced by Malcolm. Leary too ceased having any great involvement in the Code.<sup>92</sup>

As the U.C.C. article on negotiable instruments was drafted by an expert on torts, that on secured transactions was drafted by a Ph.D. in French literature.<sup>93</sup> Llewellyn chose Grant Gilmore in 1948 to start work at \$250 a month to assist Alison Dunham on what became article 9.<sup>94</sup> Gilmore writes, "Neither Dunham—for whom I had and have the highest admiration—nor I had even the slightest practical experience in the field."<sup>95</sup> Gilmore would go on to lead, along with Mentschikoff, the fight against the pro-bank article 4. In the period under study, he and Dunham, under pressure from financial institutions, would create the all-powerful article 9 security interest and drop that article's consumer and small business protection sections. Later, Gilmore would repent of his creation, the article 9 floating lien, but he showed no such remorse during its drafting.<sup>96</sup>

89. Grant Gilmore speculated that Llewellyn wanted someone he could control rather than an expert in the field. Letter from Grant Gilmore to Donald J. Rapson (Oct. 8, 1980), in Donald J. Rapson, Review, 41 BUS. LAW., 675, 676 (1986).

90. Letter from William Prosser to Karl Llewellyn (November 17, 1945) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

91. Grant Gilmore, *Formalism and the Law of Negotiable Instruments*, 13 CREIGHTON L. REV. 441, 461 (1979).

92. Rapson, *supra* note 89, at 677.

93. "Then there was Gilmore's Ph.D. in French Studies (1936). His 350-page Yale doctoral dissertation, *Stéphane Mallarmé: A Biography and Interpretation*, examined the life and work of the highly unorthodox nineteenth-century French symbolist poet. Afterwards, Gilmore taught French at Yale University from 1937 to 1941." Ronald K.L. Collins, *Gilmore's Grant*, 90 NW. U. L. REV. 7, 9 (1995).

94. Alison Dunham was hired in 1947. Minutes of Meeting of Joint Editorial Board (Jan. 30, 1948) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

95. Grant Gilmore, *Dedication to Professor Homer Kripke*, 56 N.Y.U. L. REV. 9, 10 (1981).

96. Grant Gilmore, *The Good Faith Purchase Idea, and the Uniform*

Alison Dunham and Homer Kripke both lived in Westchester County, New York, in the late 1940s and knew each other socially. Kripke was working with the CIT Financial Corporation, giving secured credit to enterprises that the banks were ignoring.<sup>97</sup> Concerned about the Code's first draft on inventory financing, he asked Dunham to introduce him to Llewellyn. So started a collaboration in which Kripke represented the interests and expertise of the financing industry in the drafting of article 9.<sup>98</sup>

Kripke was joined by J. Francis Ireton, a Baltimore attorney and chair of the ABA's Division of Mercantile Law, which oversaw the work of the ABA committees on commercial law.<sup>99</sup> Ireton was a member of a firm which practiced corporate and commercial law; his correspondence reveals that he was familiar with secured transactions.<sup>100</sup> He was critical of the first drafts of article 9 as being "leftist," as being social legislation, and as revealing a total unfamiliarity with actual secured transactions practice.<sup>101</sup> He was instrumental in eliminating article 9's consumer disclosure provisions.<sup>102</sup>

Three other practicing attorneys had a great effect on the Code. Frank Dierson represented manufacturing interests in a successful attempt to change the Code's warranty and remedy provisions. An ABA document listed him as representing "grocery and drug manufacturing businesses."<sup>103</sup> He worked for Charles Wesley Dunn, a New York attorney who represented national food and pharmaceutical associations.<sup>104</sup> Dierson reached a satisfactory compromise

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*Commercial Code: Confessions of a Repentant Draftsman*, 15 GA. L. REV. 605 (1981).

97. "So we had the field all to ourselves, and we frequently said what someone else here has already said today, that we existed only because the banks were so dumb." Kripke, *supra* note 81, at 577.

98. Article 9 started as article 6 moving through the numbers to its present designation. Rather than say "the secured transactions article," I use article 9 to refer to that article in all of its stages.

99. 6 BUS. LAW. 217 (1951).

100. 1 MARTINDALE-HUBBELL LAW DIRECTORY 1430 (1952).

101. Ireton, *supra* note 1, at 282; *see* Letter from J. Francis Ireton to Milton Kupfer (June 4, 1948) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

102. Enlarged Editorial Board, *supra* note 4, at 292-96.

103. ABA Meeting, *supra* note 72, at 1.

104. Dunn served as general counsel for the Grocery Manufacturers of America, the American Pharmaceutical Manufacturers Association, the Premium Advertising Association of America, was President of the Food Law Institute, and

with the Code drafters and withdrew his opposition to the Code.<sup>105</sup>

Walter Malcolm, Chairman of the ABA's Committee on the Proposed Commercial Code, was a Boston attorney who represented the First National Bank of Boston.<sup>106</sup> He was a graduate of Harvard Law School who had practiced in Boston since 1929 and had busied himself in community and bar activities.<sup>107</sup> A strong believer in free enterprise, he had written Soia Mentschikoff in a plea to make the Code provisions subject to agreement: "Without appearing to wax eloquent, to me, two of the greatest virtues of Anglo-Saxon legal system as well as the free enterprise economic system are the ability of these systems to adjust to changes and thus to encourage, rather than discourage, dynamic forces in society."<sup>108</sup> His proposals form the basis of article 1's provisions on variation of the Code's provisions by agreement. Violating the precept "never volunteer," he stepped into draft a revised article 4 and comments in the summer of 1951 after the ALI/NCC voted to delete article 4. His draft, the basis of today's article 4, set off the most serious rebellion in the Code's drafting history, with Mentschikoff and Gilmore leading the protest.

2. *Les Liaisons Dangereuses*. Those who acted as liaisons with business and finance played out a peculiar role.<sup>109</sup> The position of Malcolm, Kripke, Ireton, and Dierson was analogous to that of a border lord who owes allegiance to two kings and has to balance his duties to both. On one

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was Editor, Food, Drug and Cosmetic Law Journal. 3 *Who Was Who in America* 242 (1952).

105. See *infra* note 321 and accompanying text.

106.

Bingham, Dana & Gould has for many years been general counsel to the First National Bank of Boston and since I first came with the office in 1929 I have spent a major portion of my time on bank matters. Consequently, my personal background is that of a bank lawyer meeting from day to day the various operating problems of a large metropolitan bank.

Letter from Walter Malcolm to J.F. Sharman (Oct. 22, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

107. 7 *WHO WAS WHO IN AMERICA* 370 (1981).

108. Letter from Walter Malcolm to Soia Mentschikoff (October 31, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

109. Cf. CHODERLOS DE LACLOS, *DANGEROUS ACQUAINTANCES (LES LIASONS DANGEREUSES)* (Richard Aldington trans., 1957).

side, they participated in the drafting process of a set of laws that was to be neutral, balanced, and fair to all parties concerned. On the other hand, they were representing clients (Malcolm, the banks; Kripke, a secured lender; Ireton, financiers; Dierson, the food and drug industry) who had definite objectives for any new commercial law.

Writing about their role retrospectively, those who had acted as liaisons were self-congratulatory, concluding that they had been able to separate the role of impartial drafter from that of advocate.<sup>110</sup> The rancor between the drafters, for example Soia Mentschikoff's towards Walter Malcolm, was forgotten. In 1951, Mentschikoff wrote to Schnader protesting Malcolm's redrafting of article 4: "First, Walter Malcolm has not been a friend of the Code and his services have not produced anything which will make Code passage easier. In the case of article 4, his contribution will make Code passage more difficult."<sup>111</sup> By 1983, the time of an Ohio State Law Journal Symposium on the drafting history, all this bad feeling was history, and unknown history at that.<sup>112</sup>

Recent commentators on today's Code drafting process have been much more critical. Professor Edward L. Rubin writes how the bank lawyers who participated in the recent revision of articles 3 and 4 thought of themselves as being impartial and fair but could not rid themselves of their

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110. Homer Kripke, *Reflections of a Drafter: Homer Kripke*, 47 OHIO ST. L.J. 577, 578 (1982). For example, Homer Kripke writes:

Well, at any rate, I was working with them on these drafts, but for some time I felt a stand-offishness, resting on the fact that I was employed by a finance company and they didn't quite trust me. I knew that the feeling existed when the Association of the Bar of the City of New York organized its first committee to consider the drafts of this Code as it came out, and Charlie Willard, who was the first chairman of that committee, kept me off the committee and told me that Soia (Mentschikoff) had told him not to let the finance companies capture the committee.

Well, Soia's attitude subsequently changed. She has on more than one occasion expressed the point that she and the others had come to learn that I was able to wear two hats, as she put it—to know when I was an advocate for my client and when I was trying to function as a member of the Code team.

*Id.*

111. Letter from Soia Mentschikoff to William Schnader (November 4, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

112. See *Reflections of a Drafter: Soia Mentschikoff*, 47 OHIO ST. L.J. 537 (1982).

ingrained attitude that banks generally are right and that bank customers generally are unreasonable. The result is a statute which is pro-bank and effectively shuts off consumer redress. It is not that bank counsel set out to harm the bank customer, it is just that a lawyer identifies with bank interests after spending his or her professional life representing banks.<sup>113</sup> Professor Rubin notes that the bank lawyers stated, as did Kripke before them, " 'When I participate in an advisory committee, I check my clients at the door.' "<sup>114</sup> He points out, however, that although such lawyers do not represent the specific interests of their clients, they do not check their conceptual framework at the door:

Lawyers cathect with their clients. . . . It is all the more true for corporate attorneys who work within a single industry, or specialized litigators who always represent one side. When that single industry consists of people whose social class and economic status are the same as the attorney's, bonds of friendship will be added to the process of client identification. Over time, these forces generate a conceptual framework, a general orientation toward the world. It is possible for lawyers to check their clients at the door—attorneys in law firms switch clients fairly regularly, and in-house lawyers can always imagine moving to a different company within the industry. What they cannot leave behind them is a set of identifications, beliefs and personal bonds built up over decades of practice. These identifications, beliefs and bonds constitute their career, their sense of themselves as productive members of society, and form a comprehensive framework through which lawyers perceive the issues in their field.<sup>115</sup>

On the other hand, a commercial statute cannot be drafted *without* input from the relevant industry. What William Schnader wrote Mentschikoff in response to her criticisms of Malcolm was and is true—a business code has to be acceptable to those who work under it:

I have never said, and am not now saying, that the Code should be framed for the advantage of banks to the prejudice of depositors; but, after all, the purpose of the Code is to facilitate commerce, including banking, and I cannot for the life of me understand how anyone can take the position that the Code should be unworkable from the bankers' standpoint. They are the people who will work

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113. Rubin, *supra* note 56, at 749.

114. *Id.* at 749.

115. *See id.* at 752-53.

under the Code day in and day out, and it seems to me that it just must be legislation which they believe practicable and feasible.<sup>116</sup>

Drafting a commercial code without the participation of commercial attorneys would be a purely academic exercise, but involving them in the process can produce a law that ignores consumer interests. This is a problem which has never been solved.

#### *D. Limitations of the Drafting Process*

The drafting of the Code and the drafts themselves were not widely publicized, due to the limitations of information technology at that time and the lack of resources to publicize the Code. Thus it was possible for the Surety Association to find to its surprise in 1953 that a Uniform Commercial Code was being promulgated and that it contained a section<sup>117</sup> which limited a surety's rights in relation to a secured party. The "word processing system" of the ALI was Ms. Eleanor Twohig, secretary to the ALI President, who pounded out the stencils for the mimeographed copies of the drafts.<sup>118</sup>

There were not many copies of the Code available. Those were the days before the Xerox machine, to say nothing of the Internet. In 1947, Ferson Merton of the University of Cincinnati Law School requested a copy of the Code from the ALI and was lent a copy by W. D. Lewis, the Director of the ALI, "Please return it to me when you are through with it as this is one of my four remaining copies."<sup>119</sup> In 1951, Charles

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116. Letter from William Schnader to Soia Mentschikoff 2, Llewellyn Papers, AA.J.XXV.1 (November 8, 1951) (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

117.

Strange as it may seem, the Surety Association's lawyers say that they did not have any knowledge, until quite recently, of the fact that the Code was being prepared and argue that even if they had had such knowledge they would have had no reason to suspect such a revolutionary change in the law of suretyship, even in an article entitled "Secured Transactions."

Letter from William Schnader to Herbert Goodrich (Feb. 9, 1953) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

118. Letter from Mildred, Secretary to Llewellyn, to Eleanor Twohig, Secretary to the ALI (Jan. 20, 1948) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

119. Letter from W.D. Lewis, Director, A.L.I., to Merton L. Ferson (January 31, 1947) (on file with A.L.I. Archives, University of Pennsylvania Law Library,

Bunn, who was organizing a symposium in Wisconsin on the U.C.C.,<sup>120</sup> had to beg 100 or 300 copies of the Code<sup>121</sup> from the ALI.

The ALI/NCC did not have the resources to publicize the Code or to lobby widely for its passage. In 1951, Goodrich stated that there was no money for mimeographing.<sup>122</sup> There were limited resources to send people around the country talking up the Code. It was decided to fund travel only to states in which the Code was being considered for adoption.<sup>123</sup> Llewellyn and Mentschikoff's travels raised eyebrows.<sup>124</sup> Alison Dunham had the temerity to ask for an honorarium and was "spanked" by Herbert F. Goodrich and Schnader of the ALI.<sup>125</sup>

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and the Buffalo Law Review).

120. See *A Symposium on the Proposed Uniform Commercial Code*, 1952 WIS. L. REV. 197 (1952).

121. Letter from Charles Bunn to Herbert F. Goodrich (October 9, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) ("We can make good use of quite a lot of copies. They can be on cheap paper, they need not be free, and they need not contain the comments.").

122.

P.S. We cannot possibly mimeograph Comments for distribution for any but certain selected sections or Articles. At the Editorial Board meeting yesterday we counted up the approximate paging. There is not enough money in the Falk Foundation, The Rockefeller Foundation, The Carnegie Foundation or even the Ford Foundation to pay for mimeographing expense of all these pages.

Letter from Herbert Goodrich to Charles Bunn (Nov. 15, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

123.

I think Soia and Karl should be told very plainly that any trips to such states as North Dakota and Maine are out as far as they are concerned. They should be limited during the summer to visit only states which intend to introduce the Code in 1951 and press for its immediate adoption.

Letter from William Schnader to Herbert F. Goodrich, Director, A.L.I. (Apr. 25, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

124. "I hear from Mr. Dinkelspiel this morning that Soia is to go to California. He does not say who is paying for the trip. Who is?" Letter from Herbert F. Goodrich, Director, A.L.I. to Professor Karl Llewellyn (Apr. 12, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

125. In response to Dunham's request for money, Schnader wrote Goodrich, "I think the time has come for somebody to 'spank' this guy, and I think perhaps as Chairman of the Editorial Board and Director of the Law Institute, you are the person to do it." Letter from William A. Schnader to Herbert F. Goodrich (May 5, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review). Schnader himself wrote Dunham on May 5, 1950: "The



Thus there was a lack of communication about the Code. Because of the lack of funds and the lack of such facilities as faxes, duplicating machines, the internet, and jet travel, the drafting process was concentrated on the Eastern Seaboard. Exceptions included William Prosser who was working in Minneapolis,<sup>126</sup> and Charles Bunn, in Wisconsin, but most of the work took place in New York and Pennsylvania. Because of this, legislators in Indiana felt that they were far removed from the drafting process.<sup>127</sup>

Furthermore, few people outside of the drafters themselves participated in the drafting,<sup>128</sup> and there was little sustained academic interest in the developing Code. Although there was a plethora of articles giving a general description of the proposals, few came to grips with the Code's underlying premises or policies. The main academic critics included Samuel Williston<sup>129</sup> who generally argued that the U.C.C. represented unneeded charges from his Sales Act. The Harvard Law School faculty made several technical comments,<sup>130</sup> and there was a symposium in the Wisconsin Law Review, organized by Charles Bunn, who had been redrafting the Code and comments. Professor Frederick Beutel, who felt himself snubbed by the ALI,<sup>131</sup> wrote *The*

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idea that you would expect an honorarium for work of this sort never entered my mind. I must confess that I think you are pursuing a very short-sighted policy. When I was your age, I considered it worthwhile to make all the professional contracts I could. I hoped they would pay dividends later." Letter from William A. Schnader to Allison Dunham (May 5, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

126. See Letter from William Prosser to Karl Llewellyn (Nov. 17, 1945) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

127. See Letter from K.F. Panzer to William A. Schnader (Mar. 23, 1953) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

128. Kripke noted that large law firms did not, to a large extent, participate in the drafting. Homer Kripke, *The Principles Underlying The Drafting of the Uniform Commercial Code*, 1962 U. ILL. L. F. 321, 330, n. 43.

129. See Samuel Williston, *The Law of Sales in the Proposed Uniform Commercial Code*, 63 HARV. L. REV. 561, 587 (1950).

130. See *Report on Article 2—Sales by Certain Members of Faculty of Harvard Law School*, 6 BUS. LAW. 151 (1952).

131. Beutel wrote:

Dear Herbert:

Over a month has now passed since we had our exchange of correspondence on correlating the terminology in the Commercial Code. I had a short letter from Prof. Bunn before yours came, written in reply to the carbon copy of the first letter which I sent you, but have had no

*Proposed Uniform (?) Commercial Code Should Not Be Adopted*<sup>132</sup> in opposition to the Code. But that was about it. In any case, the drafters paid little attention to the academic criticism. They modified the Code primarily in response to organized groups such as the American Bar Association and the food and drug industry.

The lack of publicity affected the Code in several ways. One, it meant that outlying states such as Indiana were not going to adopt the Code before the Eastern states did so. More importantly, there was no public interest to counter-balance the industrial, commercial, and financial interests that lobbied for their own gain.<sup>133</sup>

Besides the limitations of technology, the ALI/NCC approach was elitist in having a small team of academics, drawn from the prestigious law schools located on the Eastern seaboard, draft the proposed legislation with almost no public involvement. Such an approach worked for the Restatements but was ineffective in persuading state legislatures. Although Mentschikoff talked of involving labor

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further indication that the editorial board is interested in any comments from me.

I take it I live on the wrong side of the tracks. Let's forget the whole matter.

Letter from Frederick Beutel to Herbert Goodrich (July 19, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

132. Frederick Beutel, *The Proposed Uniform (?) Commercial Code Should Not Be Adopted*, 61 YALE L.J. 334 (1952).

133. As Grant Gilmore stated:

By its nature Article 9 cannot become a matter of any great public interest—although there is a certain amount of fun in imagining the Governor of Connecticut or of North Carolina running for re-election on the issues of the after-acquired property clause and the floating charge. It is a technical statute for specialists. Unfortunately all the specialists are on the same team and there is no opposition. Financing operations in this field have become so complex that no one, except the operating men and their counsel, any longer understands them. It is a fair guess that at legislative hearings, apart from the local Commissioners on Uniform Laws, no one will show up except bank and finance company counsel, appearing either in that capacity or as representatives of local, state and national bar associations. To the extent that the passage or defeat of legislation depends on rational grounds, Article 9 will pass or fail depending on the attitude to be taken by the representatives of the financing industry.

May their choice be wise.

Grant Gilmore, *The Secured Transactions Article of the Commercial Code*, 16 LAW & CONTEMP. PROBS. 27, 48 (1951).

and women's groups, there was no attempt to consult anyone besides academics, bar associations, and businesses. The drafters, to use a Chicago phrase, just had no clout.

### E. *The Political Realities*

First, we are talking about the political realities facing a proposed commercial code in a short period of time, from 1949 to 1954, but more precisely in a two year period from summer 1950 to summer 1952. It was then that the fundamental changes in the Code's provisions were made.<sup>134</sup>

That era was perhaps the worst era in American history to seek social reform, to try to extend proposals that stemmed from the Depression era. The general political ideology which was turning away from collectivism to individualism. In my article *Between-the-Wars Social Thought*,<sup>135</sup> I argue that Llewellyn's views and his original program for the Code grew out of the matrix of the collectivist mentality of the 1930s. Llewellyn's emphasis on the enforcement of group norms by the imposition of trade usages, with the norms being decided by merchant tribunals, shows his commitment to institutionalism, a view which saw society as being made up of groups, each with its own usages and norms. Llewellyn was once part of an academic avuncular guard, a supporter of FDR in his court-packing plan, a folk dancer, a student of Boas' anthropology, part of a 1930s radical, collectivist milieu.<sup>136</sup>

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134. The changes included the changes in the Code's "Purposes," the switch from objective to subjective good faith, from Code sections being mandatory unless expressly made subject to agreement to the opposite, new limitations on warranty actions, the deletion of the consumer protection sections of article 4. The details of these changes are discussed *infra* at notes 229-67 and accompanying text.

135. Allen R. Kamp, *Legal Development: Between-the-Wars Social Thought: Karl Llewellyn, Legal Realism, and the Uniform Commercial Code in Context*, 59 ALB. L. REV. 327 (1995).

136. A 1937 letter to him from an attorney, Louis Weiss, reveals the radical world of the 1930s that Llewellyn had been in. The letter recommends a Tom Tippet, who authored WHEN SOUTHERN LABOR STIRS (1931), an analysis of the Southern textile strikes, and coauthored YOUR JOB AND YOUR PAY (1931), a textbook "which . . . is a little red for good advertising." According to the letter, Tippet "had lectured widely all over the country to colleges and bourgeois audiences." Letter from Louis Weiss to Karl Llewellyn (June 14, 1937) (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

But intellectual fashions may change as radically as those in *Vogue*. It is the most fashionable which age the worst. In Oscar Wilde's *An Ideal Husband*, Lady Marby, speaking to the advanced young woman Mabel Chiltern, put it well: "You are remarkably modern, Mabel. A little too modern, perhaps. Nothing is as dangerous as being too modern. One is apt to grow old-fashioned quite suddenly."<sup>137</sup> By the late 1940s, Llewellyn's institutionalist views were out-of-date. A painful example is Llewellyn's *What Law Cannot Do for Inter-Racial Peace*,<sup>138</sup> in which he applies an anthropological "folkways" view to racial integration. He balances the desires of those who want integration with the strain of changing one's social customs. Llewellyn's collectivist vision was obsolete in our era of individual contracting and individual rights. Making the Code acceptable to the world of commerce meant in large part basing it on an individualistic system based on freedom of contract.<sup>139</sup>

Grant Gilmore reports that article 9 was criticized as betraying "an earnest reformist zeal reminiscent of the lush days of the early New Deal . . . ." Eisenhower was about to

137. Oscar Wilde, *An Ideal Husband*, in COMPLETE WORKS OF OSCAR WILDE 514 (1966).

138. Karl N. Llewellyn, *What Law Cannot Do for Inter-Racial Peace*, 3 VILL. L. REV. 30 (1957). In his article, Llewellyn attempted to balance the ideal of racial equality with the danger of provoking too much resistance from interfering with local folkways. *Id.* at 31. He works out the balance in specific situations, hotels, restaurants, bars, and beaches. For example: "Beaches: There is little alcohol, but any crowded beach is a place of constant intrusion and of constant need for restraint. There is rarely such continuity of personnel as can lead to understanding. And crowds can mobilize too easily into trouble." *Id.* at 34.

139. In explaining what he done in redrafting article 4, Malcolm stated:

The last basic issue, or key issue in the change, outside of detailed changes, was the matter of extending and solidifying the basic principle of freedom of contract.

There was indicated in the discussion this morning of the two points of view which Mr. Tweed characterized as that of the ivory tower and that of the market place, to a very substantial extent, that same issue and problems exists with respect to Article 4, and without any question the effort that I have made has been in part to move the draft to a point where it would be acceptable by the market place.

One of the key areas where that movement is made is in solidifying this principle of freedom of contract.

PROCEEDINGS 848-49 (Joint Sessions, National Conference of Commissioners of Uniform State Laws and American Law Institute) (Sept. 15, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library).

140. Grant Gilmore, *The Secured Transactions Article of the Commercial Code*,

be elected and the country was not eager for reform. On the contrary, there was a virulent anti-communism which spilled over to attack any proposals for change. One of the many bankers opposed to the Code stated that it was "communist inspired."<sup>141</sup>

Under the pressure of McCarthyism, the country was turning away from the collectivist programs of the 1930s. Even—or especially—the academic left was valuing individualism. Paul Carter writes how Adlai Stevenson in speeches and David Riesman in *The Lonely Crowd* stressed individualism and personal autonomy.<sup>142</sup> This trend left the proponents of collective, institutional approaches behind.

Parallel to the collectivist-individualist and reformist-conservative divides, was the division among the drafters between "town and gown," the practitioners and the academics. The practitioners (e.g., Schnader, Ireton, Kripke) had little respect for the academics who had written the early drafts. Generally, the practitioners felt that the academic drafters were hopelessly impractical and out of touch with the realities of commerce.<sup>143</sup> It comes as a shock today to realize the little respect shown the secured transactions drafters, Dunham and Gilmore.<sup>144</sup> The view of the

16 L. & CONTEMP. PROBS. 27, 37 (1951).

141. As stated by Grant Gilmore, the history of the banking provisions: "Article 4 became the bloodiest battleground in the entire history of the Code. While Steffen (and others) attacked it as being 'pro-bank,' bank counsel (particularly the New York group) attacked it as a Communist plot designed to destroy the American banking system." Letter from Grant Gilmore to Donald J. Rapson (August 8, 1980), in Donald J. Rapson, Book Review, *The Law of Modern Payment Systems and Notes* by Fred H. Miller & Alvin C. Harrell, 41 Bus. L. 675, 677 (1986). Malcolm reported such a comment in April of 1954: "Would you believe it, but in a recent meeting of some fifteen or twenty banks from an equal number of large cities of the United States, the representative of the one New York bank present contended that the Code was communist inspired." Letter from Walter Malcolm to William A. Schnader (April 13, 1954) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

142. PAUL A. CARTER, ANOTHER PART OF THE FIFTIES (1983).

143. E.g., Letter from Irvin I. Livingston to William A. Beers (June 25, 1948) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) ("The foremost thought that I have is, without any reflection on the reporters, that the draft gives rather conclusive evidence that it was formulated without an adequate knowledge or understanding of practical and functional operations of inventory financing from either the borrower's or the financier's standpoint.")

144. Letter from Homer Kripke to the A.L.I. (Aug. 21, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) stated:

practitioners, that the drafters were leftist, impractical, out of touch amateurs, which was shared by the vice president of ALI, meant that the academic drafters were in a weak position. This weakness showed itself later in the controversy over article 4. Schnader sided with Malcolm and the bankers over Gilmore and Mentschikoff, using strong language to express his disapproval of the latter's going public with their protest over the pro-bank redrafting of article 4: "It is extremely difficult for me to understand what Grant Gilmore and you are trying to do."<sup>145</sup>

One of the recurring criticisms of the Code was that it was "reform," "paternalist," "leftist," or "social" legislation, not good things.<sup>146</sup> In response to Mentschikoff's complaint

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Bluntly, the history of the Article on Secured Transactions demonstrates that the joint meeting of the two bodies has been an entirely inadequate forum to obtain the considered judgment of experienced persons in this field of law. Every printed draft of this Article, including even the fantastic first draft, and the almost equally unrealistic second draft of the chapter on Inventory and Account Receivable Financing which was presented to the Seattle meeting in 1948, has been approved on the floor by the joint houses with comparatively little change and little informed discussion. While the Reporters themselves have recognized the inadequacies of their successive drafts and have gone on to revise them drastically, the joint houses have never shown any real familiarity with the problems involved, nor have even the obvious 'bugs' in each draft been mentioned on the floor. It was not until the May 1950 meetings when representatives of big city bar associations and specialist groups spoke from the floor that the discussions at the joint meetings began really to grapple with the issues in a decisive way.

*Id.* William Schnader agreed in a letter to Herbert Goodrich, dated Aug. 25, 1950:

As I was thinking the matter over yesterday, I came to the conclusion that no one ought to undertake a project of the importance of the Commercial Code with amateur draftsmen such as Article 9 has had. It seems to me to be just inexcusable for so many different drafts to have gone out on that article.

It seems that nothing that is done is given enough thought to give it a semblance of finality. However, there is no use crying over spilled milk, but we certainly were not smart in entrusting the drafting of that particular article to people who just didn't have any facility in that type of work.

Letter from William A. Schnader to Herbert Goodrich (Aug. 25, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

145. Letter from William A. Schnader to Soia Mentschikoff (November 8, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

146. *E.g.*, Letter from Homer Kripke to A.L.I. ("The vice to me of the paternalistic view of the role of law in a *commercial* code is not lessened by the fact

that the Code was being changed to accommodate special interests, by which she meant favoring "a single economic segment of the community at the expense of the general public," Schnader stated: "It seems to me we are drawing an Act to regulate special interests, and the way they do business. And I don't think any of us entered into this Code project as a reform measure in any sense of the word."<sup>147</sup>

"Social legislation" had a definite meaning in the post-war era, meaning legislation that was designed to reallocate power and wealth within society. Robert G. Swain (of the New York white shoe firm of Cravath, Swaine & Moore) wrote of "social legislation" in the 1949 American Bar Association Journal:

Over the last fifteen years the charge that the Bar serving business is anti-social has emanated principally from those who have espoused the more extreme so-called social legislation, whose objective has been the transfer of wealth from the industrious and thrifty to the indolent and prodigal and the substitution of government planning and control for our old system of private enterprise.<sup>148</sup>

A more positive definition was given by Ben W. Palmer in the same A.B.A. Journal volume, using terms that fit the Code proposals, under the section, "Adherents of the New Philosophy Criticize the Courts":

But all of these joined in the criticism of the courts, particularly of the Supreme Court of the United States as the barrier to social legislation and as the enemy to a new concept of law. That concept was of a law that did more than keep the peace. It was of a law

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that in this case, as in others, I can find no conceivable support for the comment in the language of the section.") (regarding the October, 1949 Draft) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review). Ireton characterized the secured transaction article as having "had a more definite and decided slant to the left than any of the other Articles in the Code." J. Francis Ireton, *The Commercial Code*, 22 MISS. L.J. 273, 281-82 (1951). Ireton further criticized the Consumer Credit proposals: "This is embanking upon social legislation, and there can be considerable doubt as to the propriety of including such regulation in a statutory proposal relating to the security concepts." J. Francis Ireton, *The Proposed Commercial Code: A New Deal in Chattel Security*, 43 ILL. L. REV. 794, 804 (1949); see also *infra* note 467 and accompanying text (discussing a Bar Association of New York report that damaged the Code's prospects).

147. Enlarged Editorial Board, *supra* note 4, at 320-21.

148. Robert T. Swaine, *Impact of Big Business on the Profession: An Answer to Critics of the Modern Bar*, 35 A.B.A. J. 89, 170 (1949).

that would balance the interests of conflicting social and economic groups. It would balance their interests not merely by preserving private property and a theoretical liberty of contract but by redressing the balance in favor of the economically weak. The machinery of the state was to be used also to establish and enforce rules of the game for the protection of the ethical, the better social type and of the public generally. The law was to be used to rebuild society nearer to the heart's desire of those filled with humanitarian zeal—and in some cases with envy of their neighbor's wealth.<sup>149</sup>

The criticism of “social legislation” was just part of the conservative counter-revolution of the post-war era, the extreme form of which is known as McCarthyism. At the least there was a refusal to countenance any more social change:

“Some American conservatives were avid for an all-out effort to get rid of the New Deal and turn America back toward unregulated capitalism. Others acquiesced in what the New Deal had done but insisted upon drawing a stern line, beyond this not one step further.”<sup>150</sup>

The Code had the misfortune to be seen as leftish or even Communist inspired in one of the worst eras for proposing progressive legislation.<sup>151</sup> As stated by Eric F. Goldman,

Everywhere in the United States, the fury against Communism was taking on—even more than it had before the Korean War—elements of a vendetta against the Half-Century of Revolution in domestic affairs, against all departures from tradition in foreign policy, against the new, the adventurous, the questing in any field.<sup>152</sup>

The organizational support necessary for the passage of a reformist Code just was not there. The American Bar Association was going through a reactionary phase. In the early 1950s, the Association adopted resolutions urging that attorneys be required to file affidavits of non-membership in

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149. Ben W. Palmer, *Groping for a Legal Philosophy: Natural Law in a Creative and Dynamic Age*, 35 A.B.A. J. 12, 14 (1949).

150. ERIC F. GOLDMAN, *THE CRUCIAL DECADE—AND AFTER/AMERICA, 1945-1960*, at 9 (1973).

151. At least one New York banker thought the Code was Communist inspired. Letter from Walter Malcolm to William A. Schnader (Apr. 13, 1954) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

152. GOLDMAN, *supra* note 150, at 214.



the Communist Party and that all Party members and advocates of Marxist-Leninism be expelled from the practice of law.<sup>153</sup>

Organizations that could have supported the Code were on the defensive. Ellen Schrecker points out that "McCarthyism destroyed the left."<sup>154</sup> The war against domestic Communism deradicalized social science, private foundations, the entertainment industry, the media, and labor unions. "Though the [Communist] party itself survived, all the political organizations, labor unions, and cultural groups that constituted the main institutional and ideological infrastructure of the American left simply disappeared. An entire generation of political activists had been jerked off the stage of history."<sup>155</sup>

The present U.C.C. is now presented as "traditional." But the U.C.C. as a product of compromise with the reform measures that survive, such as, the unconscionability section, being just a remnant of a much broader system of business regulation. The original U.C.C. is, in the words of Ellen Schrecker, a thing "that did not happen":

As we assess the consequences of McCarthyism's assault on the left, we encounter a world of things that did not happen: reforms that were never implemented, unions that were never organized, movements that never started, books that were never published, films that were never produced. And questions that were never asked. We are, in short, looking at "might have beens" and at a wide range of political and cultural possibilities that did not materialize.<sup>156</sup>

## II. THE ISSUES, THE DEBATE, AND THE OUTCOME

### A. *The Controversial Sections of the 1949 Code*

My article concentrates on certain sections that were the sticking points in persuading the commercial world to accept the Code. My list is somewhat arbitrary,<sup>157</sup> but it does include

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153. ARTHUR SABIN, IN *CALMER TIMES* 48 (1999).

154. ELLEN SCHRECKER, *MANY ARE THE CRIMES/McCARTHYISM IN AMERICA* 369 (1998).

155. *Id.*

156. *Id.*

157. For example, I do not discuss the debate over the specific rules only applicable to merchants (the merchant rules), mainly because Professor Wiseman

most of the issues that generated debate:

1. Whether the Code sections were to be presumed permissible (subject to agreement) or mandatory. Section 1-108,<sup>158</sup> (now permissive, section 1-102(3)).

2. Objective or subjective good faith. Section 1-201(16) (now section 1-201(19); section 3-304 (now section 3-103(4)).

3. Role of usage of trade and express terms. Section 1-205.

4. Unconscionability (now and then section 2-302).

5. Beneficiaries of warranties. (Now and then section 2-318).

6. Impleader and direct action against manufacturers for breach of warranty, sections 2-718, 2-791 (now deleted; became 402A products liability).

7. Contractual modification of remedies. Section 2-721 (now section 2-719).

8. The proto-truth-in-lending disclosures in the secured transactions article, section 8-203 (now deleted in the Code; enacted as federal law, 15 U.S.C. § 1601 et seq.).

9. Assertion of defenses against an assignee of a consumer contract. Section 8-206 (now deleted; in federal law as Federal Trade Commission Holder-In-Due-Course Regulations 16 C.F.R. pt. 433).

10. Requirement of notice before repossession. Section 8-603 (now deleted).

11. The floating lien. (Created by a set of interlocking sections in the secured transactions article, then and now).

12. Contractual modification of article 4 (now section 4-103).

One can group these topics into categories. One topic relates to basic issues about regulation of contract: whether the Code should be regulatory or rather provide back-up provisions which apply only if the parties have not contracted out of them. (Issue one.) Another, a related topic, is whether commercial contracting should be subject to strong judicial and trade regulation or whether business should be autonomous, free of outside control. (Issues two, three, four and seven.) Issues five, six, and seven involve the creation and limitation of liability on sellers for warranty. For secured transactions, issues eight, nine, and ten deal with consumer

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has already done the job. See Wiseman, *supra* note 2.

158. References are to the 1949 Uniform Commercial Code, reprinted in 6, 7 U.C.C. DRAFTS (E. Kelly ed., 1984).

debtor protection, while eleven involves the power of a financier to obtain a lien on almost all the debtor's assets. Issue twelve, involving banking, provoked a major controversy.

The 1949 Code had a different set of rules to determine the terms of a contract than we do today. First, Code provisions were mandatory unless explicitly made subject to agreement; today it is the other way around.<sup>159</sup> In 1949, there was section 1-108 (1-107 in later drafts), which provided that a Code section was to be mandatory unless it was explicitly stated that it was subject to agreement.<sup>160</sup> This was reversed—now every Code provision is subject to agreement unless stated otherwise.<sup>161</sup> White and Summers explain the modern rule:

Finally, most of the Code's provisions are not mandatory. The parties may vary their effect or displace them altogether: freedom of contract is the rule rather than the exception. Most commercial law is therefore not in Code at all but in private agreements, including course of dealing, usage of trade, and course of performance.<sup>162</sup>

The Code stated the exact opposite until 1951.

All terms of all contracts had to be read in terms of objective good faith.<sup>163</sup> Articles 3 and 4 further included the objective definitions of good faith; section 3-304 defined the notice component of being a holder-in-due-course in terms of a "reasonable man" standard.<sup>164</sup> The secured transactions

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159. U.C.C. § 1-102(3), Official Draft: Text and Comments Edition (1951), *reprinted in* 16 U.C.C. DRAFTS 477 (E. Kelly ed., 1984).

160. "The rules enunciated in this Act are mandatory and may not be waived or modified by agreement unless the rule is qualified by the words 'unless otherwise agreed' or their equivalent." U.C.C. § 1-108, Official Draft: Text and Comments Edition (1949), *reprinted in* 6 U.C.C. DRAFTS 31 (E. Kelly ed., 1984).

161. *See* U.C.C. § 1-102(3) (1989).

162. WHITE & SUMMERS, *supra* note 3, at 7.

163. " 'Good faith' means honesty in fact in the conduct or transaction concerned. Good faith includes good faith toward all prior parties and observance by a person of the reasonable commercial standards of any business or trade in which he is engaged." U.C.C. § 1-201(16), Official Draft: Text and Comments Edition (1949), *reprinted in* 6 U.C.C. DRAFTS 33 (E. Kelly ed., 1984). In commercial law talk, "honesty in fact" is seen as "subjective" good faith; defining good faith in terms of an outside standard (reasonable commercial standards) is "objective." WHITE & SUMMERS, *supra* note 6, at 517-18.

164. U.C.C. § 3-304, cmt. 2, Official Draft: Text and Comments Edition (1949), *reprinted in* 6 U.C.C. DRAFTS 330 (E. Kelly ed., 1984).

article defined a merchant to include a "financing agency."<sup>165</sup> Parties were directly bound by any course of dealing and by usages of trade.<sup>166</sup>

As to regulating agreements, both section 2-302 on unconscionability and section 2-731 on contractual modification of remedies allowed judicial policing of *unreasonable* contracts. Comment 1 to section 2-302 provided that courts can regulate unreasonable contracts. "This section is intended to apply to the field of sales the equity courts' ancient policy of policing contracts for unconscionability or unreasonableness." Section 2-721, comment 1 provided for invalidation of modifications of remedies if such modifications were unreasonable.<sup>167</sup> Comment 6 to section 1-205, usage of trade, again pointed out that courts can regulate on the basis of reasonableness under the unconscionability section and that reasonableness depends on a balance of sellers' and buyers' rights.<sup>168</sup>

Another set of issues involves warranty litigation: who

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165. U.C.C. § 2-104, Official Draft: Text and Comments Edition (1949), reprinted in 6 U.C.C. DRAFTS 53 (E. Kelly ed., 1984).

166. Sections 1-205(2) and 1-205(3) state:

(2) A usage of trade is any practice or method of dealing currently recognized as established in a particular place or among those engaged in trade or in a particular vocation or trade. Its existence and scope are questions of fact.

(3) The parties to a contract are bound by any course of dealing between them and by any usage of trade of which both are or should be aware and parties engaged in a particular vocation or trade are bound by its usages.

U.C.C. §§ 1-205(2), 1-205(3), Official Draft: Text and Comments Edition (1949), reprinted in 6 U.C.C. DRAFTS 41-42 (E. Kelly ed., 1984). Today, course of performance and usage of trade "give particular meaning to and supplement or qualify terms of an agreement." U.C.C. § 1-205(3) (1991).

167. U.C.C. § 2-721, cmt. 1, Official Draft: Text and Comments Edition (1949), reprinted in 6 U.C.C. DRAFTS 257 (E. Kelly ed., 1984).

168. Comment 6 of § 1-205 states:

The policy of this Act controlling explicit unconscionable contracts and clauses applies to implicit clauses which rest on usage of trade and carries forward the policy underlying the ancient requirement that a custom or usage must be "reasonable." However, the emphasis is shifted. The burden is no longer on the usage to establish itself as being reasonable, for the very fact of commercial acceptance makes out a *prima facie* case on that point. But in a market dominated by buyers or by sellers as the case may be, practices can become standard which are so unfair as to be unreasonable, and that aspect of the anciently established policing of usage by the courts is continued.

U.C.C. § 1-205, cmt. 6, Official Draft: Text and Comments Edition (1949), reprinted in 6 U.C.C. DRAFTS 44 (E. Kelly ed., 1984).

can sue (the beneficiaries of warranty) and whom they can sue (by impleader and direct action sections). Article 2 contained three sections dealing with products liability which raised strong protest: section 2-318 on beneficiaries of warranties, section 2-718 on the impleader of a manufacturer in warranty suits, and section 2-719 on direct action against manufacturers. The 1949 U.C.C. allowed a buyer to implead his seller "in a like manner and with like effect as is or may be provided in Federal Rules of Civil Procedure."<sup>169</sup> Section 2-719 provided for a "Direct Action Against Prior Seller":

Damages for breach of a warranty sustained by the buyer or by any beneficiary to whom the warranty extends (Section 2-318) may be recovered in a direct action against the seller or any person subject to impleader under the preceding section. An action against one warrantor does not of itself bar action against another.<sup>170</sup>

This section was the remnant of the earlier proposal to enact what would now be called strict liability in tort.<sup>171</sup> It hit a raw nerve with manufacturers calling forth strong opposition. The provisions were dropped and products liability developed as judge-made tort law.<sup>172</sup>

The consumer protection and the floating lien sections of the secured transactions article spurred debate. In general, the 1949 predecessor to article 9 was kinder and gentler than it is today. The Revision of Tentative Draft No. 2 (of the secured transaction article) (February 3, 1949) retained the prohibition against disclaiming warranties by the security agreement.<sup>173</sup> The Tentative Draft Number 3 (March 1, 1949) limited the self-help repossession where the consumer paid more than a certain percentage of the obligation.<sup>174</sup> Section 7-

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169. U.C.C. § 2-718(1)(a), Official Draft: Text and Comments Edition (1949), reprinted in 6 U.C.C. DRAFTS 253 (E. Kelly ed., 1984).

170. U.C.C. § 2-719, Official Draft: Text and Comments Edition (1949), reprinted in 6 U.C.C. DRAFTS 254 (E. Kelly ed., 1984).

171. Proposed Revised Uniform Sales Act § 28 (1941), reprinted in 1 U.C.C. CONFIDENTIAL DRAFTS 21 (E. Kelly and A. Puckett eds., 1995); see John B. Clutterbuck, *Karl Llewellyn and the Intellectual Foundations of Enterprise Liability Theory*, 97 YALE L.J. 1131, 1131-51 (1988) (discussing how Llewellyn's proposals formed the basis of strict products liability).

172. See Clutterbuck, *supra* note 171, at 1131-51.

173. U.C.C. § 7-106, Tentative Draft No. 2 (February 1949), reprinted in 5 U.C.C. CONFIDENTIAL DRAFTS 176 (Elizabeth Slusser Kelly & Ann Puckett eds., 1995).

174. U.C.C. § 7-611, Tentative Draft No. 2 (February 1949), reprinted in 5

106(2) prevented a security agreement from limiting or disclaiming express or implied sales warranties,<sup>175</sup> and section 7-321(3) stated that a merchant could always assert claims amounting to a failure of consideration against an assignee.<sup>176</sup> For non-merchant debtors, an assignee took subject to any defenses which the borrower had against the original financier.<sup>177</sup> By May of 1949, a holder in due course of a note secured by a consumer's goods had the option of claiming on the note or as an assignee. If claiming on the note as a holder in due course, the security interest would lapse; if claiming as an assignee, he could not be a holder-in-due course.<sup>178</sup> This limitation on holders in due course in consumer transactions was twenty-eight years ahead of its time; the Federal Trade Commission finally prohibited the status of holder in due course status in consumer transactions in 1977.<sup>179</sup>

Section 7-605 protected the consumer by requiring twenty days notice before repossession if the consumer had paid more than sixty percent of the obligation secured.<sup>180</sup> Section 7-611 was also nineteen years ahead of its time in providing for such credit disclosures as the cash price, the credit service charge, and the amount of each payment nineteen years before the Truth-in-Lending Act of 1968.<sup>181</sup>

Gilmore wrote that these disclosure provisions "have been attacked *in toto* as unnecessary and undesirable matter for a Commercial Code, destructive of the right of freedom of contract, and illustrative of a 'paternalistic,' even 'socialistic,'

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U.C.C. CONFIDENTIAL DRAFTS 349 (E. Kelly & A. Puckett eds., 1995).

175. U.C.C. § 7-106(2), Tentative Draft No. 2 (February 1949), *reprinted in* 5 U.C.C. CONFIDENTIAL DRAFTS 244 (E. Kelly & A. Puckett eds., 1995).

176. U.C.C. § 7-321(3), Tentative Draft No. 2 (February 1949), *reprinted in* 5 U.C.C. CONFIDENTIAL DRAFTS 294-95 (E. Kelly & A. Puckett eds., 1995).

177. U.C.C. § 7-321(2), Tentative Draft No. 2 (February 1949), *reprinted in* 5 U.C.C. CONFIDENTIAL DRAFTS 294-95 (E. Kelly & A. Puckett eds., 1995).

178. U.C.C. § 7-612, Official Draft: Text and Comments Edition (1949), *reprinted in* 8 U.C.C. DRAFTS 169 (E. Kelly ed., 1984).

179. *See* Preservation of Consumers' Claims and Defenses, 16 C.F.R. § 433 (1997).

180. *See* U.C.C. § 7-605(1)(b), Official Draft: Text and Comments Edition (1949), *reprinted in* 8 U.C.C. DRAFTS 160 (E. Kelly ed., 1984).

181. *See* U.C.C. § 7-611(1), Official Draft: Text and Comments Edition (1949), *reprinted in* 8 U.C.C. DRAFTS 167 (E. Kelly ed., 1984); Truth-in-Lending Act of 1968, 15 U.S.C. §§ 1601-1667(e) (1994). Generally, the early consumer protection sections of the Code, which were rejected in the fifties, reappeared as federal legislation in the sixties and seventies. Manufacturers direct liability re-emerged as § 402A liability.

attitude which is said to underlie much of the Code and particularly article 9.<sup>182</sup> In the words of J. Francis Ireton, the Chairman of the Division of Mercantile Law of the American Bar Association, "this can be said about the article, that of all the articles in the Code this article had a more definite and decided slant to the left than any of the other articles in the Code."<sup>183</sup>

In the area of inventory financing, the 1949 Code dropped many of its protections for non-inventory financiers and other creditors. Section 7-323 (9), however, provided that the debtor and any other secured creditor could sue the inventory financier for damages for failure to follow the prescribed default procedures. The section provided a safe harbor by having the financier's actions approved by a court or creditor's committee and thus being immunized from suit.<sup>184</sup>

The debate over article 4, which was the most serious controversy among the proponents is a story of its own. The 1949 version of article 4 was just not acceptable to the bankers. They focused on article 4's restriction of freedom of contract and believed that article was too detailed a regulation of banking practice.<sup>185</sup> The drafters' proposal would be jettisoned and Walter Malcolm would draft a replacement article 4.<sup>186</sup>

The drafters hoped that the regulatory 1949 Code would be adopted without major changes. They were wrong.

### B. *The Debates and the Outcomes*

There were several U.C.C. drafts between 1949 and the December, 1953 Draft. A quick look at these, collected in volumes 1 through 17 of Elizabeth Kelly's *Uniform Commercial Code Drafts*, supplemented by her *Confidential Drafts*, gives the impression that the changes contained in these versions were incredibly complex. The reality is simpler—almost all of the changes after 1949 were made at

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182. Gilmore, *supra* note 133, at 37.

183. Ireton, *supra* note 1, at 281-82.

184. See U.C.C. § 7-323(8), Official Draft: Text and Comments Edition (1949), reprinted in 8 U.C.C. DRAFTS 131 (E. Kelly ed., 1984).

185. See Letter from Robert H. Brown, Assistant Vice-Pres., Bankers Trust Company, to Herbert F. Goodrich (May 14, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

186. Gilmore, *supra* note 133, quoted in Rapson, *supra* note 89, at 677.

five stages:

1. The initial responses to the 1949 Draft, including the American Bar Association's initial report on the Code and the drafter's response in 1950.<sup>187</sup>

2. The American Bar Association's committee meeting of January 13, 1951<sup>188</sup> and the responsive meeting of the Enlarged Editorial Board on January 27 and 28.<sup>189</sup>

3. The Annual Meeting of the ALI and NCC in May, 1951.<sup>190</sup>

4. The ALI/NCC Joint Session of September 15, 1951.<sup>191</sup>

5. The referral of the Code to NYLRC in February of 1953 and the response to the NYLRC process.

The most important exception to the above process was the drafting of article 4. In response to vigorous opposition by the banking industry, the ALI and the NCC decided to drop article 4 in May of 1951.<sup>192</sup> Malcolm then took it upon himself to redraft article 4 in the summer of 1951. His version, not surprisingly pro-bank, inspired a rebellion by Gilmore and Mentschikoff, with Schnader trying to silence this dissent. In April of 1952, a compromise was reached which satisfied

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187. See Resolutions adopted at meeting of the Council of the Section of Corporation, Banking, and Business Law of the American Bar Association, Washington, D.C. (May 16, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) [hereinafter Resolutions (May 16, 1950)]; Report of the Committee on the Proposed Commercial Code, Llewellyn Papers, J.XII.1.g (1950) (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review) [hereinafter Report (1950)]. See generally Walter Malcolm, *The Proposed Commercial Code*, 7 BUS. LAW. 113 (1951); A.L.I./N.C.C. Consideration, *supra* note 71; Minutes of the Joint Editorial Board Meeting 1, 1-3, Llewellyn Papers, J.XII.e.f. (June 19, 1950) (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review); American Law Institute & The National Conference of Commissioners on Uniform State Laws, Transcript of Discussion on the Uniform Commercial Code 22, 22-40, Llewellyn Papers, J.XII.1.i (May 19, 1950) (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

188. See American Bar Association Meeting, *supra* note 72.

189. See generally Enlarged Editorial Board, *supra* note 4.

190. ALI/NCC, Transcript of Proceedings at the Annual Meeting of the ALI in Joint Session with the NCC, Llewellyn Papers, J.XIII.1.d (May 16-18, 1951) (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

191. See NCC/ALI, Transcript of the Proceeding of the Joint Session between A.L.I./N.C.C. (Sept. 15, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

192. See Meeting of the Enlarged Editorial Board (May 15, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).



Gilmore.

Some controversial sections survived this process, for example, section 2-302 and objective good faith in article 3.<sup>193</sup>

A micro-analysis of each Code section in our period would be tedious and unintelligible. I will focus on those sections, set out above, that were the focus of controversy. All of these sections would have restricted freedom of contract by providing for legislative, judicial, or trade regulation of commercial transactions.

### 1. *Contract Law.*

a. *Mandatory or Permissive.* The May 1949 Code provided:

Section 1-108 Mandatory Rules of This Act Not Subject to Modification by Agreement

The rules enunciated in this Act are mandatory and may not be waived or modified by agreement unless the rule is qualified by the words "unless otherwise agreed" or their equivalent.<sup>194</sup>

This section drew much protest and was changed in 1951 to the present system in which the presumption is that all sections are subject to agreement. It is, however, hard to say what difference the change made. Many sections in 1949 did say "unless otherwise agreed" and other sections, such as the warranty and damages provisions, had specific sections (as they do in today's U.C.C.) regulating contractual modification.

Of course, one can only speculate as to how courts would have interpreted a statute which was never enacted. The "mandatory if not stated to be permissive" rule, however, may have made a difference in certain sections. Under the 1949 version of section 2-207, for example, additional terms would become part of the contract.<sup>195</sup> If the section was mandatory, a

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193. The latter finally died in the NYLRC process, only to reappear in the Code in the 1990s. See U.C.C. § 3-103(4) (1991).

194. U.C.C. § 1-107, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 43 (E. Kelly ed., 1984). Since the section was renumbered to 1-107 soon after, it will be referred to as 1-107.

195. Where either a definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time states terms

merchant could not contract out of having the additional proposals become part of the contract. Similarly, section 2-508, "Cure," would be mandatory. A buyer could not contract out of the seller's right to cure. Another example was section 1-208, which then restricted the right of a creditor to "accelerate" a debt; i.e., make it immediately due and payable and thus being able take control of the collateral for the debt.<sup>196</sup>

Mr. Milton P. Kupfer, a practicing attorney, pointed out that section 1-208 read in conjunction with section 1-107 would require that

no holder of collateral would be at liberty to enforce the right to liquidate at will according to the terms that he put into his contract, except under the restrictions of 1-208—in other words, that a provision in the contract that the holder of collateral, whether it be a bank, a stock exchange house, or any other holder, would not be at liberty to liquidate his collateral for any reason or no reason.<sup>197</sup>

This would be wrong, according to Mr. Kupfer:

I have in mind the situation that confronted the stock exchange houses in the hectic days of October, 1929, where they had to enforce the terms of the customary and usual customers' agreement that permitted them to demand payment of the debit balance, and then for any reason—or for no reason, if you please—liquidate the collateral if they felt themselves unsecured.<sup>198</sup>

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additional to those offered or agreed upon "(a) the additional terms are to be construed as proposal for modification or addition; and (b) between merchants the additional terms become part of the contract unless they materially alter it or notice of objection to them is given within a reasonable time after they are received." U.C.C. § 2-207, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. Drafts 85 (E. Kelly ed., 1984).

196. Section 1-208, titled "Option to Accelerate At Will," states:

A term providing that one party may accelerate payment or performance or require collateral not on stated contingencies but "at will" or "when he deems himself insure" or in words of similar import means that he has power to do so only in the good faith belief that the prospect of payment or performance is impaired but the burden of establishing lack of good faith is on the party against whom the power is to be exercised.

U.C.C. § 1-208 (March 1, 1950); U.C.C. § 1-208, Official Draft: Text Edition (1949), reprinted in 9 U.C.C. DRAFTS 17 (E. Kelly ed., 1984).

197. A.L.I./N.C.C., Transcript, *supra* note 187, at 31-32.

198. *Id.* at 189. This passage also evidences how much of the Uniform

The drafters probably *did* intend to prevent liquidation of collateral for no reason. The mandatory section would have prevented such individual contracting out of the Code provisions. In any case, the objection to section 1-107 focused more on its symbolic significance of being against freedom of contract rather than any of its specific applications. Malcolm, for example, objected that section 1-107 would stifle the creative spirit of free enterprise:

Without appearing to wax eloquent, to me, two of the greatest virtues of the Anglo-Saxon legal system as well as the free enterprise economic system are the ability of these systems to adjust to change and thus to encourage, rather than discourage, dynamic forces in society. Assuming all the possible virtues in the Code, I think there is a very real danger that the Code system could materially injure these attributes. Under 1-107 as presently written I believe the Code *would* injure them. Under the proposed revision of 1-107 I think such danger is materially reduced, if not completely eliminated.<sup>199</sup>

In May of 1950, the Council of the Section of Corporation, Banking and Business Law of the American Bar Association requested that the adoption of the Code be postponed,<sup>200</sup> particularly criticizing the "mandatory unless permitted" section.<sup>201</sup>

Llewellyn defended section 1-107 at the Joint ALI/NCC Meeting which took place two days after the ABA report. He presented the problem as a technical drafting one: a statute could either say that the rules are mandatory unless they

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Commercial Code was written in response to the experience of the Great Depression, which was in the memories of the drafters. In my *Between-the-Wars Social Thought*, I argue that, "Thus, the entire contractual framework of Article 2, including its rejection of formal doctrines which made contracting difficult, and provisions such as cover that keep contracts alive, were responses to the problems created by the Depression." Kamp, *supra* note 25, at 390.

199. Letter from Walter Malcolm to Soia Mentschikoff (Oct. 31, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

200. See Resolutions (May 16, 1950), *supra* note 187, at 7.

201.

By way of disapproval, views by a substantial number of individual members of the Section have been expressed to the effect that under Section 1-107, the provisions of the Code are much too rigid, with the result that it will seriously interfere with freedom of contract and the necessary flexible development of commercial practices and mechanisms.

*Id.* at 3.

state that they are subject to agreement or are subject to agreement unless they state they are mandatory.<sup>202</sup> Furthermore, he just did not understand the idea that the section restricted freedom of contract.<sup>203</sup> In the discussion, Malcolm stated that if the Code were changed to permissive, "the chances of the Code being accepted by large groups of people I should think would be materially enhanced."<sup>204</sup> The motion to strike the section lost, so the mandatory provision survived a little longer.<sup>205</sup>

In response to the ALI/NCC position, an ABA report stated that "[r]ecognizing the inherent difficulties in the problem this Committee does not think section 1-107 as presently drawn is a satisfactory solution."<sup>206</sup> Malcolm informed Mentschikoff of the ABA position in October of 1950. He then made the statement that the mandatory section would injure the "dynamic forces in society."<sup>207</sup>

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202. See A.L.I./N.C.C. Consideration, *supra* note 71.

203. "It is difficult for more to see how the discrimination between rules which are subject to contract and rules which are not subject to contract, can possibly be an interference with freedom of contract." *Id.* at 176.

204. *Id.* at 181.

205. The motion had been made by Professor Frederick K. Beutel of the University of Nebraska. He would go on to criticize the mandatory provision in his The Proposed Uniform Commercial Code as a Problem, in *Codification*, 16 L. & CONTEMP. PROBS. 140, 162 (1950). "But for sheer presumptuousness and impossibility of administration Section 1-107 takes all the prizes." *Id.* at 161.

206. A.B.A. Report, *supra* note 47, at 131.

207.

Entirely aside from the matter of reconciliation of views, I urge the amendment of 1-107 along the lines discussed simply to improve the Code and what I believe to be the sound development of law as affected by the Code. Without appearing to wax eloquent, to me, two of the greatest virtues of the Anglo-Saxon legal system as well as the free enterprise economic system are the ability of these systems to adjust to change and thus to encourage, rather than discourage, dynamic forces in society. Assuming all the possible virtues in the Code, I think there is a very real danger that the Code system could materially injure these attributes. Under 1-107 as presently written I believe the Code would injure them. Under the proposed revision of 1-107 I think such danger is materially reduced, if not completely eliminated.

Consequently, I think 1-107 should be revised for these most basic reasons. With due respect, I further believe you are seriously in error in thinking the objection to 1-107 is largely happenstance and now has developed into an emotional issue. On the contrary I believe that the present 1-107 runs counter to instinctive reactions and considered judgments that are basically sound.

Letter from Walter Malcolm to Soia Mentschikoff (October 31, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law

In his letter to Mentschikoff, Malcolm could not make any promises:

Turning to what might be called the political aspects of your question, I certainly cannot commit and I doubt if I can predict the action of the Council on this matter. I will make one or two guesses. The first one is that if 1-107 is not changed the action of the Council is likely to be unfavorable, probably to the Code as a whole. On the other hand if 1-107 is revised along the lines discussed there will still be basic opposition, but reasonable chance of approval.<sup>208</sup>

Malcolm first presented his solution to the problem at the ABA Committee meeting of January 13, 1951. His proposal forms the basis of today's Code sections 1-102(3) and (4):

(3) In construing and applying this Act to effect its purpose the following rules shall apply:

(a) Definitions and formal requirements such as those determining what constitutes a negotiable instrument, a bona fide purchaser, a holder in due course, due negotiation of documents of title and the like are not subject to variation by agreement.

(b) The rights and duties of a third party except as otherwise provided by this Act may not be adversely affected by an agreement to which he is not a party or by which he is not bound by adoption, ratification or the like;

(c) The minimum obligations and warranties prescribed by this Act such as good faith, due diligence, commercial reasonableness, reasonable care *and the like* may not be disclaimed or limited by agreement but the parties may by agreement determine the standards by which the performance of such obligations and warranties is to be measured and such standards shall be conclusive unless they are manifestly unreasonable;

(d) Subject to the foregoing sub-sections and except as otherwise specifically provided in this Act, the individual provisions of this

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Review).

208. *Id.*

Act may be varied by agreement.<sup>209</sup>

Malcolm introduced his proposal to the Enlarged Editorial Board on January 27, 1951. Mentschikoff then indicated that the Reporters were not in opposition to the proposal. Section 1-107 was deleted and section 1-102 was rewritten.<sup>210</sup>

So the Code switched from being mandatory to permissive, making it possible for White and Summers to write: "Finally, most of the Code's provisions are not mandatory. The parties may vary their effect or displace them altogether: freedom of contract is the rule rather than the exception."<sup>211</sup>

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209. A.B.A. Meeting, *supra* note 72, at 4-5.

210. See U.C.C. § 1-102(3), Proposed Final Draft No. 2, Text Edition (1951), reprinted in 12 U.C.C. DRAFTS 43-44 (E. Kelly ed., 1984).

(3) In construing and applying this Act to effect its purposes the following rules shall apply;

(a) Definitions and formal requirements such as those determining what constitutes a negotiable instrument, a bona fide purchase, a holder in due course, due negotiation of documents of title and the like are not subject to variation by agreement;

(b) Except as otherwise provided by this Act the rights and duties of a third party may not be adversely varied by an agreement to which he is not a party or by which he is not bound by adoption, ratification or the like;

(c) The general obligations prescribed by Act such as good faith, due diligence, commercial reasonableness and reasonable care may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable;

(d) Provisions of this Act which are qualified by the words "unless otherwise agreed" or words of similar may be waived or modified by agreement despite the provisions of subsection (c) and the absence of such words contains no negative implication unless the subject matter comes within the foregoing subsections;

(e) Subject to the foregoing subsections and except as otherwise specifically provided in this Act, the effect of provisions of this Act may be varied by agreement;

*Id.*

211. WHITE & SUMMERS, *supra* note 17, at 7.

b. *Trade and Judicial Regulation of Contract.*

(1) *The Interlocking Sections.* The 1949 Code provided for strong trade and judicial regulation of contract, based on a set of interlocking sections. These were:

1. Section 1-201(2), defining agreement as being formed by language and the usage of trade.<sup>212</sup>

2. Section 1-201(16), defining good faith in terms of reasonable commercial standards. The pertinent comment states that the court can "inquire as to whether a particular commercial standard is in fact reasonable."<sup>213</sup>

3. Section 1-203. "Every contract within this Act imposes an obligation of good faith in its performance."<sup>214</sup>

4. Section 1-205. This was (and is) a complex section which attempted to regulate the relationship between the explicit terms of an agreement, course of dealing, and usage of trade.<sup>215</sup> Section 1-205(3) provided that merchants were directly bound by usages of trade. The comment states that usages of trade are to be seen as *prima facie* reasonable, but that courts can police them if the market is dominated by sellers or buyers in a manner "so unfair to be unreasonable."<sup>216</sup>

5. Section 2-302, unconscionability, is explained by

212. U.C.C. § 1-201(2), Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 44 (E. Kelly ed., 1984).

213. U.C.C. § 1-201, cmt. 18, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 49 (E. Kelly ed., 1984).

214. U.C.C. § 1-203, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 52 (E. Kelly ed., 1984).

215. U.C.C. § 1-205, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 53-54 (E. Kelly ed., 1984).

216. U.C.C. § 1-205, cmt. 6, Official Draft: Text and Comments Edition (1949); reprinted in 7 U.C.C. DRAFTS 56 (E. Kelly ed., 1984). The NYLRC implemented the present system in which usage of trade works through the contract language: "A course of dealing between parties and any usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware give particular meaning to and supplement or qualify terms of an agreement." U.C.C. § 1-205(3) (1999). The pertinent comment explains:

This Act deals with "usage of trade" as a factor in reaching the commercial meaning of the agreement which the parties have made.

The language used is to be interpreted as meaning what it may fairly be expected to mean to parties involved in the particular commercial transaction in a given locality or in a given vocation or trade.

U.C.C. § 1-205, cmt. 4, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 55 (E. Kelly ed., 1984). No longer does usage of trade directly regulate contract; rather, it forms the context in which the language is to be interpreted.

usages of trade. The comments state that the contract has to be in "reasonably fair form."

6. Sections 2-720 and 2-721, on liquidation, limitations, and consequential damages,<sup>217</sup> provide for changes in the remedy sections of the Code "only to an amount which is reasonable." Parties may limit consequential damages, but not in an "unfair or unreasonable manner."

Thus, the judge and the trade had the tools to regulate commercial contracts. The judge could police contracts for reasonableness under the unconscionability and damages sections, and police trade usage under section 1-201(16) and section 1-205. The trade could set standards of commercial decency under sections 1-201(16) and 1-205 (good faith), and the definition of agreement, section 1-201(2). Individual contracting was to be subject to trade and judicial supervision. The writer of a law review comment in 1950 realized that the unconscionability section "would make extensive judicial policing possible" and that the Code's approach might "cause notions of fair exchange to replace ideals of freedom of contract."<sup>218</sup>

Both judicial and trade regulation were long-standing programs of Llewellyn. To him, a judge should engage in the "Grand Style" of judging, in which the court's role is "to resolve the doubt according to wisdom, justice and situation sense within the leeways accorded by the authoritative sources."<sup>219</sup> Under the "Grand Style" of jurisprudence, courts should use their freedom to decide cases justly. The "Code was drafted in the expectation that it would be interpreted by common law trained lawyers and judges and in the hope that they would adopt 'the Grand Style' in their approach to it."<sup>220</sup> The U.C.C. was written with "faith in the court's ability to judge wisely whenever it understands the base lines for judgment."<sup>221</sup> Certainly the 1949 Code gave the judge ample power to police the reasonableness of trade usages, contract provisions, and remedy limitations.

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217. U.C.C. §§ 2-720, 2-721, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 267-69 (E. Kelly ed., 1984).

218. Comment, *Policing Contracts Under the Commercial Code*, 18 U. CHI. L. REV. 146, 150-53 (1950).

219. WILLIAM TWINING, KARL LLEWELLYN AND THE REALIST MOVEMENT 213 (1973).

220. *Id.* at 312.

221. *Id.* at 340; see also SOIA MENTSCHIKOFF, *COMMERCIAL TRANSACTIONS, CASES, AND MATERIALS* 7 (1970).



Llewellyn set out what he was trying to accomplish by his reformulation of contract law in a document entitled "Introductory Comments" or "General Comment on Parts II and III" (General Comment). The General Comment appeared in various forms from 1944 to 1948 but never became part of an official draft.<sup>222</sup>

Language about the Code being interpreted to yield "reasonableness" pervades the General Comment. "Reasonableness" is read into time and method of inspection teams or as to facilities to be provided for receiving delivery."<sup>223</sup> Llewellyn stated that "[e]xpress terms shall dominate only when such construction is reasonable."<sup>224</sup> He stressed "[t]he principle of reasonable construction and against surprise,"<sup>225</sup> and added, "This Act protects only the reasonable action and reasonable expectations of both parties."<sup>226</sup> Thus the courts have the "power and duty . . . to police against the unbalanced and the unreasonable."<sup>227</sup>

The trade through establishing custom and usage would also regulate contract. Llewellyn's emphasis on the importance of applying trade norms to regulate commercial transactions was possibly the most important of his goals for commercial law.<sup>228</sup> For a variety of reasons, it was crucial that a merchant's contract and conduct be subject to good usages of trade. Section 1-201(16), which defined good faith in terms of reasonable commercial standards, and section 1-205(3), which bound merchants to usages of trade, together imposed commercial norms on all commercial transactions.

222. See, e.g., Karl Llewellyn, Introductory Comment to Parts II and III, Formation and Construction, Llewellyn Papers, J.IX.2.a (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

223. *Id.*

224. *Id.*

225. *Id.*

226. *Id.*

227.

However, the insistence of the courts on the power and duty of the law to police against the unbalanced and unreasonable remains as sound in regard to "rules" and standard contract clauses as it does in regard to non-codified usages of trade and the basic principle of this Act against surprise and unconscionability contained in Section 2-6 (S 23) and discussed in paragraphs 7 and 8 above, recognizes this power explicitly in the case of contract terms and a fortiori in the case of non-codified usage.

*Id.* at 37.

228. See generally Kamp, *supra* notes 25, 57.

(2) *Unconscionability.*

(a) *The Version of Spring 1950.* The unconscionability section, which had started as a section regulating form contracts on the basis of reasonableness, changed again in Spring of 1950. Explicitly giving the courts power to reform contracts, it called forth criticism from the bar. In response, the drafters limited its powers and in so doing turned away from the original conception of Llewellyn. Today's section, which has caused so much commentary and controversy, is merely a remnant of what was a much more powerful and meaningful regulatory system.<sup>229</sup>

The practicing bar did not like unconscionability because it interfered with freedom of contract, gave too much power to judges to rewrite contracts, and made the enforcement of contracts too indeterminate. In fact, the ABA in 1951 almost decided to oppose any unconscionability clause.<sup>230</sup>

The drafters made changes to both the text and the comment to section 2-302 in Spring of 1950. The 1949 draft had provided that the court could "substitute for the stricken clause such provision[s] as would be implied under this article if the stricken clause had never existed."<sup>231</sup> At the May, 1950, meeting, Llewellyn reported that "Section 2-302 has met heavy fire primarily directed at the word "substitute" in line 4. Apparently the conception of a court substituting a clause for one which is written is a shocking conception."<sup>232</sup> The "substitution" language was stricken and the section read:

"If the court finds the contract or any clause of the contract to be unconscionable, it may refuse to enforce the contract or strike any unconscionable clauses and enforce the contract as if the stricken clause had never existed."<sup>233</sup>

The drafters also changed the comment to section 2-302.

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229. White and Summers devote 28 pages to the concept and state that their chapter is only an attempt, "The task demands a book of its own." WHITE & SUMMERS, *supra* note 6, at 132.

230. A motion to strike in the A.B.A.'s U.C.C. Committee lost by a tie vote, Enlarged Editorial Board *supra* note 4, at 196.

231. U.C.C. § 2-302(1), Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 94 (E. Kelly ed., 1984).

232. Consideration of Proposed Final Draft of the Uniform Commercial Code 306 (May 18, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

233. *Id.*

That of 1949 had spoken in terms of *unreasonableness*: "This section is intended to apply to the field of sales the equity courts' ancient policy of policing contracts for unconscionability or unreasonableness."<sup>234</sup> In May of 1950, it read: "This section is intended to make it possible for the courts to police explicitly against the contracts or clauses which they find to be unconscionable."<sup>235</sup> The shift from unreasonable to unconscionable narrowed the power of the courts to police contracts.

Furthermore, "superior bargaining power" was not to be a factor:

The basic test is whether in the light of the general commercial background and the commercial needs of the particular trade or case the clauses involved are so one-sided as not to be expected to be included in the agreement. The principal [sic] is one of the prevention of unfair surprises and not of disturbance of allocation of risks because of superior bargaining power.<sup>236</sup>

By rejecting unequal bargaining as a factor, the comment turned away from one of Llewellyn's primary goals of the law: achieving fairness by policing unequal bargains. It also specifically rejected a goal of the prior drafts—judicial regulation of unequal bargaining.

There was no discussion of this change in the ALI's annual meetings in 1949 or 1950. Perhaps the change was made in response to a letter sent to the ALI by Hiram Thomas in 1949. In it he points out that the term "unconscionable" has a legal meaning "which is far different from what the Comment says." The comment "authorizes the court to continue the 'ancient policy of policing contracts for unconscionability or *unreasonableness*,' and it apparently would make the various sections of the Act standards of reasonableness."<sup>237</sup> In a second memo he observed: "There seems to be a tendency in various sections and the comment to prevent one of the contracting parties from making a

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234. U.C.C. § 2-302, cmt. 1, Official Draft: Text and Comments Edition (1949), reprinted in 7 U.C.C. DRAFTS 95 (E. Kelly ed., 1984).

235. U.C.C. § 2-302, cmt. 1, Official Draft: Text and Comments Edition (Spring 1950), reprinted in 10 U.C.C. DRAFTS 117 (E. Kelly ed., 1984).

236. *Id.*

237. Memorandum from Hiram Thomas on the May 1949 Draft of the Commercial Code, to the American Law Institute (May 1949) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) (discussing article 2, Sales § 2-302).

bargain more advantageous to him than to the other party even when it is done honestly.”<sup>238</sup>

The deletion of “unreasonable” and the addition of “not of disturbance of allocation of risks because of superior bargaining power” could have been responses to meet Thomas’ objections. Maybe the phrase was not intended to reject the Code’s initial concern with equal bargaining power, but merely to point out that a judge should not invalidate a contract because one party got a better deal than another.

Read literally, however, the comment states that equal bargaining power is not a concern of unconscionability.<sup>239</sup> The changes in the comments represent the final failure of an effort to include a general requirement of equal bargaining in commercial law. The ban on unequal bargaining at the extreme continued under section 2-302, but the idea that a commercial law should police contracts for equal bargaining died with this change in the comment.

The idea of equal bargaining had been a key concept of the Code and a prime concern of Llewellyn, indeed of many economic and social thinkers. In several writings, Llewellyn insisted on its importance. In his 1930 sales casebook, he stated, “Note that if the contract form has become really standardized among competitors, or if the other bargaining party is at a bargaining disadvantage (the small apartment renter, the factory laborer, the shipper of goods by railroad, the purchaser of steel or of insurance), we have something approaching legislation by one group on its relations with another group.”<sup>240</sup> In 1938, Llewellyn again was concerned with the “little man.”<sup>241</sup>

238. Memorandum from Hiram Thomas on the May 1949 Draft of the Commercial Code, to the American Law Institute (August 1949) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) (discussing paramount public safety).

239. This change contradicted the comment to section 1-205 which in spring of 1950 still spoke in terms of “domination” by sellers or buyers. “But in a market dominated by buyers or by sellers as the case may be, practices can become standard which are so unfair as to be unreasonable, and that aspect of the anciently established policing of usage by the courts is continued.” U.C.C. § 1-205, cmt. 6, U.C.C. Proposed Final Draft (1950), reprinted in 10 U.C.C. DRAFTS 72 (E. Kelly ed., 1984).

240. KARL N. LLEWELLYN, CASES AND MATERIALS ON THE LAW OF SALES 51 (1930).

241. See Karl N. Llewellyn, *Through Title to Contract and a Bit Beyond*, 15 N.Y.U. L.Q. 183, 185 n.47 (1938) (“Leaving the matter to clauses does result, however, in penalizing little men where bigger outfits bargain out; and this is not wise lawmaking wherever the level either of factual expectation or of commercial

Llewellyn's desire for equal bargaining derived from the views of the institutional economists, whose thought formed the basis of Llewellyn's economic assumptions. These economists saw equal bargaining as a central concern.<sup>242</sup> The institutional economist, John Commons, a major influence on Llewellyn,<sup>243</sup> saw bargaining outcomes as "better" if they derived from equal bargaining.

An agreement was considered by Commons to be truly "fair" only if arrived at *solely* through persuasion (assuming no fraud is involved) or, alternatively, if coercion is absent. By the term coercion Commons meant more than the threat of violence, or duress. An individual's "willingness" to agree to another's terms is profoundly influenced by his/her power to wait for the other to give in. The one with larger resources can generally wait longer than the other, thereby using his/her *power* (to wait) to favorably influence the terms of exchange. This type of "economic coercion" was regarded by Commons, like physical coercion, to be "unfair." "Fair" therefore implies: "as resulting from bargaining between parties with equal physical and economic power." Accordingly, outcomes will be "better" as they come progressively closer to the outcomes that *would* obtain if everyone actually possessed equal power to wait for the other to give in, that is, equal bargaining power. The same interpretation of "better" would obviously apply equally to the working rules that shape those outcomes.<sup>244</sup>

Equal bargaining would promote cooperative behavior and effective laws:

Commons believed two principles were of special import to the development of a process that would actually function to promote reasonable value. The first reflected his belief that without willing cooperation, no law is likely to be effective. It was Commons's conclusion, based on his reading of American industrial and labor history, that when genuine bargaining between *equals* takes place, individuals are far more likely to think of the agreed-upon-rules as "fair," and therefore to cooperate with them, than when rules are handed down "from above." In other words, rules arrived at

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decency is such as to make the clauses normally desirable.").

242. See Kamp, *supra* note 25, at 368-70.

243. Llewellyn listed Commons as an influence in 1925 in his first work, *The Effect of Legal Institutions Upon Economics*, 15 AM. ECON. REV. 665, 665 n.1 (1925) [hereinafter *Effect*], and in his last, *THE COMMON LAW TRADITION DECIDING APPEALS* 14, 218 (1960).

244. Yngve Ramstad, *From Desideratum to Historical Achievement: John R. Commons's Reasonable Value and the "Negotiated Economy" of Denmark*, 25 J. ECON. ISSUES 431, 434 (1991).

through a process approximately, as closely as possible, equalitarian collective bargaining were seen by Commons as more likely to elicit cooperation and thus to be adhered to, than rules mandating compulsory "social responsibility" as determined by legislators or "experts."<sup>245</sup>

Commons's advocacy of regulatory commissions to be "charged with the task of formulating the general contours of 'reasonable' working rules, that is, those representing a genuine 'compromise' between the conflicting interests, and to resolve disputes arising out of their application to specific circumstances."<sup>246</sup>

Commons's proposal resembles the proposed Revised Uniform Sales Acts of 1940 and 1941 which provided for judges working in conjunction with juries of merchants to determine reasonable and good commercial practices. Llewellyn's Commercial Code was to substitute a system of equally-bargained-for trade rules, with supervision by judges and merchant tribunals, for a system of individual, unregulated bargaining.

Section 1-C of 1941 Draft evidenced Llewellyn's concerns. Although the section was withdrawn, it was the ancestor of section 2-302.<sup>247</sup> Under section 1-C, the judge was to determine if a "bloc" of provisions in a form contract was "fair and balanced" or not.

1. If the bloc as a whole is shown affirmatively to work a displacement of the Act in an unfair and unbalanced fashion not required by the circumstances of the trade, then the party wanting to apply a provision must show the other party intended the provision to displace or modify the relevant provision of this Act.<sup>248</sup>

2. On the other hand, if the bloc as a whole is "shown affirmatively to work a fair and balanced allocation of rights and duties in view of the circumstances of the trade, its incorporation into the particularized terms of the bargain is

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245. *Id.*

246. *Id.* at 435.

247. See Arthur Allen Leff, *Unconscionability and the Code—the Emperor's New Clause*, 115 U. PA. L. REV. 485 (1967).

248. Proposed Revised Uniform Sales Act § 1-C(1)(d) (1941), reprinted in 1 U.C.C. CONFIDENTIAL DRAFTS 18-21 (E. Kelly and A. Puckett eds., 1995). The withdrawn § 1-C can be found in a letter from Karl N. Llewellyn to Underhill Moore (Sept. 5, 1941) (on file with the Yale Law Library, and the Buffalo Law Review).

presumed.<sup>249</sup>

In the General Comment discussed above, Llewellyn sets out two guides to determine "whether a set of standard provisions call for sympathetic and expansive application or for a hostile attitude."<sup>250</sup> "The first index is found in the provisions of this Act itself."<sup>251</sup> The Act's "prime characteristic is a *balanced* adjustment of the rights and interests of both the buyer and the seller."<sup>252</sup> The second index is the origin of the rules as standard form. The comment distinguishes between "balanced contracts and those contracts built up wholly from and for one side of the bargain."<sup>253</sup>

The rejection in the unconscionability comment of any concern with equal bargaining power jettisoned this long-time goal of Karl Llewellyn for commercial law. It also drained much of the meaning from section 2-302. Prior to the change, one could judge any deal from the standpoint of the key question posited by the institutional economists: what kind of an agreement would be made by two parties with an equal bargaining power? This would have been an objective standard to judge unconscionability. Instead, as pointed out by Professor Leff's definitive article, *Unconscionability and the Code—The Emperor's New Clause*, unconscionability became to be defined in terms of itself.

(b) *The 1951 Changes in Section 2-302.* The next change in unconscionability came in the Enlarged Editorial Board Meeting of late January, 1951. There Malcolm reported that the ABA had concluded that unconscionability should be retained within narrower limits, after Section 2-302 had narrowly survived a motion to strike.

Mr. Bernard Broeker, who represented Bethlehem Steel,<sup>254</sup> pointed out that the problem was in the comments:

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249. R.U.S.A. § 1-C(2)(a), Proposed Revised Uniform Sales Act (1941), reprinted in 1 U.C.C. CONFIDENTIAL DRAFTS 18-21 (E. Kelly and A. Puckett eds., 1995).

250. *Id.* at 38.

251. *Id.*

252. *Id.*

253. *Id.* at 40.

254. See ABA Meeting, *supra* note 72, at 1. Note that "Broeker" is there spelled "Brocker." *Id.* Bernard D. Broeker was the Assistant Secretary and Assistant to Vice President, Bethlehem Steel Company. See Bernard D. Broeker, *Articles 2 and 6: Sales and Bulk Transactions*, 15 U. PITT. L. REV. 541 (1954).

"Unconscionable" is certainly not "unreasonable" or "unfair." And not only here but in other Sections of this Code, the Comments make it clear that the word "unconscionable" means "unreasonable." . . . I see no reason why I should not be allowed to make an unreasonable contract. . . . Quite often I know each party to a contract thinks there are some unreasonable provisions in it, but it is the best deal he can make.<sup>255</sup>

He referred also to a comment of section 2-721, which "talks about good faith, decent commercial practice, and reasonable care, which is to me a clear indication that the reporters are using the word 'unconscionable' as meaning nothing more than 'unreasonable.'"<sup>256</sup> These comments were later changed, to shift the Code from regulating on the basis of "unreasonable" to "unconscionable."

Then Professor Robert Braucher made his contribution to the unconscionability section, which is now section 2-302(2).<sup>257</sup> That sub-section provides for the introduction of evidence as to the commercial purpose and setting of challenged contract language. Llewellyn loved Braucher's proposal.<sup>258</sup>

Professor Leff questions whether this sub-section gives any help in a typical unconscionability case and creates a few hilarious scenarios in which the slick merchant testifies that the practice is to "make money."<sup>259</sup> Leff notes that what

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255. See Enlarged Editorial Board, *supra* note 4, at 172.

256. *Id.* at 173.

257. "When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable, the court may afford the parties an opportunity to present evidence as to its commercial setting, purpose, and effect as used." *Id.* at 173. Robert Braucher was at that time a professor of law at Harvard; later he became a Justice of the Supreme Judicial Court of Massachusetts. See BRAUCHER & RIEGERT, *supra* note 17, at iii.

258. See Enlarged Editorial Board, *supra* note 4, at 174 ("The Drafting Staff will welcome that, will welcome such a subsection. It clarifies definitely the meaning of the Section and addresses the court's attention to vitally important stuff.").

259.

Counsel: What is the effect of this provision?

Seller: It's hard to tell, but we think it helps a little.

Counsel: Helps do what?

Seller: Helps make more money.

Counsel: What about commercial setting? Does everybody use this clause?

Seller: How would I know? What am I, some kind of conspiracy? I guess whoever can use it uses it.

Counsel: What would happen if you didn't use such a provision in your contract?



Braucher had in mind was "testimony on the technical business requirements of particular business complexes" which would help judges "to regulate the agreements within industries on an *ad hoc* basis."<sup>260</sup> Braucher indeed justifies his proposal by explaining that if a court can ask whether a trade has regulated itself properly or whether a form contract used by an industry is unconscionable, the court should look at the particular circumstances, which may reveal that a seemingly unconscionable provision "may not be in the light of the conditions in the trade."<sup>261</sup>

Braucher and Llewellyn differ from Leff in that they saw unconscionability as a device to regulate *group* or *mass* contracting—in trade agreements or form contracts. Leff sees section 2-301 in terms of *individual* contracting. Where individual A has bilked B it makes no sense to investigate "commercial setting, purpose, and effect," but it does if section 2-302's main purpose was to regulate contracts made on a mass basis, through standardized forms or standardized trade agreements. It is this difference in conception which is a root cause of the difficulty of interpretation of section 2-302. It is yet another irony of the Code that the drafters' main purpose for section 2-302, the regulation of commercial contracts *en masse*, is seen to be a side issue by commentators and the courts.<sup>262</sup>

(c) *The Change in the Comments: "Unreasonable" to "Unconscionable."* In 1950, the comments encouraged courts to police trade usage, contract language, and commercial dealing for reasonableness and decency. The intent was to create a "kinder, gentler" commercial world.<sup>263</sup> Section 1-

Seller: I'd make less money.

Counsel: What if you sold only to people who could afford it?

Seller: I'd make much less money.

Counsel: Doesn't your conscience bother you?

Seller: Wha?"

Leff, *supra* note 247, at 545.

260. *Id.* at 543.

261. See Enlarged Editorial Board, *supra* note 4, at 174.

262. See, e.g., WHITE AND SUMMERS, *supra* note 6, at 155 ("As we remarked earlier, courts have not generally been solicitous of business persons in the name of unconscionability.").

263. Section 1-203, comment 1, stated, "This Act adopts the principles of those cases which see a commercial contract not as an 'arm's-length' adversary venture, but as a venture of material interest, when successful, and as involving due regard for commercial decencies when an expected favorable outcome fails." U.C.C. § 1-

205, "Course of Dealing and Usage of Trade," explicitly authorized judges to police one-sided trade usages,<sup>264</sup> and the comment of section 2-721 equated "unfair and unreasonable" with "unconscionable."<sup>265</sup>

The late 1953 version of the U.C.C. was the last one which contained comments until that of 1956.<sup>266</sup> The comments of late 1953, the last version before the NYLRC hearings, gave less scope for the court to regulate the "reasonableness" of commercial contracts. The change in the statute from objective to subjective good faith meant that applicable comment no longer could talk of "commercial decency." Section 1-205's comment still spoke in terms of "unfair" and "unreasonable,"<sup>267</sup> while the comment under section 2-719 substituted "unconscionable" for "unreasonable."<sup>268</sup>

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203, cmt. 1, U.C.C. Proposed Final Draft (1950), *reprinted in* 10 U.C.C. DRAFTS 68 (E. Kelly ed., 1984). The Comment to the definition of good faith pointed out that merchants "must also conform to *reasonable* commercial standards," which were not "the lax standards sometimes permitted to grow up but is intended to permit the court to inquire as to whether the commercial standard is in fact *reasonable*." U.C.C. § 1-201(18), cmt. 18, U.C.C. Proposed Final Draft (1950), *reprinted in* 10 U.C.C. DRAFTS 64 (E. Kelly ed., 1984) (emphasis added).

264. "But in a market dominated by buyers or by sellers as the case may be, practices can become standard which are so *unfair* as to become *unreasonable*, and that aspect of the anciently established policing of usage by the courts is continued." U.C.C. § 1-205, cmt. 6, U.C.C. Proposed Final Draft (1950), *reprinted in* 10 U.C.C. DRAFTS 72 (E. Kelly ed., 1984) (emphasis added).

265. "Thus any clause purporting to modify or limit the remedial provisions of this Article in an unfair or unreasonable manner is subject to deletion as unconscionable and in that event the remedies made available by this Article one applicable as if the stricken clause had never existed." U.C.C. § 2-721, cmt. 1, U.C.C. Proposed Final Draft (1950), *reprinted in* 10 U.C.C. DRAFTS 303 (E. Kelly ed., 1984) (emphasis added).

266. The late 1953 version is entitled, "UNIFORM COMMERCIAL CODE, OFFICIAL DRAFT, TEXT AND COMMENTS EDITION, 1952, WITH CHANGES AND MODIFICATIONS APPROVED BY THE ENLARGED EDITORIAL BOARD AT MEETINGS HELD ON DECEMBER 29, 1952, FEBRUARY 16, 1953, MAY 21, 1953 AND DECEMBER 11, 1953." U.C.C. Official Draft: Text and Comments Edition (1953), *reprinted in* 16 U.C.C. DRAFTS 1 (E. Kelly ed., 1984).

267. Now the comment speaks in terms of "unconscionable" and "dishonest" and leaves out "domination" by buyers or sellers. U.C.C. § 1-205 cmt.6 (1995). "But the anciently established policing of usage by the court is continued to the extent necessary to cope with the situation arising if an *unconscionable* or *dishonest* practice should become standard." *Id.* (emphasis added).

268. "Thus any clause purporting to modify or limit the remedial provisions of this Article in an *unconscionable* manner is subject to deletion." U.C.C. § 2-719, cmt. 1, U.C.C. Official Draft: Text and Comments Edition (1953), *reprinted in* 16 U.C.C. DRAFTS 289 (E. Kelly ed., 1984) (emphasis added).

Even though after these changes there was less room for judicial oversight, the Code was still criticized for giving too much power to the courts.<sup>269</sup>

## 2. *The Change From Objective to Subjective Good Faith.*

The 1949 Code provided that good faith was objective, being defined in terms of reasonable commercial standards.<sup>270</sup> This was changed to today's version in May of 1951, with good faith being defined as honesty in fact.<sup>271</sup> Articles 2 and 3 retained objective good faith,<sup>272</sup> defined in terms of conformity with trade norms. The change from objective to subjective good faith was another major change which rejected a long-standing goal of Llewellyn's for commercial law, the idea that commercial law should be regulated by "good" merchant practices.

Llewellyn wrote of the necessity of enforcing trade norms against the merchant outlaw in his first article, "The Effect of Legal Institutions Upon Economics."<sup>273</sup> To Llewellyn, law's purpose is to restrain the individual who violates community norms, whether he be the criminal or the contract breaker:

The rules of law against assault come into active play only at the individual margin when passion crosses the threshold of self-control, and come into play socially only with that marginal individual who falls below the standard of self-control commonly developed by early education. For it seems clear that, if the marginal individual were not restrained at least in the bulk of

269. The bankers stated it would "constitute an open invitation to the courts to ignore the provisions of the Code and of commercial agreements whenever their own predilections [sic] tempt them to do so." *Report of Special Committee of American Bankers Ass'n. on Proposed Uniform Commercial Code* 5 (1954), Llewellyn Papers, J. XVI. 1.b. (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

270. U.C.C. § 2-102(16), Official Draft: Text and Comments Edition (May 1949), reprinted in 7 U.C.C. DRAFTS 45 (E. Kelly ed., 1984).

271. U.C.C. § 1-201(19), Proposed Final Draft, No. 2 (Spring 1951), reprinted in 12 U.C.C. DRAFTS 35 (E. Kelly ed., 1984).

272. U.C.C. §§ 2-103(1)(b), 3-302, Proposed Draft, No. 2 (Spring 1951), reprinted in 12 U.C.C. DRAFTS 43, 127 (E. Kelly ed., 1984). Article 3 changed to the subjective good faith standard in 1955. U.C.C. § 3-302(1), U.C.C. Supplement, No. 1 (January 1955), reprinted in 17 U.C.C. DRAFTS 336-37 (E. Kelly ed., 1984). This section was changed recently and is now objective. See U.C.C. § 3-103(4) (1995). Article 3 changed to subjective good faith in 1955. U.C.C. § 3-302(1), U.C.C. Supplement, No. 1 (January 1955), reprinted in 17 U.C.C. DRAFTS 336-37 (E. Kelly ed., 1984). The section was changed recently and now is objective. 1995 U.C.C. § 3-103(4).

273. See *Effect*, *supra* note 243.

cases, either in self-defense or by imitation, laxity in the matter would spread through the group; such is the process of cut-throat competition. So, too, with the enforcement of contract obligation; and this regardless of delays, costs, and occasional acquiescence in the breach of contracts.<sup>274</sup>

Certainly Llewellyn and Mentschikoff kept pushing for including good trade standards in the commercial law. In 1951, he wanted to add "and fair dealings" to section 1-203.<sup>275</sup> Mentschikoff wrote a memo to the NYLRC in 1954 arguing (unsuccessfully) that requiring the observance of reasonable commercial standards for notes was not a new concept but was the actual law of New York.<sup>276</sup>

The U.C.C., with its emphasis on enforcing trade norms, good practice, and commercial decency, can be seen as an attempt to carry on the program of the National Recovery Act after it was declared unconstitutional.<sup>277</sup> The New Deal's first and primary program to end the Depression, the National Recovery Administration, was to establish trade standards and enforce them. The theory held "that overproduction led to lower prices and "chiseling," the lessening of the quality of goods and cheating, which further caused lower wages, decreased demand, overproduction, and finally, lower prices and chiseling again."<sup>278</sup> The NRA was to establish and enforce fair commercial practices.<sup>279</sup>

The NRA failed in part because it was unable to establish codes of fair competition. Business could not agree on what fair competition should be. As stated by Donald R. Brand, "the social consensus necessary for the NRA to succeed simply did not exist."<sup>280</sup>

History repeated itself in the early 1950s, when the lawyers of the American Bar Association resisted Llewellyn's program to police commerce in terms of commercial decency.

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274. *Id.* at 682.

275. *Minutes of Small Editorial Board Meeting Uniform Commercial Code 2* (Nov. 14, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

276. See Memorandum by Professor Soia Mentschikoff Relating to Section 3-302(1)(b) 2 (Aug. 16, 1954) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

277. *United States v. A.L.A. Schechter Poultry Corp.*, 295 U.S. 495 (1935).

278. *Kamp*, *supra* note 25, at 365.

279. BERNARD BELLUSH, *THE FAILURE OF THE NRA* 36-38 (1975).

280. DONALD R. BRAND, *CORPORATISM AND THE RULE OF LAW: A STUDY OF THE NATIONAL RECOVERY ADMINISTRATION* 105 (1988).

In 1950, the ABA Committee in the Proposed Commercial Code published a report critical of the proposed good faith standards.<sup>281</sup> The Report observes:

Prima facie it is reasonable to require good faith in the performance of contracts. However, it is of interest that this provision and certain others in the same vein have produced quite a violent reaction on the part of some businessmen and business lawyers. They say: "Why should the Code draftsmen tell us to be good? Businessmen, or at least most of them, carry on business ethically and did so long before the Code was ever conceived. The Code should not try to prescribe morals."

Undoubtedly the Code draftsmen would reply: "Such a reaction merely evidences oversensitiveness. If a businessman acts honestly and observes reasonable commercial standards he has no cause for worry. We are merely aiming at the businessman who does not."

To this the businessman might reply: "Yes, but it is unwise to prescribe in words such a rigid standard. I do the best I can and I am as honest as the next fellow, but businessmen and business houses are frequently faced with 'strike' suits. If some disgruntled customer does not like what I do I may be faced with a suit where it will be contended that I haven't observed reasonable commercial standards."<sup>282</sup>

The ABA Committee had two problems with including "observance of reasonable commercial standards" in the definition of good faith. The first was the problem of proving what a particular standard would be.

Assuming, however, that within the term there should be added to "honesty" some meaning of "commercial decency" the phrase "observance of reasonable commercial standards" carries with it the implication of usages, customs or practices. If this is true there immediately arises the very difficult problem of *what* usages, customs and practices are those intended to be included in the standard. Any lawyer who has ever attempted to prove what a usage or custom is will immediately recognize how litigious such a standard could grow to be.<sup>283</sup>

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281. See September 1949 Report Developments, *supra* note 47.

282. *Id.* at 16.

283. *Id.* at 18-19.

Llewellyn always assumed that it would be possible to ascertain good trade practices. Practicing lawyers were never as sanguine.

The second problem was that the standards could refer only to the practices of a specific time "and thereby destroy the flexibility absolutely essential to the gradual evolution of commercial practices."<sup>284</sup> The Committee therefore recommended a possible definition: "Good faith means honesty in fact in the conduct or transaction concerned and the absence of trickery, deceit, or improper purpose."<sup>285</sup>

In response, the drafters dropped objective good faith from article 1 in Spring of 1951, while retaining it in part in articles 2 and 3.<sup>286</sup> The result was the present-day anomaly of having differing definitions of good faith depending on the article in today's U.C.C.

The drafters thought that in providing for extensive regulation of contract that they were in tune with the spirit of times. Gilmore wrote in 1948: "Although the political water is doubtful, nothing is less likely than that the future will see a protracted period of unregulated private agreement. . . . What is certain is that a 19th century laissez-faire code, or a code drafted with such an underlying bias, will be far from adequate in an economy which has scrapped laissez-faire principles."<sup>287</sup>

Practicing attorneys, the organized bar, and the affected industries, however, were not as enthusiastic about judicial or trade regulation of commerce. They managed to water down these provisions, enlarging the scope of individual contracting free of such oversight. The oversight provisions that do remain are only remnants of the original system of control.

**3. *The Warranty Provisions.*** The 1949 Code contained a set of provisions concerning what now is called product liability.

In 1949, section 2-318 on warranty beneficiaries provided:

A warranty whether express or implied extends to any natural

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284. *Id.* at 19

285. *Id.*

286. See *supra* notes 271-72 and accompanying text.

287. Grant Gilmore, *On the Difficulties of Codifying Commercial Law*, 57 *YALE L.J.* 1341, 1358 (1948).

person who is in the family or household of the buyer or who is his guest or one whose relationship to him is such as to make it reasonable to expect that such person may use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.<sup>288</sup>

The comment provided that "employees of an industrial consumer are covered."<sup>289</sup>

Section 2-718 provided for impleader by an intermediate seller and its seller.<sup>290</sup> Section 2-719 upset manufacturers the most by providing for a direct action against the prior seller.<sup>291</sup> The comment indicates that the section's purpose in part was to relieve the smaller retailer.<sup>292</sup>

288. U.C.C. § 2-318, Official Draft: Text and Comments Edition (May 1949), *reprinted in* 7 U.C.C. DRAFTS 130-32 (E. Kelly ed., 1984).

289. On the other hand, employees of an industrial consumer are covered and the policy of this article intends that neither the privity concept, nor any gaps in Workmen's Compensation Acts, nor any technical construction of "employment" shall defeat adequate protection under this section. U.C.C. § 2-318, cmt. 2, Official Draft: Text and Comments Edition (May 1949), *reprinted in* 7 U.C.C. DRAFTS 130-32 (E. Kelly ed., 1984).

290. Section 2-718, titled, "Impleader by Buyer; Notice to Defend," provides:

(1) Where a buyer resells and is sued for any breach with regard to which he would have an action over against his seller he may

(a) implead his seller in like manner and with like effect as is or may be provided in the Federal Rules of Civil Procedure; or

(b) give seasonable notice to his seller to come in and defend the action.

(2) Failure of a seller to defend after receiving such notice renders any adverse judgment in the action conclusive against him and makes him liable for all costs of the action including reasonable attorney's fees.

U.C.C. § 2-718, Official Draft: Text and Comments Edition (May 1949), *reprinted in* 7 U.C.C. DRAFTS 265 (E. Kelly ed., 1984).

291. Section 2-719, titled, "Direct Action Against Prior Seller," provides:

Damages for breach of a warranty sustained by the buyer or by any beneficiary to whom the warranty extends (Section 2-318) may be recovered in a direct action against the seller or any person subject to impleader under the preceding section. An action against one warrantor does not of itself bar action against another.

U.C.C. § 2-719, Official Draft: Text and Comments Edition (May 1949), *reprinted in* 7 U.C.C. DRAFTS 266 (E. Kelly ed., 1984).

292. The purposes were:

[t]o give a direct remedy to the party injured so as to avoid any pyramiding of damages and to put the original defense in the hands best equipped to handle it while relieving from actual suit those smaller dealers who might otherwise be put out of business by an injury which they have no adequate means of preventing.

U.C.C. § 2-719, Official Draft: Text and Comments Edition (May 1949), *reprinted in* 7 U.C.C. DRAFTS 266-67 (E. Kelly ed., 1984).

The 1949 version of the direct action had been derived from a much more radical section in the 1940 draft which provided for a 402A-like liability against manufacturers.<sup>293</sup> But even the watered-down liability sections of the 1949 Code were deleted by 1951.

In 1950, there were no major changes, although there was an interesting discussion on products liability at the NCC/ALI meeting. There Llewellyn explained that the purpose of the direct action section was to avoid circuitry of action and provide enforceable judgments for the people who really have been injured. On the other hand, it would increase costs of litigation for manufacturers, although it would not change their legal liability.<sup>294</sup> Mr. Jenner argued that there was no reason or complaint to change the law.<sup>295</sup> He stated that the processors were objecting to "the spelling out of these principles in section 718" and having plaintiff's lawyers sue the processors rather than the retailer "which really he should concentrate on in 95 or 99 out of 100 cases."<sup>296</sup> Jenner stated that in most cases the injury would

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293. Section 28, titled, "(New) Obligation To Consumer Where Defect Is Dangerous," provides:

(1) Where it can reasonably be foreseen that goods, if defective in design, workmanship or material, will in the ordinary use thereof cause danger to person or property, the manufacturer thereof by selling them or delivering them under a contract to sell, when they are so defective in a manner not apparent to the ultimate users thereof, assumes responsibility to any legitimate user thereof who in the course of ordinary use is damaged in person or property by such defects.

(2) "Manufacturer," within the meaning of this section, includes any person who processes or assembles goods which he thereafter markets for ultimate use in consumption, and any person who by brand, tradename or otherwise assumes the position of a manufacturer or supervisor of manufacture.

(3) This section is subject to control by contract under section 18 only in contacts to sell or sale made by a merchant with a merchant and only so far as concerns use by the merchant buyer.

Section 28, Draft of Uniform Sales Act (1940), *reprinted in* 1 U.C.C. DRAFTS 199 (E. Kelly ed., 1984).

294. See A.L.I./N.C.C. Consideration, *supra* note 71, at 324-25.

295.

I have heard no general complaint, either by a law review or Bar Association, that there is in this field any social implication which necessitates our shifting the burden which has existed over a period of, let us say, one hundred years in this field, of having the retailer, the distributor, undertake the defense which in normal course will be properly resting on his shoulders because of intervening events.

*Id.* at 325-26.

296. *Id.* at 326.



involve foodstuffs.<sup>297</sup> Mentschikoff replied that it "would be a tragic mistake to leave these sections out of the Code originally." Schnader, however, predicted a "terrible fight on this section by the manufacturers and processors of perishable goods."<sup>298</sup>

The above discussion reveals two important points about the contemporary thinking on products liability. One, the typical products liability case was seen to be one involving tainted food. The U.C.C. drafters just did not contemplate the range of cases under strict products liability. Second, the thought that a manufacturer should be directly liable to someone injured by its product was a novel one. Williston, for example, pointed out that "Sections 2-718 and 2-719 propose to introduce new law. . . . There are numerous cases opposed to both these sections." He doubted the advisability of the direct action.<sup>299</sup>

The proposals for expanded product liability would die in the first part of that year, leaving the development of product liability to the field of torts.<sup>300</sup>

297. *Id.* at 325.

298.

MENTSCHIKOFF: But it would seem to me personally—and on this I have not consulted my brethren on the Reporting Staff—that it would be a tragic mistake to leave these sections out of the Code originally; that what that would be doing would be saying that because we fear that in some legislatures these sections will be stricken, even though we recognize the importance of this kind of procedure and the actual desirability of it in the commercial law field, we still do not have sufficient courage of our convictions to put it in to inform these legislatures that in that area at least, such practice is desirable.

CHAIRMAN SCHNADER: I would like to ask the Reporter a question, if I may. Do you think there is any state in the United States in which you would not have a terrible fight on this section by the manufacturers and processors of perishable goods?

MISS MENTSCHIKOFF: Yes, sir.

CHAIRMAN SCHNADER: I don't.

MISS MENTSCHIKOFF: Well . . . .

*Id.* at 332.

299. Williston, *supra* note 129, at 587.

300. The disappearance of these sections from the Code has also produced the non-integration of warranty and tort law.

In a classic law review article, Professor Marc Franklin foresaw the coming collision between warranty and contract on the one hand and the torts of strict liability, negligence, fraud and misrepresentation on the other. The collision has produced even more chaos and has had more significant reverberations than Professor Franklin anticipated.

WHITE & SUMMERS, *supra* note 6, at 383-84. See generally Marc Franklin, *When Worlds Collide: Liability Theories and Disclaimers in Defective Products Cases*, 18

At the A.B.A. meeting of January 13, 1951, Broeker, of Bethlehem Steel, and Dierson, representing grocery distributors and drug manufacturers, attacked the Code's product liability sections. Broeker complained that "extension of the tort rule to contract" would be O.K. in case of Coca Cola, but not "to all kinds of goods." Furthermore, liability would extend to the future.<sup>301</sup>

Dierson stated that the food industry would object to sections 2-314, 2-318, 2-718, and 2-719. "The lawyers in the industry think the provisions are very harsh."<sup>302</sup> Malcolm noted that the products liability issue "is the most serious issue that exists." Ireton, the head of ABA Division of Mercantile Law, stated, "Please come in with suggestions. Ultimately we are going to approve this Code. Now let us make it as good a code as we can."<sup>303</sup>

The parameters of the negotiation, therefore, were that the Code was going to be approved but that its provisions were negotiable. The affected industries thus had every incentive to come up with language more favorable to themselves. Ireton directed those concerned: "I think in many

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STAN. L. REV. 974 (1966) (claiming that for the worlds to collide, they first had to be separated, and they were so only in response to the lobbying which omitted direct manufacturers' products liability from the Code).

301. ABA Meeting, *supra* note 72, at 22 ("Example: A manufacturer of railroad cars sells freight car to Pennsylvania Railroad. If a wheel falls off 15 years from now and kills 50 people all they show is the wheel fell off. They don't have to show negligence. You could not even insure against this.")

302.

DIERSON. Food Industry will object to the following: Sec. 2-314, 2-318, 2-718, 2-719. I am not going to give a technical analysis. The lawyers in this industry think the provisions are very harsh. The argument you can insure against the risk does not answer the objection of unfairness. (1) They think this is liability without fault. (2) It creates liability without privity of contract. (3) It is new language. (4) Where the consumer has direct action against the manufacturer we do not glance at facts. *Example*: Jar is broken in transportation—middleman—housewife. This is an area which the manufacturer can't check at all. (5) The word "protection" appears. The consumer should sue the person on the spot. It is social insurance to take away the responsibility from the middleman. Does consumer suffer at the hands of manufacturers? Some years ago Mr. Dunn went into this. A code was worked out. Very fair. Eliminated fraud. The draftsman of this code made changes to take care of difficulties which don't exist. For every case that it litigated in food law 10,000 are settled out of court. There is a great deal of fraud in these cases.

*Id.* at 23-24.

303. *Id.* at 24.

cases the Code has been worked out *ex parte*. Now that you have notice go ahead and work something out."<sup>304</sup>

Two weeks later, on January 27, 1951, the Enlarged Editorial Board met to hear the ABA's concerns. Malcolm reported that Dierson "in the Division of Food, Drug and Cosmetic Law, advises me that with tremendous energy and drive he has been attempting to pull together representatives of the industry and draft specific suggested changes, and has not completed them."<sup>305</sup> Ben Heineman<sup>306</sup> reported that the General Counsel of Sears "did not want the liability, as Sears, the seller at retail, to extend to the members of the family, when the wife or husband purchased, or whatever."<sup>307</sup> Mr. Broeker reiterated his complaints about products liability.<sup>308</sup> He saw no reason to expand to the public at large:

Certainly I do not see any reason at all for saying a manufacturer of an ordinary article of commerce, whether it is steel or railroad cars or adding machines, or anything, why you must put on that manufacturer obligations to people with whom he has no relations, people whom he never knew.<sup>309</sup>

Gilmore suggested that section 2-318 be revised to limit the warranty to "any person who is in the family or household of a buyer or who is a natural person."<sup>310</sup> Broeker objected to the Code's making issues of liability into questions of fact and said the very reason manufacturers exclude consequential damages "is that the issue of fact is so difficult to try and so expensive and time consuming that we just refuse to be put in a position of having to try it."<sup>311</sup> Dierson

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304. *Id.* at 25.

305. *Id.* at 81.

306. Ben Heineman went on to be the founder and chairman of Northwest Industries, and a member of the board of directors of several business and civic organizations. WHO'S WHO IN AMERICA 2000, at 2113 (54th ed. 1999).

307. See Enlarged Editorial Board, *supra* note 4, at 163.

308.

There may or may not be reason for making that new law as applied to food products or something like that, but I do not believe there is any reason for extending it to industry generally, particularly, the industry with which I work sells steel. I think this Article puts us in the position where we have got 150 million people that can sue us and there is nothing we can do about it.

*Id.* at 110.

309. *Id.* at 115.

310. *Id.* at 121.

311. *Id.* at 123.

then spoke for the food and drug industry. He first spoke of the problem of fraud in these claims: "[W]e have known that suits are encouraged by quick settlement of insurance companies and that they rapidly create a serious trade evil when they are permitted to be handled in that way."<sup>312</sup>

Also, the fault is usually not that of the manufacturer, but is that of the "intervening distributor or the consumer himself."<sup>313</sup> The consumer is "very, very well protected by National Food and Drug Laws and by those of states and municipalities."<sup>314</sup> Leaving the manufacturer to "the tender mercies of the jury" has "astonished the lawyers who have tried to defend the manufacturer."<sup>315</sup>

Shortly after the January Meeting, the Editorial Board decided to delete sections 2-718 and 2-719.<sup>316</sup> During the first half of March, 1951, counsel for food and drug manufacturers met with Soia Mentschikoff over the warranty provisions.<sup>317</sup> It was agreed that section 2-318 would extend warranties only to "any natural person who is in the family or household of his buyer."<sup>318</sup> The Spring 1951 Draft adopted the proposed language.<sup>319</sup> The comments to section 2-318 adopted in the

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312. *Id.* at 127.

313. *Id.* at 131.

314. *Id.*

315. *Id.* at 132.

316. Letter from J. Randolph Wilson, representing the National Canners Ass'n, to the Hon. Herbert F. Goodrich, Chairman, Editorial Board, *Uniform Commercial Code* (March 15, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review) (noting the Board's decision to delete § 2-718 and § 2-719).

317. Letter from Frank T. Dierson to the Hon. Herbert F. Goodrich, Director, American Law Institute 4 (Mar. 16, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

In conclusion I record the fact that we invited to these conferences counsel for various food and drug manufacturers who are members or representatives of one or more of the following organizations: Division of Food, Drug and Cosmetic Law, Section of Corporation, Banking and Business Law, American Bar Association; Section on Food, Drug and Cosmetic Law, New York State Bar Association; Grocery Manufacturers of America, Inc.; and American Pharmaceutical Manufacturers' Association.

*Id.*

318. *Id.* at 3.

319. Section 2-318, titled, "Third Party Beneficiaries of Warranties Express or Implied," provides:

A seller's warranty whether express or implied extends to any natural person who is in the family or household of his buyer or who is a guest in his home if it is reasonable to expect that such person may use,

1952 Draft, reproduce the recommendations by the National Canners Association. Comments 1 and 2 to section 2-318 of today's Code read almost exactly the same as the Canner's recommendation.<sup>320</sup>

This deal ended the dispute between the manufacturers and the Code drafters. Dierson afterwards wrote John MacDonald, the Executive Secretary of the NYLRC, that "the text and comments of article 2 were adopted in a form

consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.

U.C.C. § 2-318, U.C.C. Proposed Final Draft, No. 2 (Spring 1951), *reprinted in* 12 U.C.C. DRAFTS 64 (E. Kelly ed., 1984).

320. Memorandum, Warranty Provisions—Recommendations by the National Canners Association 8-9 (March 13, 1951), Llewellyn Papers, J. XIII.2.a. (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review); *see* U.C.C. § 2-318, Official Draft. Text and Comments Edition (1952), *reprinted in* 14 U.C.C. DRAFTS 148-49 (E. Kelly ed., 1984). The 1952 Official Draft comments read:

1. The last sentence of this section does not mean that a seller is precluded from excluding or disclaiming a warranty which might otherwise arise in connection with the sale provided such exclusion or modification is permitted by Section 2-316. Nor does that sentence preclude the seller from limiting his own buyer's remedy, or any beneficiary of a warranty under this section, in any manner provided in Sections 2-718 or 2-719. To the extent that the contract of sale contains provisions under which warranties are excluded or modified, or remedies for breach are limited, such provisions are equally operative against beneficiaries of warranties under this section. What this last sentence forbids is exclusion of liability by the seller to the persons to whom the warranties which he has made to his buyer would extend under this section.

2. The purpose of this section is to give the buyer's family, household and guests the benefit of the same warranty which the buyer received in the contract of sale, thereby freeing any such beneficiaries from any technical rules as to "privity." It seeks to accomplish this purpose without any derogation of any right to remedy resting on negligence. It rests primarily upon the merchant-seller's warranty under this Article that the goods sold are merchantable and fit for the ordinary purposes for which such goods are used rather than the warranty of fitness for a particular purpose. Implicit in the section is that any beneficiary of a warranty may bring a direct action for breach of warranty against the seller whose warranty extends to him.

3. This section expressly includes as beneficiaries within its provisions the family, household, and guests of the purchaser. Beyond this, the section is neutral and is not intended to enlarge or restrict the developing case law on whether the seller's warranties, given to his buyer who resells, extend to other persons in the distributive chain.

*Id.*

acceptable to all parties.”<sup>321</sup>

Unfortunately for those represented by Mr. Dierson, the “novel theory of manufacturers’ liability without fault” re-emerged as strict products liability in tort. In retrospect, the results obtained by Dierson were the worst possible for his clients the food and drug industry. If products liability had remained in the Code, its development would have been under the control of the legislatures and subject to lobbying by the manufacturers. Because it was dropped from the Code and left to the courts, it escaped political control. Dierson and his clients won the sales battle but lost the tort war.

#### 4. *Secured Transactions.*

a. *The 1949 Code.* Professor Richard L. Barnes describes differences between articles 2 and 9 in today’s Code in terms of their normative content: “In my view, Article Two is due great deference when it establishes a rule of commercially correct behavior, as in its provisions on unconscionability and disclaimers of warranty. By contrast,

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321. The letter reads:

I have received a report that I, and those for whom I have spoken, are in opposition to the sales article of this Code. This is untrue, and I desire to clarify any misunderstanding.

Representing Mr. Charles Wesley Dunn, and in behalf of the Food, Drug & Cosmetic Law Section of the New York State Bar Association, the Corporation and Banking Law Section of the American Bar Association, and Grocery Manufacturers of America, Inc., and the American Pharmaceutical Manufacturers’ Association, Inc., I have for several years conferred with the American Law Institute and its Editorial Board about Article 2, particularly as regards the law of implied warranty in the sale of food, drugs and cosmetics. The original draft of these provisions proposed a novel theory of manufacturers’ liability without fault whereby necessary incentives for proper handling, storage and delivery of these products by intervening dealers were seriously weakened to the likely detriment of the consuming public. Over the years I organized meetings of counsel for the affected industries, some of which were attending by representatives of the ALI, and finally the text and comments of Article 2 were adopted in a form acceptable to all parties. I have regularly informed industry counsel about progress and development of the Code and have as often invited further comment on its status. As of this date I have no criticism to offer on this subject, and I approved the present language of Article 2 in my statement before the Commission on February 15, 1954.

Letter from Frank T. Dierson to John W. MacDonald, Executive Secretary, State of New York, Law Revision Commission (Jun. 21, 1954) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

Article Nine is less devoted to correct commercial behavior, instead emphasizing proper procedures such as public notice.<sup>322</sup> Article 2 speaks in terms of the standards of good faith and commercial reasonableness while article 9 is concerned with bright-line rules of creation, attachment, and priority of property interests.

In 1949, however, the articles were just starting to diverge. Remember that objective good faith still applied to the entire Code, not just to article 2. Article 9 itself continued several provisions, soon to be omitted, that protected the debtor and limited the power of the secured lender.

The floating lien had not yet developed into the unitary device covering present and future assets which is today's supreme security interest. Prior to the March 1949 meeting, the secured transactions drafters had questioned the primacy of the inventory financier. They noted, "[a]s now drafted, a financing institution can so get a lien on the inventory of a business as to claim all the assets ahead of other creditors."<sup>323</sup> It was fair to protect secured lenders against other lending institutions, but "laborers and small merchandise and service creditors" may also need some protection.<sup>324</sup> The drafters proposed a resolution that some creditors be allowed to reach a certain percentage of inventory. Moreover, they questioned whether it was "good policy to permit inventory liens on the inventory of retail establishments?"<sup>325</sup> They proposed that "bulk mortgages" on retailers be permitted only if the proceeds of the loan were put into the business.<sup>326</sup>

The May 1949 Draft still distinguished between "general" and "special" inventory liens.<sup>327</sup> A "special inventory lien" did not include after-acquired inventory.<sup>328</sup> Furthermore, the

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322. Richard L. Barnes, *Toward a Normative Framework for the Uniform Commercial Code*, 62 TEMP. L. REV. 117, 120 (1989).

323. Preliminary Questions of Policy for Consideration in Connection with Article VII 1 (undated) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review). The document's reference to Article VII and to "the March meeting" probably places it in early 1949. *Id.*

324. *Id.*

325. *Id.* at 2.

326. *Id.* at 3.

327. U.C.C. § 7-302, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 109 (E. Kelly ed., 1984).

328. "[A] financier does not acquire an interest in accounts or chattel paper as they arise," but "a special inventory lien given for new value in current course containing a term that it secures other indebtedness is a lien for new value." U.C.C. § 7-313, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 119 (E. Kelly

security interest did not automatically attach to accounts or chattel paper.<sup>329</sup> The May 1949 Draft provided for a preference if the security interest was not for new value and insolvency proceedings were begun within four months of the later of attachment or perfection.

Speaking of the early inventory secured finance procedures, Mr. Ireton declared them to be unworkable:

The other kind of inventory lien that could be taken was a lien on a conglomerate mass, such as a pile of coal or cotton seeds in a warehouse; this was a general lien and on default the lender was under the obligation of giving all creditors notice, calling them in, securing the borrower's consent, then proceeding with liquidation of the lien with the obligation of a trustee. You can imagine what these provisions would have done. There just would be no inventory financing. Small business would suffer irreparable harm.<sup>330</sup>

The May 1949 Code provided for certain debtor protections. All non-merchants could not waive defenses against assignees and merchants could not waive defenses that amounted to failure of consideration.<sup>331</sup> A purchase money security agreement could not limit or disclaim warranties,<sup>332</sup> and a note containing a security agreement was not negotiable in the first place.<sup>333</sup> Acceleration could only be done "in the good faith belief that the prospect of performance is impaired."<sup>334</sup> For consumer goods, disclosures of financing terms were required. A holder of a note secured by consumer goods would waive his status as a holder-in-due-course if he asserted any rights against the goods.<sup>335</sup> Repossession without notice was banned if the consumer had

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ed., 1984).

329. U.C.C. § 7-313, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 119 (E. Kelly ed., 1984).

330. Ireton, *supra* note 1, at 282.

331. U.C.C. § 7-108, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 89 (E. Kelly ed., 1984).

332. U.C.C. § 7-108, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 119 (E. Kelly ed., 1984).

333. U.C.C. § 7-108, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 89 (E. Kelly ed., 1984).

334. U.C.C. § 7-109, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 590 (E. Kelly ed., 1984).

335. U.C.C. § 7-612, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 169 (E. Kelly ed., 1984).



paid more than sixty percent of the obligation.<sup>336</sup>

By spring 1951, the restrictions on the floating lien's automatic attachment to after-acquired property would disappear and the consumer protections would be severely limited or dropped altogether.

*b. The Background of the Controversy.* In considering the proposed protections for consumer lending and also for lending against inventory and receivables, we should realize that our present consumer culture, with its infrastructure of advertising and financing, was just getting started in the post-war years. Banks were not doing consumer lending and consumer finance was done more on a local level.<sup>337</sup> Asset-based lending was a minuscule fraction of what it is today. In 1946, there was only \$5.8 billion of secured loans outstanding in total.<sup>338</sup> By 1994, General Motors Acceptance Corporation had made a *single* offering of \$8 billion.<sup>339</sup>

Gilmore characterized the fight over the consumer protection sections of article 9 to be "one of the most violent in the history of the Code's drafting."<sup>340</sup> It was, along with the banking conflict, one of the few disputes that surfaced into public knowledge, but whether it was that violent is questionable. The objectors to the early drafts were not angry

336. U.C.C. § 7-605, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 160 (E. Kelly ed., 1984).

Kripke strenuously objected to the sixty-day notice provision: "Lenders do not attempt to repossess without several notices to repossess.... The real risk is concealment, not destruction, damage or loss." Editorial Board Report to the Council and the Commercial Acts and Property Acts Sections 20 (Mar. 1, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review). The secured lender was given the right to repossess without notice and judicial process in the 1950 code. U.C.C. § 9-503, Proposed Final Draft: Text and Comments Edition (Spring 1950), *reprinted in* 11 U.C.C. DRAFTS 297 (E. Kelly ed., 1984).

337. See Homer Kripke, *The Importance of the Code*, 21 U. TOL. L. REV. 591, 593 (1990). It was argued that consumer legislation was not needed because a local lender's concern for its reputation would prevent abuses. His comment shows that the drafters saw the commercial world as smaller, more personal, more locally shared than today's. See Note, *Negotiability of Conditional Sales Contracts: The Consumer and Article III of the Commercial Code*, 57 YALE L.J. 1414, 1417 (1948).

338. Albert R. Koch, *Economic Aspects of Inventory and Receivables Financing*, 13 LAW. & CONTEMP. PROBS. 566, 572 (1948).

339. SIDNEY RUTBERG, *THE HISTORY OF ASSET-BASED LENDING* 3 (1994).

340. 1 GRANT GILMORE, *SECURITY INTERESTS IN PERSONAL PROPERTY* 293 (1965).

and in fact agreed with many of the goals of the proposals. They did have severe doubts about their practicality.

Kripke and Ireton represented the voice of experience in secured transactions; as mentioned above, they thought of the drafters as inept reformist amateurs, an opinion shared by Schnader.<sup>341</sup> Kripke saw the secured transaction proposals as "paternalistic."<sup>342</sup> Ireton saw article 9 as "the most leftist."<sup>343</sup> As reported by Gilmore, "It is said that Article 9 betrays an earnest reformist zeal, reminiscent of the crusading moralism of the lush days of the New Deal, entirely out of place in a commercial codification."<sup>344</sup> The archives do not reveal any parties outside the drafters who wanted more consumer and merchant protection, other than Ben Heineman, who was in favor of the provisions for disclosure of credit terms and wanted the Code to have the support of "broad public groups."<sup>345</sup> According to Mentschikoff, Gilmore felt that the disclosure provisions were inadequate and the matter should be left to an administrative agency.<sup>346</sup> Mentschikoff and Llewellyn, however, were in favor of the disclosure provisions. In fact, it was in the middle of the discussion on the disclosure provisions that Mentschikoff made her statement that "In the last two years as amendments have been made to the Code, and changes in policy made, the Code has consistently moved onto a special-interest type of legislation and away from a public-interest type of legislation."<sup>347</sup>

The Enlarged Editorial Board of January 1951 noted the lack of political support for the consumer protection sections.<sup>348</sup> The drafters decided to jettison consumer

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341. See *supra* notes 143-45 and accompanying text.

342. Letter from Homer Kripke to A.L.I., *supra* note 146, at 1 ("Earlier drafts of Article 9 contained much paternalistic protection of the debtor against the lender who was assumed to be ruthless. This material has been largely eliminated, except with respect to consumer transactions. Similar paternalism still appears elsewhere in the Code, however, and has reflections in Article 8.")

343. "Since last December this Article has been almost completely re-written; but this can be said about the Article, that of all the Articles in the Code this Article had a more definite and decided slant to the left than any other Articles in the Code." Ireton, *supra* note 1, at 281-82.

344. Gilmore, *supra* note 62, at 37.

345. Enlarged Editorial Board, *supra* note 4, at 292-94.

346. See *id.* at 314-15. In 1964, the Truth-in-Lending Act, 15 U.S.C. § 1601, required such disclosures and gave the Federal Reserve Board regulatory authority.

347. Enlarged Editorial Board, *supra* note 4, at 284.

348. See *id.* at 293-96.

protection from article 9; the floating lien emerged as a security interest without restrictions. The most leftish of all the articles, first written under the assumption that the debtor needed protection from the financiers, became the article which gave unrestricted power to the financiers.

*c. The Floating Lien.*

(1) *The Arguments for the Floating Lien.* The restrictions on the floating lien soon disappeared. Ireton, who occupied the commanding position of being the Chairman of the ABA Division of Mercantile Law,<sup>349</sup> was critical of the division between "specific" and "general liens."<sup>350</sup> In 1949, Ireton had criticized the concept of the general lien and the original default rule, in which the financier would liquidate the inventory as a trustee for the benefit of creditors. "The effect of such a provision would merely be that no financier would ever seriously take a general lien."<sup>351</sup> On the other hand, a specific lien would limit the security "to a definite collateral value per unit."<sup>352</sup>

Kripke also published an article in 1949 criticizing the secured transactions provisions. He could see no reason for preserving the distinction between special and general inventory liens. Moreover, he made an argument which today seems peculiar. In 1949, inventory financing was not common

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349. *Of the Section of Corporation, Banking and Business Law—Divisions and Committees*, 6 BUS. LAWYER 210, 217 (1950).

350.

At one time there was a provision in there that a secured lender, insofar as lending on an inventory was concerned, could only take one of two types of lien. He could take a specific lien in connection with specific and separately described items but on default under such a lien the lender could not get the benefit of any equity over and above the related collateral value on each separate item. The other kind of inventory lien that could be taken was a lien on a conglomerate mass, such as a pile of coal or cotton seeds in a warehouse; this was a general lien and on default the lender was under the obligation of giving all creditors notice, calling them in, securing the borrower's consent, then proceeding with liquidation of the lien with the obligation of a trustee. You can imagine what these provisions would have done. There just would be no inventory financing. Small business would suffer irreparable harm.

Ireton, *supra* note 1, at 282.

351. Ireton, *supra* note 146, at 815.

352. *Id.*

and was only done by a few specialized lenders.<sup>353</sup> In the late forties and early fifties, banks were not making secured loans to small businesses and consumers.<sup>354</sup> Now it is common, and, thanks to article 9, the first to file an inventory lien takes precedence over almost all other creditors.<sup>355</sup> Kripke argued that since inventory financing was experimental, it should have few legal restrictions on it that would discourage its growth.<sup>356</sup> Llewellyn had questioned whether it was a good idea to allow inventory liens on small retailers, e.g., "The 'poppa and momma store.'" Kripke felt, however, that the small amounts and minimal worth involved would make such financing unattractive. "Thus, without any real danger the useful result will have been achieved that the law will provide a mechanism by which the business and financial practice can be developed if it stands the test of trial." Today,

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353. See Homer Kripke, *The "Secured Transactions" Provisions of the Uniform Commercial Code*, 35 VA. L. REV. 577, 600 (1949).

354. See Kripke, *supra* note 337, at 593.

355. For example:

In the early days of the commercial finance industry, which really began to get off the ground in the 1920s and 1930s, the business was linked with companies that were on the brink of bankruptcy. Rates were high, risks were high, and the business was small. The total loan volume of the commercial finance industry in 1934 was estimated at \$50 million, and 20 years later it had increased to around \$500 million. In 1987, loan volume of the asset-based financial services industry topped \$75 billion.

In recent years, Wall Street has discovered asset-based lending and, starting with the popular mortgage-backed securities, it has moved into packaging consumer accounts receivable and selling paper secured by them. The largest underwriting ever was the sale of \$4 billion (that's right, billion) in securities backed by automobile receivables. In a deal managed by First Boston Corp., 54 billion was raised on Oct. 16, 1986, through the sale of receivables General Motors Acceptance had amassed in a promotion offering GM car buyers 2.9 percent and 4.8 percent annual interest rates. (In 1994, GMAC had registered a shelf offering of asset-backed paper totaling \$8 billion.)

RUTBERG, *supra* note 339, at 3.

356.

Inventory financing is still a relatively new field, and a particularly unattractive one in an unsettled economy. The financier who uses it is still a pioneer. Some financiers will have none of it. Others who have gone into it extensively have taken heavy losses. It has been resorted to by the most marginal types of borrowers. To impose legal restrictions on the right of the financier to salvage his position on default would have been to discourage further business and financial experimentation with this form of financing.

Kripke, *supra* note 353, at 600.

anyone can be a secured lender. By removing the complexity, the U.C.C. enabled anyone to take a security interest. The experimental, esoteric inventory financiers became the dominant creditors in the financial world.<sup>357</sup>

(2) *The Statutory Changes—The End of Restrictions.*

One of the first limitations on the security interests to go was the preference provision of the May 1949 Code.<sup>358</sup> Kripke noted that the Code provision dropped the then federal requirement of knowledge of insolvency and criticized the provision for making it too easy to invalidate liens.<sup>359</sup> The provision disappeared by the September 1949 Revisions.<sup>360</sup>

The distinction between "special" and "general" inventory liens also disappeared.<sup>361</sup> By the October 1949 Revisions, restrictions on after-acquired property clauses also disappeared. The only restriction was on future crops and

357.

While the UCC made life simpler for commercial finance companies by standardizing the requirements for protecting collateral, it removed much of the complexity that made the expertise of the entrepreneur essential. No longer did the manager of a commercial finance company need to know regulations in 50 different states nor deal with a mass of differing and often conflicting laws.

Said A. Bruce Schimberg, of the Chicago law firm of Sidley & Austin, with the passage of the UCC, "you didn't have to be smart to be in the business. You didn't have to create ten different forms. It diluted the expertise of the key people who could cope with the complications."

RUTBERG, *supra* note 339, at 8. Another writer with a clouded crystal ball argued that the law should not provide for inventory financing because such financiers would be wiped out in the inevitable post-war depression. "Indeed, in view of the extraordinary high current price level and volume of business sales, most concerns with inventory or receivables on hand financed in whole or in part by bank or other debt would do well to liquidate their debt at the earliest opportunity." Koch, *supra* note 338, at 578.

358. Section 7-111, titled, "Security Interest to Secure Obligation Not For New Value; When a Preference," provides: "A security interest may be avoided in insolvency proceedings to the extent it is not for new value if insolvency proceedings are begun within four months from the date when the security interest attaches or is perfected, whichever is later." U.C.C. § 7-111, May 1949 Draft, *reprinted in* 8 U.C.C. DRAFTS 89 (E. Kelly ed., 1984). "Preference" laws prohibit a debtor from paying ("preferring") one creditor over another. The concept is codified in federal bankruptcy law, 11 U.S.C. § 547 (2000).

359. Kripke, *supra* note 353, at 601-03.

360. U.C.C. § 7-111, September 1949 Revisions of Article 8, *reprinted in* 8 U.C.C. DRAFTS 281-82 (E. Kelly ed., 1984).

361. *Id.*

consumer goods.<sup>362</sup>

In the September Revisions, the Secured Transactions Article finally coalesced the various types of security devices into a unitary security interest. In May of 1949, the article had been divided into "Parts," each with its own type of security interest.<sup>363</sup> In July, Schnader proposed merging the various security devices, thus creating the modern unified article 9 security interest.<sup>364</sup> By September, these Parts were discarded, and the U.C.C. security interest applied to all types of collateral. The drive to simplify wiped out the distinctions.

The end of restrictions on after-acquired property and the merger of the distinct security interests created today's unitary security interest and the primacy of the floating lien.

#### d. *The Consumer Provisions.*

(1) *Waiver of Defenses.* The May 1949 U.C.C. prohibited a debtor from waiving defenses against an assignee and prevented a note containing a grant of a security interest from being negotiable. Even a merchant could not waive defenses amounting to a failure of consideration.<sup>365</sup> The provisions drew a lot of criticism, with various proposals being made.<sup>366</sup> Mentschikoff proposed a compromise<sup>367</sup> which

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362. U.C.C. § 8-203, October 1949 Revisions of Section 1-105, Bank Collections Part of Article 3, Section 6-303 and Articles on Secured Transactions and Bulk Transfers, reprinted in 8 U.C.C. DRAFTS 488-89 (E. Kelly ed., 1984).

363. Part 2 "Pledge," Part 3 "Inventory and Accounts Receivable Financing," Part 4 "Equipment Financing," Part 5, "Agricultural Financing," Part 6, "Consumer's Goods Financing," Part 7, "Bulk Transfers," and Part 8, "Vehicle Liens." U.C.C. Article 7, May 1949 Draft, reprinted in 8 U.C.C. DRAFTS 20, 20-23 (E. Kelly ed., 1984).

364.

Schnader: Is there anything in Article 7 as redrafted which would not be applicable to agricultural financing? to [sic] consumer goods financing? You may be able to run through your general stuff and then have an index section referring to the section of the general material which particularly affect your particular financing.

A.L.I., Minutes of Meeting of July 25-27, 1949 6 (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

365. U.C.C. § 7-108.8, May 1949 Draft, reprinted in 8 U.C.C. DRAFTS 87 (E. Kelly ed., 1984).

366. Transcript of Discussion on the Uniform Commercial Code, Joint Meeting, The American Law Institute and the National Conference of Commissioners on Uniform State Laws 273-79 (May 1950) (on file with the Llewellyn Archives, University of Chicago Law Library, and with the Buffalo Law Review).

she was not happy with, but she did feel it represented the majority view.<sup>368</sup> Thus, the blanket prohibition was replaced by a complicated compromise which lasted until 1957 when the present neutral position of article 9 was adopted.<sup>369</sup> Also, the Spring 1950 Draft allowed a negotiable instrument to refer to the taking of security and still be negotiable.<sup>370</sup>

(2) *The Disclosure Provisions.* The 1949 and 1950 drafts included mandatory disclosures of credit terms in consumer transactions. The opposition to them was based on a variety of grounds. One was the philosophical one that disliked such legislation as "social" and felt that it did not belong in a commercial code.<sup>371</sup>

367.

MISS MENTSCHIKOFF: The motion is to the effect that the section 9-205 206(3) be amended so as to permit the creation of a holder in due course of a note which would be necessarily a conditional sale or chattel mortgage in the type of situation envisaged by Section 9-205, but with the proviso that if a holder in due course is created, at his option he can either maintain that status, in which case the defense of breach of warranty is cut off, or he can waive his holder-in-due-course status and rely upon his security with the commercial paper article, of course, dealing with the question of whether he has such notice as to make him a holder in due course or not a holder in due course.

*Id.* at 278.

368.

And it really seems to me that what this amendment does is to represent the composite view of the people who have worried about the problem in a way which is more representative of their thinking than in my opinion is really justified by what the right answer ought to be.

*Id.*

369. The present section 9-206 reads:

(1) Subject to any statute or decision which establishes a different rule for buyers or lessees of consumer goods, an agreement by a buyer or lessee that he will not assert against an assignee any claim or defense which he may have against the seller is enforceable by an assignee who takes his assignment for value, in good faith and without notice of a claim or defense, except as to defenses to a type which may be asserted against a holder in due course of a negotiable instrument under the Article on Negotiable Instruments (Article 3). A buyer who as part of one transaction signs both a negotiable instrument and a security agreement makes such an agreement.

U.C.C. § 9-206 (1999). The language is almost identical to that adopted in U.C.C. § 9-206, Official Text (1957), reprinted in 20 U.C.C. DRAFTS 161 (E. Kelly ed., 1984).

370. U.C.C. § 3-112(1)(b), Proposed Final Draft: Text and Comments Edition (Spring 1950), reprinted in 10 U.C.C. DRAFTS 334 (E. Kelly ed., 1984).

371.

It has been stated that the primary concern of Chapter 1 dealing with Consumer Credit is the protection of the debtor against the

Another problem was that the idea of consumer disclosure was a new one. At the Enlarged Editorial Board Meeting of January, 1951, Mr. Pantzer<sup>372</sup> pointed out that such information was not disclosed to consumers:

In the second place, you are not required to disclose whether the refrigerator is gas-operated or electrically operated, whether you are buying a Servel or a Frigidaire, whether you are getting nine cubic feet of storage space or four. You don't have to warrant that. Finally, you don't have to warrant—which I think is the most important disclosure of all—whether it will last<sup>373</sup> or whether it will continue to operate for one year or five years.

Today, the buyer of a refrigerator gets disclosures of all features, plus Truth-in-Lending, Magnusson-Moss Warranty, and energy efficiency.

There were two technical problems with the disclosures. First, Ireton doubted that the local finance companies and merchants had the time or the technical expertise necessary to make the correct disclosures on interest and insurance charges.<sup>374</sup> Another problem was that the disclosure of

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overreaching creditor. Competition usually takes care of this supposed inequality. This is embarking upon a field of social legislation, and there can be considerable doubt as to the propriety of including such regulation in a statutory proposal relating entirely to security concepts.

Ireton, *supra* note 351, at 804. Mentschikoff reported that Grant Gilmore took the position that such regulation should be done by an administrative agency, not by the U.C.C. Enlarged Editorial Board, *supra* note 4, at 314-15.

372. An Indiana attorney who was active in the Code drafting. See Letter from Kurt Pantzer to William Schnader, *supra* note 127. See also Enlarged Editorial Board, *supra* note 4, at 293.

373. Enlarged Editorial Board, *supra* note 4, at 293-94.

374.

MR. IRETON: It does not affect our volume of business. Where it has an adverse effect along that level is that where you do a mass volume of business—for example, I think the company I represent is buying notes at the rate of nine or ten million dollars a day. When you have a volume flowing through like that, that has to be routine to a point where everything is done as a matter of form. The minute you have to lift anything out of that routine and hand-handle it, or do a tailor-made job on it, you begin to lose money on that deal.

But that is not the only point about this disclosure. We run anywhere from 30 to 35 per cent errors. The Pennsylvania Department has had us on the carpet for a year and a half. They have threatened to take our license away. With the help that the companies have, you just can't get that percentage of error down. But the impracticability and the unfeasibility of the thing, of course, is one thing.

*Id.* at 301-02.



interest charges could conflict with the "time price doctrine", a device which allowed sellers and financiers to side-step the usury laws. That doctrine held that a car dealer, for example, selling at an interest rate higher than allowed by the usury laws, was actually just selling at a higher price, and not charging interest.<sup>375</sup> Ireton pointed out that because the Code used the term "secured lender" and the disclosure section used the term "any other lender," the Code could subject the time seller to state interest and usury laws.<sup>376</sup>

On the other hand, Mentschikoff felt that the consumer should be informed.<sup>377</sup> Consumers should be made aware of the possibility "of shopping for rates of interest, that that would materially reduce the rates which are now being charged."<sup>378</sup> She felt that if groups such as labor unions and women's groups could be educated, they would support the reform efforts of the Code:

We are not convinced that this means it will always have tough sledding. We think part of the answer to that again lies in the education of the groups that have not been consulted about the Code, know nothing about the Code, (and here I speak of labor union groups and women's groups in particular), and that political power of such groups, if it is subject to arousement at all, is really in our opinion considerably more effective than the political power of the groups which have been effectively organized up to this point.<sup>379</sup>

Ireton had a different take on the political realities. Eleven or twelve years previously, he had tried to get a bill enacted and received no help from labor unions. Banks would oppose the legislation. Furthermore, the local financier would fight it: "Your opposition is going to come from your local time seller who lives at every crossroads throughout any state you go into, who wields a powerful influence. Your public support

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375. See, e.g., *Gen. Motors Acceptance Corp. v. Weinrich*, 262 S.W. 425, 429 (Mo. Ct. App. 1924) (holding that a sale is not a loan, that "this was a bona fide sale of the automobile; and . . . Reuter [the dealer] had the right to sell the car on time for more than the cash price thereof").

376. Letter from J. Francis Ireton to Herbert Goodrich, Director, A.L.I. (Apr. 24, 1950) (on file with A.L.I. Archive, University of Pennsylvania Law Library, and the Buffalo Law Review).

377. Enlarged Editorial Board, *supra* note 4, at 282.

378. *Id.*

379. "I know this, because I did it. I went to a labor union to enlist their aid, and got nowhere. They just weren't interested." *Id.* at 292-93.

would be somewhat apathetic, I think. I don't think you will arouse much support over this thing.<sup>380</sup>

Evidently, the drafters decided to side with Ireton as the consumer disclosure provisions were dropped in the April 15, 1951, draft.<sup>381</sup>

The debate over the consumer-lending provisions did have a strange but temporary effect in section 1-102(g) which read "Prior drafts of texts and comments may not be used to ascertain legislative intent."<sup>382</sup> It was felt that the dropping the consumer sections would be used by opponents of such legislation to argue that the ALI and the UCC did not think such legislation was needed. Schnader then stated, "Isn't the answer to that that we ought to change 102 to say, 'neither lobbyists nor courts shall look at the legislative intent?' (laughter)."<sup>383</sup> Evidently, Schnader's suggestion was codified as section 1-102(g). That section was dropped in 1956.<sup>384</sup>

Article 9 emerged as the stripped down version that exists today, with its empowerment of the secured party and its exclusion of consumer protection. We again see the triumph of business autonomy over a regulatory system. With the change from objective to subjective good faith in article 1,<sup>385</sup> the rejection of judge-made limitations on secured transactions,<sup>386</sup> and the disappearance of the consumer protection requirements, a financier could make loans without disclosures, to use any type of collateral as security, and to realize on that collateral in any manner. Secured transactions law was left to the private agreement of the lender and the debtor.<sup>387</sup> And that contract may deprive

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380. *Id.* at 296.

381. U.C.C. Proposed Final Draft No. 2, Text Edition (Spring 1951), *reprinted in* 12 U.C.C. DRAFTS 1 (E. Kelly ed., 1984).

382. U.C.C. § 1-102(g), Official Draft: Text and Comments Edition (1952), *reprinted in* 14 U.C.C. DRAFTS 44 (E. Kelly ed., 1984).

383. Enlarged Editorial Board, *supra* note 4, at 281.

384. U.C.C. § 1-102(g) (deleted), *reprinted in* 18 U.C.C. DRAFTS 26 (E. Kelly ed., 1984). For a different, and excellent, treatment of what ignoring drafting history could mean, see John M. Breen, *Statutory Interpretation and the Lessons of Llewellyn*, 33 LOY. L.A. L. REV. 263 (2000).

385. *See supra* note 160 and accompanying text.

386. *See* U.C.C. § 9-208, Proposed Final Draft, Text and Comments Edition (May 1950), *reprinted in* 11 U.C.C. DRAFTS 240 (E. Kelly ed., 1984). Today, U.C.C. § 9-205 repeals the rule of *Benedict v. Ratner*, 268 U.S. 353 (1925), which required a financier to police actively its collateral in order to preserve its lien. *See* U.C.C. § 9-205, cmts. 1-5 (1991).

387. U.C.C. § 9-201, Proposed Final Draft No. 2: Text Edition (Spring 1951), *reprinted in* 12 U.C.C. DRAFTS 273 (E. Kelly ed., 1984) ("Except as otherwise

others, who also have claims against the debtor, of their ability to collect their debts.

It was the codification in article 4 of this ability of A and B to agree to deprive C of rights that did create the most violent controversy in the Code's history, the battle over the banking article.

### 5 *The Banking Article.*

a. *The Opposition of the Bankers.* The story starts with Fairfax Leary, then a young professor at Penn, drafting the banking law component of the Code. Bankers immediately opposed even the idea of having the Code regulate their activities. The Federal Reserve Board's Special Committee on the Code questioned whether the Code proposals were needed. It felt that the check collection was well enough governed by contract and Federal Reserve Regulations. The new Code would create more problems than it would solve.<sup>388</sup>

Leary brought up the Fed's objections at the NCC/ALI meeting in May 1949. He argued that legislation was necessary to end the chaos in banking law created by conflicting state decisions.<sup>389</sup> Willard B. Luther, a bank lawyer from Massachusetts, pointed out that the Fed and the American Bankers Association had that veto power over any banking provisions.<sup>390</sup> The ALI/NCC continued to draft bank legislation, with the realization that the bankers and the Fed had a veto power. In 1950, Schnader also warned that the Code would have to be acceptable to lobbies and regulatory bodies. However, Professor Frederick Beutel, who would become the first major academic opponent of the Code,

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provided by this Act . . . a security agreement is effective according to its terms between the parties, against purchasers of the collateral and against creditors.").

388. Memorandum of Comments submitted by Special Committee of Counsel of the Federal Reserve Banks (Apr. 5, 1949) [hereinafter *Memorandum of Comments*] (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

389. "[A]nybody who attempts to analyze the current course of decisions under the free contract gets a feeling of rather helpless bewilderment when he looks at the national picture as a whole. The cases are very complex. You can find authority for practically any proposition . . . that you want." 3 PROCEEDINGS 145 (26th Annual Meeting of the A.L.I. in joint session with the Nat'l Conf Commissioners, May 18-21, 1949) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

390. See *id.* at 147-49.

wanted to stand firm for principle.<sup>391</sup>

The bankers, however, remained adamantly opposed to the Code. Some dropped their opposition with the revision prepared by Malcolm in 1951, but others remained steadfastly opposed, even labeling the Code as "Communist inspired."<sup>392</sup> Gilmore, who took over the drafting of article 4 after Leary left, called it "the bloodiest battleground in the entire history of the Code. While Steffen (and others) attacked it as being "pro-bank," bank counsel (particularly the New York group) attacked it as a Communist plot designed to destroy the American banking system."<sup>393</sup>

Why were the bankers so opposed to the Code; in fact being the one group that remained in opposition even after the compromises of 1951?<sup>394</sup> It may be because the bankers

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CHAIRMAN SCHNADER: One thing I think all of us have to remember is that we are not restating the law here; we are preparing a statute which we hope to get through the legislatures, and we cannot go too far, because there are such things as lobbies in this country and in the various states. If we try to do things that are just not practical, we might as well forget the Code.

MR. BEUTEL: It is part of our job here—and I think it is very important that we understand it is part of our job—to make a statute which is fair and which we, as American lawyers in the American Law Institute and the Commissioners, regard as fair.

Of course we are up against lobby pressure, but we ought to stand firm for what we regard as fair, regardless of lobby pressure . . . [sic] If the bankers are opposed to the thing, the bankers ought to know we have considered it and have passed what we consider is a fair rule. It is not our job to simply pass something that the lobby people will agree to. If this Code is not a fair Code it isn't going to get by any legislature.

CHAIRMAN SCHNADER: I didn't say anything about bankers.

MR. BEUTEL: Well, I did! [Laughter]

CHAIRMAN SCHNADER: I was talking about certain regulatory bodies, regulatory bodies that are so powerful that if they say no to this Article it won't be passed. That is what I am saying. We have to keep that in mind, because we are not just working this Code for mental exercise; we want to see something enacted.

A.L.I./N.C.C. Consideration, *supra* note 71, at 97.

392. Fairfax Leary, Jr. and Michael A. Schmitt, *Some Bad News and Some Good News from Articles Three and Four*, 43 OH. ST. L. J. 611, 614 (1982); Letter from Walter Malcolm to William A. Schnader 2 (April 13, 1954) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

393. Letter from Grant Gilmore to Donald J. Rapson (Oct. 8, 1980), in Donald J. Rapson, *Review of the Law of Modern Payment Systems and Notes*, 41 BUS. LAW 675, 677 (1985).

394. For the depth of feeling see, for example, Letter from William L. Kleitz, President, Guaranty Trust Co., to Lloyd D. Brace, President, First National Bank of Boston (Jan. 2, 1953) (on file with A.L.I. Archives, University of Pennsylvania

felt they were "performing almost a gratuitous and public service" in processing checks and thus should not be regulated.<sup>395</sup> Another reason may have been that the bankers had never been under a NCC or ALI uniform act, unlike merchants of goods or secured financiers. The only prior uniform act governing them had been the American Bankers' Association Bank Collection Code, which had been drafted by the Bankers' Association itself.<sup>396</sup> Most bankers did not feel any need for change.<sup>397</sup> Now the ALI and the NCC, at best a bunch of self-appointed left-wing reformers, at worst, Communist-inspired radicals, were gratuitously attempting to butt in. Despite the drafters' effort to reach a compromise, the animosity of the bankers to the Code managed to delay its adoption by years.

b. *Malcolm Steps Into the Breach.* In face of the opposition, by May of 1951 the ALI/NCC voted to delete article 4 from the Code.<sup>398</sup> Walter Malcolm then took it upon himself to salvage article 4 and prepared a new draft over the summer.<sup>399</sup>

There are differing views on exactly what happened. Professor Rubin writes:

Article 4 had a stormier history. Leary produced a draft that represented a reconceptualization of the field, and thus a significant departure from the American Bankers Association's Bank Collection Code. It reflected a thorough knowledge of the check collection process, and combined a realistic recognition of industry needs with a rare sensitivity to consumer interests. But the New York Clearing House Association reacted with fury, promptly informing Llewellyn that it would oppose the passage of

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Law Library, and the Buffalo Law Review). Klein wrote, "What I am really hoping is that we can kill the thing [the U.C.C.] entirely." A.B.A. Committee Disapproves Proposed Uniform Commercial Code in Its Entirety; Report of Special Committee of American Bankers Association on Proposed Uniform Commercial Code and Accompanying Press Release (Oct. 20, 1954) (on file with Llewellyn Archive, University of Chicago Law Library, and the Buffalo Law Review).

395. Ireton, *supra* note 1, at 281.

396. See Hal S. Scott, *The Risk Fixers*, 91 HARV. L. REV. 737, 762 (1978).

397. *Memorandum of Comments*, *supra* note 388.

398. Letter from Robert Goodrich, Director, to Members of the California Bar on Article 4 (May 28, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

399. Letter from Walter Malcolm to Arthur Littleton (May 30, 1950) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

the entire U.C.C. if Article 4 remained. Llewellyn responded by relieving Leary of his duties, and eliminating Article 4. The bankers then decided that it would not be a bad idea to have a bank collection article after all, provided that they were the ones to draft it, and Llewellyn graciously agreed. So a committee of bank counsel, headed by Walter Malcolm, set to work and produced a refurbished version of the Bank Collection Code. With relatively few alterations, this became the current Article 4.<sup>400</sup>

Gilmore in 1952 wrote that Leary “withdrew from active participation in the drafting of article 4 during the summer of 1950 because of the increasing demands of his practice.”<sup>401</sup>

Malcolm describes his revising article 4 as a volunteer effort, done to rescue article 4 from being discarded.<sup>402</sup> Aware of conflicts of interest, he justified his ambiguous situation by stating that he and his fellow American Bar Association members working on the Code had “exercised great care to recognize at all times that the Code would affect all segments of the business community and the public generally, and consequently, to refrain as much as reasonably possible from being special pleaders for the particular lines of business in which we were engaged in private practice.”<sup>403</sup>

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400. Edward Rubin, *Efficiency, Equity and the Proposed Revision of Articles 3 and 4*, 42 ALA. L. REV. 551, 555 (1991).

401. Grant Gilmore, *The Uniform Commercial Code: A Reply to Professor Beutel*, 61 YALE L. J. 364, 374 n.22 (1952).

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By May of 1951, I had acquired the personal conviction that though Article 4 still had some serious “bugs” in it, and had some sections somewhat unfavorable to banks, on the whole it was fairly close to being a workable Article and in addition, at that time was substantially more favorable to banks than the converse. By saying that the Article was favorable to banks I do not mean that the various sections stated rules giving banks unfair advantage at the expense of depositors or the public generally but rather that in section after section a rule was stated in a form satisfactory to banks where previously the area covered was in doubt and contained dangers to banks.

Having this personal conviction I was disappointed when at the meeting in Washington in May 1951, the Sponsors voted to set Article 4 on one side. Since I believed that without too substantial change from the general framework of the Article it should be possible to eliminate the really serious “bugs” existing in it, on my own initiative I tried rewriting enough of the sections of the Article to meet at least the major objections that I knew about.

Letter from Walter Malcolm to J.F. Shuman (Oct. 22, 1951) (on file with A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

403. *Id.*

By 1980, Grant Gilmore had a different slant on it:

[A] committee of bank counsel, headed by Walter Malcolm of Boston, was authorized to prepare what became the final (1952) draft—an arrangement I once described as tantamount to appointing a committee of dogs to draw up a protective ordinance for cats (feelings ran high in those days). Malcolm, who was a man of the highest personal integrity, understood that it was his function to do whatever was necessary to placate the New York group (who, nevertheless, refused to be placated).<sup>404</sup>

Malcolm did work over the summer and came up with a revised version of article 4. According to Beutel, the new article was mailed, in fragmentary form, to the members of the ALI and NCC less than three weeks before the September 15, 1951 meeting.<sup>405</sup> At the Meeting of the NCC Committee of the Whole (September 10 through September 15, 1951), Malcolm explained that he was, in his individual capacity, proposing certain revisions. Other than certain revisions he termed “technical,” he made two basic policy changes. One was substituting the negligence standard of “[t]he exercise of ordinary care” for the phrases “improper handling” or “proper handling.”<sup>406</sup> The second was the issue that started the firestorm of protest—the extent to which

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In my own case, in the case of Article 4, I attempted to solve this matter of possible conflict of interest between the banking industry and to the public generally something along the following lines. If in any particular case I observed myself or learned from bankers or bank lawyers that a particular provision simply would not work or was completely unacceptable to a substantial segment of the industry, I felt justified in pointing out these facts to the Reporters and Sponsors. I also adopted the practice rather early, in cases of this kind, of suggesting specific redrafts that I thought might work or might be acceptable. Since this has been going on for two years to more, a fair number of my suggested revisions were accepted by the Reporters and incorporated in the drafts. On the other hand, in cases where the Reporters or Sponsors had a policy decision to make which involved drawing some sort of line between banks on the one hand and depositors or the public generally on the other hand, and the line drawn was reasonably fair and workable, I did not feel justified in urging that the line be drawn more favorably to banks, and I did not do so.

*Id.*

404. Letter from Grant Gilmore to Donald J. Rapson, *supra* note 393, at 677.

405. Beutel, *supra* note 132, at 359 & n.141.

406. Meeting of the National Conference of Commissioners Committee of the Whole 24-25 (Sept. 10-15, 1951) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

banks could contract out of article 4.

Malcolm saw the problem as one “of extending and solidifying the basic principle of freedom of contract.”<sup>407</sup> He saw “solidifying this principle of freedom of contract” as a move away from the ivory tower “to a point where it would be acceptable by the market place.”<sup>408</sup> He, as way of background, described how check-clearing operated at high-volume,<sup>409</sup> and thus, only “a fast-moving, streamlined operation” would work.<sup>410</sup> Also, the items moved nationwide, going from San Francisco to New York to Maine to Washington, and elsewhere.<sup>411</sup>

Because of the high volume and the large number of banks involved across the country, one could not have rigid rules:

One basic principle on which I operated was that it was unwise and rather naive to think that it would be possible to lay down absolutely the rules that would control that type of operation and not make mistakes, or to be able to lay down the rules that would control that type of operation and would control them successfully five years to ten years from now in the manner in which they would be controlled at the present time.<sup>412</sup>

Another underlying problem was that local banks adopt procedures on how handle items in a certain city, but this adopted procedure may affect people nationwide.

Malcolm proposed two solutions. The first was freedom of contract: “The first one was to provide for almost absolutely complete freedom of contract, to make provision for the future change or development or development or the development of unforeseen conditions which none of us can appreciate or fully understand at the present time.”<sup>413</sup>

The second solution was to provide for flexibility so that not everyone “affected by the multiple transactions involved” would have to join in agreement.<sup>414</sup>

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407. *Id.* at 25

408. *Id.*

409. “They undoubtedly run to the stage of several million every day.” *Id.*

410. *Id.*

411. *Id.* at 26. Malcolm’s basic principle was that the virtue of both a free enterprise society and freedom of contract was their being able to adjust to new circumstances. See discussion *supra* note 108 and accompanying text.

412. *Id.*

413. *Id.*

414. *Id.*



Thus Malcolm proposed his version of section 4-103.<sup>415</sup> Malcolm was proposing a system whereby A and B could agree to affect the rights of C. He did, however, wish to keep his proposal within narrow bounds.

So far as I was concerned, at no time did I ever intend that that principle of varying the provisions of this article by agreement without the concurrence of the interested or affected parties would go any further than a narrow or a reasonably narrow area, and that narrow area is simply where there is a general agreement of the type of federal reserve regulations or operating letters or Clearing House rules.<sup>416</sup>

He proposed two definitions to keep his proposal limited in scope: one of "general agreement" to mean "Federal Reserve regulation or operating letters, Clearing House rules or the like," and "special agreement" to mean "an agreement between affected parties with respect to particular items or particular situations."<sup>417</sup>

Mentschikoff seconded the motion to amend section 4-103, stating that "with the two definitions present, the fears which were envisaged by the Section as to the possible meaning of (1) in particular, Section 4-103, become materially

415. See section 4-103, titled, "Variation by Agreement; Measure of Damages":

(1) The effect of the provisions of this Article may be varied by general or special agreement except that no agreement can disclaim a bank's responsibility or limit the measure of damages for its own lack of good faith or failure to exercise ordinary care.

(2) The measure of damages for failure to exercise ordinary care in handling an item is the amount of the item reduced by an amount which could not have been realized by the use of ordinary care and where there is bad faith, it includes consequential damages, if any.

(3) Action or non action approved by this Article or pursuant to a general agreement between banks or, in the absence of special instructions, consistent with a practice or usage of banks, in ordinary care.

(4) The specification or approval of certain procedures by this Article does not preclude an agreement authorized by subsection (1), nor constitute disapproval of other procedures which may be reasonable under the circumstances.

*Note: The Comment to this Section must make it clear that the phrase "ordinary care" is used in the ordinary tort sense, and not in a special sense relating to bank collections.*

U.C.C. § 4-103, Article 4—Bank Deposits and Collections: Text Edition (Sept. 3, 1951), reprinted in 12 U.C.C. DRAFTS 343-44 (E. Kelly ed. 1984).

416. Meeting of the National Conference of Commissioners Committee of the Whole, *supra* note 406, at 27.

417. *Id.*

reduced, if not nonexistent.”<sup>418</sup>

Something seems to have happened between September 15 and October 30, 1951, which set off Mentschikoff and Gilmore, since the acquiescence shown at the September meeting was replaced by enraged protest. Malcolm’s article 4 drew the only pointed academic criticism of the Code in Professor Beutel’s *The Proposed Uniform[?] Commercial Code Should Not Be Adopted* and also drew forth the bitter exchange of letters among Gilmore, Mentschikoff, and Schnader.

Beutel’s article has become a minor classic. Called “the first publication of the Critical Legal Studies movement,” the article represents the only example of legal scholarly writing which positively attacked the Code. Other professors, the best example of whom is Williston,<sup>419</sup> took the position that the Code should not be enacted because it would not be an improvement over present law. Beutel attacked the U.C.C. with a battle-ax, arguing that it would make commercial law worse. Because the banking conflict was one of the few instances where the dispute over policy entered public discourse<sup>420</sup> it is often cited in articles about the U.C.C.<sup>421</sup>

The private correspondence between Beutel and the ALI reveals that he may have been holding a grudge. He had written the ALI suggesting changes in terminology, but the ALI did not respond. On July 19, 1951, he wrote to Goodrich, the ALI Director:

Over a month has now passed since we had our exchange of correspondence on correlating the terminology in the Commercial Code.

I had a short letter from Prof. Bunn before yours came, written in reply to the carbon copy of the first letter which I sent you, but have had no further indication that the editorial board is interested in any comments from me.

I take it I live on the wrong side of the tracks. Let’s forget the

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418. *Id.*

419. See Williston, *supra* note 129.

420. See HULL, *supra* note 86, at 298-300.

421. See, e.g., Rubin, *supra* note 400.

whole matter.<sup>422</sup>

Later, on August 22, he wrote, "The side of the tracks may not have anything to do with it, but it is perfectly clear to me that your Editorial Board does not want any help from me."<sup>423</sup>

One can read a lot into "I take it I live on the wrong side of the tracks." The statement could refer to the fact that Professor Beutel taught at the University of Nebraska, not at the elite schools of Columbia, Pennsylvania, Yale, and Harvard as did the drafters. He was out West, not located on the East Coast where the drafting was centered. Beutel's latter criticism of article 4 as "vicious class legislation" indicates that to him "wrong side of the tracks" did have a class connotation: he felt he was being excluded from the Eastern elite legal establishment.

Beutel's article attacked the Code on several fronts. He starts by saying it was a rush job, and goes on to criticize the Code's draftsmanship, prolixity, and terminology. For article 4, he let loose and called it "A Piece of Vicious Class Legislation."<sup>424</sup> According to Beutel, article 4 would put all risks on the bank customer while insulating the bank from liability.<sup>425</sup> "A careful examination of the wording of the act will show that this article was drafted entirely with the purpose of protecting the banks so that they could carry on their business at the risk of the customer."<sup>426</sup> He ends by accusing the ALI and NCC of a deliberate sell-out.<sup>427</sup>

422. Letter from Frederick K. Beutel, Professor, University of Nebraska College of Law, to Herbert Goodrich, Director, A.L.I. (July 19, 1951) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

423. Letter from Frederick K. Beutel, Professor, University of Nebraska College of Law, to Herbert Goodrich, Director, A.L.I. (Aug. 22, 1951) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

424. Beutel, *supra* note 132, at 357.

425. *Id.* at 360-61.

426. *Id.* at 361.

427. Beutel asserts:

This article is a deliberate sell-out of the American Law Institute and the Commission of Uniform Laws to the bank lobby in return for their support of the rest of the "Code." . . . The banks now have a piece of class legislation more favorable to their interests than the American Bankers Association Bank Collections Code which their lobby failed to put over on the legislatures. This one-sided piece of class legislation is now backed by the prestige of the American Law Institute and the

Gilmore wrote a reply to Professor Beutel in his usual erudite and witty style.<sup>428</sup> After dismissing most of Beutel's points, he agreed with him as to article 4. He also saw section 4-103 as the objectionable section.

This Section as drafted provides that banks may by general or special agreement contract out of any of the rules laid down in the balance of the Article, provided only that a bank may not disclaim responsibility for the exercise of good faith and ordinary care. The proviso is, however, subject to a double-barrelled exception: 1) banks may agree on what constitutes ordinary care; 2) even in the absence of agreement, any action taken by a bank which is consistent with "a banking usage" is ordinary care. It should be noted further that the "general agreements" by which banks may amend the Article as they see fit, or agree on what ordinary care is, are agreements between banks to which the customer who deposits an item for collection is not a party but by which he will be bound.<sup>429</sup>

Letting the banks contract out of article 4 and allowing them to decide for themselves the meaning of ordinary care was "carrying a good joke too far."<sup>430</sup>

Gilmore advised keeping cool and suggested a compromise:

Let us not overstate the case. I do not believe that it is time to man the barricades. Our way of life will not be in jeopardy even if Article 4 is enacted. Luncheon at the Bankers' Club is not given over to devising ways and means of hoisting the poor customer each day a little higher on his own petard.<sup>431</sup>

If the article "were revised so as to place appropriate limitations on contracting out of the statute, there would be

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Commission on Uniform Laws. Such a sell-out is beneath the dignity of both organizations and is a tremendous blow to their prestige as scientific bodies . . . .

. . . .

If the "Code" in its present form is pushed through the New York Legislature by its high sounding backers, the Act will mark the beginning of the end of fairness and uniformity in the commercial law.

*Id.* at 362-63.

428. Grant Gilmore, *The Uniform Commercial Code: A Reply to Professor Beutel*, 61 *YALE L.J.* 364 (1952).

429. *Id.* at 375 (footnote omitted).

430. *Id.*

431. *Id.* at 376.

no insuperable objections to the balance of the article."<sup>432</sup>

Gilmore's restrained tone in his reply was not present in his correspondence with the ALI and his fellow drafters. In fact, his and Mentschikoff's letters constituted a rebellion in the ranks of the ALI.

c. *The Article 4 Rebellion*. It seems that Malcolm's drafting the comments to article 4 as well as drafting the article was what set off the controversy. Perhaps Mentschikoff and Gilmore, after having lost on the direct action against manufacturers of article 2 and the consumer protection of article 9, felt that having the bankers draft article 4 and its comments was the last straw. On October 30, 1951, Grant Gilmore wrote Llewellyn and many others, protesting Schnader's authorization of Malcolm to draft article 4's comments.<sup>433</sup>

Schnader responded vigorously. He started by correcting Gilmore: "Your very first paragraph contains a serious misstatement of fact." He stated he merely persuaded Malcolm to prepare a draft of the comments. Furthermore, Malcolm had not worked with bankers but rather had prepared a draft on his own. He felt that the ALI, the NCC, and the drafting staff owed "a great deal to Walter Malcolm. Indeed, in my view, if it had not been for the work which Walter did, the whole Code effort would have blown up in our faces."<sup>434</sup> He then questioned Gilmore's ethics:

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432. *Id.* at 377.

433. Gilmore wrote:

I have a warm personal regard for Walter as well as great admiration for his professional ability. Nevertheless, it seems to me to be a most unhappy arrangement that the Comments as well as the statutory text are to be prepared by the banking group without the least pretense of supervision or control by either the Law Institute or the Conference of Commissioners. One might as well commission a group of dogs to draft a protective ordinance for cats.

For the past several weeks I have been studying the present draft of Article 4 in detail. If at the time of the New York meeting I had understood some of its implications as well as I believe I do now, I would have spoken on the floor against its adoption.

Letter from Grant Gilmore, Professor, Yale University Law School, to Karl Llewellyn, Professor, University of Chicago Law School (Oct. 30, 1951) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

434. Letter from William A. Schnader, Esq., Schnader, Harrison, Segal & Lewis, to Grant Gilmore, Professor, Yale University Law School 2 (Nov. 1, 1951) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the

Finally, I question the ethical propriety of anyone who has been a paid employe of the drafting staff of the Code writing any article urging that a part of the Code be deleted. It would at least be bad taste for anyone who was a salaried employe of the drafting staff to write such an article.<sup>435</sup>

Mentschikoff then entered into the fray, repenting of her acquiescence at the New York meeting.<sup>436</sup> She then lit into Malcolm: "First, Walter Malcolm has not been a friend of the Code and his services have not produced anything which will make Code passage easier."<sup>437</sup> Malcolm's appraisal of ABA politics "has been consistently incorrect—he simply does not know how that organization runs."<sup>438</sup> He also did not understand state legislators. It was not necessary to sell out on article 5<sup>439</sup> and Wall Street did not have power over the New York legislature.<sup>440</sup> Outside knowledge that New Yorkers and Bostonians had drafted part of the Code would be the kiss of death.<sup>441</sup> The Code proponents have been

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Buffalo Law Review).

435. *Id.*

436. Letter from Mentschikoff to Schnader, *supra* note 111, at 1 ("I was silent in New York and I now think that was a mistake for which the Code in due course will suffer.").

437. *Id.*

438. *Id.*

439. Mentschikoff argued: "The second major false impression under which I think some of you have been laboring is that it was politically necessary to sell out to a few New York banking counsel on Article 5." *Id.* at 2.

440. Mentschikoff stated:

Somehow, we ought to find time for a long exchange of views on political expediency for the sources of information of some of you seem to be at considerable odds with mine and with my experience with various groups. We must not act at cross-purposes as the Code gets polished and put into the hopper. Especially we must not cross purpose on New York. Let me say again, the Wall Streeters do not have either understanding of or a significant influence on the course of legislation in Albany. As an ex-Wall Streeter, I had shared the illusion common to most of us that what we thought was legislatively important. Since I have been meeting with some of the legislators, I have discovered it is not so.

*Id.*

441.

A close approximation of the kiss of death in Illinois would be general knowledge that Articles 4 and 5 had been drawn by New Yorkers or Bostonians. We almost lost Ben Heineman's and Bert Jenner's support in September. Ben still refuses to commit himself. If we do not have their support, we have lost Illinois. This seems a big price to pay for the appeasement of Backus or Malcolm.

seriously mistaken:

You gentlemen have been playing with fire without adequate knowledge of its nature and as a result are in danger of losing enthusiastic friends in exchange for politically non-significant lukewarm adherents. I cannot help but feel that you are making a serious mistake which must be rectified as much as possible by the comments since the text is now out of our hands. I think that Grant's letter should be looked at in the light of this situation.<sup>442</sup>

To say that Schnader went ballistic in response would not be an exaggeration. On November 8, he fired back a letter, making several points. One was that the bankers had a veto over the Code.<sup>443</sup> The Code was not intended to be reform legislation.<sup>444</sup> He maintained that the Code *should* have the approval of the industry it governed.<sup>445</sup>

Then Schnader took the debate to an entirely different level. He attempted to silence the drafters, reminding them that they were, after all, the hired help:

So far as concerns the propriety of a member of the drafting staff attacking any part of the Code, it just seems to me that you and I have different standards of professional ethics. It is not a case of academic freedom about which the teaching staffs of our educational institutions sometimes get themselves excited.

Rather, it is a situation similar to one in which a lawyer employed to do a reorganization job for a corporation, accepted

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*Id.*

442. *Id.* at 2-3.

443. Schnader wrote:

One thing that I am sure of is that if in Pennsylvania the important bankers of Philadelphia and Pittsburgh, the State Bankers Association, and the Federal Reserve people were to let the legislature know that they disapproved of a part of the Code, there would not be a Chinaman's chance of obtaining enactment.

Also, what you said about Wall Street may be perfectly true, but I am satisfied that if the New York State Bankers Association and the important bankers in Buffalo, Rochester, Syracuse, and the other large cities outside of New York City, plus the Federal Reserve, were to express opposition to the Code, it would not be enacted in New York.

Letter from Schnader to Mentschikoff, *supra* note 84, at 2.

444. "I do not think that anybody entered upon the Code undertaking with the idea that it was to be a piece of reform legislation and that the persons who should be consulted about it should be the social service agencies." *Id.* at 3.

445. *Id.* at 2. Schnader's view is discussed *supra* at note 116 and accompanying text.

compensation for his work, and then stepped out and attacked the plan with a view to getting the stockholders to defeat it.

Goodness knows, nobody on the drafting staff was silenced at any time as far as the Editorial Board or the membership of either Conference or Institute was concerned; but after a joint meeting has spoken and placed its approval on the product, it seems to me that it would be the worst of bad taste, to say the least, for any of the paid staff to start a campaign to defeat all or any part of the Code.<sup>446</sup>

In Schnader's opinion, the Code was not under the control of Karl Llewellyn, but the Editorial Board: "My understanding was that the entire Code project was in charge of the Editorial Board and that it made assignments of work to various people. Apparently, you have a different understanding and feel that that is Karl's prerogative."<sup>447</sup>

Schnader's attempt to silence the drafters drew a protest from Professor Charles Bunn, who had been working on redrafting comments at the University of Wisconsin. He stated that he would resign if he were "bound not to oppose any part of the Code."<sup>448</sup> He made a distinction between public and private issues:

Is not the true position rather this:

The adoption of the Code in any state is not a private issue, but an important public question. On such questions, the public has the right to the honest judgment of all informed persons. People who have worked on the Code, whether for pay or not, have some knowledge of its contents and some judgment of its probable effect. The public has a right to that knowledge and that judgment. Their public duty therefore is neither silence nor a party line, but honest public statement of what they really think. And since the question is a public one, the public duty is controlling.<sup>449</sup>

Herbert Goodrich, the Director of the ALI, tried to calm

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446. *Id.* at 4.

447. *Id.* at 5.

448. Letter from Charles Bunn, Professor, University of Wisconsin Law School, to William A. Schnader, Esq., Schnader, Harrison, Segal & Lewis 1 (Nov. 9, 1951) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

449. *Id.* at 1-2.



things down. On November 15, observing that "[e]motional thermometers have recorded much too high a degree of tension for the good of the circulatory system of those involved,"<sup>450</sup> he requested that Bunn redraft the comments for articles 4 and 5 in neutral fashion. "The Board is unanimous in wanting Comments that do not slant either way but are, so far as possible, a fair expression of the text as adopted by the Joint Meeting."<sup>451</sup> He wanted to get the job done:

A moderate amount of violence between persons, as I understand from the psychiatrists, is a valuable method of letting off steam. But I really think on the Comments to Articles 4 and 5 we have had plenty of steam and now it would be a good thing if we got the job done.<sup>452</sup>

Later, on December 5, he again wrote to Bunn, trying to smooth the waters.

The Institute has never said anything and I am sorry that anybody else has. I would rather not say anything at this moment. But after some of the smoke dies down I think we can get a statement that will satisfy you and everyone else. Of course I am sure that none of us has the slightest desire to gag you or anyone else.<sup>453</sup>

Malcolm evidently again redrafted article 4 and came up with compromise acceptable to both Gilmore and the Federal Reserve Board. On April 12, 1952, Schnader wrote Professor Maurice H. Merrill, who had joined Gilmore in opposition, announcing the agreement over Malcolm's redraft.

Several days ago I received from Walter Malcolm, Chairman of the Committee on Commercial Code of the Section on Corporation, Banking and Business Law of the American Bar Association, a letter containing a revised draft of the entire section, together with comments thereto.

As I understand it, this draft has the approval of Professor Gilmore of Yale University Law School, who joined you in vigorous

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450. Letter from Goodrich to Bunn, *supra* note 122, at 1.

451. *Id.*

452. *Id.*

453. Letter from Herbert F. Goodrich, Director, A.L.I., to Charles Bunn, Professor, University of Wisconsin Law School (Dec. 5, 1951) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

opposition to the section as it originally stood, and also of counsel for the Federal Reserve System, although the latter are always very careful to say that they are not speaking officially.<sup>454</sup>

The compromise version of section 4-103 has lasted with few changes to the present day. It permits banks to contract out of article 4 and allows some contracts between banks to affect the rights of third-parties, the customers of banks. Its complicated provisions reflect the fact that it was a product of negotiation.

Section 4-103(1) states that the article's provisions may be varied by agreement, but "no agreement can disclaim a bank's responsibility or limit the measure of damages for its own lack of good faith or failure to exercise ordinary care."<sup>455</sup>

Subsection (2) departs from the rule that a contract between two parties cannot deprive a third party of rights by stating:

(2) Notwithstanding the provisions of Section 1-102(3)(b), Federal Reserve Regulations and operating letters, clearing house rules, and the like, have the effect of agreements under subsection (1), whether or not specifically assented to by all parties interested in items handled.

Furthermore, action pursuant to such regulation, agreement, and general banking usage constitutes *prima facie* ordinary care:

(3) Action or non-action approved by this Article or pursuant to Federal Reserve regulations or operating letters constitutes the exercise of ordinary care and, in the absence of special instructions, action or non-action consistent with clearing house rules and the like or with a general banking usage not disapproved by this Article, *prima facie* constitutes the exercise of ordinary

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454. Letter from William A. Schnader, Esq., Schnader, Harrison, Segal & Lewis, to Maurice H. Merrill, Professor, University of Oklahoma Law School 1 (Apr. 12, 1952) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

455. This language is identical to that of § 4-103(1), titled "Variation by Agreement," which was also proposed by Malcolm. U.C.C. § 4-103, Official Draft: Text and Comments Edition (1952), *reprinted in* 16 U.C.C. DRAFTS 477 (E. Kelly ed., 1984). The language was first proposed in U.C.C. § 4-103, Proposed Changes in Article 4 (May 16, 1952), *reprinted in* 13 U.C.C. DRAFTS 111 (E. Kelly ed., 1984).

care.<sup>456</sup>

Comment 3 attempted to limit what "and the like" meant. It would include agencies and additions of banks that function like clearinghouses, but it would not include all agreements between banks.<sup>457</sup>

Because conformance "with clearinghouse rules or the like or with such banking usages" constitutes only the *prima facie* exercise of ordinary care, the courts had "the ultimate power to determine ordinary care in any case where it should appear desirable to do so. The *prima facie* rule does, however, impose on the party contesting the standards to establish that they are unreasonable, arbitrary or unfair."<sup>458</sup>

The compromise section 4-103 gave the bankers great flexibility and freedom to modify the statutory rules. It represents again the triumph of contract. "Contract" is stretched to include the fine print in banking forms and general authorizations.<sup>459</sup> Contracts between banks acting in concert can also affect others' rights.

### III. THE CODE FROM 1952 TO 1954

#### A. *The Failure of Immediate Enactment*

Unfortunately for the Code, the bankers were not

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456. U.C.C. § 4-103, Official Draft: Text and Comments Edition (1952), reprinted in 16 U.C.C. DRAFTS 477 (E. Kelly ed., 1984).

457. "An agreement between a number of banks or even all the banks in an area simply because they are banks, would not of itself, by virtue of the phrase 'and the like,' meet the purposes and objectives of subsection (2). U.C.C. § 4-103, cmt. 3, Official Draft: Text and Comments Edition (1952), reprinted in 16 U.C.C. DRAFTS 481 (E. Kelly ed., 1984).

458. U.C.C. § 4-103, cmt. 4, Official Draft: Text and Comments Edition (1952), reprinted in 16 U.C.C. DRAFTS 482 (E. Kelly ed., 1984).

459. For example, comment 2 states:

The agreement may be direct, as between the owner and the depository bank; or indirect, as where the owner authorizes a particular type of procedure and any bank in the collection chain acts pursuant to such authorization. It may be with respect to a single item; or to all items handled for a particular customer, e.g., a general agreement between the depository bank and the customer at the time a deposit account is opened. Legends on deposit tickets, collection letters and acknowledgments of items, coupled with action by the affected party constituting acceptance, adoption, ratification, estoppel or the like, are agreements if they meet the tests of the definition of "agreement."

U.C.C. § 1-201(3), cmt. 2, Official Draft: Text and Comments Edition (1952), reprinted in 16 U.C.C. DRAFTS 478 (E. Kelly ed., 1984).

mollified. Malcolm's draft of article 4, even though bitterly criticized by Beutel, Gilmore, and Mentschikoff as a sell-out to the bankers, still did not assuage that group. The bankers still hoped to kill the entire U.C.C.<sup>460</sup> and remained in opposition.<sup>461</sup> The Code was adopted in Pennsylvania, but the bankers' opposition damaged its chances of adoption in Indiana, and most importantly, persuaded Governor Dewey to defer its passage until after review by the NYLRC.<sup>462</sup>

New York, however, was the key state. At first the Code's proponents were hopeful about enactment there. Governor Dewey, however, seemed to have cold feet. Schnader wrote Mentschikoff that the Governor was not backing the Code strongly:

As far as New York is concerned, things there are not in the cozy situation in which you seem to feel they are. I personally had a long talk with Governor Dewey's Legislative Counsel a day or so ago. He told me that there had been a misunderstanding about the Governor's position; that until the text and comments of the Code were available, the Governor was clearly not in a position to advocate passage of the Code; and that the only thing that he deemed possible was to have the Governor mention the Code in his 1952 message and ask the Legislature to study it prior to the 1953 session.

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460. See Letter from Kleitz to Brace, *supra* note 394.

A committee of the Commerce and Industry Association of New York, of which I am acting chairman, brought in a recommendation, which was unanimously approved by the directors of the Association, to ask Governor Dewey to postpone consideration of the Code for at least a year. . . . What I am really hoping is that we can kill the thing entirely. *Id.*; see also Letter from Marcus E. Conrad, Vice President, The Chase National Bank, to James G. Hall, Executive Vice President, First National Bank, Birmingham, Alabama (Feb. 9, 1953) (characterizing the Code as making "extensive and radical changes" and requesting an effort "to have the introduction of this legislation delayed until there has been an opportunity to study it and make changes which we believe would be advantageous") (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

461. See, e.g., News Release of American Bankers Ass'n News Bureau, A.B.A. Committee Disapproves Proposed Uniform Commercial Code in its Entirety—Recommends Incorporation of Desirable Sections into Existing Statutes by Amendments (Oct. 20, 1954), Llewellyn Papers, J. XVI.1.b. (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review); Twining, *supra* note 219, at 293.

462. See Letter from Pantzer to Schnader, *supra* note 127, at 1-2 (concerning Indiana); TWINING, *supra* note 219, at 293 (concerning New York).

That is a shocking disappointment to me, but it just emphasizes the fact that now is no time for any of us to start fighting with each other because somebody doesn't like the work which somebody else did on Code or Comments.<sup>463</sup>

In a letter of May, 1952, Schnader speaks of "Governor's change of heart" making "it impossible for us to proceed with our plan to let the text, as adopted by the New York Legislature in 1952, become the official text by action of the Institute and the Conference at their May and September meetings, respectively."<sup>464</sup>

In the same letter, Schnader describes how Llewellyn went off on his own and introduced his own version of the U.C.C. in the New York legislature! Perhaps Llewellyn, sharing his wife's sanguine view of the Code's chances in the New York legislature,<sup>465</sup> decided to take matters in his own hands.<sup>466</sup> Evidently, Schnader's pessimistic view of the Code's changes were more accurate than Llewellyn's, for nothing more was heard of Llewellyn's initiative.

The Report of the Association of the Bar of the City of New York, presented on January 20, 1953, further damaged the Code's prospects.<sup>467</sup> The Association came out against the U.C.C.'s enactment, saying it needed more study.<sup>468</sup> The bar group noted that the proposed act was "social," which at that time meant that it would work toward redistributing wealth and power in society.<sup>469</sup> The Report did object to the new meanings and complicated nature of the language of the Code, but moreover commented that the Code revealed "new social tendencies."<sup>470</sup> Later, the Report lists unconscionability and the regulations on limiting consequential damages as

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463. Letter from Schnader to Mentschikoff, *supra* note 84, at 3.

464. Letter from William A. Schnader, Esq., Schnader, Harrison, Segal & Lewis, to Martin J. Dinkelspiel, Esq. 5 (May 5, 1952) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

465. See Letter from Mentschikoff to Schnader, *supra* note 111, at 2.

466. "Incidentally, after the Executive Committee meeting in Chicago, Karl Llewellyn took himself to Albany and made thirty-five changes in the text of the Code, and, as thus modified, the Code was introduced into the New York Legislature in the closing hours of the 1952 session." Letter from Schnader to Dinkelspiel, *supra* note 464, at 2.

467. The Association's Report is reprinted in 15 U.C.C. DRAFTS 309-50 (E. Kelly ed., 1984).

468. *Id.* at 318.

469. Palmer, *supra* note 149, at 14.

470. Report of the Association of the Bar of the City of New York, *reprinted in* 15 U.C.C. DRAFTS 317 (E. Kelly ed., 1984).

new social concepts.<sup>471</sup> The Report's Appendix pointed out that "The Code would extend the 'public policy' concept to areas where neither statutes nor decisions have heretofore reached."<sup>472</sup> It notes that article 2 would change contract law, for example, in allowing indefinite contracts and firm offers by merchants.<sup>473</sup> All in all, the New York Bar Association was negative, recommending further study.

The Code drafters thought they were done in 1951. "The UCC is now finished and here it is."<sup>474</sup> One year later, they stated, "We hope that these may be the last changes which the Editorial Board may find it necessary to approve."<sup>475</sup> They had bad luck, however. In Indiana, the opposition of the Chase National Bank "did a great deal of damage." Moreover, the Code had to compete in the Indiana legislature with a proposed Model Probate Code and a Criminal Code, which both "took up very much of the time of the legislators." Then the Code stepped into the middle of a fight between the Eisenhower Republicans in the Indiana House led by Governor Craig, and the Taft Republicans in the Indiana Senate. Since Governor Craig was in favor of the bill, a key committee chair who was a Taft Republican did not support it.<sup>476</sup>

In Massachusetts, the Code hit another road block. The chair of a key committee was one Senator Ralph V. Clampt, "a man of very limited capacity and [who] at the same time has an exalted opinion of his position and his role in the legislature."<sup>477</sup> He took the position that "he personally had to check, argue about, and be convinced of substantially every

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471. Report of the Association of the Bar of the City of New York, *reprinted in* 15 U.C.C. DRAFTS 327-28 (E. Kelly ed., 1984).

472. Report of the Association of the Bar of the City of New York, *reprinted in* 15 U.C.C. DRAFTS 321 (E. Kelly ed., 1984).

473. Report of the Association of the Bar of the City of New York, *reprinted in* 15 U.C.C. DRAFTS 325-26 (E. Kelly ed., 1984).

474. Forward, U.C.C. Final Text Edition (Nov. 1951), *reprinted in* 12 U.C.C. DRAFTS 414 (E. Kelly ed., 1984).

475. See U.C.C. § 9-312, Recommendations of the Editorial Board (Dec. 29, 1952), *reprinted in* 15 U.C.C. DRAFTS 352 (E. Kelly ed., 1984); *see also* Letter from Milton P. Kupfer, Esq., Kupfer, Silberfeld, Nathan & Danziger, to Herbert F. Goodrich, Director, A.L.I. (Feb. 5, 1952) (stating that his suggestions about proposed comments must be narrow "since we all should now regard the Text as 'frozen'") (on file with the Buffalo Law Review).

476. See Letter from Pantzer to Schnader, *supra* note 127, at 3.

477. Letter from Walter D. Malcolm, Esq., Bingham, Dana & Gould, to Carl W. Funk, Esq., Drinker, Biddle and Reath 1 (Oct. 6, 1954) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

provision in it."<sup>478</sup> He also wanted the Code to be subject to interstate compacts. Since Senator Clampit did not understand all the Code, he set out to stall it. Thus the Massachusetts proponents of the Code decided not to run the risk of having the Code defeated by his opposition and decided to wait till 1955 to reintroduce it.<sup>479</sup>

All hopes of quick passage were dashed by Governor Dewey's referral of the U.C.C. to the New York Law Revision Commissions on February 8, 1953. The arduous NYLRC review process took three years and cost "nearly one-third of a million dollars."<sup>480</sup> The drive to have the Code enacted was postponed. In the words of Malcolm, "I have picked up from several sources that state after state is waiting to see what New York does."<sup>481</sup> Pennsylvania enacted the Code in 1953, but it remained the only state to adopt the Code until Massachusetts in 1957.<sup>482</sup> The drafters and proponents again had to wait and continue to amend their work. Here, one has to step back and express one's respect, admiration, and awe at the proponents' tenacity. In 1942, Llewellyn had predicted completion by 1946.<sup>483</sup> By 1953, after working for thirteen years, the drafters were faced with another massive process of revision, but undertook it and finally succeeded, years later, in obtaining the Code's enactment.

### B. *Initial Response to the NYLRC Proceedings*

There were few changes to the Code between 1951 and the start of the NYLRC process. As stated above, a compromise was reached as to the banking article. One change was caused by the Surety Association's sudden realization that a Uniform Commercial Code was in the works and that it might affect its members. As drafted, section 9-312(7) gave priority to a secured party over a construction surety. In response to the Surety Association's protest, that sub-section was stricken.<sup>484</sup>

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478. *Id.*

479. *Id.*

480. TWINING, *supra* note 219, at 293.

481. Letter from Malcolm to Schnader, *supra* note 141, at 1.

482. Robert Braucher, *The Legislative History of the Uniform Commercial Code*, 58 COLUM. L. REV. 798 (1958).

483. Commercial Law, Time Schedule (1942) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

484. See U.C.C. § 9-312, Recommendations of the Editorial Board (Dec. 29,

The drafters were gearing up to deal with the NYLRC. Malcolm felt that the Commission or at least part of it had a "friendly disposition toward the Code. . . . On the other hand, the public reaction to the Code in New York is predominantly hostile. A major part of this hostility is traceable to the New York City banks, abetted and perhaps led by some of their counsel." Malcolm felt that the Commission was bound to be affected by the bank's opposition. The bankers criticized every section of articles 4 and 9, going so far as to claim the Code was "communist inspired."<sup>485</sup>

In response, Malcolm proposed the creation of groups that would consider and respond to criticisms of the Code. These could work with the NYLRC and the opposing groups. The drafters' groups would cooperate with the NYLRC to find mutually satisfactory solutions.<sup>486</sup>

The Code Editorial Board instituted Malcolm's proposals at its meeting of June 14, 1954. Teams were set up to study objections, answer them, and in the case of well-founded objections, prepare revisions to the sections.<sup>487</sup> These subcommittees were formed and prepared reports.<sup>488</sup> Furthermore, the NYLRC agreed to distribute the reports of NYLRC meetings to the Code subcommittees.<sup>489</sup> Thus the Code drafters could change the Code in response to the NYLRC before that organization's final report. Many of the subcommittee's recommendations appeared in "Supplement No. 1" of 1955.<sup>490</sup>

The end result of the NYLRC process was that the U.C.C., which had started as a commercial system in which merchants were subject to regulation by trade norms, merchant tribunals, mandatory legislation, and judicial

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1952), *reprinted in* 15 U.C.C. DRAFTS 414 (E. Kelly ed., 1984).

485. Letter from Malcolm to Schnader, *supra* note 141, at 2.

486. *Id.* at 3-5.

487. See Herbert F. Goodrich, Chairman, Minutes of the Meeting of the Editorial Board of the U.C.C. 1 (June 14, 1954) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

488. See, e.g., Uniform Commercial Code, Report of Subcommittee on Article 2 to Editorial Board of Sponsoring Organizations (Sept. 30, 1954), Llewellyn Papers J.XVI.2.a. (on file with the Llewellyn Archives, University of Chicago Law Library, and the Buffalo Law Review).

489. See Memorandum from the NYLRC to Members of the Enlarged Editorial Board of the U.C.C. 1 (Nov. 30, 1954) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

490. See U.C.C. Supplement No. 1 (1955), *reprinted in* 17 U.C.C. DRAFTS 307-507 (E. Kelly ed., 1984).



oversight, became even more based on laissez-faire.

The 1957 Official Text adopted an explicit mention of "freedom of contract" as a purpose of the Code.<sup>491</sup> "Usage of trade's" role of directly governing merchant behavior was changed to that of a principle of contract interpretation. The 1956 Recommendations changed the rule that usages of trade bound contracting parties to today's language, in which a course of dealing and any usage of trade "gives particular meaning to and supplements or qualify terms of an agreement."<sup>492</sup> The pre-1956 U.C.C. provided that an "agreement" could be found equally from either contract language or usage of trade.<sup>493</sup> Now usage of trade was demoted to be only a way of understanding the controlling language of the parties.<sup>494</sup>

Thus ended Llewellyn's drive to put in place the folkways of merchants, the norms of decent commercial behavior, as the cornerstone of commercial law.

The doctrine of unconscionability, another basis for regulating private contracts, was also cut back. In response to the initial NYLRC hearing in 1955, the drafters amended section 2-302 to make clear that the issue was a matter of law and that unconscionability had to exist "at the time it [the contract] was made."<sup>495</sup> Juries were not to be turned loose on business behavior; nor could judges consider developments occurring after a contract was made.

Section 4-103 was changed to allow the parties to a banking transaction (i.e., the banker) to determine the standards to measure "good faith" and "ordinary care."<sup>496</sup> The

491. "Subsection (3) states affirmatively at the outset that freedom of contract is a principle of the Code: 'the effect' of its provisions may be varied by 'agreement.'" U.C.C. § 1-102, cmt. 3, Official Text (1957), *reprinted in* 16 U.C.C. DRAFTS 477 (E. Kelly ed., 1984).

492. U.C.C. § 1-205(3), Recommendations (1956), *reprinted in* 18 U.C.C. DRAFTS 40 (E. Kelly ed., 1984). The change was made to meet "an objection made on behalf of the American Bankers Association." U.C.C. § 1-205(3), Recommendations (1956), *reprinted in* 16 U.C.C. DRAFTS 477 (E. Kelly ed., 1984).

493. Agreement could be found in "the language of parties or in course of dealing or usage of trade or course of performance." U.C.C. § 1-201(3), Recommendations (1956), *reprinted in* 18 U.C.C. DRAFTS 32 (E. Kelly ed., 1984).

494. "This act deals with 'usage of trade' as a factor in reaching the commercial meaning of the agreement which the parties have made." U.C.C. § 1-205, cmt. 4, Official Text with Comments (1957), *reprinted in* 19 U.C.C. DRAFTS 65 (E. Kelly ed., 1984).

495. U.C.C. Supplement No. 1, § 2-302(1) (1955), *reprinted in* 17 U.C.C. DRAFTS 326 (E. Kelly ed., 1984).

496. U.C.C. § 4-103, Recommendations (1956), *reprinted in* 18 U.C.C. DRAFTS

"Reason" given read: "The additional changes are to reconcile this Section 4-103(1) with Section 1-102(3)."<sup>497</sup>

Allowing private contracting to set standards in banking has its own peculiar ramifications. The bank's customer has no power to bargain for favorable standards. Also, the banking article defines agreement to include "Federal Reserve regulations and operating letters, clearing house rules and the like,"<sup>498</sup> so standards may be set inside the banking industry with no customer participation whatsoever. Llewellyn's program to achieve equal bargaining and participation in law making and adjudication here met total defeat.

A similar defeat occurred in article 9, where the 1956 Recommendations edited out the last vestiges of the consumer protection provisions. Section 9-206 had provided for some preservation of consumer defenses against the secured lender or an assignee. This protection was deleted in 1956.<sup>499</sup> In 1951, Grant Gilmore had written that financiers were being offered a deal: a vastly improved secured transactions law in return for consumer protection.<sup>500</sup> By 1956, the financiers had an unhindered security device, but the consumer protection sections were gone.

### *C. The Assumptions of the NYLRC Proceedings*

As we have seen, the NYLRC shifted the Code to be even more based on private, unregulated contract. Most of its work, however, was on the details of the Code, perfecting and polishing the Code language. Although the NYLRC would spend one-third of a million dollars and three years critiquing the Code, the issue of ultimate approval was never really in doubt. In October of 1954, Walter Malcolm had a confidential conference with Professor John MacDonald, the Executive Secretary and Director of Research of the NYLRC. Malcolm reported that the Commission wanted a Code, that it accepted the basic framework, organization and structure of

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159 (E. Kelly ed., 1984).

497. U.C.C. § 4-103, Recommendations (1956), reprinted in 18 U.C.C. DRAFTS

159 (E. Kelly ed., 1984).

498. *Id.*

499. U.C.C. § 9-206, Recommendations (1956), reprinted in 18 U.C.C. DRAFTS

294 (E. Kelly ed., 1984).

500. See Gilmore, *supra* note 62, at 47.

the Code.<sup>501</sup> The Commission did have problems with

501. A portion of Malcolm's Confidential Summary is set out below:

CONFIDENTIAL October 14, 1954

Summary of Conference With

Professor John MacDonald

and his assistant, October 13, 1954

1. Emphatically Professor MacDonald (and he thinks the Commission) would like to see a Code. They have no desire to kill the Code.

a. If the Code were killed or died, the Commission would have "twenty years" of work to achieve much that is in the Code.

2. The Commission questions the original policy decision to treat the subject matter of the various articles all at one time, as distinguished from dealing with particular subject matters piecemeal. The Commission criticizes strongly the failure of the Code's sponsors and reporters to thoroughly research all subject matter first and then draft on the basis of such research. *However*, now that the Code has reached the stage that it has, the Commission is prepared to accept the basic framework of the Code *as is*.

a. There has not been and is not now any serious criticism of the basic organization and structure of the Code, e.g.

1. The treatment of bonds and debentures in Article 8 under the general heading of Investment securities.

2. The shift from the title theory in Article 2 on Sales.

3. The general treatment of secured transactions in Article 9.

b. In fact, Professor MacDonald indicated that the Commission agreed with these major decisions.

c. The objections the Commission has to the Code have to do with individual sections or in a few instances specific problems appearing in up to, say, five or six sections.

3. In the area of individual rules appearing in single sections or groups of sections, the Commission thinks there is a *lot* of work still to be done on the Code.

a. The Article causing most trouble and concern is Article 2 on Sales.

1. Article 2 contains *many* excellent rules which the Commission likes.

2. However, in many instances, Text and Comment are inconsistent or Comment definitely goes beyond Text and states substantial rules of law not in Text.

(a) In many instances the Comment states a *desirable* rule that either is not in Text or is inconsistent with Text.

3. A number of the defects in Article 2 would throw the law back fifty or seventy-five years.

4. Illustrations of defects include:

(a) The rules regarding insurable interests, anticipating breach.

(b) The use of language in regard to offer and acceptance, etc. broad enough to apply to the general law of contracts as distinguished from the law of sales.

(c) Failure to provide a statute of frauds for an outright sale of accounts, e.g. by a dentist, selling by practice. Professor Braucher's answer to this in his report is not sufficient.

(d) The *definition* of "merchant" Professor MacDonald does not object in the least to separate rules for a "merchant"-in fact, likes them *very*

individual sections, however, particularly with those of article 2. The worst case scenario would be that the report of the NYLRC would say that twenty-five percent of the sections needed changes but that there was "a strong desire to continue and extend cooperation between the Commission and the sponsors (presumably to the end that the Commission could approve the Code, with amendments)."<sup>502</sup>

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*much.*

(e) Treatment of creditors [sic] rights.

5. Proper redrafts of objectionable sections would not materially lengthen present Text. In many places would shorten.

b. The proposed changes in Article 4 in our sub-committee's draft report eliminate 75% of Commission's problems with Article 4.

c. Article 9 is in quite good shape and was a well-drafted article.

d. Articles 7 and 8 are farther behind other articles in processing by the Commission. In Article 8, the Commission is disturbed by problem of "allocation securities", the full implications of which I did not get.

4. The work and future activities of the Commission are affected by political considerations. Governor Dewey has taken a definite interest in the Code. This interest in the Code has definitely not been one of hostility but rather one of "where do we go from here?" (Presumably to get a Code.). The Commission is not sure what the reaction of either of the present candidates for Governor will be.

5. The present appropriations of the Commission will expire on March 31, 1955, but this does not mean it must stop work on the Code at that time. It should be able to get further appropriations.

6. The Commission must fill some sort of report out early in 1955. Professor MacDonald is sure this will not be a report that the Code should be enacted in New York in 1955. No decision has yet been made as to what report will be filed.

a. If the relative attitudes of the sponsors and the Commission should be non-cooperative, the report might say that 25% of the sections needed changes. (This was not stated by Professor MacDonald but since this is a present estimate of "defective" sections, this possibility should be envisaged.)

b. If further and more extensive cooperation between the two groups could be developed, it would be perfectly possible for the Commission to file in early 1955 some innocuous interim report of "progress" and merely publish the report of the hearings.

7. On the assumption that further means of cooperation between the two groups could be developed, I inquired as to the Professor's estimate as to how long it would take to get the "25%" of questionable sections in shape so that the Commission would be satisfied with the Code. His first rough estimate was 18 months. However, later he thought it would be entirely feasible to get all work done so that a bill could be filed, e.g. in Massachusetts, in time for the 1956 legislature.

Walter Malcolm, Summary of Conference with Professor John MacDonald 1-6 (Oct. 14, 1954) (on file with the A.L.I. Archives, University of Pennsylvania Law Library, and the Buffalo Law Review).

502. *Id.* at 7.

Thus the NYLRC process did not focus on the basic assumptions that underlay the Code's drafting. Such fundamental concepts as using trade usage as commercial law norms, the flexible contract provisions, the non-inclusion of consumer legislation, and the unitary and all-powerful article 9 security interest were not debated. Since then, almost all Code commentary has been on the details rather than the whole. Most commentators on the U.C.C. start with the NYLRC's study of the Code.<sup>503</sup> In doing so, they ignore the fundamental decisions about commercial law made by the drafters. And so we leave our study of the Code where others start.

#### D. *Where are They Now (or the Return of the Repressed)*

Like seeing a trailer at the end of a movie which tells of the fate of the characters, it is entertaining to see what happened to the proposals we have studied. Many of the proposed reforms rejected by the Code drafters have come back into the law by other routes. Turning back to the original list on page 399, we see that article 3's objective good faith, dropped in the NYLRC process, re-enters as today's section 3-103(4). The sections about beneficiaries of warranties and the use of direct actions against manufacturers re-emerges as the tort law of product liability. The consumer disclosures of article 9 reappear as the federal Truth-in-Lending Act (15 U.S.C. § 1601). The assertion of defenses against an assignee of a consumer contract is now enabled by the FTC Regulation (16 C.F.R. pt. 433). The floating lien has been somewhat restricted in the bankruptcy law (11 U.S.C. § 547(b)(5)). The flexibility of Malcolm's article 4 has been limited by the FRB's Regulation CC (19 C.F.R. Pt. 229), which closely regulates the return of unpaid checks. Llewellyn's changes in contract law have been adopted outside of the confines of article 2 by the Restatement (Second) of Contracts.

But, as the controversy over product liability shows,<sup>504</sup> the

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503. "The 'legislative history' has come to mean the New York Law Revision Commission's Report of 1954-56 on the 1952 Official Draft and the subsequent revisions." Wiseman, *supra* note 2, at 467 (footnote omitted).

504. See, e.g., *A Symposium on the ALI's Proposed Restatement (Third) of Torts: Products Liability*, 61 TENN. L. REV. 1043 (1994); *Special Issue: Review of the System of Products Liability Law*, 36 SO. TEX. L. REV. 227 (1995); *Products Liability Symposium*, 30 U. MICH. J. L. REFORM 197 (1997). In 1998, the ALI

wars over these issues are far from over. The compromises made by the Code drafters and the affected parties were only temporary truces made in an ongoing conflict.

### CONCLUSION

Under the original proposals, merchants would contract under the control of trade norms, judicial supervision, and legislature dictate, with their fellow merchants reviewing their performance. The deviant merchant would be controlled by the Code and the judge acting together with merchant tribunals to decide commercial issues using standards given by trade norms. The judge and the merchant tribunals would measure the reasonableness of the contract and the contract performance by using the yardsticks of equal bargaining power, trade norms, and the provisions of the Code.

The original version changed into today's U.C.C., which exists more as a set of default rules that govern only if the private contracting does *not* cover the issues. Many sections just give green light/red light rules (e.g., F.O.B., C.I.F., F.A.S.) which formally allocate rights and responsibilities in the absence of contrary agreement.

Today the U.C.C. serves as a framework for private contracting. This means that the seller of consumer goods, the banker, and the financier get to structure the terms of the deal. A statute that originally was to empower the trade as a whole, the small decent merchant, and the consumer turned into one that empowers commercial entities. Freed of outmoded rules and restrictions, sellers, bankers, and financiers can now get what they want. "Freedom of Contract" submerged the academic-regulatory proposals. But these proposals still surface in such provisions as unconscionability, the objective good faith of articles 2 and 3, the reading of trade usage into contract language, and the "reasonables" pervading the Act. There is still much opportunity for judicial and trade regulation. Federal law and tort law now embody the discarded consumer protection sections. Much of the litigation generated by the U.C.C. stems from the conflict between the ideals of business autonomy and the achievement of good trade practices by regulation.

The change from the original proposals to what we have

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promulgated its RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY (1998).

now has taken sixty years. It has not been a process of applying neutral expertise to craft a technically perfect commercial law. It has been a political process that has created winners and losers. The present controversies over such issues as strict liability in tort, bankruptcy, and consumer rights, show that the battles over such values are not over and that we can decide on these values anew.