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## Is Article 2 the Best We Can Do?

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# Is Article 2 the Best We Can Do?

by  
ROBERT E. SCOTT\*

## Introduction

You will all be happy to know that, having listened to my colleagues for the last three hours, I have completely forgotten what I was planning to say. But I haven't forgotten why I am here. I am the proverbial skunk at the garden party, and I hope to fulfill my role as the only skeptic in the group. I must tell you candidly, however, that I agree with everything Gail Hillebrand had to say. That doesn't mean she is going to agree with anything that I have to say, but perhaps there are two skeptics here this afternoon.

My perspective differs significantly from my colleagues on the panel, although they are all people whom I respect enormously. My colleagues are all, in one way or another, uniform laws' insiders. I have had only one foray into this process as a member of the Article 9 study group, and it cured me permanently of any further inclinations to join Dick Speidel in the uniform laws trenches.<sup>1</sup> My perspective, therefore, is largely informed by legal theory. Many of my fellow panelists have shared with me, some privately, others in print, their skepticism about the role of theory in this debate.<sup>2</sup> That is to be expected. Commercial lawyers are, after all, hard-nosed realists. In any event, those of us who do theory have as our first article of faith that skepticism about theory is always justified. But the point I would make is that, while skepticism about theory is justified, ignorance of theory is not. So, while I don't hope to persuade any hard-nosed realists that have held out thus far this afternoon (certainly not after three hours), I do hope that some of you will pause for a moment to

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1. My own version of the experience of making uniform-laws sausage is described in Robert E. Scott, *The Mythology of Article 9*, 79 MINN. L. REV. 853, 856-58 (1995), and in Robert E. Scott, *The Politics of Article 9*, 80 VA. L. REV. 1783, 1807-10 (1994).

2. See, e.g., Fred H. Miller, *Realism Not Idealism in Uniform Laws—Observations from the Revision of the UCC*, 39 S. TEX. L. REV. 707 (1998).

think about the larger theoretical and structural questions that inform this debate.

Here are the central questions of institutional design that this debate needs to engage: What does positive political theory tell us about the uniform laws process in general?<sup>3</sup> And, what does the economics of incomplete contracting tell us about the UCC project, and most especially Article 2, in particular?<sup>4</sup> I don't claim that any of my views on those questions are right. But I do claim that they are considered, and that they are informed by work from other disciplines that, on its own terms, is respected and influential. Moreover, as Lance Liebman so correctly said, these are questions that deserve to be asked and, more importantly, deserve to be debated. I have written on these topics myself, but I would be the first to tell you that whatever I have offered thus far is only the first cut at very difficult questions.<sup>5</sup>

To clarify the debate at the outset, there are actually two separate issues here. The issues overlap, but they are distinct, and it

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3. The analyst using the tools of positive political theory identifies the utility functions that participants in the legislative process maximize, specifies the institutional structures that transform participant preferences into legislative outcomes, and then shows what outcomes these preferences and structures will produce. See Kenneth A. Shepsle & Barry R. Weingast, *Structured-Induced Equilibrium and Legislative Choice*, 37 PUB. CHOICE 503 (1981).

4. Much of the incomplete Contracts literature can be seen as a natural extension of the transactions cost literature most associated with the work of Oliver Williamson. See OLIVER WILLIAMSON, *MARKETS AND HIERARCHIES: ANALYSIS OF ANTITRUST IMPLICATIONS* (1975). These models focus on the costs of describing or specifying ex ante all of the contractual contingencies for every possible state of nature. Owing to these costs, parties will write incomplete contracts and then renegotiate when a particular state of nature is realized. See, e.g., Oliver Hart & John Moore, *Foundations of Incomplete Contracts*, 66 REV. ECON. STUD. 115 (1999). The inability of these exogenous transactions cost explanations of incompleteness to predict the contracts that we see in the world has led to efforts to explain incompleteness in a world where transactions costs are zero. These models explain incompleteness as endogenous owing to asymmetric information. Under these conditions, parties choose not to complete contracts so as to avoid moral hazard or adverse selection problems. See, e.g., B. Bernheim & M. Whinston, *Incomplete Contracts and Strategic Ambiguity*, 88 AM. ECON. REV. 432 (1998).

5. For my take on both of these questions, see Alan Schwartz & Robert E. Scott, *The Political Economy of Private Legislatures*, 143 U. PA. L. REV. 595 (1995) (using positive political theory to analyze the products of the uniform laws process) [hereinafter Schwartz & Scott, *Political Economy*]; Robert E. Scott, *The Politics of Article 9*, 80 VA. L. REV. 1783 (1994) (same); Robert E. Scott, *The Uniformity Norm in Commercial Law: A Comparative Analysis of Common Law And Code Methodologies*, in *THE JURISPRUDENTIAL FOUNDATIONS OF CORPORATE AND COMMERCIAL LAW* 127 (Cambridge University Press, 2000) [hereinafter Scott, *Uniformity Norm*]; Robert E. Scott, *The Case for Formalism in Relational Contract*, 94 NW. U. L. REV. 847 (2000) (using both the theory of incomplete contracting and some empirical evidence to suggest that the formal modes of interpretation employed in the common law may well produce more uniformity than the functionalist, incorporation approach of Article 2).

is important for us to keep them distinct. The first issue, the one that is the primary focus of this session, is to ask: What is the efficacy of the uniform laws process of the ALI and NCCUSL (what I have previously called the process of private legislatures)?<sup>6</sup> The questions that underlie this issue go something like this: What does this process do relatively well and what does it do relatively badly in comparison to an appropriate baseline such as the ordinary legislative process? And further, are there systematic or structural factors that bias the products of the uniform laws process notwithstanding the good will, the intelligence, and the effort of those that have labored for many years in the law reform trenches?

There is a second issue, one that is also fundamental, at least to those of us who are commercial lawyers: what do we make of the UCC project itself? It seems the right time to evaluate this grand experiment in the codification of commercial law. As Henry Gabriel said, we are at fifty years now, and we have a body of experience—both good and bad—in codifying a uniform commercial law. In appraising the success of the UCC, it is appropriate to cabin Article 2 and sales law as being (as we all recognize) fundamentally distinct from the other products of the UCC project. The questions here are somewhat different. What do we mean by uniformity? Has the UCC and particularly Article 2 succeeded on its own terms in promoting uniformity? Is the effort to join mandatory consumer protection with commercial law default rules in a single statute wise? Obviously, I can't address all these questions adequately in the time remaining, and you would, I suspect, vote with your feet were I to try to do so, but I would like to sketch some ways of thinking about the most salient ones.

## I. An External Critique: The Political Economy of the Uniform Laws Process

First, let's take a moment to focus on the political economy of the uniform laws process. Dick Speidel told a moving story. I've not heard it before. He left one part of the story out, however, and I want to fill in that piece of the puzzle, because it provides you with my perspective. Five years ago, my colleague Alan Schwartz and I wrote a law review article on the political economy of private legislatures that arose out of our experiences with the uniform law process, mine in Article 9, his with the products liability project.<sup>7</sup> And, we tried to inform our analysis with positive political theory (because that's what

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6. See Schwartz & Scott, *Political Economy*, *supra* note 5.

7. Alan Schwartz & Robert E. Scott, *The Political Economy of Private Legislatures*, 143 U. PA. L. REV. 595 (1995).

we like to do as self-indulgent law professors). We presented the paper, quite coincidentally, right here in San Francisco in January, 1995. I think it might have been in this room.

Here is what we said. We made a prediction. The prediction was that the Article 2 process which was then underway would result in a vague and open-ended revision that largely reinforced the status quo. This prediction would hold, we said, irrespective of the dedication, the effort, and the integrity of the participants in the process. This is because the outcome of the uniform laws process is the product of structural—not personal—forces. Whenever there is competition among interest groups with no single group dominating, as in the case of Article 2, our prediction was that the process would result in vague and imprecise rules that delegated broad discretion to courts. These rules would result, not from their intrinsic merits, but because dedicated academic reformers, such as Linda Rusch and Dick Speidel, would propose them when they were unable to get bright line rules enacted.<sup>8</sup> In sum, our argument was that the pressure to formulate rules that will be uniformly adopted distorts the rules themselves in ways that may, quite perversely, undermine the very objective of a uniform law in the first instance.

Now, to the interesting part of the story. After our presentation, there were several commentators. The commentators thought the ideas were pretty wacky and, after the session, Dick came up to talk to Alan and me. Parenthetically, you need to know that Dick Speidel is the reason why I am a legal academic. He was my first mentor. So I have taken very seriously everything he has ever said about my work. Consequently, I remember the moment clearly. Because Dick is a very kind and gentle man, he began by saying some generally very nice things: “Your paper is very provocative, it’s very interesting.” “But,” he said, “you are completely wrong. Let me tell you that what you have predicted will not occur in the case of the Article 2 revision process.” Well, five years later, I believe that the evidence strongly supports the accuracy of our prediction.<sup>9</sup> But I still have not convinced Dick. Nor have I convinced Fred Miller, either, for that matter.

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8. *Id.* at 645-47.

9. The decision by NCCUSL to postpone indefinitely final approval of Revised Article 2 offers especially vivid evidence to support Schwartz’s and my predictions. The postponement was apparently agreed to in order to protect the objective of securing uniform adoption of the revisions in State Legislatures. Note for example the remarks of Arizona Commissioner James M. Bush to the effect that any Revised Article 2 must have a reasonably good chance of being enacted in substantial numbers of jurisdictions. Mr. Bush stated that the current draft didn’t meet that test and that “uniformity would be lost.” See Scott, *Uniformity Norm*, *supra* note 5, at 607 n.27.

Dick believes that the problems with the Article 2 revision process were caused by small “p” politics. That is to say that there were strategic decisions made by the NCCUSL leadership (albeit in good faith) that compromised the process and that were made without consultation with the Drafting Committee or the Reporters.<sup>10</sup> I continue to believe, to the contrary, that the problems are structural and not personal. In other words, the difficulties with the Article 2 revision were caused by the inherent limitations of the uniform laws process itself. In short, the problem is capital “P” political economy at work, and not small “p” politics.<sup>11</sup>

To make my point, I’d like to take as an example the Article 9 revision process that Dick cites by way of illustration. This is the one law reform effort I know a little bit about. Dick says, in his remarks, that the Article 9 revision is one instance where the ALI and NCCUSL “got it right,” because the revision was adopted with little opposition and is ultimately going to be enacted in all the states. I would just say, by way of response, don’t tell Elizabeth Warren or Lynn LoPucki or Jay Westbrook that Article 9 got it right.<sup>12</sup> The Article 9 process triumphed because a single interest group, secured creditors and their lawyers, were dominant. The dominant interest group did give a bit on Part 6-Default,<sup>13</sup> because that was the one part of the statute important to consumer interests. But in my view, those concessions were not terribly important to the folks in charge. And the folks in charge were large commercial credit granting institutions that rely on securitization and asset based financing. This dominant interest group was successful in preserving, throughout the Article 9 process, a key assumption which has driven the UCC project for fifty years. The assumption is that what is good for large commercial financing institutions is good for the USA.<sup>14</sup> That may be true. All I’m suggesting is that it also may be false.

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10. See Richard E. Speidel, *Revising UCC Article 2: A View from the Trenches*, 52 HASTINGS L. REV. 607(2001).

11. See Schwartz & Scott, *Political Economy*, *supra* note 5, at 650-52.

12. See, e.g., Memorandum from Elizabeth Warren, to the Council of the American Law Institute (Apr. 25, 1996) (on file with the author) (proposing an Article 9 set-aside for unsecured creditors); Lynn M. LoPucki, *The Unsecured Creditors's Bargain*, 80 VA. L. REV. 2103 (1994).

13. See U.C.C., Revised Article 9, Secured Transactions (Proposed Final Draft, April 15, 1998) §§ 9-601 to 9-627.

14. The original aphorism, attributed to Charles Wilson, former CEO of General Motors and Defense Secretary under President Eisenhower, was that “what is good for General Motors is good for the USA”. Wilson actually testified before the Senate Armed Services Committee on his proposed nomination that “for years I thought what was good for our country was good for General Motors, and vice versa.” *Excerpts from two Wilson Hearings Before Senate Committees on Defense Appointment*, N.Y. TIMES, Jan. 24, 1953, at 3.

What happens when a single interest group dominates, as in the case of Article 9, or as Ed Rubin has told us, in the case of Articles 3 and 4?<sup>15</sup> The process then generates a large number of precise, bright-line rules, that have two primary effects. At one level, these rules are admirable. Those of us who are legal academics like them because they generate predictable outcomes. We can figure out how they all fit together. We can teach them to our students. In short, the rules of Article 9 are clear and coherent. And, in that sense, therefore, maybe Article 9 does "get it right." But there is a darker side. The darker side is this: Those bright line rules also preserve the victory of the dominant interest group in the lawmaking process. And they do that by confining the discretion of courts who are subsequently asked to interpret these rules. Thus, Article 9 gets it right only if it is right that secured credit does not redistribute wealth away from unsecured creditors and debtors and toward secured creditors.<sup>16</sup> And, as anyone who has spent time worrying about that question is forced at the end of the day to admit, we simply do not know the truth of that proposition.<sup>17</sup> So, just to put it bluntly, you either get mush, which gives you formal uniformity but no predictability, or you get what the dominant interest group wants, and you hope that they want the right thing.

Why does the uniform laws process perform badly relative to the ordinary legislative process? This is an important part of the argument. As many of my fellow panelists have said, it's fine to stand up here and say the process is not perfect, but you need to offer an alternative. We do need to compare the uniform laws process to a baseline, and the baseline I suggest is the ordinary legislative process.

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15. See Edward L. Rubin, *Efficiency, Equity and the Proposed Revisions of Articles 3 and 4*, 42 ALA. L. REV. 551 (1991); Edward L. Rubin, *Uniformity, Regulation, and the Federalization of State Law: Some Lessons from the Payment System*, 49 OHIO ST. L.J. 1251 (1989).

16. The distributional critique of Article 9 rests on a fairness concern stimulated by the evidence of significant redistribution in debt financing. The claim is that secured debt redistributes wealth in the wrong direction. Sophisticated lenders, such as banks and finance companies, will know of the existence of security. These creditors can (and do) protect themselves against the issuance of secured debt through the interest rates that they charge, or they share in the gains that security generates by forcing the debtor to split the pie. Creditors who are unlikely to know of the existence of security or unable to protect themselves against it include employees with wage claims, consumer purchasers who have warranty contracts with the debtor, actual and potential tort claimants, and small suppliers. Secured credit may, in fact, disadvantage all of these creditors. Hence to the extent that the distributional story holds, security tends to redistribute wealth from the relatively poor and uninformed to the rich and sophisticated. Shifting wealth in this direction is contrary to generally prevailing redistributional theories. See Robert E. Scott, *The Truth About Secured Financing*, 82 CORNELL L. REV. 1436, 1462-65 (1997).

17. The debate about the social effects of Article 9 takes place in a vacuum of empirical data. See, e.g., *id.*

Here I agree with Gail Hillebrand that this comparison is not favorable to the ALI and NCCUSL. In fact, I would go even farther than she does. There are inherent limitations in the uniform laws process that are not found in the ordinary legislative process. These limitations include the lack of standing committees and of standing committee structures for gathering information, providing empirical data, and monitoring the efforts of interest groups. They include as well the lack of organized political parties, and of the useful practice of logrolling that enables the process of legislative consensus and of harmonizing critical value choices to proceed.<sup>18</sup> At bottom, therefore, we need to remember that the founders of the ALI believed that the uniform laws process would work well when it focused on projects that required technical expertise but did not involve fundamental value choices. On the other hand, they believed, the process would work badly when it tackled the legal regulation of complex commercial and economic endeavors about which there were strong and competing views.<sup>19</sup> I continue to believe that the founders were right. We, not they, are the ones who have lost our way.

## **II. An Internal Critique: Does Article 2 Undermine True Uniformity?**

The second major issue, separate from the first in important respects, involves an internal rather than an external critique. How best to evaluate the effects of the codification in Article 2 of what had formerly been the common law of contract and sales? Does Article 2, in fact, achieve its underlying purposes of making "uniform the law among the various jurisdictions"<sup>20</sup> and permitting "the continued expansion of commercial practices through custom and usage?"<sup>21</sup> Here the appropriate baseline against which to compare the Code is the evolving common law of Contract.

Any comparison of the Code and Article 2 against the common law should, at the outset, distinguish between rules for commercial parties on the one hand, and those for consumers on the other; and between default rules on the one hand, and mandatory rules on the other. This is an important distinction. Although the appropriate role for Legislatures in formulating efficient commercial default rules is open to debate, it is uncontroversial that the issue of socially optimal mandatory consumer protection laws is a proper subject for the legislative process. To be sure, in the case of optimal consumer protection, one can argue about what legislative process is best. But

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18. Robert E. Scott, *The Politics of Article 9*, 80 VA. L. REV. 1783, 1810-1816 (1994).

19. Schwartz & Scott, *Political Economy*, *supra* note 5, at 651-52.

20. U.C.C. § 1-102(2)(c) (1995).

21. U.C.C. § 1-102(2)(b) (1995).

that is a battle for another day. My comments with respect to comparing the Code against the common law are focused on an evaluation of those default rules that govern contracting between commercial sellers and commercial buyers.

Every commercial lawyer believes in uniformity. It is our Holy Grail. Uniformity, however, is much like mom and apple pie. If you think about it for a moment, uniformity qua uniformity is, at bottom, an empty concept.<sup>22</sup> At the broadest level of generality, what uniformity conventionally means to uniform laws activists is what I have called "formal uniformity."<sup>23</sup> Formal uniformity is simply the widespread adoption by American jurisdictions of facially identical rules. But a substantively meaningful concept of uniformity has to embrace both jurisdictional uniformity and temporal uniformity—that is, uniformity at a minimum requires the same rules being interpreted in the same way both across jurisdictions and over time. The question, then, is how well has Article 2 succeeded in promoting meaningful, substantive uniformity?

Assume, for example, as is the case in Article 2, that those uniformly adopted Code rules are so vague and so ill-defined that their primary effect is to delegate broad, perhaps unfettered, discretion to courts. And that courts, in the exercise of their delegated authority, interpret identical contractual language in fundamentally inconsistent and unpredictable ways.<sup>24</sup> Surely the parties to such contracts whose expectations have been frustrated by

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22. Uniformity as a generalized construct has no traction because there are two quite different dimensions to any concept of uniformity. This first dimension is primarily temporal. It assumes a single state decision-maker and looks to consistency and standardization over time. A quite different dimension of uniformity is embodied in jurisdictional uniformity, which focuses on consistent decision making by different courts in different jurisdictions. A plausible goal, therefore, is for the law to seek to optimize both dimensions. I have called this concept "substantive" uniformity so as to distinguish it from purely formal uniformity, e.g., the coincidence of similar rules across jurisdictions. Scott, *Uniformity Norm*, *supra* note 5, at 153.

23. *Id.*

24. Courts resolving contract disputes under Article 2 frequently have been called upon to interpret the apparently fixed price and quantity terms of a supply contract together with contextual evidence of a customary understanding that such terms are only "fair estimates" or that "reasonable variations" should be permitted. *See, e.g.*, *Columbia Nitrogen Corp v. Royster Corp.*, 451 F.2d 3 (4th Cir. 1971); *Modine Mfg. Co. v. N.E. Indep. Sch. Dist.*, 503 S.W. 2d 833 (Tex. Civ. App. 1973). In such cases, filling gaps in the incomplete contracts by invoking a "reasonable" interpretation of the prevailing custom or usage may often lead to widely divergent and non-uniform interpretations of the facially unambiguous expressly dickered terms of the contract. *See, e.g.*, *Brunswick Box Co. v. Coutinho, Caro & Co.*, 617 F.2d 355 (4th Cir. 1980); *Steuber Co. v. Hercules, Inc.* 646 F.2d 1093 (5th Cir. June 1981); *Nanakuli Paving & Rock Co. v. Shell Oil Co.*, 664 F.2d 772 (9th Cir. 1981).

non-uniform interpretations are not comforted by the fact that the source of the courts' authority is a "uniform" law.

The discretion to reach non-uniform outcomes is found in the majority of the "rules" of Article 2 that purport to allocate fundamental risks based on the norm of commercial reasonableness.<sup>25</sup> The statutory direction that a given outcome holds if the action was "reasonable" urges courts to do what Llewellyn asked them to do—to find the imminent law embedded in the particular commercial context and then incorporate that practice as part of the legal, contractual relationship.<sup>26</sup>

As a matter of theory, this "incorporation strategy" could be implemented in a manner that encourages the production of widely useful "tailored" default understandings that emerge from local norms and customs.<sup>27</sup> Thus, a court, directed by Article 2 to find the commercially reasonable outcome, could first take evidence on particular commercial practices or specific usages and customs that fine tune the general default rules for particular classes of buyers and sellers. Thereafter, the court could incorporate those understandings as part of the parties' "contract" (as that term is defined in the Code).<sup>28</sup> While the meaning of particular contract terms might vary

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25. The norm of commercial reasonableness is variously expressed in Article 2, sometimes just with the injunction "reasonable," but always directed to or qualified (usually explicitly) by a broader reference to commercial practice. See, e.g., §§ 2-103(1)(b), 2-204, 2-205, 2-206, 2-208, 2-305, 2-308, 2-309, 2-211, 2-402, 2-503, 2-510, 2-513, 2-603, 2-604, 2-605, 2-607, 2-608, 2-609, 2-610, 2-614, 2-706, 2-709, 2-710, 2-712, and 2-714.

26. Llewellyn believed that a major purpose of the Code was to resolve disputes according to the "best" commercial norms. In his view, the task of the courts was to identify and select the best commercial prototypes that were revealed in a particular commercial environment. One obvious objection to this strategy, however, is that courts lack the expertise to observe and evaluate merchant practice. Llewellyn responded to this concern by proposing a super eminent norm of "commercial reasonableness." The norm of commercial reasonableness was intended as an empirical direction: to delegate discretion to a merchant jury, and not to lay judges and jurors. As I have suggested on previous occasions, the elimination of the merchant jury from Article 2 while retaining the pervasive notion of commercial reasonableness was, in consequence, a drafting disaster. Scott, *Uniformity Norm*, *supra* note 5, at 170.

27. The State, by assigning a standard meaning to emerging customs and usages, can potentially reduce many errors that otherwise inhere in the contracting process. The process by which such standardized terms mature and are subsequently recognized by courts provides a collective wisdom and experience that parties are unable to generate individually. See Charles G. Goetz & Robert E. Scott, *The Limits of Expanded Choice: An Analysis of the Interactions Between Express and Implied Contract Terms*, 73 CAL. L. REV. 261, 267-8 (1985). For a theoretical defense of the incorporation idea, see Jody S. Kraus & Steven D. Walt, *In Defense of the Incorporation Strategy*, in *THE JURISPRUDENTIAL FOUNDATIONS OF CORPORATE AND COMMERCIAL LAW* (Cambridge Univ. Press 2000).

28. U.C.C. § 1-201(11) (1995) defines "contract" as the total legal obligation which results from the parties agreement. "Agreement," in turn, is defined in § 1-201(3) as the

from context to context, no contractors would be surprised by subsequent interpretations since incorporation would only embrace those usages that were known (or should have been known) to both parties at the time of contract. Thus, within each interpretive community, the contractual terms—both written and implied from context—would be predictable and transparent and, thus, uniform.

This is a great idea. But unhappily, judicial practice has not followed the theory. Instead, courts interpreting contract language under Article 2 have retained functionalist (and thus unpredictable) modes of interpretation, but the other side of the equation—incorporation of context— simply has not occurred in a meaningful way. A systematic examination of the litigated cases interpreting the “commercial reasonableness” standards of Article 2 shows that courts have consistently viewed their job as requiring deductive speculations about “Code policy” rather than the incorporation of particular commercial norms and prototypes.<sup>29</sup> When this occurs, the result from the parties’ perspective is not uniform at all. At least it’s not uniform in the sense of the same contract terms being interpreted in the same way both across jurisdictions and over time.

We all know—having taught Contracts—about the ways in which there are built-in interpretive biases in Contract Law. It didn’t take Behavioral Law and Economics to tell many of us that default rules are sticky and that opting out is hard to do.<sup>30</sup> Recent experimental work by Russell Korobkin and others<sup>31</sup> has only confirmed the

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”bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance . . .”

29. A detailed examination of fifty-five randomly selected cases from a base pool of 165 cases interpreting commercially reasonable practices under Article 2 reveals only two cases where the court saw its task as a search for the embedded commercial usage or practice. See *Havaird Oil Co. v. Marathon Oil Co.*, 149 F.3d 282 (4th Cir. 1998); *Cattle Fin. Co. v. Boedery, Inc.*, 795 F. Supp. 362 (D. Kan. 1992). In a majority of the remaining cases, the court attempted to intuit through a standard deductive approach what the commercially reasonable practice would be without taking any evidence on the nature of the commercial practice or usage. See, e.g., *Meyer v. Norwest Bank Iowa*, 112 F.3d 946 (8th Cir. 1997); *U&W Indus. Supply v. Martin Marietta Alumina, Inc.* 34 F.3d 180 (3d Cir. 1994), and cases cited in Scott, *The Uniformity Norm, supra* note 5, at n.68.

30. First year law students learn this distressing reality early in their study of contracts. See, e.g., *Jacob & Youngs v. Kent*, 129 N.E. 889 (N.Y. 1921) (New York Court of Appeals, in a famous opinion by Cardozo, implied a substantial performance default rule despite contract language that “any work which is not fully in accordance with the drawings and specifications in every respect, will be rejected and is to be immediately torn down, removed and remade or replaced in accordance with the drawings and specifications, whenever discovered.”).

31. See Russell B. Korobkin, *Inertia and Preference in Contract Negotiation: The Psychological Power of the Default Rules and Form Terms*, 51 VAND. L. REV. 1583 (1998); Russell B. Korobkin, *The Status Quo Bias and Contract Default Rules*, 83 CORNELL L. REV. 608 (1998); Marcel Kahan & Michael Klausner, *Path Dependence in Corporate Contracting: Increasing Returns, Herd Behavior and Cognitive Biases*, 74 WASH U. L.Q.

intuitions many of us have long held that Article 2 default rules and expressly dickered contract terms are often interpreted in inconsistent, unpredictable and *non-uniform* ways.<sup>32</sup> So, what does it mean, exactly, to get an Article 2 default rule “right”? I would argue, if you really want to get it right, if we are trying to make good commercial law, then true or “substantive” uniformity means that the default terms of the contract as well as the expressly dickered terms must be transparent to the contracting parties and predictable to other parties, both in different jurisdictions and over time.

Clearly, the implications of this notion of substantive uniformity are open to debate. For me, the value of predictability suggests, quite counter-intuitively, that there are good reasons to favor acontextual modes of interpretation. In other words, true or substantive uniformity argues for a return to textualist, formal rules of interpretation.<sup>33</sup> As Gail Hillebrand intuitively recognizes, bright-line rules (such as the plain meaning rule) are not necessarily a bad thing. Depending on your normative perspective, clear, predictable rules can as often be used as swords for consumer interests as well as shields to protect commercial interests.

One who argues for a return to acontextual modes of interpretation has to concede, and I do, that there are real costs to a return to the common law approach. Common law plain meaning interpretation ignores the commercial context except where the parties have expressly written relevant customs and usages into their contracts. Writing contracts in a formalist world becomes very much more laborious and error prone. Moreover, textualist interpretation imposes a social cost on future contracting parties because formal modes of interpretation reduce the stock of tried and true understandings, customs and usages that can be incorporated from

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347 (1996). *But see*, Jennifer Arlen, *Comment: The Future of Behavioral Economic Analysis of Law*, 51 VAND. L. REV. 1765 (1998) (urging caution in generalizing from the results of laboratory experiments); Robert E. Scott, *The Limits of Behavioral Theories of Law and Social Norms*, 86 VA. L. REV. 1603, 1639-46 (2000) (same).

32. *See*, e.g., Charles C. Goetz & Robert E. Scott, *The Limits of Expanded Choice: An Analysis of the Interactions between Express and Implied Contract Terms*, 73 CAL. L. REV. 261 (1985).

33. Both heterogeneity of contracting behavior and heterogeneity of contracting parties argue for a single-minded insistence on preserving the quality of the signals used by contracting parties to allocate risk. Given the difficulty of identifying whether a contract is incomplete because of high transactions costs or because of asymmetric information, the best instrumental strategy for courts may well be to interpret *literalistically* the facially unambiguous terms of the contract. A rigorous application of the common law plain meaning and parol evidence rules would preserve the value of predictable interpretation and also encourage parties to take precautions in selecting terms with well-defined meanings. *See* Robert E. Scott, *The Case for Formalism in Relational Contract*, 94 Nw U. L. Rev. 847, 871-74 (2000).

the context and thereafter announced by courts as useful defaults for other contacting parties.<sup>34</sup> Llewellyn's fundamental insight was to recognize the benefits that could *potentially* flow from this incorporation process. As I have suggested earlier, the theoretical possibility of those benefits should be acknowledged straightforwardly. But if we are going to evaluate Article 2 on its own terms, we must look to what courts do rather than to what Llewellyn wanted them to do. And on its own terms the incorporation process simply has not occurred. Courts don't do it.<sup>35</sup>

There are several plausible reasons why that might be so. I have come to agree with David Charny's view. In his view, the incorporation process has failed because it is grounded in the belief in a mythical pre-modern age "a nostalgia for intimate local communities of shared value and custom enforced by knowledge, reputation, and ties of affectional loyalty."<sup>36</sup> What we see instead, if Lisa Bernstein is to be believed, is the evolution of intermediaries and the development of custom by trade association rulemaking.<sup>37</sup> To be sure, Bernstein's claim may not be totally supported by subsequent investigation. Indeed, we should all welcome further analysis to determine if there is, in fact, an "immanent law" out there. But if there is no custom to be found or if courts under the Code cannot or will not find it, then the incorporation process as practiced by courts undermines substantive uniformity with very little positive pay-off to justify it.

## Conclusion

Finally, what about the mandatory rules that seek to protect consumers from information asymmetries, the life's work of Gail Hillebrand and others? Here it's important to remember Dick Speidel's story. The Article 2 process, at least his part of that process,

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34. Thus, in a formalist world, contracting parties will be required to incur the costs of developing standard-form prototypes for expressly allocating common risks that contract law might otherwise have assigned by default. This task may well prove quite costly. The limits of copyright law create an initial barrier to such innovation by denying contractors substantial property rights in their standard-form terms. An inherent collective action problem will thus retard the production of innovative, standardized terms for emerging relationships. So long as individual parties are incapable of capturing the full benefits of their innovative contractual expressions, the menu of standard-form terms and clauses will be under-produced. See Scott, *The Case for Formalism*, *supra* note 27, at 860.

35. See Imad D. Abyad, *Commercial Reasonableness in Karl Llewellyn's Uniform Commercial Code Jurisprudence*, 83 VA. L. REV. 429 (1997); Scott, *The Uniformity Norm*, *supra* note 5, at n.68.

36. David Charny, *The New Formalism in Contract*, 66 U. CHI. L. REV. 842, 846 (1999).

37. Lisa Bernstein, *Merchant Law in a Merchant Court: Rethinking the Codes Search for Immanent Business Norms*, 144 U. PA. L. REV. 1765 (1996).

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founded on just those rules: basic consumer protection, including the scope of warranties, actions by remote buyers, and the like. We may draw different inferences from that fact. Here is mine. I think it's naive to believe that a non-governmental, non-elected, elitist body of insiders can ever get those kind of rules right, whatever we mean by "right." Consumer issues raise important value choices and difficult normative questions that are best resolved through the ordinary legislative and judicial process. One can argue about whether federal or state regulation is preferable. But given the stakes, it's hard to claim, so far as I can see, that the uniform laws process is the way to go. And in closing, I simply remind you, once again, that the founders of the ALI didn't think so either.