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Robert K. Cullen
Kentucky Court of Appeals

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By Robert K. Cullen*

When and if all of the states adopt the Uniform Commercial Code, conflict-of-laws problems in the commercial field will be reduced to those that grow out of transactions involving foreign countries, and those that may grow out of differences between states in the judicial interpretation of the Code. However, at the present time, with only four states having adopted the Code, with fairly slow progress to be expected in its adoption by other states, and with ultimate adoption by all the states a goal that past experience with uniform acts would indicate will not be achieved, we may anticipate the need to be concerned about conflict-of-laws problems.

At the outset, it should be emphasized that there are two main points of time at which the conflict-of-laws aspects of a commercial transaction require the attorney's attention. The first is the time of entering into the transaction and drafting the contract papers. As will presently be brought out, the Code offers the parties an opportunity, at the drafting stage, to exercise some control over the question of which state's law shall govern. The second point of time is, obviously, when litigation arises. Here again the party bringing the litigation may have some limited power of control over which state's law will govern, to the extent that he has any choice in the selection of the forum.

With respect to six particular types of transactions, the Uniform Commercial Code[1] states a specific rule as to which state's law shall govern. The scope of the transactions to which the specific rules apply is limited, and for that reason discussion of the specific rules will be deferred to a later point in this presen-

* B.A., LL.B., University of Wisconsin; Commissioner, Court of Appeals, Frankfort, Kentucky.

[1] Ky. Acts 1958, ch. 77, Legislative Research Commission, Informational Bulletin No. 24 (1959) (hereinafter cited as UCC).

tation. For commercial transactions generally, including practically all transactions of sales and commercial paper, the Code merely sets forth two general principles, one relating to the right of the parties to choose the applicable law, and the other relating to the application of the Code in the absence of an agreement. The main portion of this discussion will be addressed to those provisions.

The general conflict-of-laws provisions of the Code are set forth in section 1-105. Subsection (1) of that section is as follows:

> Except as provided hereafter in this section, when a transaction bears a reasonable relation to this state and also to another state or nation the parties may agree that the law either of this state or of such other state or nation shall govern their rights and duties. Failing such agreement this Act applies to transactions bearing an appropriate relation to this state.

The exception introducing the subsection has reference to the six specific rules of which mention has been previously made, and in subsection (2) of the section it is stated in substance that where one of the specific rules specifies the applicable law, a contrary agreement is effective only to the extent permitted by the law so specified. For the moment, all that is important to keep in mind with respect to the exception is that the specific rules for particular transactions may limit the right of the parties, at the contracting stage, to choose the applicable law.

The requirements of an orderly presentation lead us to consider first the scope and extent of the right of the parties to choose the applicable law in commercial transactions generally, under the provision that when a transaction bears a reasonable relation to this state and also to another state, the parties may agree as to which of those state's law shall apply. One consideration will involve the meaning of this provision as it may be interpreted by the courts of this state when litigation over a commercial transaction arises in this state. Another will be, to what extent may the courts of another state, not having adopted the Code, recognize a contractual choice by the parties of the applicable law, when litigation over the transaction arises in such other state.

As concerns the interpretation of the Code provision by the courts of a state which has adopted the Code, it is obvious that

the key words are "reasonable relation." The Code says that the parties may agree to the application of the law of any state to which the transaction bears a reasonable relation. In the official comments of the drafters of the Code, it is stated that the test of "reasonable relation" is similar to that laid down by the Supreme Court in *Seeman v. Philadelphia Warehouse Co.*[2] In that case, the question was whether a contract for the lending of money should be governed by the law of New York, where the contract was made, or by the law of Pennsylvania, where the contract required the repayment to be made. Under the New York law the contract would be invalid as usurious, but under the Pennsylvania law it would be a valid contract. The Supreme Court, in holding that the Pennsylvania law applied, indicated that the parties may lawfully contract for the application of the law of any state which has a "normal relation" to the transaction, and quoted from Wharton's text a statement to the effect that the *motive* of the parties in contracting that the law of a particular jurisdiction shall apply is of no concern if the designated jurisdiction has a "natural and vital connection with the transaction."[3]

Another statement from the official comments is that ordinarily the law chosen must be that of a jurisdiction where a "significant enough portion" of the making or performance of the contract is to occur or does occur. So we find, for what help it may be, that "reasonable relation" may mean "normal" relation, or "natural and vital connection with," or "significant enough portion."

Some indication of what attitude the Kentucky courts may be expected to take in regard to the right of the parties to determine by contract what state's law shall govern, may be found in the decision in *Big Four Mills, Ltd. v. Commercial Credit Co.*[4] The facts were that Commercial Credit Company, a Maryland corporation, loaned money to Big Four Mills, a Kentucky corporation. The contract was made in Maryland, and the money advanced to Big Four was credited to Big Four's account in a Maryland bank. Repayments were made to Commercial in Maryland. The contract provided that it should "be construed and gov-

[2] 274 U.S. 403 (1927).
[3] *Id.* at 408.
[4] 307 Ky. 612, 211 S.W.2d 831 (1948).

erned by the laws of the state where it is accepted by Commercial Credit," which was Maryland. Under Kentucky law, the contract would be a usurious one; under Maryland law the defense of usury would not be available. In holding that the Maryland law applied, the Kentucky Court of Appeals quoted from *American Jurisprudence* to the effect that the courts will apply the law of the state called for in the contract, if the parties were "acting in good faith and not for the purpose of evading the law of the real situs of the contract,"[5] and that the only question for the court is whether the parties "acted in good faith or in bad faith and for the purpose of evading the law of the place to which their contract was really referable."[6] We may note here that we are supplied with two more possible substitutes for the Code's term, "reasonable relation;" namely, "real situs" and "really referable."

Following the quotations from *American Jurisprudence,* the Kentucky Court of Appeals, by way of supplementation, added these words:

> Implicit in the rule is that some vital element of the transaction (*i.e.* execution, performance, intent) is connected with the state whose law is sought to be invoked. If so, we should respect the presumption that the parties intend to enter into a legal rather than an illegal contract. . . .[7]

So we may add "vital element" to our list of substitute terms for "reasonable relation."

It is significant to notice that although the Kentucky court quoted with apparent approval the language of *American Jurisprudence* with respect to "good faith" and "bad faith," when the court came to state the rule in its own language it placed emphasis on the question of the connection of a vital element of the transaction with the state whose law is called for in the contract, and invoked a presumption of good faith. This is consistent with the view taken by the Supreme Court in the *Philadelphia Warehouse* case, that *motive* is not a controlling consideration.

It is believed that it may be reasonably safe to predict that the Kentucky Court of Appeals will not take a critical attitude towards provisions of commercial contracts specifying what state's

[5] 11 Am. Jur. *Conflict of Laws* § 157, at 462 (1937).
[6] *Ibid.*
[7] 307 Ky. at 622, 211 S.W.2d at 837.

law shall govern, and will be liberal in applying the "reasonable relation" test of the Code, to the end of giving effect to the contract's choice of territorial law wherever at all reasonable. Trouble maybe anticipated only in situations where one broad commercial transaction involves a series of component transactions that separably involve only one phase of commercial law. For example, a particular business deal may involve a sale, and the issuance and transfer of commercial paper, letters of credit, and documents of title. May the parties validly contract that the law of a designated state shall govern the entire transaction, even though some of the components of the transaction, considered alone, do not have any connection with that state? Frankly, the answer to that question is not known, nor can it be said where the answer may be found. One can only guess that the answer may depend on the extent to which the various components are interrelated and connected, and the relative proportion of the entire transaction that may be considered to have a relation to the designated state.

So far, we have been considering the question of possible interpretations, by the courts of a state which has adopted the Code, of the Code provision concerning the right of the parties to contract for the application of the law of a designated state. Of equal importance is the question of what attitude may be expected to be taken towards this right of contract by the courts of states in which the Code is not in effect. It is reasonable to assume that some states will follow the test laid down in the *Philadelphia Warehouse* case, of "normal relation" or "natural or vital connection." Others may approach the question from the standpoint of good faith or bad faith, or fraud.[8] However, it probably is safe to say that in most jurisdictions the parties' contractual choice of the state whose law shall govern will be accepted, if there is any reasonable and legitimate basis for it. So, in the final analysis, it may be said that the provision of the Code with respect to the right of the parties to choose by contract what law shall apply does not represent any substantial change from the general common-law rule.

We now come to the question of the application of the Code to transactions in which the parties have not exercised their

[8] See 11 Am. Jur. *Conflict of Laws* § 119, at 404-7 (1937).

right to select by contract which state's law shall apply. Section 1-105 of the Code makes this simple statement: "Failing such agreement this Act applies to transactions bearing an appropriate relation to this state."

An obvious question at the outset is: What is the difference between a "reasonable relation" and an "appropriate relation?" The official comments shed no light on this question, and do not indicate from what source came the term "appropriate relation." The comments speak of the question of whether a transaction has "significant contacts" with the state which has adopted the Code, but seem to indicate that having significant contacts is not synonymous with having an appropriate relation—rather that the question is whether the contacts have *enough* significance to justify classifying the relation as appropriate. My guess would be that a relation must be something more than barely reasonable, in order to be considered appropriate. This is on the basis that the Code indicates a policy to give effect to the *parties'* choice of applicable law if at all reasonable, but to condition the *court's* choice of applicable law upon such a relation of the transaction to the state as would of itself suggest appropriateness.

Before further exploring this phase of the question, it would be well to present two quotations that will give indication of the difficulties under which we labor. One is from the *Big Four Mills* case, previously mentioned. It is this:

> The question as to the particular state law which shall govern the construction and enforcement of a contract is one of the most confusing in the field of conflict of laws. Decisions from various jurisdictions apply three different rules: (1) the place of making, (2) the place of performance and (3) the place of intent. . . .[9]

The writer of the opinion might well have added that his own court has applied at least two different rules. In such cases as *Clarey v. Union Central Life Insurance Co.*,[10] and *Fry Bros. v. Theobold*,[11] the Kentucky court said that a contract is governed and controlled, and its validity determined, by the laws of the state where it is made. But in *Arnett v. Pinson*,[12] and in *Wedding*

[9] 307 Ky. at 619, 211 S.W.2d at 835.
[10] 143 Ky. 540, S.W. 1014 (1911).
[11] 215 Ky. 146, 265 S.W. 498 (1924).

v. First Nat'l Bank,[13] the court said that the place of performance governs the validity and construction of the contract.

The other quotation is from *American Jurisprudence*, as follows:

> It is apparent . . . that there is more confusion in this field of conflict of laws than in any other. Even upon a casual inspection of the authorities, the reader is met with the apparently illogical situation that all three rules—the place of making, the place of performance, and the place of intent—are cited as the controlling principle. Very generally, and often in a particular jurisdiction, any one or two and even all three of these principles have been laid down in different cases, and occasionally, even in the same case. Not only do the cases not mention each other or generally try to reconcile these apparent inconsistencies, but the problem itself has been obviously disregarded by the courts. . . . As a rule no effort has been made to distinguish between the problems and either one rule or another has been generally quoted and applied in a very desultory and irresponsible fashion.[14]

Upon this optimistic and encouraging note we will continue the discussion.

It should be said that although confusion seems to be predominant, there have been some instances of attempted reconciliation of the inconsistent common-law rules. For example, the Supreme Court, in *Scudder v. Union Nat'l Bank*,[15] attempted to segregate the rules as follows: (1) matters bearing upon the execution, interpretation, and validity of the contract are to be determined by the law of the place where the contract is made; (2) matters connected with the performance are to be regulated by the law of the place where the contract by its terms is to be performed; and (3) matters relating to procedure depend upon the law of the forum.

The *Restatement of Conflict of Laws*, in sections 332 and 358, makes a comparable segregation of the rules as between the place of making and the place of performance.

It is doubtful, however, whether the conflicts provision of the Code contemplates any such parceling out of a commercial

[12] 33 Ky. L. Rep. 86, 108 S.W. 852 (Ct. App. 1908).
[13] 280 Ky. 610, 133 S.W.2d 931 (1939).
[14] 11 Am. Jur. *Conflict of Laws* § 116 (1937).
[15] 91 U.S. (1 Otto) 406 (1875).

transaction among the laws of several states. The Code says that it applies to "transactions bearing an appropriate relation to this state," and the implication is that if there is an appropriate relation, the Code shall govern the entire transaction. Of course, this raises again the question, mentioned at an earlier point in this discussion, of whether a general commercial deal, involving several subordinate contractual arrangements, is one transaction. Again, the answer is not clear, and probably will depend upon the extent of inter-relation of the various components, and the relative importance of those components that do have a direct relation to the Code state.

At this point it would seem appropriate to call attention to the fact that in the original draft of the Code, which was adopted in Pennsylvania, section 1-105 spelled out in detail a set of rules for determining when the Code should apply to a multi-state transaction. These detailed rules were severely criticized by the New York Law Revision Commission, and were given a sound thumping by Professor Max Rheinstein.[16] However, Judge Goodrich wrote of them with approval.[17]

The net result of the criticism was that the detailed rules were discarded in favor of the simple statement of the requirement of an "appropriate relation," which appears in the present official text of the Code as adopted by Massachusetts, Kentucky, and Connecticut.

A brief reference to one set of the former detailed rules may perhaps be of some value in shedding light on the question of what may be considered to be an appropriate relation of a commercial transaction to a Code state.

Subsection (2) of former section 1-105 provided that the articles on Sale, Documentary Letters of Credit, and Documents of Title should apply whenever any contract or transaction within the terms of *any one* of those articles either:

> (a) was made, offered or accepted or the transaction occurred within the Code state; or
>
> (b) was to be performed or completed wholly or in part within the Code state; or

[16] Rheinstein, "Conflict of Laws in the Uniform Commercial Code," 16 Law & Contemp. Prob. 114 (1951).

[17] Goodrich, "Conflicts Niceties and Commercial Necessities," 1952 Wis. L. Rev. 199.

(c) related to or involved goods which were to be or were in fact delivered, shipped or received within the Code state; or

(d) involved a bill of lading, warehouse receipt or other document of title which was to be or was in fact issued, delivered, sent or received within the Code state; or

(e) consisted of an application or agreement for a credit made, sent or received within the Code state, or involved certain credits issued in the Code state, or involved any negotiation within the Code state of a draft drawn under a credit.

It will be observed that these rules would permit application of the Code to a transaction which touched the Code state only in a most casual, or even accidental, way. For illustration, if a Michigan businessman vacationing in Kentucky sent a wire accepting an offer for a sales contract previously made to him, at home, by another Michigan businessman, for the sale and delivery of goods in Michigan, Kentucky courts could apply the Code to the entire transaction because the acceptance was made in Kentucky. Or if through pure accident, goods intended to be shipped from Illinois to Georgia were in fact shipped to Kentucky, the courts of this state could apply the Code to all questions arising with respect to the sales contract.

It is very doubtful that such casual or accidental contacts as these would be held to constitute an "appropriate relation" under the terms of the present Code. A reasonable assumption would be that in abandoning the former detailed rules the intention was to require some more substantial contact than the minimum contacts permitted under the former rules.

It is possible that some of the courts of Code states may apply the so-called "grouping of contacts" test, under which effect if given to the law of the state which has the most significant contacts with the matter in dispute.[18] However, there is nothing in the language of the Code provision to require a weighing of significant contacts, and there would seem to be full justification for applying the Code where the transaction has some significant contacts with the Code state, even though these contacts may not be the most significant.

[18] See Vanston Bondholders Protective Committee v. Green, 329 U.S. 156 (1946); Rubin v. Irving Trust Co., 305 N.Y. 288, 113 N.E.2d 424 (1953).

It might appear that the courts of the Code states will be subject to no controls other than their own discretion in finding whether a particular transaction has an appropriate relation to their state. But in case of an extreme or purely arbitrary decision, it may be that the full faith and credit and due process clauses of the Constitution will come into play.[19]

The only sure conclusion that can be reached with respect to the "appropriate relation" test of section 1-105 is that there is no way of knowing at this time what the courts will find to be an "appropriate relation." Some courts may fall back on the old common-law tests. Others may go to the other extreme and apply the tests set forth in the original section 1-105. In the comments to the official text, there seems to be a hope expressed that the courts will lean towards finding the Code applicable wherever possible, the particular comment being that application of the Code "may be justified by its comprehensiveness, by the policy of uniformity, and by the fact that it is in large part a reformulation and restatement of the law merchant and of the understanding of a business community which transcends state and even national boundaries." While there is no way of foretelling what attitude the courts may take, there may be some hope, at least, that the courts will be encouraged by the Code provisions to give more deliberation to the conflicts-of-laws problems which in the past they have completely ignored or have treated in a desultory or irresponsible fashion.

Brief consideration will now be given to the six particular conflict rules that are stated by the Code for certain specific kinds of transactions. It will be remembered that these rules are exempted from the general provisions of section 1-105.

The first specific rule is found in section 2-402, relating to rights of the seller's creditors against sold goods. It provides in substance for application of the law of the state in which the goods are situated, as to whether retention of possession of the goods by the seller is to be considered fraudulent, and as to whether delivery or identification of goods to the contract con-

[19] See Hartford Accident & Indemnity Co. v. Delta & Pine Land Co., 292 U.S. 143 (1934); Smith, "Conflicts and Chaos or Contracts and Uniformity: The Uniform Commercial Code," 2 Kan. L. Rev. 11 (1953).

For a discussion of several problems that may arise in transactions between Code and non-Code states in the field of commercial paper, see Note, 24 Notre Dame Law. (1959); see also Rheinstein, *supra* note 16 *passim*.

stitutes a fraudulent transfer or voidable preference. This rule would seem to be consistent with the generally recognized principle of the common law that the law of the situs should govern problems relating to the title of corporeal things.

The second rule appears in section 4-102, dealing with bank deposits and collections. It is that the liability of a bank for action or non-action with respect to any item handled by it for the purposes of presentment, payment, or collection is governed by the law of the place where the bank is located. It is stated in the official comments that this provision is designed to state a workable rule for the solution of otherwise vexatious problems of conflict of laws, and that the routine and mechanical nature of bank collections make it imperative that one law govern the activities of one office of a bank. It appears that the rule intends that the law of the place where the bank is located shall apply from the inception of the collection process of an item through all phases of deposit, forwarding, presentment, payment and remittance or credit of proceeds. General comment with regard to this rule has been favorable.

The third specific rule is contained in section 6-102, having to do with bulk transfers. It provides simply that the Code shall apply to the transfer of goods located within this state. Again this is a matter of recognizing the law of the situs of tangible property, as concerns questions of ownership.

The fourth rule relates to investment securities, and is set forth in section 8-106. It provides that the validity of a security and the rights and duties of the issuer with respect to registration of transfer are governed by the law of the jurisdiction of organization of the issuer. The official comments recite that the purpose of this rule is to state, in accordance with the prevailing case law, a specific conflicts rule applicable in the securities field. It seems to be a sensible rule.

The fifth and sixth specific rules have reference to secured transactions, and appear in sections 9-102 and 9-103. These rules are somewhat complicated, and space will not permit me to do more than outline their provisions. Section 9-102 states the general proposition that the article on Secured Transactions shall apply in so far as it concerns personal property and fixtures within the jurisdiction of this state. In substance, this recognizes the

common-law principle that the law of the state where the collateral is located should be the governing law, without regard to possible contacts with other jurisdictions. Presumably, the converse of the rule is true, that the Code cannot be applied to govern a secured transaction where the property is not located in the Code state.

Section 9-103 sets forth exceptions to the general rule of section 9-102, as concerns certain kinds of multiple-state transactions. In general, they are:

> (1) In the case of intangibles consisting of accounts or contract rights, the validity and perfection of a security interest therein and the possibility and effect of proper filing are governed by the law of the state where the assignor has an office at which he keeps his records.
>
> (2) With respect to intangibles generally, and with respect to certain types of mobile goods, the validity and perfection of the security interest, and filing aspects, are governed by the law of the state wher the debtor's chief place of business is located.
>
> (3) If tangible property generally is already subject to a security interest when brought into the Code state, the validity of the interest is to be determined by the law of the state where the property was when the security interest attached, unless the parties understood when the security interest attached that the property would be kept in the Code state and it was brought into the Code state within thirty days, in which event the validity of the security interest is to be determined by the law of the Code state.
>
> (4) In certain instances where property is covered by a statutory certificate of title, the perfection of the security interest is governed by the law of the state which issued the certificate.

The official comments on section 9-103 cover some six double-column pages in the publication of the official text of the Code. It is recommended that these be read for a more complete understanding of the problems of conflict of laws as they relate to secured transactions.

In concluding this discussion, it is difficult to avoid mentioning the unhappy thought that the adoption of the Code may have the effect, for the immediate future, of creating additional areas of conflict of laws, particularly in the fields of sales and

commercial paper, in which in the past the fairly wide-spread adoptions of the Uniform Sales Act and Uniform Negotiable Instruments Act had established some degree of uniformity among the states. However, the prospects for adoption of the Code by additional jurisdictions seem hopeful, and in the meantime perhaps some benefits may accrue through more attention being devoted by the courts to conflicts problems.

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