

# NOTES AND COMMENTS

## THE UNIFORM COMMERCIAL CODE, SECTION 1-206— A NEW DEPARTURE IN THE STATUTE OF FRAUDS?

THE 1952 Official Edition of the Uniform Commercial Code contained Statute of Frauds provisions in Article 2,<sup>1</sup> applying to the sale of goods, Article 8,<sup>2</sup> applying to the sale of investment securities, and Article 9,<sup>3</sup> applying to secured transactions. These three provisions do not comprehend contracts for the sale of all forms of personal property. Because the UCC supersedes the single Statute of Frauds section of the Uniform Sales Act,<sup>4</sup> which had been construed to embrace all forms of personal property,<sup>5</sup> contracts for the sale of many forms of intangible personal property were released from Statute of Frauds requirements by the 1952 Code.<sup>6</sup> Section 1-206 was added to the UCC in 1957 to "fill the gap."<sup>7</sup> Captioned a "Statute of Frauds for Kinds of Personal Property Not Otherwise Covered," section 1-206 applies to all contracts for the sale of personal property which are not covered by the other three Statutes of Frauds.

With this one provision, the Commissioners have attempted to cover contracts involving a wide variety of intangible personal property. The UCC divides all forms of personal property into seven categories: goods,<sup>8</sup> documents

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1. UNIFORM COMMERCIAL CODE § 2-201 (1958) [hereinafter cited as UCC].

2. UCC § 8-319.

3. UCC § 9-203, which provides certain conditions for the enforceability of security interests, is "in the nature of a Statute of Frauds." UCC § 9-203 comment 5.

4. See UCC § 10-102; see also UCC Title and comment thereto.

5. UNIFORM SALES ACT § 4(1) states, "A contract to sell or a sale of any goods or choses in action . . ." Williston cites *State v. Frost*, 91 N.H. 229, 17 A.2d 441, 132 A.L.R. 528 (1941) to suggest that contracts for the sale of all personalty are covered. 1 WILLISTON, SALES § 60 n.1 (rev. ed. 1948). There is some opinion that patents and patent rights are not choses in action for the purpose of § 4. *Beacon Oil Co. v. Perelis*, 263 Mass. 288, 160 N.E. 892 (1928). *But see Lathrop v. Rice & Adams Corp.*, 17 F. Supp. 622, 628 (W.D.N.Y. 1936) (dictum); RESTATEMENT, CONTRACTS § 199 illustration 7 (1932); 1 WILLISTON, SALES § 67 (3d ed. 1957).

6. *A Comparison of the Statute of Frauds Sections of the Uniform Sales Act and Uniform Commercial Code in Pennsylvania*, 58 DICK. L. REV. 373, 374 (1954). This article, written about the 1952 Code, neglects to mention UCC § 9-203, covering security agreements.

7. UCC § 1-206 comment; see Young, *Scope, Purposes and Functions of the Uniform Commercial Code*, 48 KY. L.J. 196 (1960). Section 1-206 was adopted in Pennsylvania in 1959. PA. STAT. ANN. tit. 12A, § 1-206 (Supp. 1959).

8. Defined in UCC § 2-105; another definition for the purposes of Article 9 appears in UCC § 9-105(f).

of title,<sup>9</sup> instruments,<sup>10</sup> accounts,<sup>11</sup> contract rights,<sup>12</sup> chattel paper<sup>13</sup> and general intangibles.<sup>14</sup> The scope of section 1-206 may be determined by subtracting from these categories those forms of personal property covered by the other three Statutes of Frauds. Contracts for the sale of goods are governed by Article 2 of the Code;<sup>15</sup> these transactions must comply with the Statute of Frauds requirements of section 2-201 rather than section 1-206. Transactions involving documents of title to goods are principally controlled by Article 7 of the UCC,<sup>16</sup> which contains no Statute of Frauds provision. Arguably, contracts for the sale of documents of title would thus be subject to section 1-206.<sup>17</sup>

The term "instruments" as used in the Code includes investment securities, negotiable instruments, and similar evidences of debt.<sup>18</sup> Investment securities are governed by Article 8, which contains its own Statute of Frauds provision.<sup>19</sup> Contracts for the sale of those "instruments" which are not investment securities fall under section 1-206, since they are not governed by any other Statute of Frauds provision.

Sales of accounts, contract rights, or chattel paper—usually financing devices<sup>20</sup>—are as a general rule governed by Article 9,<sup>21</sup> and are considered

9. Defined in UCC § 1-201(15); see UCC §§ 7-102(1)(e), 9-105(1)(e).

10. Defined in UCC § 9-105(1)(g); discussed at text accompanying note 18 *infra*. The term "instrument" has a limited meaning in Article 3, defined in UCC § 3-102(e).

11. Defined in UCC § 9-106: "'Account' means any right to payment for goods sold or leased or for services rendered which is not evidenced by an instrument or chattel paper." The word "account" has a special meaning in Article 4, defined in § 4-104(1)(a).

12. Defined in UCC § 9-106: "'Contract right' means any right to payment under a contract not yet earned by performance and not evidenced by an instrument or chattel paper."

13. Defined in UCC § 9-105(1)(b): "'Chattel paper' means a writing or writings which evidence both a monetary obligation and a security interest in or a lease of specific goods. When a transaction is evidenced both by such a security agreement or a lease and by an instrument or a series of instruments, the group of writings taken together constitutes chattel paper."

14. Defined in UCC § 9-106; discussed in text accompanying notes 25-27 *infra*.

15. UCC § 2-102.

16. See UCC § 7-101 & comment.

17. Nowhere in the Code is it made clear whether the sale of a Document of Title is a sale of the goods it represents for the purposes of UCC § 2-201. "Goods" has a special meaning in Article 7, UCC § 7-102(f).

18. Defined in UCC § 9-105(1)(g). The term "negotiable instrument" has a different meaning in Article 8, UCC § 8-105(1).

19. UCC § 8-319. For the provision governing investment securities, see UCC § 8-101 & comment.

20. There has been some confusion from the wording of § 9-102(1)(b) in the 1952 draft of the UCC adopted in Pennsylvania which stated, ". . . to any financing sale of accounts, contract rights or chattel paper." The comment to that draft stated that, "The principle test whether a transaction comes under the Article is: is the transaction intended to have effect as security?" UCC § 9-102 comment 1 (1952 draft). But it also stated that ". . . all 'financing' sales of accounts, chattel paper and contract rights,

"security agreements" within its Statute of Frauds provision, section 9-203.<sup>22</sup> But there are certain exceptions to this rule. Section 9-104(f) excludes from Article 9 the sale of accounts, contract rights, or chattel paper when sold as a part "of the business out of which they arose" or when assigned to an agent for the purpose of collection. Therefore, these transactions are not governed by section 9-203, but by section 1-206. Also excluded from Article 9 are contract rights transferred to a party who is "to do the performance under the contract"<sup>23</sup> and all claims for wages, salary, or other compensation for services rendered (considered "accounts" by the Code).<sup>24</sup> Contracts for the sale of these rights also fall within the coverage of section 1-206.

All forms of personal property not included within one of the other six categories are grouped under the heading "General Intangibles."<sup>25</sup> Some of the more common transactions involving general intangibles are: the sale of rights and duties under bilateral contracts; the sale of patents, royalty rights, and copyrights; the transfer of tort claims and rights represented by judgments where transfer is permitted by local law; and the transfer of rights and claims under insurance policies.<sup>26</sup> Any contract for the sale of a general intangible is governed by section 1-206. It is this class of contracts which the section was primarily designed to cover.<sup>27</sup>

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whether made for security or not . . ." except for those mentioned in UCC § 9-104(f), were within the scope of Article 9. UCC § 9-102 comment 3 (1952 draft). The word "financing" was dropped in the 1958 draft, probably as redundant, since the comment to the 1952 draft had stated that "the kinds of sales meant to be excluded by the qualification 'financing' are identified in § 9-104(f)" by which all of UCC § 9-102 is limited. *Ibid.* "Financing" was also removed from UCC § 1-201(37). See ALI, 1956 RECOMMENDATIONS OF THE EDITORIAL BOARD FOR THE UCC pp. 12, 254. But when, in 1957, Kentucky studied § 9-102 without the word "financing," it was understood that "Subsection (1)(b) brings under this all sales of accounts, chattel paper and contract rights, whether made for security or not." UCC § 9-104(f) was overlooked. See UCC—ANALYSIS OF EFFECT ON EXISTING KENTUCKY LAW 339 comment 2 (Legislative Research Commission, December, 1957).

21. See UCC § 9-102(1)(b).

22. See UCC §§ 9-105(1)(h), 1-201(37).

23. UCC § 9-104(f). When contract rights are assigned to a party who is to do the performance, these transactions are not "the sale of bilateral contracts," see UCC § 1-206 comment, where rights and duties are transferred in one transaction. See 4 CORBIN, CONTRACTS § 867 (1951).

24. UCC § 9-104(d).

25. UCC § 9-106.

26. The comment to UCC § 1-206 states, "The principal gap relates to sale of the 'general intangibles' defined in Article 9 (Section 9-106) and to transactions excluded from Article 9 by Section 9-104. Typical are the sale of bilateral contracts, royalty rights or the like." Since bilateral contracts and royalty rights are not excluded from Article 9 by § 9-104, it seems reasonable to assume that they fall under the heterogeneous group "general intangibles."

Transfers of tort claims are excluded from Article 9 by § 9-104(k), judgment rights by § 9-104(h), and insurance rights by § 9-104(g).

27. See UCC § 1-206 comment, quoted in note 26 *supra*.

Unfortunately, what the Commissioners intended to do about these contracts is not made clear by the provision they adopted. Section 1-206 is susceptible to two, or possibly three, interpretations. It provides:

. . . a contract for the sale of personal property [not covered by other Statute of Frauds provisions of the Code] is not enforceable by way of action or defense beyond five thousand dollars in amount or value of remedy unless there is some writing which indicates that a contract for sale has been made between the parties at a defined or stated price, reasonably identifies the subject matter, and is signed by the party against whom enforcement is sought or by his authorized agent.

If the statutory language is given the obvious interpretation, i.e., if "amount" is taken to refer to the amount of monetary damages awarded for a breach and if "value of remedy" refers to the value of other "remedies" such as the liability avoided in an action where the contract is used only as a defense, then section 1-206 focuses entirely on the remedy sought and disregards the face value of the contract.<sup>28</sup> Under this reading, a parol contract for the sale of a personal property interest with a face value of 10,000 dollars on which a party sues for 4,000 dollars in damages would be enforceable for that amount. But a parol contract for the sale of similar personal property for 4,000 dollars, with 10,000 dollars worth of potential damages, would be enforceable only up to 5,000 dollars.

Under the second reading, "in amount" refers back to the face-value of the contract, and "value of remedy" refers to the damages claimed. In this case section 1-206 not only limits remedies on parol contracts to 5,000 dollars, but also makes a parol contract completely unenforceable if the face amount exceeds 5,000 dollars. A parol contract to sell personal property subject to section 1-206 with a face value of 4,000 dollars, and with 10,000 dollars worth of damages claimed for breach, would be enforceable up to 5,000 dollars, because the contract is below 5,000 dollars in "amount," but the "value of remedy" exceeds the 5,000 dollar limit. But a parol contract for the sale of the same property at a

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28. A defense can be regarded as a "remedy" which has "value" by virtue of the definition of "remedy" in § 1-201(34) which includes a right to self-help. Proof of the contract as a defense effectuates the right to self-help because it immunizes the self-helper from liability to the victim of the self-help.

Determining the "value" of the contract as a defense will probably require determination of the plaintiff's damages. For example, assume that plaintiff claims that defendant has wrongfully collected accounts receivable belonging to him and claims damages of \$10,000; defendant answers that the accounts were sold him by an oral contract as part of the business he purchased from plaintiff. Under the first interpretation of § 1-206, defendant will be allowed to prove the contract, and plaintiff will be allowed to collect whatever damages over \$5,000 he can prove.

One weakness of the "value of remedy" formula is the difficulty of valuing specific performance. What is the value of a court order commanding the transfer of a patent or copyright? Courts dealing with the ordinary Statute of Frauds provisions would not have been troubled by such questions, for the sole issue under the usual Statute of Frauds is the face amount or value of the contract, regardless of the remedy sought. Perhaps, however, the draftsmen believed that courts would be reluctant to give specific performance for the type of contracts of sale covered by § 1-206.

face value of 10,000 dollars on which a party sues for 4,000 dollars would be completely unenforceable since the contract exceeds 5,000 dollars "in amount."

The caption and the comment accompanying section 1-206 point to a third possible interpretation. The caption characterizes the section as a "Statute of Frauds for Kinds of Personal Property Not Otherwise Covered." The term "Statute of Frauds" has traditionally been applied to statutes barring proof of parol contracts when the contract price or the value of property sold is above a fixed amount;<sup>29</sup> it is so used in Article 2 of the Code.<sup>30</sup> Although the Code itself fails to explain the significance of captions, the law of many jurisdictions provides that captions may be used in interpreting statutory provisions.<sup>31</sup> If the caption governs the interpretation of the entire section, the reference to "value of remedy" might be ignored and the provision could be taken to mean simply that no contract over 5,000 dollars in "amount" would be provable. This interpretation might also be supported by reference to the brevity of the comment to section 1-206; the cursory discussion suggests that the authors of the comment did not view the section as a major departure from traditional Statute of Frauds provisions.

*Purposes:* To fill the gap left by the Statute of Frauds provisions for goods . . . securities . . . and security interests. . . The Uniform Sales Act covered the sale of "choses in action"; the principal gap relates to sale of the "general intangibles" defined in Article 9 . . . and to transactions excluded from Article 9 by Section 9-104. Typical are the sale of bilateral contracts, royalty rights or the like. The informality normal to such transactions is recognized by lifting the limit for oral transactions to \$5,000. In such transactions there is often no standard of practice by which to judge, and values can rise or drop without warning; troubling abuses are avoided when the dollar limit is exceeded by requiring that the subject-matter be reasonably identified in a signed writing which indicates that a contract for sale has been made at a defined or stated price.<sup>32</sup>

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29. The original Statute of Frauds reads: ". . . no contract for the sale of any goods, wares, and merchandizes, for the price of ten pounds sterling or upwards . . ." Statute of Frauds 1677, 29 Car II c. 3 § 17. The Uniform Sales Act changed the words to "of the value of five hundred dollars or upwards . . ." UNIFORM SALES ACT § 4(1); see 3 WILLISTON, CONTRACTS 685-87 (Rev. ed. 1960).

30. UCC § 2-201. UCC § 8-319 and § 9-203 bar the proof of parol transactions at any price.

31. See, e.g., *State v. Faro*, 118 Conn. 267, 272, 171 Atl. 660 (1934); *Burbank v. Sinclair Prairie Oil Co.*, 304 Ky. 833, 838, 202 S.W.2d 420, 424 (1946); *Commonwealth v. Flynn*, 285 Mass. 136, 139, 188 N.E. 627, 629, 92 A.L.R. 206 (1934); *Glen Alden Coal Co. v. City of Scranton*, 282 Pa. 45, 51, 127 Atl. 307, 309 (1925).

32. UCC § 1-206 comment. Section 1-102(3)(f) of the UCC (1952 edition), which provides that comments "may be consulted in the construction and application of this Act," was deleted in the 1957 edition of the Code "because the old comments were clearly out of date and it was not known when new ones could be prepared." ALI, 1956 RECOMMENDATIONS OF THE EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE 3. Pennsylvania has conformed to this amendment. PA. STAT. ANN. tit. 12A (Supp. 1959). The Code, however, retains the section of the comment to the Title which states, "To aid in uniform construction these Comments set for the purpose of various provisions of this Act to promote uniformity, to aid in viewing the Act as an integrated whole, and to safeguard against misconstruction."

Although this language sheds little light on the section itself, the statement that the section is intended to recognize the informality normal to these transactions by "lifting the limit for oral transactions to 5,000 dollars" might be taken as added evidence that the draftsmen of the comment viewed section 1-206 as a provision similar to other Statutes of Frauds, but with a higher statutory sum.<sup>33</sup>

As a traditional Statute of Frauds, section 1-206 would have the advantage of certainty; if the controlling dollar amount were the face value, it would usually be clear at inception whether or not a writing would be essential to enforcement. But the language of section 1-206, with its reference to "amount or value of remedy," seems incapable of supporting this third interpretation. If a traditional Statute of Frauds is all that was intended, redrafting to eliminate this language is in order.

It is possible, however, that the section's reference to the "amount or value of remedy" was intended, as a recognition and logical extension of the changed function which Statutes of Frauds now serve in commercial litigation. The Statute of Frauds historically required written formality to prevent the perjured assertion of nonexistent contracts.<sup>34</sup> But as the rules relating to introduction of evidence and competency of witnesses developed and were refined, courts became increasingly competent to determine truth through oral testimony; consequently the validity of this historical justification has become doubtful.<sup>35</sup> The primary value now attributed to the statutes is their *in terrorem* effect of causing important contracts to be put in writing, which, it is claimed, has the advantage of encouraging careful thinking and providing an accurate record in case of disagreement.<sup>36</sup>

All previous Statutes of Frauds have assessed the importance of a contract by focusing on its face amount or value, creating an absolute bar to the proof of parol contracts above a given price or value.<sup>37</sup> Informality has been permitted for any contract below the fixed dollar amount. Placing a monetary limit on the amount of remedy, the innovation which exists under both the first two interpretations of section 1-206, tends to broaden the *in terrorem* effect of a Statute of Frauds. In view of the difficulty of forecasting damages, businessmen may be induced to formalize many contracts below a 5,000 dollar face amount, whenever there is a possibility that damages will exceed 5,000 dollars. Thus the "remedy" innovation of section 1-206 may discourage informality of contract to a greater extent than would a traditional

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33. For example, UCC § 2-201 makes all parol contracts for the sale of goods for a price of more than \$500 unenforceable. Some Uniform Sales Act enactments have adopted a higher figure. See, e.g., OHIO REV. CODE ANN. § 1315.05 (Page, 1953) (\$2,500).

34. 2 CORBIN, CONTRACTS 3 (1950); 3 WILLISTON, CONTRACTS 340-41 (3d ed. 1960); Willis, *The Statute of Frauds—A Legal Anachronism*, 3 IND. L.J. 427, 427-28 & n.5 (1928).

35. 2 CORBIN, CONTRACTS 8-9 (1950); Willis, *supra* note 34, at 429-32.

36. Llewellyn, *What Price Contract?—An Essay in Perspective*, 40 YALE L.J. 704, 747-48 (1931); see 2 CORBIN, CONTRACTS 13 (1950).

37. See note 29 *supra*.

Statute of Frauds provision with a 5,000 dollar "face value" limit. This increased formality may be desirable. A small contract with potential damages of more than 5,000 dollars seems just as deserving of caution and formality as a contract having a total price of more than 5,000 dollars.

Recognizing that the statute's focus on the amount of the remedy may have been intended does not solve the interpretive question posed initially—whether section 1-206 acts solely as a limitation on the amount of remedy, or whether it also acts as an absolute bar to recovery when the face amount of the contract exceeds 5,000 dollars. The difference between the interpretations is essentially one of severity. The first interpretation would always allow recovery up to 5,000 dollars for breach, whatever the face amount of the parol contract. If this reading is adopted, persons unfamiliar with the Statute of Frauds would not be as heavily penalized for their ignorance as they would be under a statute imposing an absolute bar on recovery. By the same token, the prospect of at least 5,000 dollars in damages might help to deter persons aware of the statute from willfully breaching oral contracts.<sup>38</sup> Whether this interpretation would reduce the statute's *in terrorem* effect is uncertain. The Commissioners might reasonably have believed that if a contractor is aware of the Statute of Frauds at all, his uncertainty as to the possible applicability of the Statute of Frauds will lead him to be more cautious than ever. If this view is an accurate appraisal of business conduct, the knowledgeable businessman will observe writing formalities for all contracts over 5,000 dollars in face amount, as well as for many below that figure, and the second interpretation's absolute bar against enforcement of contracts over 5,000 dollars would serve no purpose but to penalize the unknowing contractor. On the other hand, businessmen may not be quite so cautious; they may ignore formalities for both large and small contracts whenever damages of 5,000 dollars are not reasonably foreseeable. In this case, the *in terrorem* effect of the first interpretation would be considerably less forceful than that of the second. The choice between the two interpretations would then depend upon whether the first interpretation's limited *in terrorem* effect is sufficient to satisfy the policy underlying a Statute of Frauds.

The language of section 1-206 and its accompanying comment do not indicate which, if any, of these premises were adopted by the draftsmen. Therefore, even if the "remedy" language is intentional, the section should be redrafted, not only to give certainty to the drafting of contracts in this area, but also to promote uniformity of interpretation among jurisdictions—a basic purpose of the Uniform Commercial Code.<sup>39</sup>

If this section is redrafted, two additions should be considered. First, unlike the Statute of Frauds provisions of the Code which apply to goods and securities,<sup>40</sup> section 1-206 has no provision for partial performance. The

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38. Abuse of a Statute of Frauds in this manner is the basis of much criticism directed at such provisions. See, *e.g.*, 2 CORBIN, CONTRACTS 3 & n.2.

39. See comment to the Title of the UCC.

40. UCC §§ 2-201, 8-319.

Statute of Frauds of the Uniform Sales Act was inoperative for the entire contract where there was partial performance.<sup>41</sup> Sections 2-201 and 8-319 of the UCC limit this exception, making contracts enforceable only for the personal property accepted, or for which payment has been made.<sup>42</sup> Partial performance was added as an exception to the Statute of Frauds sections of Article 2 and Article 8 because the performance serves as a substitute for a memorandum, "an unambiguous overt admission by both parties that the contract exists," at least to the extent of performance made.<sup>43</sup> There seems to be no reason why section 1-206 should not follow the other Statute of Frauds provisions of the Code in this regard. Secondly, sections 2-201 and 8-319 explicitly make the Statute of Frauds unavailable to parties who admit the existence of the contract in pleadings, testimony, or otherwise in court.<sup>44</sup> To allow a party to rely on the formal defense of the Statute of Frauds while admitting the existence of the contract to the court seems purposeless.<sup>45</sup> Section 1-206 should also be made to conform explicitly to this provision.

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41. UNIFORM SALES ACT § 4(1); see, *e.g.*, *Rutt v. Roche*, 138 Conn. 605, 87 A.2d 805 (1952); *Invincible Parlor Frame Co. v. Elegant Leather Goods*, 187 Misc. 454, 62 N.Y.S.2d 398, (Sup. Ct. 1946), *aff'd*, 272 App. Div. 795, 71 N.Y.S.2d 924 (1947).

42. UCC §§ 2-201(3) (c), 8-319(b).

43. UCC § 2-201 comment 2.

44. UCC § 8-319(d) states that a contract for the sale of securities is not enforceable by way of action or defense unless "the party against whom enforcement is sought admits in his pleading, testimony or otherwise in court that a contract was made for sale of a stated quantity of described securities at a defined or stated price." It is not clear from the language of this section whether a contract would be enforceable beyond the extent of the securities admitted. Courts may interpret this section to conform with UCC § 2-201(3) (b) which limits recovery to the amount stated in the admission. The UNIFORM SALES ACT § 4 made no such exception for admissions. See 2 CORBIN, CONTRACTS 13 & n.20 (1950).

45. Corbin goes farther to suggest that, "An amendment to the statute would probably be desirable providing that it shall not be effective as a defense except to a party who is willing to submit himself to examination in court on the merits of the case and who under oath denies making the promise as alleged." 2 CORBIN, CONTRACTS 13 (1950).