OHIO AND THE UNIFORM COMMERCIAL CODE

By Boris Auerbach*

One of the major bills before the 103rd General Assembly was House Bill No. 264, which would have incorporated the Uniform Commercial Code into Ohio law. Although the bill did not pass this session, every indication is that it will be enacted by the 104th General Assembly in 1961. When the bill was first considered during this current session it was given little chance of passage but as hearings were held more and more support was generated. The bill was passed by the House and was recommended for passage by the Senate Judiciary Committee unanimously. However, in the remaining days of the session it was not possible for the bill to be placed upon the Senate calendar.

The bill both in scope and size was one of the most extensive measures before the General Assembly. House Bill 264 would have enacted 387 sections of new law while repealing 489 sections and amending 18 others. Although no other piece of legislation in recent years has been as thoroughly discussed and examined in law review literature¹ and while no other piece of legislation has been as thoroughly gone over by interested groups, the very size and nature of the Code proved to be of some difficulty. For this reason, it is the purpose of this article to indicate what benefits would accrue to the people of Ohio should this legislation be enacted at the forthcoming session of the General Assembly.

The Commercial Code itself covers practically all the commercial law: sales of personal property, commercial paper, bank collections and the relationship of banks with customers, letters of credit, bulk sales, documents of title, investment securities and the entire field of security in personal property. Generally speaking, the Commercial Code continues the law as it is today, both case law and statutory, but it does make changes in substance and clarifies the law where it is now uncertain and provides answers which are not readily found. Each of the substantive sections of the Code retains from the past rules which have been proven by experience. The functional approach has been adopted throughout the Code and conceptual distinctions are abandoned where they have not proved to be the easiest solution to a problem.

The Code is the joint product of the Commissioners on Uniform State Laws² and the American Law Institute, both of which have contributed greatly to the present state of Ohio law. In fact, many of the

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¹ Over three hundred articles have been written on some phase or other of the Code. A number of books have already been prepared on this subject.

² Ohio has three commissioners on uniform state laws, who are appointed by the governor pursuant to Ohio Rev. Code § 105.21 (1953).
sections of law that would be repealed by the Commercial Code were originally prepared by the Commissioners on Uniform State Laws. For the most part, however, it has been over fifty years since these existing uniform acts were prepared and as we are well aware, our commerce has made great advances during that time. Our commercial laws need to be brought up to date to recognize these developments. This is one of the great benefits of the Commercial Code.

In considering the Code, reference should be made to excellent articles which appeared in the Ohio State Law Journal in 1953 and 1954 and which discussed in considerable detail the substance of the Code. In addition, the study of the Ohio Legislative Service Commission which appeared in February 1958 contains a detailed section by section comparison of the sections of the Commercial Code with existing Ohio statutes and Ohio cases.

In general the Code would benefit not only lawyers in the sense that it makes the law more accessible, more easily understood and more up to date, but it would be a benefit to businessmen, bankers, retailers and consumers in general.

It should be noted, however, that it is a basic policy of the Code to avoid, insofar as possible, what might be called class or "social" legislation. The type of legislation that is designed to protect one group against another group, as for example, the small loan act, is not affected by the enactment of the Commercial Code. Research has disclosed that there is substantial variation in regulatory statutes between states and that there is no reasonably established norm that could be adopted as a standard. In addition, it was felt that any provision of this type would be highly controversial. The Code deals in what might be called the mechanical rules of commerce. There is no doubt that setting forth the rules of commerce in the areas of sales, bills and bank collections and secured transactions has an effect upon different groups or classes. However, every conscious effort was made to avoid giving the Code the slightest degree of slant or bias either in one direction or another. This policy of neutrality was very effectively carried out. In the drafting, the personnel actively

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3 E.g., Ohio Rev. Code §§ 1315.01-76 (1953) (Uniform Sales Act); Ohio Rev. Code §§ 1323.01-.99 (1953) (Uniform Warehouse Receipts Act); Ohio Rev. Code §§ 4965.01-.49 (1953) (Uniform Bills of Lading Act).

4 The Uniform Negotiable Instruments Law was promulgated in 1896, the Uniform Warehouse Receipts Act and the Uniform Sales Act in 1906, and the Uniform Bills of Lading Act and the Uniform Stock Transfer Act in 1909.

5 14 Ohio St. L. J. 1-93 (1953).

6 15 Ohio St. L. J. 1-75 (1954).


8 Ohio Rev. Code §§ 1321.01-.99 (1953).

working on the Code were well balanced as to different possible points of view. Practicing specialists and representatives of business or industry were able to make substantial contributions by reason of expert knowledge. Although regulatory legislation has been avoided, the Code has been carefully drafted to avoid interfering with existing regulatory legislation. For example, Article 9 dealing with secured transactions, provides specifically that the Ohio small loan act and the retail installment sales act continue in force and that in the event of any conflict, these special acts would control.

Both the merchant and the retailer will benefit considerably from the modernization of our law of sales. The experience in both Pennsylvania and Massachusetts has shown the merits of having common commercial understanding clearly spelled out by statute. The elusive search for title would under the Commercial Code play a small role in the field of sales. Instead problems as to risk of loss, insurable interest, the seller's right to recover the purchase price and the buyer's right to possession are dealt with directly. Although the results in many cases will be the same, the answers are more readily determined and recourse to an artificial determination of intent by a jury will be eliminated. Of great benefit to the merchant is the recognition of the Commercial Code of practices which have long existed in the commercial area. For example, a firm offer as between merchants is recognized. Provisions are made in regard to the so-called battle of forms. It is now provided that because there may be some variation in the forms used by the parties there is still a contract and that the additional different terms operate only as an offer to modify unless acceptance is expressly conditional upon approval. The question is simply whether the parties are better off operating without any contract at all although they may believe they have actually contracted as under the existing law or whether there should not be a contract unless these additional terms materially alter the contract or the offer is expressly limited to acceptance of terms. This is an example of the lessening of harsh technical rules as between merchants because of their own commercial understanding.

10 Ibid. See also Braucher, The Legislative History of the Uniform Commercial Code, 58 Colum. L. Rev. 798 (1958).
11 Uniform Commercial Code §§ 9-203.
17 Uniform Commercial Code § 2-709.
18 Uniform Commercial Code § 2-716.
19 Uniform Commercial Code § 2-205.
There are other benefits to both the buyer and seller. The harsh rule that a buyer who seeks to rescind a contract because of the non-conformity of goods is not entitled to any damages has been eliminated. In addition, the buyer is given the right to purchase in the open market and to recover from the defaulting seller the difference between the cost of the goods so purchased and the contract price. This right has long existed in the seller in regard to resale but this commercially reasonable practice of "cover" has never been given any legal recognition as to the buyer.

Another example is the benefit to both the buyer and seller where goods are nonconforming but of a perishable nature. At present the buyer is often afraid to take any action to cut down the seller's possible loss because of the fear that he may have been found to have accepted the goods. This problem is clearly resolved by the Code which in fact imposes an obligation on the buyer to minimize damages in such event without fear of an acceptance being implied.

Perhaps the greatest benefit to the manufacturer, the distributor and the retailer comes from the reforms made in the area of secured transactions. At the present time, there is no one way in which a manufacturer, for example, can give security in both his equipment and inventory or stock in trade. We have under the existing Ohio law, chattel mortgages, conditional sales, trust receipts, factor's lien and accounts receivable. Each of these devices must be used with caution and is often not available for a specific type of financing. Under the existing Ohio law, after acquired property may be used as a basis for security in certain limited areas. The concept is not new to Ohio, but its use is severely limited by statute to certain areas. These limitations are based primarily upon historical accident and the chaotic manner in which our security law has developed. The Commercial Code provides a simple system with formalities reduced to a minimum, which can be used by economic vendor or financier alike and which will cover inventory and equipment presently owned or after acquired.

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21 Uniform Commercial Code § 2-608. Under Ohio Rev. Code § 1315.70 (1953) the rescinding buyer may recover only that portion of the price that he may have paid and has no other remedy.

22 Uniform Commercial Code § 2-712.


24 Uniform Commercial Code §§ 2-603.


29 Ohio Rev. Code §§ 1325.01-08 (1953).


By recognizing as entirely respectable the taking of security in personal property, by placing as few obstacles as possible in the way of the secured party in taking and keeping security and in providing a simple well organized and comprehensive system, the cost of financing to the manufacturer and the retailer alike will be reduced and the need for cumbersome and often dangerous financing contrivances will be eliminated.

The fundamentals of any system of securing personal property are simply ones of conferring upon a particular creditor a priority in certain property against the risk of insolvency and the providing of the means of notifying competing creditors of the secured interest either by possession or by some other feasible means such as filing. Article 9 is based on this approach. A simple agreement is needed to create the secured interest and the means of notifying competing creditors are not complex. To avoid confusion with older concepts, a single set of new terms is used to cover all types of cases. It should be noted, however, that to avoid any unnecessary break with the past, Article 9 specifically provides that if any prior form of instrument meets the simple fundamental requirements of Article 9 it can still be validly employed regardless of what it is called. This simply means that after the effective date of the Commercial Code, a chattel mortgage form may still be used to give a valid secured interest under the Commercial Code. An excellent detailed examination of the effect of the Commercial Code upon the existing Ohio security law is to be found in two articles which appeared in the Ohio State Law Journal.

One of the major groups that would be affected by the enactment of the Commercial Code, is the banking industry. The banks are affected not only by the provisions on secured financing but also the provisions relating to bank deposits and collections. It is in the latter field that there is little existing Ohio statutory law. Most of the Ohio law on the subject is found in a few scattered statutes, some court decisions, federal reserve regulations, clearing house rules and in the fine print often to be found on the back of a deposit slip or other form of agreement between the depositor and his bank.

32 Malcolm, op. cit. supra note 9 at 71.
33 UNIFORM COMMERCIAL CODE § 9-203.
34 UNIFORM COMMERCIAL CODE §§ 9-401, 9-402.
36 These instruments will obviously meet the simple requirements of UNIFORM COMMERCIAL CODE §§ 9-201, 9-402.
39 See cases cited in OHIO LEGISLATIVE SERVICE COMMISSION, op. cit. supra note 7 at IV - 1 to 13.
The bank collection process is of major importance to our economy. It has been estimated that from twenty-five to fifty million items per day are handled by our banks. Although banks handle this tremendous volume quickly and efficiently with surprisingly little litigation, when a case does develop it is quite difficult to determine what the law is in the state of Ohio.

For example, the key factor in any bank collection case is when an item is finally paid by the payor bank. Under the Ohio law there is no easy answer to this question. In this country there are no less than ten different rules as to when an item is finally paid.

Article 4 provides workable rules which take into account the tremendous volume of operations for modern day banking. These provisions have been well accepted by banks in Pennsylvania and Massachusetts on the basis of their experience. Two features have been specifically cited by banks. One of these deals with the problems raised by the use of drafts by insurance companies to collect premiums from policyholders and the other deals with the problem of simplifying bank endorsements for use in connection with electronic handling of checks. In the latter connection it should be noted that these provisions are quite flexible in light of the rapid development in the machine processing of collection items.

The provisions relating to secured financing have also been of benefit to the banks. One banker stated that after he had handled a few loan transactions under the Code he found that the taking of security became much simpler and less burdensome. The approach of basing the validity of the security on the nature of the transaction and the intent of the parties rather than the type instrument used is practical and has not created litigation.

When the Code was before the last session of the General Assembly, some thirty-five letters were received from banks, both large and small, from the state of Pennsylvania, testifying as to their five year experience with the Commercial Code. Without exception their experience has been highly favorable. It should be noted that in the states where the Commercial Code has been enacted, it has been backed by the bankers' association of that state. Awareness of the benefits to be derived by the enactment of the Commercial Code has been growing among the banking industry in this state as well.

44 Id. at 19.
A word should also be said about such industries as truckers, road builders, and other companies which are extensively engaged in interstate operations. In the case of truckers or other motor carriers, rolling stock is usually the main source of security. For the trucker who operates in more than one state the problem is particularly difficult. One carrier testified before a congressional committee that in order to comply with pre-commercial code law it was necessary to file every mortgage not less than twenty-three times at an average cost of $225.00.\(^{45}\) The road building contractor faces a difficult problem in that his equipment is always on the move in an irregular pattern causing considerable problems as to filing. General adoption of the Code would provide a simplified system of security with adequate source of information for all those who had legitimate reason to seek it.

Another industry which would be greatly benefited by the enactment of the Commercial Code is that dealing with the issuance of investment securities. Transfer agents, issuing corporations and brokers will find that Article 8 of the Commercial Code will provide them with a much improved system for handling all transfers of securities. Under existing law bearer bonds are treated as being in the negotiable instruments law with unhappy results since that law was drafted primarily in terms of short term paper. Under existing law registered bonds and other registered securities other than stocks have been left without adequate statutory guides.\(^{46}\)

Among those benefiting from Article 8 are executors, administrators and other fiduciaries. Anyone who has had occasion to settle an estate which includes investment paper has realized what an extremely arduous and complex procedure is involved. Under the Commercial Code, all the issuer or transfer agent of a stock security need require from the estate or a trustee in order to protect himself is a guarantee of the signature, a certified copy of the letters of the administration or trusteeship or a certificate from a responsible party that the person is a trustee, and a tax waiver if involved.\(^{47}\) None of the many documents now usually required by transfer agents need be furnished. In fact, if the transfer agent requires them, then he is bound by any limitations on power contained in the documents; if he does not demand them, he is not.\(^{48}\)

Perhaps the largest group to benefit, at least indirectly from the enactment of the Code, is the group to which all of us belong, the consumer. Whether the consumer is a bank president, lawyer, or truck driver, the clarification and simplification of our commercial laws will ultimately inure to his benefit. Almost all consumers have contact with commercial


\(^{46}\) Walker, Uniform Commercial Code, Article 8—Investment Securities, 14 Ohio St. L. J. 57 (1953).

\(^{47}\) Uniform Commercial Code § 8-402.

\(^{48}\) Ibid.
law in regard to sales. If it should ever happen that recourse to law is necessary in regard to a sales problem, the consumer would find that it had been worked out much more completely and with greater clarity than under existing law. He is also likely to find out that his problem would be solved with a greater respect for fair play on the part of all parties. One section of the Code gives the court the authority to refuse to enforce an unconscionable contract or an unconscionable clause in the contract. However, the parties are given sufficient opportunity to present evidence as to commercial setting, purpose and effect of a challenged provision. This, of course, is simply the equity rule which has long been enforced in specific performance cases and is designed to allow a direct examination of what may be a highly inequitable situation without forcing the court to resort to strained interpretations.

The provisions relating to warranties will also be of benefit to the consumer. The disclaimer of warranty of title for example must be clearly set forth. In addition, where a buyer makes known his needs and relies upon the seller's judgment to provide him with the needed article, there is an implied warranty that the article would be suitable for that purpose. Unfortunately, under the existing statute it has been found that this warranty does not exist if the article bears a patent or tradename. The Commercial Code eliminates this unfortunate distinction. Another provision will clearly extend the benefits of certain warranties to all members of the buyer's household and makes it clear that the warranty runs to the guest. We are all acquainted with the problem of the guest who bites on the ground glass in a jar of baked beans. It is comforting to know that there is an immediate seller's warranty and that the difficult task of showing negligence against the manufacturer is avoided.

The consumer will himself profit by the simplification of the process by which he can give security when he makes a purchase. Under existing Ohio law because of formalities which are needed in order to make security valid against third parties there are times when the secured party loses its security by inadvertance. The levying creditor may gain a windfall or the purchaser to whom the buyer wrongfully sold may take the article free of the lien. In either of these cases the debtor himself does not profit by the secured parties' loss for he himself remains liable. Moreover, debtors as a class must pay the increased cost of such financing. The Code not only reduces the formalities to a minimum but provides that the creditor and purchaser with actual knowledge of a

49 Uniform Commercial Code § 2-302.
51 Uniform Commercial Code § 2-312.
52 Ohio Rev. Code § 1315-16 (A) (1953).
53 Uniform Commercial Code § 2-315.
54 Uniform Commercial Code § 2-318.
secured interest could not take advantage of the slip as is the case in Ohio today.\textsuperscript{55}

In our status as consumer or otherwise, all of us use checks, either writing them or receiving them. Therefore, the greater certainty which has been introduced under the Commercial Code in regard to the rules under which the check moves from bank to bank in the collection process is of general benefit. The right of the drawer of the check to stop payment, which under Ohio law is not always clear,\textsuperscript{56} is clarified by the Code. The Code makes it clear that the bank must honor the stop order\textsuperscript{57} but provides in all fairness that the bank will be subrogated to the rights of the person it has paid so as to avoid unjust enrichment at the bank's expense.\textsuperscript{58} What rights the bank may have now if it improperly pays over a stop order are highly questionable.

These are but some of the reasons why the Commercial Code will be of benefit to industry and to the general public in Ohio.

It may be of some interest to note the type of objections which were raised in the hearings held before the House and Senate Judiciary Committees during the recent session. Very few of the objections raised went to the substance of the Code. In general they were of the nature of asking for more time. It was the belief of those who appeared in opposition that the action should be deferred until a future date so that we may have the experience of other states. In order to make this argument the differences between the Massachusetts and Pennsylvania versions of the Code were somewhat exaggerated. Pennsylvania, of course, adopted the Code in 1953 while Massachusetts adopted the Code in 1957. The amendments that were made as a result of the tremendous study made by various interested groups, particularly that of the New York Law Revision Commission, are in the Massachusetts law. Most of the amendments were not of substance and it is accepted that the Massachusetts version which was incorporated in the Ohio bill was superior.\textsuperscript{59} The opponents, of course, overlooked the fact that if the Code had worked so well for five years in Pennsylvania without these changes that there certainly should be little difficulty with the revised bill.\textsuperscript{60}

Perhaps the only substantial question raised was in regard to the floating lien problem. The floating lien refers to the situation where a secured party may obtain a lien on all the assets of the debtor regardless of whether he now owns them or is in possession of them to cover present

\textsuperscript{55} \textit{Ohio Rev. Code} §§ 1319.01, .11 (1953); \textit{Ohio Legislative Service Commission, op. cit. supra} note 7 at IX—8, 9.

\textsuperscript{56} As to Ohio, see \textit{Ohio Legislative Service Commission op. cit. supra} note 7 at IV-11.

\textsuperscript{57} \textit{Uniform Commercial Code} § 4-403.

\textsuperscript{58} \textit{Uniform Commercial Code} § 4-407.


\textsuperscript{60} \textit{Ibid.}
and future advances simply by the filing of a financing statement. This objection was based on both "economic" grounds and grounds that the lien would not stand up in bankruptcy. The arguments, however, somewhat overstated the position of the Commercial Code and on the other hand ignored existing provisions in Ohio law which to a large degree already permits this type of financing.

Under the Code, the after acquired property clauses are not valid as to consumer goods unless the debtor acquires rights within ten days after value is given. A further limit is made as to crops. Also, provisions are made to protect purchase money security interests, a buyer in the ordinary course of the collateral, a holder in due course and a person having lien for services.

Under Ohio law, a lien may be obtained on collateral which may be subsequently obtained. It is true that this cannot be done by chattel mortgage because of the description requirements. However, there are two exceptions to the present chattel mortgage law. One of these recognizes mortgages on crops to be planted within a year from the date of the mortgage and the second relates to railroad and public utility mortgages.

It is clear that future accounts may be financed under the accounts receivable act and inventory may be financed under the factor's lien act. The factor's lien act is somewhat similar to the Commercial Code in regard to this type of financing. Reference should also be made to the provisions of the trust receipts act which was enacted in 1957 particularly in regard to the provisions on notice filing and priorities.

Every indication from the states of Pennsylvania and Massachusetts discloses that there has been no monopolization of available credit. The technical objection in regard to bankruptcy was also raised. Under the 1950 amendment to section 60 of the Bankruptcy Act the trustee in bankruptcy was put into the position of subsequent lienholder. In general,

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62 Uniform Commercial Code § 9-204 (4) (b).
63 Uniform Commercial Code § 9-204 (4) (a).
64 Uniform Commercial Code § 9-312 (3).
66 Uniform Commercial Code § 9-309.
68 Francisco v. Ryan, 54 Ohio St. 307, 43 N.E. 1045 (1896); Coe v. Columbus P. & I. R. Co., 10 Ohio St. 372 (1859); Chapman v. Wiener and Steinbocher, 4 Ohio St. 481 (1855).
71 Ohio Rev. Code § 1325.01 (Supp. 1958).
72 Ohio Rev. Code § 1311.60 (1953).
the applicable state laws are followed as to the perfection of secured interests. The lien created will be upheld in bankruptcy proceedings provided that the lien by virtue of the state laws is superior to a subsequent lien obtained by legal process. It might be noted in passing that should the lien created by the Code not stand up in bankruptcy the same results would be reached under our existing factor’s lien act\textsuperscript{75} and accounts receivable act.\textsuperscript{76} It should be stressed that there is nothing in the Commercial Code which requires parties to tie up the debtor’s collateral with one secured party.\textsuperscript{77} Contact with credit men in other states shows satisfaction with the provisions of Article 9.\textsuperscript{78}

The provisions of Article 9 making credit easier for smaller businesses will simply be another step forward in assisting the economic growth of this state and will keep Ohio in line with other states that have or will enact the Commercial Code. The enactment of modern simplified commercial laws would seem to be essential to Ohio to maintain commercial leadership. It is hoped that in 1961, the Code will have the support of all groups that may be affected and that the Code will be enacted by the 104th General Assembly.

\textsuperscript{75} OHIO REV. CODE § 1311.60 (1953).
\textsuperscript{76} OHIO REV. CODE §§ 1325.01-08. (1953).
\textsuperscript{77} Coogan, Article 9 of the Uniform Commercial Code: Priorities Among Secured Creditors and the “Floating Lien”, 72 HARV. L. REV. 838 (1958).
\textsuperscript{78} A survey of members of the National Association of Credit Management in Pennsylvania disclosed that the great majority of members felt that the Code had not been detrimental to credit interests and in a number of instances has proved beneficial. The Pennsylvania, Massachusetts, and Connecticut groups actively favored the Code in their states. Letter from Robert L. Roper, Legislative Director, National Association of Credit Management to William A. Schnader, Chairman, Uniform Commercial Code Committee, National Conference of Commissioners on Uniform State Laws. (July 31, 1959).