63 1/5/68

Memorandum 68-19

Subject: Study 63 - Evidence (Commercial Code Revisions)

BACKGROUND

The California Evidence Code was enacted in 1965 upon recommendation of the California Law Revision Commission. Resolution Chapter 130 of the Statutes of 1965 directs the Commission to continue its study of evidence. One of the projects that the Commission has undertaken pursuant to this directive is a study of the other California Codes to determine what changes are needed in view of the enactment of the Evidence Code.

The Commission submitted a recommendation relating to the Commercial Code to the 1967 legislative session. See attached blue pamphlet containing Recommendation Relating to the Evidence Code: Number 3--Commercial Code Revisions (October 1966). After the proposed revision of Commercial Code Section 4103 was deleted from the bill recommended by the Commission, the bill was enacted substantially as recommended by the Commission. The revision of Section 4103 was deleted because the Commission, after further consideration, was unable to ascertain the intent of the UCC section and, hence, was unable to state with confidence that the revision merely made that intent clear.

The Permanent Editorial Board was established by the National Conference of Commissioners on Uniform State Laws to consider and review all amendments adopted in various states to the Uniform Commercial Code and to determine whether such amendments were desirable. At the Commission's direction, the Executive Secretary wrote to the Chairman of the Permanent Editorial Board requesting the views of the Board on the 1967 legislation enacted upon recommendation of the Commission and on the meaning of UCC Section 4-103 (California Commercial Code Section 4103).

This memorandum presents the results of an interchange of correspondence between the Permanent Editorial Board and the Executive Secretary.

GENERAL VIEWS OF PERMANENT EDITORIAL BOARD ON AMENDMENTS OF THE UNIFORM COMMERCIAL CODE

The Permanent Editorial Board has, with rare exceptions, disapproved all amendments to the Uniform Commercial Code that have been made in various states. The reason for this disapproval is stated in a letter (September 19, 1966) from the Chairman of the California Commission on Uniform State Laws to the Commission:

> Secondly, we are very much concerned with the approach to drafting the solution of the problem. As you know, the Uniform Commercial Code has now been adopted in forty-seven states, the District of Columbia and two territories of the United States, and it is anticipated that it will be uniform in all states in the near future. One of the principal benefits of uniformity in the commercial field is certainly its desirability in interstate transactions. There are, however, a number of other benefits from uniformity, not the least of which is the benefit of decisions in other jurisdictions on identical language.
>
> The approach to drafting set forth in your tentative recommendation is destructive of the uniformity in language between California and other states in a number of sections of the Uniform Commercial Code. While it is true that California departed from uniformity in language in a number

> of provisions of the Code when it was adopted in 1963, a major effort is under way to bring back as many of these sections as possible to conformity with the official text. Further departures from the official text are not desired and should not be made unless it is absolutely essential.

The same view is expressed in Exhibit I (pink) which is an extract from the Report of the Advisory Committee to the Senate on the Editorial Aspects of the Uniform Commercial Code. See also Exhibit II (yellow) and Exhibit III (green)(pages 1-3) attached for additional expressions to the same effect.

JUSTIFICATION OF 1967 LEGISLATION

The various attached exhibits take the position that uniformity is so essential that any revisions of the Commercial Code that are not officially promulgated must be disapproved. In connection with this objection to the 1967 legislation and to the enactment of any further clarifying legislation, consider the following extract from a letter from the Commission to the Chairman of the California Commission on Uniform State Laws (November 9, 1966):

> The Commission has concluded that legislation is needed to classify the Commercial Code presumptions and to clarify certain other provisions affecting the burden of proof or the burden of producing evidence. Absent such legislation, the California trial courts will be required to construe the Commercial Code provisions in accordance with the Evidence Code provisions. However, partly because the Commercial Code provisions were not drafted with the Evidence Code provisions in mind, the result that a particular trial court will reach in construing a particular evidentiary provision of the Commercial Code cannot be predicted with certainty. The Commission believes that it would be undesirable to delay the enactment of legislation that would eliminate this uncertainty.

The Commission has also concluded that the addition of the Uniform Commercial Code definition of a presumption to the California Commercial Code would confuse rather than clarify the California law. There are two reasons for this conclusion:

(1) The California Evidence Code definitions of a presumption affecting the burden of proof and a presumption affecting the burden of producing evidence were drafted after a careful study; the Commercial Code definition of a presumption is incomplete and was criticized by the California study of the Commercial Code for this reason. (As you know, when California adopted the Uniform Commercial Code, the definition of a presumption was deleted because the Law Revision Commission was studying the law relating to evidence and the view was taken that the Commercial Code should conform to the scheme of presumptions that would ultimately be adopted after the Commission had completed its study. This study has now been completed and the Commercial Code presumptions provisions can be revised to be consistent with the detailed Evidence Code scheme on presumptions and at the same time to effectuate the apparent intent of the drafters of the Uniform Code.)

(2) Some of the provisions of the Commercial Code are not phrased in terms of presumptions but use the phrase "prima facie evidence" or a similar phrase. Because of Evidence Code Section 602, these provisions create presumptions. It appears that applying the Commercial Code definition of a presumption to these "prima facie evidence" provisions would, in some cases, be contrary to the apparent intent of the drafters of the Uniform Code.

The Evidence Code does not affect the substance of the Commercial Code provisions, but it does govern the procedural aspects of the evidentiary problems that may arise under that code. The Commission's recommendation seeks to make certain clarifying changes that will minimize the problems that will arise when various presumptions provisions of the Commercial Code are applied in California.

California lawyers will soon be familiar with the Evidence Code scheme on presumptions and the scheme should be the same for all codes, including the Commercial Code. The Commission has concluded that it would be very undesirable to have a different procedure (of an unknown nature) for dealing with evidentiary problems arising under the Commercial Code than is used to deal with evidentiary problems arising under all the other codes. The recommendation will revise the Commercial Code in conformity with the Evidence Code scheme and will permit evidentiary problems under that code to be handled in the same uniform manner that all other evidentiary problems are handled. In this connection, the Commission believes that it would be particularly undesirable to use decisions from other states in interpreting the presumptions provisions of the Commercial Code in view of the carefully drafted California scheme on presumptions and the generally unsatisfactory state of the law relating to evidence--and presumptions in particular--in most other states.

With respect to the substance of the recommendation, it should be noted that the Commission did not exercise an independent judgment on how the presumptions in the Commercial Code should be classified. The Commission attempted to effectuate the intent of the drafters of the Uniform Code to the extent that that intent can be ascertained and to adapt it to the California scheme on presumptions.

For the reason indicated above, the Commission has decided to submit a recommendation on this subject to the 1967 Legislature.

Despite the philosophical objections to revising the Uniform Commercial Code, the Legislature accepted the view of the Law Revision Commission and enacted the substance of the legislation recommended by the Commission. The attached exhibits merely express the philosophical objection to lack of uniformity and do not make a persuasive case that the 1967 legislation enacted upon Commission recommendation should be repealed.

REVISION OF COMMERCIAL CODE SECTION 4103

The Commission directed the staff to obtain the views of the Permanent Editorial Board concerning the meaning of California Commercial Code Section 4103. The letter the staff sent to the Permanent Editorial Board included the following statement concerning this section. This statement requires careful study so that the need for the suggested revision of the section will be understood:

Before considering the problem the Commission believes exists in Section 4103, the provisions of UCC section 1-102(3) should be considered. This subdivision provides:

(3) The effect of provisions of this code may be varied by agreement, except as otherwise provided in this code and except that the obligations of good faith,

diligence, reasonableness and care prescribed by this code may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.

This subdivision appears to require the party seeking to rely upon a standard established by agreement to establish that such standard is not manifestly unreasonable. This interpretation appears to be contrary to the official comment which states: "However, the section also recognizes the prevailing practice of having agreements set forth standards by which due diligence is measured and explicitly provides that, in the absence of a showing that the standards manifestly are unreasonable, the agreement controls." To make it clear that the party contesting the standard established by such an agreement has the burden of showing its unreasonableness, subdivision (3) might be revised to read:

> . . . but the parties may by agreement determine the standards by which the performance of such obligations is to be measured ~~if~~ unless such standards manifestly are ~~not manifestly~~ unreasonable.

The Commission's primary concern in U.C.C. section 4-103 [set out below] is the meaning of the phrase "prima facie constitutes the exercise of ordinary care" which appears in subdivision (3). The meaning of the phrase "prima facie" is far from clear when used in statutes, and the Commission has been unable to ascertain its meaning as used in subdivision (3). What burden, if any, is placed on the other party

upon proof by one party of "action or nonaction consistent with clearinghouse rules and the like or with a general banking usage not disapproved by this division"? Possibly, the meaning of the section would be made clear if it were revised to read as follows:

4-103. (1) The effect of the provisions of this division may be varied by agreement except that no agreement can disclaim a bank's responsibility for its own lack of good faith or failure to exercise ordinary care or can limit the measure of damages for such lack or failure; but the parties may by agreement determine the standards by which such responsibility is to be measured ~~if~~ unless such standards manifestly are ~~not manifestly~~ unreasonable.

(2) Subject to subdivision (3), Federal Reserve regulations and operating letters, clearinghouse rules, and the like, have the effect of agreements under subdivision (1), whether or not specifically assented to by all parties interested in items handled.

(3) Action or nonaction approved by this division or pursuant to Federal Reserve regulations or operating letters constitutes the exercise of ordinary care . ~~and, in~~ In the absence of special instructions, proof of action or nonaction consistent with clearinghouse rules and the like or with a general banking usage not disapproved by this division ~~, prima facie constitutes~~ establishes a rebuttable presumption of the exercise of ordinary care. This presumption is a presumption affecting the burden of proof and may be rebutted by proof

that the standards established by clearinghouse rules and the like or with a general banking usage manifestly are unreasonable.

(4) The specification or approval of certain procedures by this division does not constitute disapproval of other procedures which may be reasonable under the circumstances.

(5) The measure of damages for failure to exercise ordinary care in handling an item is the amount of the item reduced by an amount which could not have been realized by the use of ordinary care, and where there is bad faith it includes other damages, if any, suffered by the party as a proximate consequence.

In considering the revision of this section, the effect of the last clause of subdivision (1) as applied to the regulation, etc., listed in subdivision (2) should be taken into account. For example, despite the last clause of subdivision (1), the standards established by Federal Reserve regulations and operating letters apparently are not subject to an objection that the standards so established manifestly are unreasonable. See first sentence of revised subdivision (3).

The official comment to Section 4-103 states: "The prima facie rule does, however, impose on the party contesting the standards to establish that they are unreasonable, arbitrary or unfair." Does this mean something other than the phrase "manifestly are unreasonable" used in revised subdivisions (1) and (3) of section 4-103.

> One of the major contributions to the improvement of California law that the Commission hopes to accomplish is to substitute more precise language in place of such phrases as "prima facie evidence" and "prima facie constitutes." Your view on the appropriate form of revision of U.C.C. sections 1-102(3) and 4-103 would be of substantial assistance.

The two responses we received to our inquiry objected to any revision of Section 4103. See Exhibits II and III. Subject to this general objection, Exhibit III states that the revision of subdivision (3) of Uniform Code Section 4-103 (California Section 4103) set out in the material quoted above "are satisfactory and reflect the subdivision's original purpose."

The staff has no doubt that the revision of UCC Section 1-102(3) and UCC Section 4-103 would clarify those provisions to state the apparent intent of the Commercial Code more clearly. There is no assurance, however, that the provisions will be construed in California in a manner that is consistent with the intent of the Commercial Code. (The fact that the Commission was unable to agree on the meaning of Section 4103 indicates that the courts will have difficulty in determining the meaning of the section.)

Nevertheless, the staff has serious reservations as to whether the Commission should undertake to clarify these provisions. Although the provisions clearly deal with allocation of burden of proof and, hence, deal with evidentiary matters, we might encounter substantial objections to the revisions because they tend to defeat the general policy of retaining uniformity in the various states. The Commission,

however, may wish to prepare a tentative recommendation, distribute it for comment, and consider the comments received on the tentative recommendation before it takes any final action on this matter.

Respectfully submitted,

John H. DeMoully
Executive Secretary

EXHIBIT I

REPORT OF THE ADVISORY COMMITTEE TO THE SENATE ON THE EDITORIAL ASPECTS OF THE UNIFORM COMMERCIAL CODE

TO THE HONORABLE DONALD L. GRUNSKY, CHAIRMAN, AND THE MEMBERS OF THE SENATE INTERIM COMMITTEE ON JUDICIARY:

The Advisory Committee to the Senate on the Editorial Aspects of the Uniform Commercial Code has maintained a watchful eye on the Uniform Commercial Code since its effective date in California on January 1, 1965. While a number of problems manifested themselves at the time the Code became effective in California, the great majority of these problems seemed to work themselves out within a relatively short time with the growing familiarity of the Bar and industry with the provisions of the Code.

In addition to watching the progress of, and developments under, the Uniform Commercial Code in California, the Advisory Committee has watched with interest the progress of the Uniform Commercial Code in other states. When the Uniform Commercial Code was adopted by the California Legislature at its 1963 session, only slightly more than twenty states had adopted the Code. Since that time the Uniform Commercial Code has been adopted in the great majority of the remaining states, so that it has now been enacted in forty-nine states and the District of Columbia, as well as some of the territories of the United States. With each subsequent adoption the value of uniformity in the language of the Code has become greater.

In enacting the Code in California in 1963 the Legislature made more than 120 changes in the official text

of the Code, far more than have been made by any other state. These changes had been suggested by the State Bar of California, the California Bankers Association, and numerous other interested groups who had made a study of the Code, and were subsequently recommended by the Advisory Committee. Some of these changes were made in the interests of clarifying the language of the Code; others were made in the interest of retaining existing California law which differed in some degree from the official text of the Code. Others were made in the belief that a particular rule of law contrary to that provided in the official text of the Code was the better rule, although in many such instances the primary concern was to have a stated rule so that the public would know what the rule was and could, if desired, contract for a different rule in a given situation.

Following the widespread adoption of the Code by legislatures of various states in 1963, the Permanent Editorial Board for the Uniform Commercial Code, which had been set up by the sponsoring organizations for the Code, the American Law Institute and the National Conference of Commissioners on Uniform State Laws, reviewed all of the unofficial amendments which had been made in the respective states in enacting the Code. This review included all of the amendments which had been made to the Code in enacting it in California in 1963.

Under date of October 31, 1964 the Permanent Editorial Board issued its Report No. 2 covering all the unofficial amendments made in the states up to that time. The general conclusion of the Permanent Editorial Board was that "none of the unofficial variations is such an improvement over the 1962 official text of the Code as to lead the Board to

recommend it at this time." The report went on to examine each amendment which had been made in the various states and set forth its reasons for the rejection of each.

Subsequently the Permanent Editorial Board has promulgated its "1966 Official Recommendations for Amendment of the Uniform Commercial Code" which adopts two of the amendments to the official text adopted in California (Sections 2702 and 7209). In a prefatory note to that publication the chairman of the Permanent Editorial Board announced" a restudy in depth of Article 9 on Secured Transactions."

With the almost universal adoption of the Uniform Commercial Code in the United States, the value of literal conformity with the official text of the Code as it exists in almost all states is increased. With the increasing ease of transportation and the consequent multiplication of interstate transactions, the necessity of having such things as checks, contracts of sale, letters of credit, investment securities and security agreements mean the same thing in each state has likewise increased. While there are many values for uniformity in the law as between the states, one of the values most overlooked is the value which comes from having court decisions of all of the states available to construe a given provision or provisions of the law.

With these considerations in mind, the Advisory Committee has carefully reviewed the provisions of the California Uniform Commercial Code in the light of Report No. 2 of the Permanent Editorial Board for the Uniform Commercial Code and as a result has reached the conclusion that there are a substantial number of the amendments which were made in California to the official text of the Code which may

be changed so that the California sections may be amended back to conform to the official text of the Uniform Commercial Code. In addition to the amendments to conform the California Uniform Commercial Code to the official text, the Advisory Committee has considered a number of other problems concerned with the application of the Code in California and includes certain recommendations for changes in the Code or in other statutes which would be affected by the Code.

Because of the decision of the Permanent Editorial Board to have a restudy in depth of Division 9 on Secured Transactions, the Advisory Committee is making only those recommendations for amendment in Division 9 which it considers necessary or helpful on an interim basis until the results of that restudy are revealed.

The Advisory Committee therefore recommends to the Senate that the following amendments to the California Uniform Commercial Code be adopted at the 1967 session of the Legislature:

Memorandum 68-19

LAW OFFICES
SCHNADER, HARRISON, SEGAL & LEWIS
1719 PACKARD BUILDING
PHILADELPHIA, PA. 19102

EXHIBIT II

August 8, 1967

Mr. John H. DeMoully,

Executive Secretary,
California Law Revision Commission,
School of Law,

Stanford, California 94305.

Dear Mr. DeMoully:

Thank you ever so much for your letter of July 31 regarding California amendments to the Uniform Commercial Code to bring it in line with the California Evidence Code which was enacted in 1965.

If you will send me sufficient copies of the printed material which accompanied your letter I shall have enough duplicates of your letter made here to enable me to circularize the Permanent Editorial Board and the Chairmen of its subcommittees.

I cannot avoid being frank in replying to your letter.

I am very sorry, indeed, that California found it necessary to still further destroy the uniformity of the Uniform Commercial Code by making changes in it to conform to the California Code of Evidence. It would have been far preferable to state

in the California Code of Evidence that this Code shall not be deemed to modify in any way any provision of the Uniform Commercial Code.

Imagine the confusion which would exist if the 50 states each amended the Uniform Commercial Code to make it conform to a local Code of Evidence, which could conceivably be different in each of the 50 states!

The Uniform Commercial Code is by far the most important uniform act ever promulgated by the National Conference of Commissioners on Uniform State Laws. It covers a field in which uniformity of law among the states has become more, and more, and more desirable.

Experience of the Commissioners on Uniform State Laws during the 75 years of the Conference's existence has demonstrated beyond the shadow of a doubt that, difficult as it is to obtain the original passage of a comprehensive uniform act in all of our jurisdictions, it is still more difficult, and vastly so, to interest the states in enacting amendments promulgated by the Conference.

As I have spent a substantial number of years in assisting in the passage by all of the states except Louisiana, of the Uniform Commercial Code, I have more than a passing interest in this matter. There are now far too many non-uniform amendments of the Code on the statute books of the states which have enacted

it. We are doing everything in our power to get the states to clean up their Codes so as to render them consistent with the latest Official Text.

I hope that you can understand my dismay at the thought of having each of the 51 jurisdictions which now have the Code on their books, making non-uniform amendments so as to render the Code consistent with a local Code of Evidence or any other local code.

However, the views I have expressed are solely my own. I shall be only too glad to circulate your letter among the other members of the Permanent Editorial Board and the Chairmen of its subcommittees. To enable me to do this I shall require 15 additional copies of the printed pamphlet and Senate Bill No. 249.

Sincerely,

Wm. A. Schnader

Memorandum 68-19

EXHIBIT III

BINGHAM, DANA & GOULD
ONE FEDERAL STREET
BOSTON, MASSACHUSETTS 02110

TELEPHONE 617 542-7756
CABLE "BIDDGHAM"

September 8, 1967

William A. Schnader, Esq.
1719 Packard Building
Philadelphia, Pennsylvania 19102

Re: Correspondence with Mr. John H. DeMoully, Executive Secretary of the California Law Revision Commission Regarding Actual and Proposed Amendments of the Uniform Commercial Code as Enacted in California for the Purpose of Reconciling the UCC with the California Evidence Code Enacted in 1965

Dear Bill:

This is in reply to your letter dated August 28, 1967 to the Members of the Permanent Editorial Board and the Chairmen of its Subcommittees enclosing an exchange of correspondence between Mr. DeMoully and yourself dated July 31, August 8 and August 10, 1967 and enclosing a copy of the 1965 California Evidence Code with Comments and a copy of the Recommendation of the California Law Revision Commission relating to the Evidence Code and Commercial Code revisions.

In glancing through the 300 plus page Evidence Code, there is every indication that this is a very thorough, careful and scholarly product that undoubtedly is of value to the State of California and which deserves commendation from anyone interested in quality workmanship. Since the Evidence Code indicates the location of the California Law Revision Commission is at the School of Law, Stanford

University, I assume the Commission is based in the Stanford Law School and that its staff, if not the Commission, is drawn largely from the Law School. Perhaps Mr. DeMoully is a member of the Law School faculty.

Before commenting on the specific matters referred to by Mr. DeMoully, I think your correspondence with him justifies a few words regarding general approach. The American Law Institute, the National Conference of Commissioners on Uniform State Laws and the California Law Revision Commission are all dedicated to the general objective of improvement of the law and, in varying degrees, presumably are faced with similar problems.

In my own very considerable work on the UCC since 1946, one of the recurring and difficult problems faced in drafting the UCC and in presenting the UCC to legislatures has been that of perfectionism. Repeatedly, the Reporters, Editorial Board and Sponsors have been faced with individuals who, for varying reasons and in varying degrees, approved of our general and specific objectives but contended that we should do something more or make certain changes to improve or "perfect" the ultimate product.

I think it can be said that, generally speaking, when any critic or commentator pointed out genuine and serious defects, those responsible for the Code attempted to correct the defects and, in the long, evolutionary process required for the development of the Code, generally were able to do so. In many other cases, however, we simply had to adopt the position that it was infinitely more important to complete and obtain enactment of a Code than it was to strive endlessly for the impossibility of perfection. Repeatedly, therefore, while the Code was being drafted we had to say to many "perfectionists" making comments and suggestions, "There is some merit in what you say but we cannot keep making changes forever and the Code will have to stand as it is if we are to ever have any Code at all." Similarly, after the Code was completed and enacted in a number of states we have had to say, "There is some merit in what you say but the task of drafting and obtaining enactment of amendments is so prodigious, we think it is much better for everyone concerned if individual states avoid making separate amendments and the Editorial Board itself avoid drafting and promulgating amendments unless there is strong and clear necessity to do so."

Mr. DeMoully's letters raise another general problem. He advocates the existing and proposed California amendments to obtain "more precise" statutory language. I think there are two sides to this statutory objective. In a certain sense and in some cases greater precision in language is desirable. On the other hand, in a general "Code" generality in language is frequently highly desirable. Almost certainly the UCC will be the prevailing law of the country for the next 25-50 years or more. In this time and in view of the Code's very wide coverage, generality or flexibility in statutory language to permit accommodation to new and unforeseen situations can be very valuable. Taking a long view of the Code and future operations under it, I hazard the guess that in a majority of cases flexibility will prove to be of more value than precision.

Approaching Mr. DeMoully's inquiries against this background, I do not think the presumption problems he has raised were or are serious enough to justify the amendments already enacted in Chapter 703 of the Statutes of 1967 or proposed in his letter of July 31. At least this conclusion would have been justified if California had retained Section 1-201(31) when it enacted the Code or if it had simply enacted this subsection in 1967. One difficulty inherent in separate and individual variations by any one state is that when this process starts, it is difficult to stop. Mr. DeMoully's letter itself furnishes two examples of this truism. When California enacted the Code, it elected to omit Section 1-201 (31). This omission created much of the uncertainty leading to the presumption difficulties which, in turn, led to 1966 Pamphlet No. 3 and this, in turn, to Chapter 703 of the Statutes of 1967. A second example lies in the fact that in the 1966 Pamphlet No. 3, amendments were proposed in subsection (3) of Section 4-103 but in Mr. DeMoully's letter of July 31, 1967, amendments are proposed in subsections (1), (2) and (3) of Section 4-103 and also in subsection (3) of Section 1-102.

Having thus expressed views as to the general approach adopted by the California Law Revision Commission, I make the following specific comments on the several amendments in Chapter 703 of the Statutes of 1967 and Mr. DeMoully's further proposals:

In the revised form of Section 1-202, I think it was unwise for California to put in the statute the limitation of the section rule to an action arising out of the contract which authorized or required the document. I can easily visualize actions on letters of credit or papers other than the contract itself where the rule of 1-202 would be useful. Admitting that Official Comment 2 justifies the California limitation, in this instance I think greater statutory precision does more harm than good. I have no quarrel with the stating in Section 1-202 of two different types of presumption but I question whether this "clarification" was necessary.

I am delighted that the California Law Revision Commission elected to recommend Section 1-209 rather than amending the nine different sections referred to in the Pamphlet No. 3 Comment and "clarified" by Section 1-209. One can only wish, however, that when California originally enacted the Code, it had retained Section 1-201(31) which would have made unnecessary enactment of Section 1-209 in 1966. Of course, I do not object to the substance of Section 1-209.

I think the revised form of Section 2-719(3) is somewhat more clear than the Sponsor's text but I question whether this change was necessary.

With respect to Mr. DeMoully's proposed further changes in Section 1-102(3) and 4-103(3) set forth in his letter of July 31, there may be a slight implication from the existing UCC text that the party seeking to rely upon a standard established by agreement must "establish that such standard is not manifestly unreasonable"; but this is far from clear and the contrary result is clearly indicated by the language in the Official Comments to both 1-201(3) and 4-103(1) "in the absence of a showing that the standards manifestly are unreasonable, the agreement controls." Inserting this language in the statutory text, as suggested by Mr. DeMoully, is an apt illustration of perfectionism which, while achieving some greater

"precision", is not essential and, certainly from the point of view of the Sponsors, is clearly outweighed by the desirability of uniformity.

In Section 4-103(2) the insertion of the qualifying phrase "Subject to subdivision (3)," is accurate but contrary to the general drafting style of the Code. UCC provisionsare, in general, so interrelated that if this type of qualifying phrase were to be required consistently, I would hazard the guess it should be inserted in the UCC in not less than a thousand places.

Assuming the California Law Revision Commission will insist upon amending Section 4-103(3), I think the proposed amendments of this subsection are satisfactory and reflect the subsection's original purpose. See the last sentence of Comment 4 to UCC, Section 4-103. In view of that last sentence, again I question whether the change is necessary. Incidentally, in rereading this last sentence, I believe the words "the duty" were somehow omitted after the word "standards" and should be inserted the next time we correct errors in Comments.

I am enclosing a copy of this letter which you may send to Mr. DeMoully if you so desire.

Sincerely yours,

Wallace D. Malcolm

Enclosure