



Digital Commons@

Loyola Marymount University
LMU Loyola Law School

Loyola of Los Angeles Law Review

Volume 26
Number 3 *Is the UCC Dead, or Alive and Well?*

Article 9

4-1-1993

Using Fundamental Principles of Commercial Law to Decide UCC Cases

Steven L. Harris

Follow this and additional works at: <https://digitalcommons.lmu.edu/llr>



Part of the [Law Commons](#)

Recommended Citation

Steven L. Harris, *Using Fundamental Principles of Commercial Law to Decide UCC Cases*, 26 Loy. L.A. L. Rev. 637 (1993).

Available at: <https://digitalcommons.lmu.edu/llr/vol26/iss3/9>

This Symposium is brought to you for free and open access by the Law Reviews at Digital Commons @ Loyola Marymount University and Loyola Law School. It has been accepted for inclusion in Loyola of Los Angeles Law Review by an authorized administrator of Digital Commons@Loyola Marymount University and Loyola Law School. For more information, please contact digitalcommons@lmu.edu.

USING FUNDAMENTAL PRINCIPLES OF COMMERCIAL LAW TO DECIDE UCC CASES

*Steven L. Harris**

Judges, as Karl Llewellyn suggested, breathe life into the letter of the law.¹ Any assessment of the vitality of the Uniform Commercial Code must take into account how the UCC has been construed and applied by the judiciary. This Essay lays the groundwork for a small piece of such an assessment by examining two examples of the judiciary's failure to apply properly the basic principles of personal property conveying that underlie the UCC. The Essay advances some tentative explanations for this phenomenon and offers some suggestions for improving the situation.

I.

The UCC affords judges more independence than does a civil-law commercial code. Rather than preempt the field entirely, the UCC specifically invites judges to supplement its provisions with "principles of law and equity."² To accept this invitation, judges must be able not only to understand non-UCC principles but also to discern when resort to those principles is necessary.

Sometimes the need to look outside the UCC is readily apparent. For example, suppose a case implicates the competing claims of the original owner of goods and a person who bought them from a thief, or from a person who obtained them by fraud. The closest that the UCC comes to resolving the dispute is section 2-403(1). It informs us that "[a] purchaser of goods acquires all title which his transferor had or had power to transfer" and that "[a] person with voidable title has power to transfer a good title to a good faith purchaser for value."³ To apply the rules one

* Professor, University of Illinois College of Law; B.A., 1970; J.D., 1973, University of Chicago.

1. The names we learned while the eye-balls burned
put life into the letter
Names of judges who never turned
From making the morrow better.

Karl N. Llewellyn, *A Come-All-Ye for Lawyers*, in *THE COMMON LAW TRADITION* 399 (1960).

2. U.C.C. § 1-103 (1990).

3. *Id.* § 2-403(1).

needs to know what title the thief and fraud obtained. Inasmuch as the UCC is silent on this point, resort to the non-UCC law is an obvious course of action. And once the common law supplies the missing piece, answering the problem becomes easy.⁴

Sometimes the text of the UCC prompts the reader to refer to non-UCC law—for example, by using the undefined term “voidable title”⁵ in the second sentence of section 2-403(1). In other instances, the official comments extend a guiding hand. For example, the official comment to section 2-403 explains that the statute, when coupled with supplementary principles of law, “continue[s] unimpaired all rights acquired under the law of agency or of apparent agency or ownership or other estoppel, whether based on statutory provisions or on case law principles.”⁶ Sometimes, however, the need to consult other law is not readily apparent from either the text or the comments; rather, the burden falls upon the reader to supply the necessary non-UCC background principles upon which the statute was drafted.

One of these principles, the one upon which this Essay focuses by way of example, is the fundamental conveyancing principle that predates the UCC and that is reflected in the first sentence of section 2-403(1): A transferee of property ordinarily acquires whatever rights the transferor had.⁷ Thus, when the transferor enjoys good title, free of third-party claims, then the transferee acquires good title. This rule protects both parties to the transfer. It “shelters” the transferee from third-party claims to the same extent that the transferor would have been immune. For example, a transferee who acquires property from a person who has acquired good title under the voidable-title rule likewise would acquire good title.⁸ By “sheltering” the transferee, the rule also protects the value of the property for the transferor. Thus, a person who qualifies as a good faith purchaser for value and acquires good title under the voidable-title rule can convey that good title to virtually anyone, even to a transferee who takes the property as a gift and who, therefore, would not qualify as a good faith purchaser for value.

4. A thief has “void title,” which affords no rights at all; in contrast, a fraud acquires “voidable title” and has the power to give the purchaser a “good title.” RALPH E. BOYER, *SURVEY OF THE LAW OF PROPERTY* 712 (3d ed. 1981). Thus, the original owner prevails against the person who took from the thief but not against the person who took from the fraud.

5. U.C.C. § 2-403(1).

6. *Id.* § 2-403 cmt. 1. Curiously, the comment makes no reference to the common-law doctrines of title that are necessary to resolve the problem posed in the preceding paragraph.

7. *See id.* § 2-403(1).

8. BOYER, *supra* note 4, at 712.

There is another aspect to this principle, an aspect expressed in the Latin phrase *nemo dat qui non habet*.⁹ The transferee acquires whatever rights the transferor had *and no more*. When the transferor has less than good title—for example, owns only a one-half interest in the property—this principle operates to limit the transferee's rights accordingly. Thus *nemo dat* is a “derivation” principle, whereby the transferee's title derives from and is limited to that of the transferor.

Although several articles of the UCC contain specific rules reflecting the shelter/derivation principle (which this Essay refers to as *nemo dat*),¹⁰ section 1-103 suggests that application of the principle is not limited to those specific rules.¹¹ Rather, *nemo dat* forms part of the background against which other rules were drafted and should be construed. Moreover, the principle is a useful tool for approaching the resolution of competing claims to property. A proper understanding of both aspects of the principle can help to clarify otherwise opaque statutory provisions.

II.

Examples abound of courts that have misapplied, or have failed to apply, *nemo dat*. These examples are by no means limited to lower courts; federal courts of appeals and state supreme courts also have been known to miss the mark. Consider two fairly recent cases decided by the Second Circuit under UCC Article 9, *Aircraft Trading & Services v. Braniff, Inc.*¹² (*ATASCO*) and *MNC Commercial Corp. v. Joseph T. Ryerson & Son*.¹³ In *ATASCO*, the court failed to appreciate that the shelter aspect of *nemo dat* protects the transferor, as well as the transferee. As a result, the court inappropriately curtailed the transferee's rights and increased the rights of a third party. In *MNC*, the court failed to recognize how *nemo dat* limits the rights of a transferee. As a consequence,

9. “He who hath not cannot give.” BLACK'S LAW DICTIONARY 1037 (6th ed. 1990).

10. See U.C.C. §§ 3-305(a) (defenses to obligations on instruments), 3-306 (claims to instruments), 7-504(1) (documents of title), 8-301 (investment securities), 9-318(1)(a) (certain rights to payment).

11. “[P]rinciples of law and equity” shall supplement the UCC. *Id.* § 1-103.

12. 819 F.2d 1227 (2d Cir.), *cert. denied*, 484 U.S. 856 (1987).

13. 882 F.2d 615 (2d Cir. 1989). The Second Circuit is not the only court of appeals that has mishandled fundamental UCC conveyancing principles. For an example from the Fifth Circuit, see *National Bank v. West Texas Wholesale Supply Co. (In re McBee)*, 714 F.2d 1316 (5th Cir. 1983), which I have criticized on these grounds and others. See Steven L. Harris, *The Interaction of Articles 6 and 9 of the Uniform Commercial Code: A Study in Conveyancing, Priorities, and Code Interpretation*, 39 VAND. L. REV. 179 (1986); Steven L. Harris, *Trade Names, Bulk Sales, and Name Changes—The Challenges of In re McBee to Inventory Financiers*, in PETER F. COOGAN ET AL., 1C SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 22A-1 (1992); see also David G. Carlson, *Bulk Sales Under Article 9: Some Easy Cases Made Difficult*, 41 ALA. L. REV. 729 (1990) (analyzing *McBee* in detail).

the court inappropriately afforded the transferee greater rights than those of the transferor, thereby depriving a third party of its rights.

The *ATASCO* opinion is familiar to most Article 9 aficionados. It has been criticized by David Carlson and the Permanent Editorial Board (PEB) for the UCC, among others, and has prompted the PEB to revise the official comment to section 9-301.¹⁴ The case concerned competing claims to a jet aircraft engine. In December 1982, ATASCO sold the engine to Northeastern Airlines and took a purchase money security interest to secure the purchase price.¹⁵ ATASCO did not record its chattel mortgage with the Federal Aviation Administration until March 1985.¹⁶ In the interim, Northeastern had sold the engine to Braniff; Braniff had sold it to Condren; and Condren had leased it to International Air Leases, Inc. (IAL) with an option to buy.¹⁷ IAL learned of ATASCO's chattel mortgage in April 1985, and exercised its option to purchase the engine a few months thereafter.¹⁸

ATASCO brought a suit in conversion, replevin and forfeiture of the engine against Braniff, Condren and IAL. The district court denied ATASCO's motion for summary judgment against IAL and entered summary judgment for the defendants.¹⁹ The Second Circuit reversed the summary judgment in favor of IAL and the denial of ATASCO's motion for summary judgment, holding that IAL's rights were subordinate to ATASCO's security interest.²⁰

The court's analysis of Article 9 began with a discussion of whether ATASCO's security interest survived the series of transfers.²¹ The court concluded that it did. To determine the relative priority of ATASCO's security interest and IAL's ownership claim, the court turned to section 9-312(5)(a) of the UCC, which provides that "[c]onflicting security interests rank according to priority in time of filing or perfection."²² Observing that IAL perfected (recorded) after ATASCO did, the court

14. See Carlson, *supra* note 13, at 748-62; *PEB Commentary* No. 6 [PEB Commentaries] U.C.C. Rep. Serv. (Callaghan) (Mar. 10, 1990). Professor Carlson and the PEB agree on the proper result but adopt different readings of the UCC. See Carlson, *supra* note 13, at 757-59.

15. *ATASCO*, 819 F.2d at 1229-30.

16. *Id.* at 1230.

17. *Id.*

18. *Id.*

19. *Id.* at 1229.

20. *Id.*

21. A discussion of the Federal Aviation Act precedes the discussion of Article 9. See *id.* at 1230-32. For purposes of this Essay, I assume the court's discussion is correct.

22. U.C.C. § 9-312(5)(a).

concluded that ATASCO's security interest prevailed over IAL's interest.²³

To its credit, the court attempted a detailed analysis of a number of potentially relevant provisions of both Article 9 and Article 2. However, the court's failure to appreciate the policy underlying *nemo dat* led the court to some incorrect conclusions.

Inasmuch as IAL's rights derive from those of Condren, and Condren's from those of Braniff, application of *nemo dat* begins with the rights of Braniff. Generally, security interests are governed by the *nemo dat* rule of section 9-306(2): A security interest continues notwithstanding sale of the collateral.²⁴ Like other articles of the UCC, Article 9 contains specific provisions overriding *nemo dat* and enabling certain good faith purchasers for value to acquire greater rights than those of their transferors.²⁵ The court found that Braniff qualified for the protection of one of these good-faith-purchase rules—that of section 9-301(1)(c).²⁶ Braniff was a buyer that took delivery and gave value without knowledge of ATASCO's unperfected security interest, and did so before the security interest was perfected. Accordingly, ATASCO's unperfected security interest became subordinate to Braniff's rights; that is, as long as Braniff continued to own the engine, ATASCO would have been unable to enforce its security interest in the engine. Section 9-301(1)(c) likewise would have enabled Condren to prevail over ATASCO. As long as Condren owned the engine, ATASCO was, in effect, unsecured.

Unlike Braniff and Condren, IAL exercised its option to purchase the engine after ATASCO's security interest was perfected. The court found that, because IAL exercised the option after ATASCO's security interest was perfected, IAL did not itself qualify for the protection of section 9-301(1)(c).²⁷ The court concluded that, as a consequence, the sale to IAL revived ATASCO's ability to enforce its security interest.²⁸ This conclusion is faulty. Under *nemo dat*, which forms part of the foun-

23. *ATASCO*, 819 F.2d at 1236.

24. See U.C.C. § 9-306(2).

25. See, e.g., *id.* §§ 2-403(1)-(2) (good faith purchaser for value acquires good title from person with voidable title; buyer, in ordinary course of business, of entrusted goods from merchant who deals in goods of that kind acquires rights of entruster), 3-305(b) (holder in due course of instrument takes free of certain defenses), 3-306 (holder in due course of instrument takes free of claims), 7-502(1)(b) (person to whom negotiable document of title is duly negotiated takes free of certain claims), 8-302(3) (bona fide purchaser of investment security takes free of adverse claims).

26. *ATASCO*, 819 F.2d at 1233.

27. *Id.* at 1236.

28. *Id.*

dation upon which Article 9 rests, IAL would acquire whatever rights Condren enjoyed, including the right to use the engine without interference by ATASCO.

Application of *nemo dat* to protect IAL would be consistent with the purpose of section 9-301(1)(c): to impose upon secured parties the burden of publicizing—that is, perfecting—their security interests, upon pain of subordination to those who are likely to have parted with value in the expectation of acquiring unencumbered goods. The rule is intended to give buyers like Braniff and Condren the benefit of their bargain. Taking the goods free from the secured party's ability to repossess the collateral is only part of the buyer's bargain. An owner has not received what was bargained for if he or she cannot transfer the right to unencumbered enjoyment of the goods.

A proper analysis of *ATASCO* illustrates what some have called the "shelter" aspect of *nemo dat*. The court should have afforded IAL all of Condren's rights, including the right to use the engine free from ATASCO's interference.

In *MNC Commercial Corp. v. Joseph T. Ryerson & Son*,²⁹ the Second Circuit failed to appreciate the "derivation" aspect of the principle. Rather than limiting the secured party's rights to those of its debtor, the court erroneously afforded the secured party greater rights, to the detriment of a third party.

Although the facts of *MNC* are complicated by the bankruptcy of one of the parties, for our purposes they can be pared down considerably. From time to time Ramco purchased hot rolled bar steel products from Inland, processed them into cold products and sold the cold products to Ryerson, a wholly-owned subsidiary of Inland.³⁰ A setoff clause in Ryerson's order forms reserved "the right to apply any monies to become due [Ramco] . . . toward the payment of any sums which [Ramco] . . . may now or hereafter owe to us or to our parent company, Inland Steel Company.'"³¹ In May 1984, MNC took and perfected a security interest in Ramco's accounts receivable.³² In July 1985, Ryerson stopped paying Ramco, and Inland notified Ramco that Ryerson's debt to Ramco would be held as an offset against a debt owed by Ramco to Inland.³³ Nevertheless, Ramco continued to ship steel to Ryerson.³⁴

29. 882 F.2d 615 (2d Cir. 1989).

30. *Id.* at 616-17.

31. *Id.* at 617 (quoting language from Ryerson's order forms).

32. *Id.*

33. *Id.*

34. *Id.*

On October 30, 1985, after Ramco entered bankruptcy, Ryerson issued a check payable to Ramco for about \$304,500, stamped it canceled and paid that amount to Inland.³⁵ MNC subsequently sued Ryerson for about \$333,600, which was later reduced to about \$307,400.³⁶ One of Ryerson's defenses was that the amount at issue properly had been setoff against Ramco's debt to Inland.³⁷

The district court granted summary judgment for MNC on two theories. The first was that the setoff clause in Ryerson's order forms did not become a term of the contract and so was ineffective to create a setoff right.³⁸ The second was that the setoff violated the automatic stay that arose when Ramco entered bankruptcy.³⁹

On appeal, the Second Circuit affirmed on other grounds. It found that, because MNC brought its lawsuit after the stay had been lifted, bankruptcy law was irrelevant to the outcome of the dispute.⁴⁰ Holding against Ryerson under Article 9, the court had no need to address the battle-of-the-forms issue under Article 2.

The court analyzed the Article 9 problem as one of the relative priority of MNC's perfected security interest and Ryerson's right of setoff. Acting on the belief that Article 9 does not expressly resolve this priority conflict, the court purported to follow *Bank Leumi Trust Co. v. Collins Sales Service*⁴¹ and applied the first-to-file-or-perfect rule of section 9-312(5) by analogy. Specifically, it analogized Ryerson's right of setoff to an unperfected security interest, which it subordinated to MNC's perfected security interest.⁴²

The court rejected the idea that Ryerson might prevail under section 9-318(1)(a).⁴³ That section contains a specific application of *nemo dat*, and provides that, absent agreement to the contrary, "the rights of an assignee [MNC] are subject to . . . all the terms of the contract between the account debtor [Ryerson] and assignor [Ramco] and any defense or claim arising therefrom."⁴⁴ Relying on the New York Court of Appeals' opinion in *Bank Leumi*, the Second Circuit held that the setoff clause

35. *Id.*

36. *Id.*

37. *Id.*

38. *Id.*

39. *Id.*; see 11 U.S.C. § 362(a)(7) (1988) (filing of bankruptcy petition operates as stay of setoff of pre-petition debt owing to debtor).

40. *MNC*, 882 F.2d at 618.

41. 393 N.E.2d 468 (N.Y. 1979).

42. *MNC*, 882 F.2d at 619-20.

43. *Id.* at 620.

44. U.C.C. § 9-318(1)(a).

"did not alter Ryerson's underlying obligation,"⁴⁵ but rather at best established "a collateral agreement [regarding] the method of payment."⁴⁶

Although it purported to apply first-in-time principles, which often are consistent with *nemo dat*, the Second Circuit ultimately missed the point. To focus on the issue, let us put aside the bankruptcy question and assume that Ryerson's order form was part of the contract. Let us also assume that, under New York law, the setoff clause in Ryerson's order form did not create a right of setoff but rather stated an agreed method of payment—that is, a method by which Ryerson could discharge its obligation to Ramco.

Much of what the court said is quite correct. For example, it suggested that, because Ryerson never acquired Inland's claim against Ramco, Ryerson could not raise this claim against MNC.⁴⁷ Ordinarily, one person cannot defend against an obligation on the ground that the obligee has failed to perform its contract with a third person. In this regard, section 9-318(1) is unremarkable. It permits an account debtor (Ryerson) to assert against an assignee (MNC) only its own claims and defenses against the assignor (Ramco), not those of third parties. Ramco's unpaid debt to Inland does not constitute a defense to Ryerson's debt to Ramco.

In the actual case, however, Ryerson did not assert Inland's rights. It asserted its own. The facts suggest that Ryerson discharged its liability to Ramco on October 30, when it paid \$304,497.29 to Inland.⁴⁸ Under section 9-318(1)(a), MNC takes its security interest in Ramco's accounts subject to all the terms of the contract between Ryerson and Ramco, including the term that (by hypothesis) permits Ryerson to discharge its obligation to Ramco by paying Inland. Also under that subsection, MNC takes subject to a defense arising under the Ramco-Ryerson contract—the defense that the debt to Ramco was discharged by payment to Inland. Stated otherwise, Ryerson would not have been obligated to pay Ramco. Inasmuch as MNC's rights are no greater than Ramco's, Ryerson should have won the day.

45. *MNC*, 882 F.2d at 620.

46. *Id.* (quoting *Bank Leumi Trust Co. v. Collins Sales Serv.*, 393 N.E.2d 468, 470 (N.Y. 1979)).

47. *MNC*, 882 F.2d at 620.

48. *See id.* at 617-18.

III.

What is one to make of the shortcomings of these opinions?⁴⁹ Coming, as they do, from the Second Circuit Court of Appeals—one of the most prestigious courts in the country—they cannot simply be dismissed as examples of the uneven quality of the American judiciary.⁵⁰ If these opinions are emanating from the Second Circuit, what should one expect from judges who are less esteemed?

The opinions represent a lack of understanding of one of the fundamental concepts of commercial law and, for that matter, all property law. The failure properly to utilize *nemo dat* evidences a failure to comprehend the concept's role in commercial law jurisprudence. *Nemo dat* is not some newfangled statutory idea that one schooled in common-law principles must struggle to understand. Rather, *nemo dat* has a long tradition, predating the birth, let alone the legal training, of the judges now called upon to apply it. And it is a remarkably simple principle. Can it be that the law professors of the 1950s and 1960s failed to present this basic principle to their students in ways in which their students would internalize it? Or was the ability to apply the principle instinctively developed in law school but lost through years of desuetude in law practice?

There is little doubt that law practice has become increasingly specialized and that increased specialization may divert one's attention from underlying principles to specific applications. The consequence may be that the basics are lost. But more seems to be at work here. The *ATASCO* opinion is not the product of ignorance. The opinion reflects the court's awareness not only of the "shelter" rule of section 2-403(1) but also of a scholarly article anticipating the very issue in dispute and

49. The fact that, in both cases, the secured party prevailed, might lead one to the conclusion that secured parties as a class are the beneficiaries of judicial favoritism. There seems to be little basis upon which such a bias would be predicated. Although some judges might be inclined to favor business entities over individuals, all the parties to the cases under discussion were businesses. In addition, one of the secured parties (ATASCO) was described as "a Panamanian company engaged in the business of selling and leasing aircraft and aircraft engines," and so appears not to have been a typical financing agency akin to a bank or finance company. *Aircraft Trading & Servs. v. Braniff, Inc.*, 819 F.2d 1227, 1229 (2d Cir.), *cert. denied*, 484 U.S. 856 (1987).

50. Nor do they appear to be aberrational for the Second Circuit. The court's analysis in *Septembertide Publishing v. Stein & Day, Inc.*, 884 F.2d 675 (2d Cir. 1989) (implicating U.C.C. § 9-318), is wanting, and its opinion in *Sanyo Elec. Corp. v. Howard's Appliance Corp.*, 874 F.2d 88 (2d Cir. 1989) (awarding equitable lien to unperfected secured party), has been criticized.

resolving it consistently with that principle.⁵¹ What, then, explains the court's having reached its erroneous conclusion in spite of having been so well informed?

Two aspects of the court's analysis are worthy of comment. The first is the court's approach to statutory interpretation. The court gave great weight to the "plain meaning" of the UCC, which appears not to contradict the court's holding. It emphasized the precision of the statutory language, as evidenced by the differences in phrasing between section 9-307(1), under which a buyer "takes free" of a security interest, and section 9-301(1)(c), under which the security interest is "subordinate to" the rights of the buyer,⁵² and it observed that the drafters included an explicit shelter provision when they found it appropriate.⁵³

Standing alone, this method of statutory construction violates the UCC. The UCC explicitly rejects a literalist approach. Section 1-102(1) instead requires judges to construe and apply the UCC "liberally . . . to promote its underlying purposes and policies."⁵⁴ An analysis that begins and ends with what the statute says, without inquiring into what the statute means, may well lead to error. One saw opinions of this kind when the UCC was newly enacted. Some of these were characterized by barely masked hostility: If the result that the statute compels was unintended, so be it; the drafters should have done a better job. One still sees the same blind reliance on the language of the statute now that the UCC has aged. Ironically, the reliance stems not from hostility to the UCC but from an exceedingly high regard for the drafters' prowess.⁵⁵

While this "literal" approach to statutory construction may explain some erroneous decisions, it does not fully explain *ATASCO*. There the court went beyond the language of the UCC to test its conclusion against the underlying purposes and policies of the statute. Unfortunately, as I explained, the court misapprehended the purpose of section 9-301(1)(c).

51. See David G. Carlson, *Death and Subordination Under Article 9 of the Uniform Commercial Code: Senior Buyers and Senior Lien Creditors*, 5 CARDOZO L. REV. 547, 547-63 (1984).

52. *ATASCO*, 819 F.2d at 1232-33.

53. *Id.* at 1235.

54. U.C.C. § 1-102(1). According to official comment 1 to section 1-102:

The text of each section should be read in the light of the purpose and policy of the rule or principle in question, as also of the [UCC] as a whole, and the application of the language should be construed narrowly or broadly, as the case may be, in conformity with the purposes and policies involved.

Id. § 1-102 cmt. 1.

55. The Seventh Circuit's assessment, that "[t]he Uniform Commercial Code is an uncommonly well drafted statute," is typical of the judiciary's attitude towards the UCC. *Merrill Lynch, Pierce, Fenner & Smith v. Devon Bank*, 832 F.2d 1005, 1008 (7th Cir. 1987), *cert. denied*, 485 U.S. 1008 (1988).

Had it properly understood what that section means, the court could have, and should have, reached the correct result by reading the statute "cheerfully" (as Grant Gilmore used to say).⁵⁶

MNC involves a somewhat different problem. As applied to the facts of that case, section 9-318(1) means what it says. The statute did not present a difficult interpretational issue, but the Second Circuit missed its meaning nevertheless. The court appears to have been led astray by its framing of the issue as "a conflict between a setoff claimant and a holder of a security interest in receivables."⁵⁷ Although characterized as a setoff in Ryerson's purchase orders, Ryerson's right to extinguish its debt to Ramco by paying Ramco's debt to Inland, does not give rise to a common-law right of setoff. A true setoff can be exercised only when the debts are mutual, as when Ramco owes Ryerson and Ryerson owes Ramco. The characterization of the "setoff" in *Bank Leumi*—"a collateral agreement [regarding] the method of payment"⁵⁸—would have been more apt in *MNC* as well.

At one point, the court seemed to accept this characterization, but asserted that the collateral agreement "did not alter Ryerson's underlying obligation."⁵⁹ Had the court approached section 9-318(1) with *nemo dat* in mind, and had the court an intuitive appreciation of the meaning of the statute, it might have realized that the agreement meant that Ryerson had discharged its obligation to Ramco and that, accordingly, Ryerson's defense of payment should have defeated the claim of Ramco's assignee, MNC. Then the court might have found a way to distinguish *Bank Leumi*, rather than treat that case as controlling.

In fact, *Bank Leumi* is easily distinguishable from *MNC*. Although both cases concerned a tripartite relationship that the parties mistakenly characterized as a setoff, the relevant facts were quite different. As we have seen, in *MNC* the account debtor (Ryerson) enjoyed the "setoff" right: It was permitted to satisfy its debt to the Article 9 debtor (Ramco) by paying one of the debtor's creditors (Inland). Having paid the debt, it owed no obligation either to the debtor or to the debtor's assignee (MNC). In *Bank Leumi*, the parties afforded a "setoff" right to the debtor.⁶⁰ The debtor was permitted to satisfy its debt to its creditor by giving value (delivering goods) to the account debtor.⁶¹ As the court of

56. The authorities cited *supra* note 13 suggest two readings the court could have adopted.

57. *MNC*, 882 F.2d at 619.

58. *Bank Leumi Trust Co. v. Collins Sales Serv.*, 393 N.E.2d 468, 470 (N.Y. 1979).

59. *MNC*, 882 F.2d at 620.

60. *Bank Leumi*, 393 N.E.2d at 469.

61. *Id.*

appeals observed, the debtor's payment of its debt to its creditor did not constitute a defense to the account debtor's obligation to the debtor.⁶² Inasmuch as the account debtor was obligated to pay the debtor, it was obligated to pay the debtor's assignee, the secured party.

Judges, of course, do not act in a vacuum. They enjoy the services of law clerks, who are among the most talented of the recent law school graduates. Coming fresh from law school, as most do, the law clerks can be expected to bring their education with them to their jobs. What kind of legal education have the clerks received? Much has been written on the appropriate places of doctrine and theory in the law school curriculum. Perhaps contemporary commercial law professors have directed the focus too far away from fundamental principles—either to nuts and bolts or to meta-theory—to the disadvantage both of their students and of those who in turn rely upon them.

Of course, the population of law clerks is not a random sample of law school graduates. Particularly at the appellate court level, law clerks tend to be chosen from among those who have excelled in their studies at the most prestigious institutions. Students who avail themselves of the opportunity to become federal appellate court clerks may well be disposed to elect courses like federal courts and constitutional theory and to bypass commercial law. The law schools themselves may encourage their students along these lines. The encouragement may be subtle, as where the institutional culture leads students to believe that a career in the private practice of law is for those whose minds or spirits are not really first-rate. (An institutional culture of this kind sometimes is evidenced by hiring decisions: Constitutional law vacancies are filled only with experts; commercial law vacancies are filled with adjuncts or with full-time faculty who teach in the area as an accommodation.) The encouragement may be more direct; professors may counsel those students who are "clerkship material" to elect public law courses. In a few extreme cases, the institution may not even afford its students the opportunity to elect commercial law at all.⁶³

And what about the lawyers? Sometimes they are to blame, arguing areas of law with which they have no familiarity, losing sight of the forest for the trees, or lacking the advocacy skills to drive home what should be a winning argument. Such failures do happen, but nothing in the opinions in *ATASCO* and *MNC* suggests that they occurred in those cases.

62. *Id.* at 470.

63. In 1984 I received a note from an articles editor of the *Yale Law Journal* informing me that Yale students were ill-equipped to evaluate my Article on the UCC because Yale did not offer a commercial law course.

Perhaps some of the fault lies in the UCC. As I observed at the start of this Essay, section 1-103 specifically invites judges to refer to non-UCC law unless it has been "displaced by the particular provisions" of the UCC.⁶⁴ Unfortunately, the UCC affords little additional guidance. Neither section 1-103 nor the official comment explains generally how to determine whether non-UCC law has been displaced. Although official comments address displacement in a number of instances, the statutory text itself rarely does. Notable exceptions are found in the new Article 3 and Article 4A, in which the drafters showed a fondness for incorporating non-UCC law into the UCC by reference.⁶⁵

Ironically, inclusion of specific references to non-UCC law may widen the way for a court to infer erroneously, from the absence of such a reference, that otherwise applicable non-UCC law has been displaced. Accordingly, the Article 9 study committee recommended against revising Article 9 to address explicitly the circumstances under which UCC provisions do and do not displace other law.⁶⁶ The committee recommended instead the promulgation of official comments or PEB commentary to address specific problems that have arisen in the reported cases.⁶⁷ This approach may blunt the impact of a few erroneous decisions (one cannot expect a comment or commentary on every wrongly decided case), but it would do little to help courts approaching an issue for the first time.

Ultimately, education may be the best answer. Judges, law clerks and lawyers who have internalized the principles that underlie the UCC are the best hope of keeping the UCC alive and well.

64. U.C.C. § 1-103.

65. See, e.g., *id.* §§ 3-116(b) (making jointly and severally liable party responsible for contribution "in accordance with applicable law"), 3-202(b) (permitting rescission of negotiation "[t]o the extent permitted by other law"), 3-420(a) (applying law of conversion of personal property to instruments), 4A-303(c) (allowing recovery under "the law governing mistake and restitution").

66. PEB STUDY GROUP UNIFORM COMMERCIAL CODE ARTICLE 9: REPORT (DECEMBER 1, 1992) § 12 (1992).

67. *Id.*

