UCC Bulletin

A monthly newsletter highlighting and commenting upon recent noteworthy developments relating to the Uniform Commercial Code

May 1995 Clark Boardman Callaghan

IN THIS ISSUE . . .

SMASHING THE BROKEN MIRROR: THE BATTLE OF THE FORMS, UCC §2-207, AND LOUISIANA'S IMPROVEMENTS*

[Part One of a Two-Part Article]

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I. INTRODUCTION

While a broken mirror is supposed to bring seven years of bad luck, the breaking of the common law's mirror image rule by **§2-207** of the Uniform Commercial Code has been seen in a more positive light. The UCC abolished the mirror image rule because it is problematic and can lead to unjust results. In Louisiana, where the UCC has not been completely adopted, the mirror image rule, as embodied by Louisiana Civil Code Article 1943, has recently been eliminated as well.

On January 1, 1995, Article 1943 was superseded by new Louisiana Civil Code Articles 2601 and 2602, which closely follow the structure of **UCC §2-207**. Articles 2601 and 2602 were part of the Sales Revision Project of the Louisiana State Law Institute, and are designed such that some of the defects of **§2-207**, which have become apparent over time, may be avoided. To the extent that these articles accomplish this goal, they are a "new and improved" version of **§2-207**, and can be a guide for further modification of **§2-207**. To that end, this paper will examine Louisiana's solutions to some of **§2-207**'s problems.

II. THE MIRROR IMAGE RULE AND THE LAST-SHOT PRINCIPLE

Under the mirror image rule, a purported acceptance which does not perfectly "mirror" the terms of the offer is not an acceptance; instead, it is a rejection and counter-offer. An ostensible acceptance of *this* counter-offer may, by the same token, be instead a counter-counter-offer. The true acceptance occurs when a party finally starts performing, after receiving the latest counter-offer of the other party. By the performer's acceptance, the contract embodies the terms of the last counter-offer. In this way the mirror image rule leads to the last-shot principle: he

Published by
CLARK BOARDMAN CALLAGHAN
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who makes the last offer (i.e., the "last shot") before performance or acceptance has his terms locked into the contract. As White and Summers state: "The original draftsman of **2-207** designed it (though not exclusively) to keep the welsher in the contract. He had cases like **Poel v. Brunswick-Balke-Collender Co.**, 110 NE 619, 621 (NY 1915), in mind. There the buyer's underling sent back its own order form which happened to coincide with the seller's terms except in one minor respect. It added: 'The acceptance of this order . . . in any event you must promptly acknowledge.' Thereafter, the seller failed to acknowledge, and the buyer for other reasons backed out. When the seller sued the buyer, the court held that the buyer's order form did not constitute an acceptance. At common law an acceptance had to be a mirror image of the offer. The buyer's form therefore could not be an acceptance; it was a counter-offer. The rigidity of the common law rule ignored the modern realities of commerce. Where preprinted forms are used to structure deals, they rarely mirror each other, yet the parties usually assume they have a binding contract and act accordingly. Section **2-207** rejects the common law mirror image rule and converts many common law counter-offers into acceptances under **2-207(1)**." James J. White & Robert S. Summers, Uniform Commercial Code 29-30 (3d ed 1988) (footnotes omitted). Hereafter "White & Summers."

The last-shot principle was largely eliminated by the enactment of **UCC §2-207**. Some escaped total elimination; also, the application of **§2-207** is not without certainty. Section **2-207** is not yet perfect.

III. FORMATION OF CONTRACTS IN LOUISIANA -- PRESENT AND FUTURE

Under new Louisiana Articles 2601 and 2602, the mirror image rule is repealed in favor of a provision similar to **§2-207** of the UCC. New Article 2601, which corresponds to **UCC §§2-207(1)** and **(2)**, reads as follows: "Art. 2601. Additional terms in acceptance of offer to sell a movable. An expression of acceptance of an offer to sell a movable thing suffices to form a contract of sale if there is agreement on the thing and the price, even though the acceptance contains terms additional to, or different from, the terms of the offer, unless acceptance is made conditional on the offeror's acceptance of the additional or different terms. Where the acceptance is not so conditioned, the additional or different terms are regarded as proposals for modification and must be accepted by the offeror in order to become a part of the contract.

"Between merchants, however, additional terms become part of the contract unless they alter the offer materially, or the offer expressly limits the acceptance to the terms of the offer, or the offeree is notified of the offeror's objection to the additional terms within a reasonable time, in all of which cases the additional terms do not become a part of the contract. Additional terms alter the offer materially when their nature is such that it must be presumed that the offeror would not have contracted on those terms."

New Article 2602, which corresponds to **UCC §2-207(3)**, reads as follows: "Art. 2602. Contract by Conduct of the Parties. A contract of sale of movables may be established by conduct of both parties that recognizes the existence of that contract even though the communications exchanged by them do not suffice to form a contract. In such a case the contract consists of those terms on which the communications of the parties agree, together with any applicable provisions of the suppletive law." For ease of comparison, **UCC §2-207**, "Additional Terms in Acceptance or Confirmation," provides: "(1) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms. (2) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless: (a) the offer expressly limits acceptance to the terms of the offer; (b) they

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materially alter it; or (c) notification of objection to them has already been given or is given within a reasonable time after notice of them is received. (3) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this Act."

IV. UCC §2-207 PROBLEMS AND CIVIL CODE SOLUTIONS

A. Where Acceptance is "Expressly Conditional"

1. The Meaning of "Expressly Conditional." **UCC §2-207** attempts to solve problems arising from the mirror image rule by eliminating the rule. Under **§2-207(1)**, an "expression of acceptance . . . operates as an acceptance even though it states terms additional to or different from those offered. . . ." Thus, the mere fact that an ostensible acceptance does not perfectly mirror the offer does not mean that it cannot operate as an acceptance. By this provision the traditional mirror image rule is eliminated. However, under **§2-207(1)** the offeror can invoke the mirror image rule, preventing the reply from being an acceptance, if the "acceptance is expressly made conditional on assent to the additional or different terms." The courts have encountered some problems in deciding whether a purported acceptance was "expressly" made conditional on the offeror's assent to the additional or different terms. For example, in **Roto-Lith, Ltd. v. F.P. Bartlett & Co.**, 1 UCC Rep Serv 73; 297 F2d 497 (1st Cir 1962), the court held that a responding document which contained a condition (a disclaimer) was expressly conditional and thus did not operate as an acceptance, even though, according to White and Summers (at 33), this holding was inconsistent with the policies embodied in **UCC §2-207**. Professor Hawkland suggests that courts should "emphasize the words 'expressly made conditional.' " William D. Hawkland, Uniform Commercial Code Series §2-207:02, at Art. 2, p. 160 (1992). Hereafter "Hawkland." Thus, to be "expressly conditional," a purported acceptance would have to explicitly state, in unambiguous language and in a conspicuous position on the form, that acceptance is "expressly conditioned" upon the offeror's assent to such conditions. Under **UCC §2-207(1)**, an "acceptance" which contains the "expressly conditional" language buried in small type or in an inconspicuous place on the form usually will not be sufficient to prevent the form from being a true acceptance. "The placement and nature of the qualifying language in the purported acceptance is critical in determining whether or not there is an acceptance under the first part of **§2-207(1)**, or a rejection and counter-offer under the second part. The qualifying language does not have to use the word 'condition' to become expressly conditional within the meaning of the proviso, but it must be stated in such a place, manner and language that the offeror will understand in the commercial setting of the transaction that no acceptance has occurred, despite initial language stating that the offeree is happy to accept." *Id.* at 161 (citations omitted).

The jurisprudence is consistent with this reading of **§2-207(1)**. In **Clifford-Jacobs Forging Co. v. Capital Engineering & Manufacturing Co.**, 34 UCC Rep Serv 24, 26; 437 NE 2d 22, 24 (Ill App, 1982), the court stated that an acceptance will be considered a counter-offer only if the acceptance is *expressly* made conditional on *assent* to the additional terms. This provision of the statute has been construed narrowly to apply only to an acceptance which clearly shows that the offeree is unwilling to proceed absent assent to the additional or different terms. In **Mace Industries, Inc. v. Paddock Pool Equipment Co.**, 42 UCC Rep Serv 825; 339 SE 2d 527 (SC App, 1986), the court held that to convert an acceptance into a counter-offer under **UCC §2-207(1)**, the conditional nature of the acceptance must be clearly expressed in a manner sufficient to notify the offeror that the offeree is unwilling to proceed with the transaction unless the additional or different terms are included in the contract.

2. Article 2601: Omission of "Expressly" -- Apparent Disadvantages. Article 2601, in stating that an "expression of acceptance . . . suffices to form a contract . . . unless acceptance is made conditional on the offeror's acceptance of the additional or different terms," does not require the acceptance to be *expressly* conditional, unlike **UCC §2-207(1)**. This appears to be, at first glance, a major and unfortunate change from the wording of **§2-207**, for it will be easier for an "acceptance" to fail to be a true acceptance, because the conditioning need not be express. Thus, under Article 2601, the communications

between the parties will fail to form a contract more frequently than under the UCC. Where subsequent conduct of the parties nevertheless recognizes the existence of a contract, suppletive terms, not those of (one of) the parties, will define the contract. Consequently, there will be more resort to Article 2602, which covers this situation and supplies suppletive terms, than there is to **§2-207(3)** under the UCC, which also provides for suppletive terms. An advantage of the "expressly conditioned" language in **UCC §2-207(1)** is that it allows an ambiguous acceptance -- e.g., one which is conditional, but not expressly so -- to be held against the offeree. Hawkland, §2-207:02 at Art. 2, p. 161. Under Article 2601, a similarly "ambiguous" acceptance possibly would not be held against the offeree, but would instead prevent acceptance altogether, because Article 2601 does not require the conditioning of acceptance to be express; i.e., the absence of the word "expressly" allows more ambiguous conditioning of acceptances to bar formation of a contract. Courts may still attempt to hold ambiguous conditioning of acceptances against the offeree, but will be less able to do so because the removal of the word "expressly" clearly indicates that a court should more often find that there was no acceptance. Lack of the word "expressly" in Article 2601 will allow offerees to condition more ambiguously -- i.e., less expressly -- their "acceptances" and still avoid the contract being formed on the offeror's terms.

3. Article 2601: Omission of "Expressly" -- Advantages. There is, however, some reason in support of such an eased standard for conditioning one's acceptance. Conditions attached to an acceptance (though not expressly), in a sense, still convey a rejection of the offer. If the conditioned acceptance were to form a contract on the offeror's terms, there would exist a situation similar to that arising under the "last shot principle" that revocation of the mirror image rule was meant to eliminate. When an offeree's "acceptance" is, indeed, "conditioned" on the offeror's assent to additional or different terms -- even if not "expressly" conditioned -- the offeree's "acceptance" is not a true acceptance, technically speaking. Thus, omission of the word "expressly" is an improvement because it will actually remove some of the remaining vestiges of the last shot principle. Some courts have worried that a more lenient standard for finding no true acceptance, because the acceptance was conditioned, would actually lead to a *resurgence* of the mirror image rule. For example, in **Boese-Hilburn Co. v. Dean Machinery Co.**, the court stated: "[T]his court believes that the drafters of the Uniform Commercial Code, by use of the language 'expressly made conditional,' clearly intended that an acceptance which merely implied that it was 'conditional' on an offeror's assent to a different or additional provision was insufficient to convert an acceptance into a rejection and a counter-offer. Otherwise, many of the problems which prompted the drafting and adoption of UCC **§2-207** would not be alleviated and the specter of the 'mirror image' rule would still haunt the marketplace." In this case, the court was concerned that a looser standard for finding that an acceptance is "conditional" may lead to an increase in mirror image results. The court's concern appears to be unfounded for, rather than finding that a failed acceptance is a counter-offer -- whose terms will rule if the offeror then performs (an example of the last shot principle) -- the court could find that there has been no contract formed at all by the writings of the parties, and instead resort to suppletive law, as provided in **UCC §2-207(3)** and in new Louisiana Civil Code Article 2602. That is, when a reply to an offer is conditioned so that it is not an acceptance, the offeree does not get his terms embodied in the contract if the offeror then performs; rather, suppletive terms are applied.

Let us assume a situation where no contract exists under **UCC §2-207(1)**, but the parties nevertheless perform. A court can proceed to analyze contract formation in one of two ways. "First, a court can take the common law, **Roto-Lith**, approach and find that the second document is a counter-offer and hold that subsequent performance by the party who sent the first document constitutes acceptance. This approach gives one party (who fortuitously sent the second document) all of his terms. In our view, Code draftsmen did not choose to take this approach. Instead, they proceeded on to contract formation via section **2-207(3)**. . . ." White & Summers, at 42 (footnote omitted). Similarly, under Articles 2601 and 2602, if an "acceptance" fails to form a contract because it is conditioned on additional or different terms, instead of being a counter-offer and the offeree getting his terms under the last shot principle if the offeror were to perform, Article 2602 would instead look to the suppletive law to determine the terms of the ensuing contract. Thus, making

it easier to condition one's acceptance by not requiring it to be "express" will lead to greater use of the suppletive law, not to increased last-shot results. And while increased occurrence of last-shots results may be undesirable, increased resort to suppletive law may, in many situations, be a beneficial change in the law, because it would in some situations prevent the counter-offeror from getting the "last shot." If the parties go on to perform the contract, where the offeree conditioned his acceptance (though not expressly), there is some justice in holding them equally "at fault" for failing to reach an agreement by their communications, so that neither is in a position to complain about suppletive law determining the terms of the contract. In a sense then, a more equitable system results from the removal of the word "expressly" and the corresponding increased ability of an offeree to condition his offer, because neither offeror nor offeree receives an inordinate advantage; rather, where there has been acceptance only by performance, both parties, having performed, are subjected to the suppletive law as mandated in Article 2602.

[Part 2 of this article will appear next month-Ed.]

MATTERS OF MAJOR INTEREST

LATE FILER BEATS TRUSTEE THROUGH SUBROGATION TO PRIOR CLAIM

[See UCC Case Digest ¶¶1102.13, 1103.1(9), 1103.8, 1201.25(9), 1201.37(3), 9102.4, 9102.22, 9201.9, 9301.12, 9302.1, 9302.32, 9302.33, 9312.3, 9403.7, 9405.1]

District Judge Marvin J. Garbis of the United States District Court for the District of **Maryland** decides that a bank that failed to file any financing statements regarding its security interest in the debtor's assets until well within the ninety-day preference period preceding the debtor's filing for bankruptcy still prevails over the bankruptcy trustee. How is this result possible? Because three years before the bankruptcy, the bank -- First Union National Bank of Maryland ("First Union") -- paid off the debtor's debt to another creditor which had previously perfected its security interest through filing. This act (of payoff), according to Judge Garbis, resulted in the equitable subrogation of First Union to the perfected security interest of that paid-off creditor. Under the case-law-established rules of equitable subrogation, the judge explains, it was not necessary that the prior creditor make a formal assignment of its lien to First Union. Moreover, First Union stepped into the shoes of the prior creditor immediately upon making the payment. The trustee's argument that First Union should be denied equitable subrogation by its failure to file anything itself for three years is rejected on the grounds that **UCC §1-103** expressly permits "principles of . . . equity" to "supplement" the provisions of the UCC. The trustee's second argument that the bank's "negligence" should bar its claim is also repudiated: "First Union's alleged negligence in failing to meet the statutory recording requirements does not rise to the gross or 'inexcusable neglect' necessary to preclude relief. As soon as First Union discovered the oversight of its previous counsel, it had the proper forms executed and filed. Moreover, the Trustee has not established that any intervening lienholder detrimentally relied upon First Union's failure to file. Indeed, because the statutory filings of [the paid-off creditor] for the same property remained on record, any potential lender would be put on notice of the outstanding security interest in the [debtor's] collateral." Finally, Judge Garbis relies on a precedent from **New Jersey** to reject the trustee's assertion that Bankruptcy Code §544(a), the so-called "strong-arm" clause, gives the trustee the power to prevail. In **Kaplan v. Walker**, 25 UCC Rep Serv 871; 395 A2d 897 (NJ, 1978), the court was unimpressed by a very similar argument made by the debtor's receiver. **Rinn v. First Union Nat. Bank of Maryland**, 25 UCC Rep Serv 2d 1057 (US Dist Ct, D Md, decided January 5, 1995).

> **Comment:** *What if the paid-off creditor had released its lien and there was nothing in the records to provide notice to potential creditors of First Union's security interest? The court suggests that the trustee would still have to have shown actual prejudice.*

NON-NEGOTIABLE, NON-TRANSFERABLE CERTIFICATES OF DEPOSIT GOVERNED BY ARTICLE 9 AS "GENERAL INTANGIBLES"

[See UCC Case Digest ¶¶1105.2, 1105.6, 3104.12, Rev3104, 9102.41(1), 9103.1, 9103.2, 9103.4, 9105.5, 9105.9, 9105.20, 9106.5(7)]

Creditor Fleet Credit Corporation's failure to file a financing statement for two writings pur-