

§ 1-105. Territorial Application of the Act; Parties' Power to Choose Applicable Law and Judicial Forum

(a) Unless the law determining the rights and obligations of parties with respect to any aspect of a transaction governed by this Act has been selected by agreement pursuant to subsection (b), and except as provided in subsection (c), the law determining those rights and obligations is the law that would ordinarily be selected by application of this state's conflict of laws principles [unless:]

Subsection (a)(1) - Alternative A

[(1) application of such principles would result in the invalidation of a contract [that is not a consumer transaction], or a portion thereof, that is valid under the law of this state, and this state has an appropriate relation to the transaction, in which case the law governing those rights and duties is the law of this state;] [or]

Subsection (a)(1) - Alternative B

[(1) application of such principles would result in the invalidation of a contract [that is not a consumer transaction], or a portion thereof, and there is at least one jurisdiction having an appropriate relation to the transaction under whose law the contract or portion thereof is valid, in which case the law governing those rights and duties is:

- (i) if there is one such jurisdiction, the law of that jurisdiction;**
 - (ii) if there is more than one such jurisdiction (a “validating jurisdiction”), the validating jurisdiction that would be selected by application of this state’s conflict of laws principles] [or]**
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[(2) (i) application of such principle would result in the selection of the law of a state or nation that has not adopted a law [substantially similar to the Uniform Commercial Code as promulgated from time to time by the National Conference of Commissioners on Uniform State Laws and the American Law Institute] [substantially similar to this Act] and (ii) this state has an appropriate relation to the transaction, in which case the law governing those rights and duties is the law of this state.]

(b) Except as provided in subsection (c) or (d), the parties to a transaction governed in whole or in part by this Act may agree that any or all of [their rights and obligations] [the rights and obligations with respect to each other] shall be determined:

Subsection (b)(1) - Alternative A

(1) by the local law of another state or nation

(i) if such state or nation has an appropriate relation to the transaction or either of the parties and, if the transaction is a consumer transaction, is the state or nation in which the consumer party resides at the time the transaction becomes enforceable or within 30 days thereafter or is the state or nation in which, pursuant to the contract establishing the transaction, the consumer party is to use the goods, services, or other consideration provided to the consumer; or

(ii) if paragraph (i) does not apply, to the extent that, under this Act (Section 1-102(3)), the parties could effectively agree to the rights and obligations that would result from application of such law; or

Subsection (b)(1) - Alternative B

(1) by the local law of another state or nation

(i) if the transaction is not a consumer transaction; or

(ii) if the transaction is a consumer transaction, if such state or nation has an appropriate relation to the transaction and is the state or nation in which the consumer party resides at the time the transaction becomes enforceable or within 30 days thereafter or is the state or nation in which, pursuant to the contract establishing the transaction, the consumer party is to use the goods, services, or other consideration flowing to the consumer;

(2) by any recognized body of rules or principles applicable to commercial transactions [to the extent that, under this Act (Section 1-102(3)), the parties could effectively agree to the rights and obligations that would result from application of such body of rules].

(c) Where one of the following provisions of this Act specifies the applicable law, that provision governs and a contrary agreement is effective only to the extent permitted by the law (including the conflict of law rules) so specified:

(1) Section 2-402 (Rights of creditors against sold goods)

(2) Sections 2A-105 [and 2A-106] (Applicability of the Article on Leases)

(3) Section 4-102 (Applicability of the Article on Bank Deposits and Collections)

(4) Section 4A-507 (Governing law in the Article on Funds Transfers)

(5) Section 5-116 (Letters of Credit)

(6) Section 6-103 (Bulk sales subject to the Article on Bulk Sales)

(7) Section 8-110 (Applicability of the Article on Investment Securities)

(8) Section 9-103 (Perfection provisions of the Article on Secured Transactions)

[(d) A written agreement of the parties designating a particular judicial forum for resolving disputes arising out of or relating to a transaction a significant aspect of which is transaction governed by this Act:

(1) is effective [, if that forum is in this state,] to confer jurisdiction on that forum to resolve such disputes unless:

(i) for reasons other than lack of personal jurisdiction, the judicial forum designated does not have the power to adjudicate the dispute under the law of the forum's jurisdiction;

(ii) utilization of that forum would effectively deprive a party of the ability to bring, or defend against, an action regarding such a dispute[, or would otherwise be fundamentally unfair]; or

(iii) if the transaction is a consumer transaction and the action is brought against the consumer, the judicial forum would not otherwise have jurisdiction over the consumer; and

[(2) is effective to confer exclusive jurisdiction on that forum to resolve such disputes if (i) the agreement so provides in writing, and (ii) under the law governing that forum, that forum has jurisdiction to adjudicate the dispute, unless subsection (d)(ii) or (d)(iii) applies]]

REPORTER'S NOTES

a. Choice of law in the absence of contractual designation; generally. Subsection (a) replaces the last sentence of current UCC section 1-105(1), which determines which jurisdiction's law governs a transaction in the absence of an effective contractual choice by the parties. This provision, by providing that the law of the forum (*i.e.*, the UCC) applies if the transaction bears "an appropriate relation to this state" rather than, say, requiring that the forum be the location of the "most significant contact, expresses a bias in favor of applying the forum's law. This bias, while not universally respected by the courts, was most justifiable in light of the uncertainty that existed at the time of drafting as to whether the UCC would be adopted by all the states; the pro-forum bias would assure that the UCC would be applied so long as the transaction bore an "appropriate relation to the forum. Inasmuch as the UCC has been adopted, at least in part, in all American jurisdictions, the vitality of this point is minimal in the domestic context. Whether international comity concerns militate against continuing the pro-forum, pro-UCC bias in transnational transactions is an important question. Bracketed subsection (a)(2) addresses this issue. See Reporter's Note *c, infra*. When the choice is between the law of two jurisdictions that have adopted the UCC, but whose law differs (whether because of differences in enacted language or differing judicial interpretations), there is no strong justification for directing a court to apply different choice-of-law principles to its determination than it would apply if the matter were not governed by the UCC. Similarly, given the wide variety of operative choice of law principles applied by the states, it would not be prudent to designate only one such principle as the proper principle for transactions governed by the UCC. Accordingly, with the exception noted in Reporter's Note *b, infra*, revised UCC section 1-105(a)

simply directs the forum to apply its general choice of law principles to determine which jurisdiction's law governs.

b. Invalidating law. Once it is determined that there has been sufficient agreement to conclude that a contract has been formed, the law, with very few exceptions, treats the parties as intending to be bound by the terms of that contract. Nonetheless, the Uniform Commercial Code limits freedom of contract in several contexts, and the law of particular jurisdictions may limit such freedom in additional contexts. If a contract is formed that has an appropriate relation with more than one jurisdiction, and the law of one of those jurisdictions would invalidate the contract or a portion thereof while the law of another of those jurisdictions would validate it, the choice of law issue is critical. Given the intent to be bound that is presumed by the law, a strong argument can be made that if the forum's general choice of law principles would result in the application of the law of a different jurisdiction that would invalidate the contract or a portion of it, even though under the Uniform Commercial Code and other law of the forum that contract or portion would be held valid, the forum should apply its own validating law so as to effectuate the parties' intent. See ABA Task Force Report. Such a rule would prevent transactions valid under the forum state's UCC from invalidation by application of another jurisdiction's non-UCC law. See Alternative A of subsection (a)(1).

The argument can also be made that this principle of validation should require a court to select the law of a different jurisdiction when the forum would otherwise choose its domestic law and that law would invalidate the contract or a portion of it. To the extent, though, that such a rule, set out in Alternative B of subsection (a)(1), would direct a court in a UCC jurisdiction not to apply the UCC (as it would if it applied its general choice of law principles) but, rather, non-UCC law of another jurisdiction, the argument may be somewhat weaker.

c. Preference for Uniform Commercial Code. As noted in Reporter's Note *a*, current UCC § 1-105, by providing that the law of the forum (*i.e.*, the UCC) applies if the transaction bears "an appropriate relation to this state," expresses a bias in favor of applying the forum's law. Given the uncertainty that existed at the time of drafting as to whether the UCC would be adopted by all the states, the pro-forum bias served to assure that the UCC would be applied so long as the transaction bore an "appropriate relation to the forum. Subsection (a), as set out in this draft, generally eliminates that pro-forum bias. Subsection (a)(2) would, if adopted, retain the pro-forum bias for the limited purpose of assuring that the Uniform Commercial Code, rather than the non-Code law of another jurisdiction, applies. Inasmuch as choice of law determinations involving a non-Code jurisdiction will almost always be in international transactions, though, subsection (a)(2) ought to be examined closely in light of concerns regarding international comity and the effect of such a rule on the likelihood that courts of foreign jurisdiction would apply the UCC when appropriate.

d. Contractual choice of law. Many commercial contracts include a provision selecting the jurisdiction whose law will govern the transaction. Subsection (b) determines the extent to which such provisions are effective. Selecting the "law governing a transaction, of course, involves two related, but separate, choices. The first choice is that of the substantive rules that will govern the relationship between the parties making the choice. With limited exceptions, parties are given great autonomy to order the relationship between them by UCC section 1-102. To the extent that selecting the law of a jurisdiction is, in effect, accomplishing no more than what is within the parties' power under section 1-102, this section makes such a selection effective without regard to the relationship between the parties or the transaction and the jurisdiction whose rules are used to set the parameters of the relationship between the parties. See subsection (b)(1)(ii), Alternative A. (To the extent that Alternative B of that subsection provides the parties broad freedom to select the governing law, this point is not addressed separately in that Alternative.)

The second choice that is made by parties when they select the law of a particular jurisdiction to govern their transaction is the choice of that jurisdiction's rules of validity and enforceability; that is, rules that could not have adopted by application of UCC section 1-102. There is significant difference of opinion as to the appropriate rule here. Some believe that only jurisdictions bearing an appropriate relationship to the transaction or the parties may be selected. Under this approach, set out in Alternative A of subsection (b)(i), the parties would be able, in effect, to select only from among those states that would be potential candidates for the choice of law in the absence of a contractual designation under subsection (a). Others believe that the parties should, within the general bounds of autonomy of contract, have freedom to designate the law of any jurisdiction. This approach is set out in Alternative B of subsection (b)(i).

e. Consumer transactions. Several provisions in this draft embody a distinction between “consumer transactions” and other transactions. If these distinctions are adopted, “consumer transaction” will be defined in this Section or in Section 1-201. In subsection (a)(1) of this section [in both Alternative A and Alternative B], the preference for judicial selection of a law that validates the parties’ transaction arguably should not apply in the case of consumer transactions. Limits that a state imposes on freedom of contract in consumer transactions are usually representative of a strong public policy interest. If the law that would be judicially selected but for the application of the rule in subsection (1)(a) would invalidate a contract or portion thereof in a consumer transaction, the preference for a rule of validation would be in conflict with such public policy interests. Accordingly, this draft includes bracketed language that would exclude application to consumer transactions of the preference for a rule of validation.

Both alternatives of subsection (b)(1) of this Section limit the parties’ ability in a consumer transaction to contractually select the jurisdiction whose law will govern. Both alternatives limit the parties’ choice in consumer transactions to a “state or nation [that] has an appropriate relation to the transaction and is the state or nation in which the consumer party resides at the time the transaction becomes enforceable or within 30 days thereafter or is the state or nation in which, pursuant to the contract establishing the transaction, the consumer party is to use the goods, services, or other consideration flowing to the consumer. This limitation is adapted from the similar limitation in current Section 2A-106.

Similarly, subsection (d)(3) declines to enforce forum selection clauses in consumer transactions if the judicial forum selected “would not otherwise have jurisdiction over the consumer. This provision, too, is adapted from Section 2A-106.

f. Designation of non-legal codes. Subsection (b)(2) authorizes the parties to designate “any recognized body of rules or principles applicable to commercial transactions” as supplying governing principles for their transaction. As such bodies of rules gain currency, this authorization may take on added importance. Bracketed language at the end of this provision would limit the effect of the authorization to authorizing terms that the parties could agree upon pursuant to Section 1-102(3). Section 5-116(c), speaking to the same issue in the context of letters of credit, takes an intermediate position. That section limits incorporation of “rules of custom or practice, such as the Uniform Customs and Practice for Documentary Credits” to those that do not conflict with nonvariable provisions specified in Section 5-103(c), but does not restrict the freedom of parties to incorporate such rules even if such incorporation would otherwise violate Section 1-102(3) because it would effectively disclaim an obligation of good faith, diligence, reasonableness or care.

g. Primacy of other UCC choice of law rules. Subsection (c) repeats the list in current Section 1-105(2). This list has not been updated to reflect drafts of Article 2B and of revised Articles 2, 2A, and 9.

h. Contractual choice of forum. The use of contractual choice of forum clauses has expanded as judicial hostility to them has faded. See, e.g., *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991); *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972). See also Restatement of the Law (Second), Conflict of Laws § 80 (1971); Model Choice of Forum Act (1968, withdrawn 1975). Subsection (d) would govern the designation of a particular forum to adjudicate disputes arising from a transaction a significant aspect of which is governed by this Act whether that designation is exclusive or non-exclusive. Paragraph (1) determines whether the courts of this state may adjudicate the dispute in light of the contractual choice. Of course, this statute cannot govern the power of a court in another state or nation to adjudicate a matter. Paragraph (2) determines whether the selection of a forum as the exclusive location for litigation will be effective.