ESSAY

TRADE USAGE IN THE COURTS: THE FLAWED EVIDENTIARY BASIS OF ARTICLE 2’S INCORPORATION STRATEGY
Lisa Bernstein*

INTRODUCTION

The Uniform Commercial Code (“Code”) directs courts deciding disputes between merchants to look to usages of trade and other commercial standards and practices to interpret contract provisions and fill contractual gaps. This so-called incorporation approach1 was the brainchild of the Code’s principal drafter, Karl Llewellyn,2 and was an important application of legal realist

* Wilson-Dickenson Professor of Law, The University of Chicago. I would like to thank the Lynde and Harry Bradley Foundation, the John M. Olin Foundation, and the Sarah Scaife Foundation for financial support and Douglas Baird, Uri Benoliel, Edward Bernstein, Brian Bix, Steve Burton, Shai Dothan, Chris Drahozol, Robin Effron, Jake Gerson, Philip Hamburger, William Hubbard, Emily Kadens, Louis Kaplow, Avery Katz, Saul Levmore, James Lindgren, Stewart Macaulay, Ariel Porat, Richard Posner, Yuval Procaccia, Susan Rosenberg, Margaret Schilt, David Schraub, Eyal Zamir, and participants at the Hebrew University of Jerusalem Workshop, the Columbia Law School Legal Theory Workshop, the University of Iowa Faculty Workshop, the Academic Center for Law and Business Faculty Workshop, the Georgetown Contract As Promise Meeting, the Hebrew University International Contract Conference, the Israeli Law and Economics Association Annual Meeting, the Empirical Legal Studies Conference, and the Tel Aviv University Law and Economics Workshop for useful comments. I would also like to thank Mary La Brec, Sara Weber, Vania Wang, Kimberly St. Clair, Marc Blitz, Jeremy Bates, Jamie McCloud, Gladys Zolna, Donn Parsons, and Marissa Maleck for outstanding research assistance.

1 The term “incorporation approach” refers to the Code’s incorporation of course of dealing, usage of trade, and course of performance. This essay, however, focuses solely on the incorporation of trade usages and other commercial standards in the trade. For a discussion of the reasons why it is undesirable to incorporate course of dealing and course of performance into commercial contracts see Lisa Bernstein, Merchant Law in a Merchant Court: Rethinking the Code’s Search for Immanent Business Norms, 144 U Pa. L Rev. __ [Hereinafter, Merchant Law]

2 The drafts of the Code that preceded the public hearings and the adjustments required by the demands of interest group politics, were more sensitive to the procedural and strategic considerations identified in this essay. These early drafts contained a provision for determining the content of customs through the use of what Llewellyn termed “Merchant Experts on Mercantile Facts,” see Report and Second Draft: The Revised Uniform Sales Act, (1941) at 251, who would determine
philosophy to commercial law. The incorporation approach was both endorsed and expanded in the most recent proposed revision of Articles 1 and 2 of the Code. It also plays a prominent role in the most important international commercial law statutes and is at the jurisprudentia heart of the recently completed Common European Sales Law, an optional instrument that was designed to govern transactions in the sale of goods across the European common market.

Although the Code’s incorporation strategy has been in operation in US courts for over seventy years and has influenced commercial law around the globe, neither the conceptual model underlying the strategy, nor the theoretical arguments invoked to justify it, have ever been explored against the background of the way that its trade usage component operates in practice. This essay presents a detailed study of all of the sales-related trade usage cases digested under the Code’s trade usage provision from 1970-2007. Subject to the usual methodological limitations of studies based on reported cases, the study paints a picture of the way that the usage component of the incorporation strategy works in practice that differs along important dimensions from the way it has long been assumed to work in theory. The essay then draws on this picture to

the content of usages relating to a variety of subjects including, but not limited to: the conformity or nonconformity of goods; whether a nonconformity was substantial; the reasonableness of actions; and other issues within the purview of “special merchant’s knowledge rather than general knowledge” id at Section 59 p. 254. Llewellyn recognized that these determinations were ill-suited to adversarial litigation in front of lay juries, explaining that it “could take three weeks of trial time merely to determine whether a shipment of Textiles were conforming, and that if such matters were left to a jury, representatives of the parties’ . . . would be the main witnesses bringing their obvious bias’ with them.”

3 See William Twining, Karl Llewellyn and the Realist Movement (1993)[hereinafter Realist Movement] (describing the realist jurisprudential bent of the Code, but noting that no realist style social scientific research was done to justify its adjudicative approach).

4 See James J. White, Good Faith and the Cooperative Antagonist, 54 SMU L. Rev, 679 (2001)[hereinafter “Cooperative Antagonist”] (noting that the invocation of commercial standards that rely on usage of trade for their content has been “expanded” in the revised Code).


reevaluate the core justification for the strategy, namely, the claim that, as compared to a more formalist approach to adjudication, incorporation decreases specification costs without unduly increasing interpretive error costs.7

After reexamining the justifications for the incorporation of usage in light of both the data presented and the doctrinal rules that have emerged to guide the implementation of the strategy, the essay concludes that there are reasons to seriously question whether the strategy reduces specification costs. It also concludes that the strategy most likely imposes significant interpretive error costs on the parties. The data clearly demonstrate that the types of “objective” trade usage evidence that the strategy relies on to minimize the risk of interpretive errors--such as expert witness testimony, trade codes, and statistical evidence--are rarely introduced in sales-related litigation. In light of these and other findings about the strategy’s effect on motions for summary judgment and transactors’ ability to engage in litigation-related strategic behavior, the essay concludes that it is time to seriously consider either shifting the background interpretive presumptions of American commercial law in a more formalist direction and/or restricting the domain of incorporationist

7 Kraus and Walt, In Defense of the Incorporation Strategy, in Jody S. Kraus and Steven D. Walt, The Jurisprudential Foundations of Corporate and Commercial Law (Cambridge, 2000); Clayton P. Gillette, Harmony and Stasis in Trade Usages for International Sales, 39 Va. J. Int’l Law 707 [hereinafter “Harmony and Stasi”] 707-7099 (1999) (noting that “[t]he commercial law literature contains a somewhat traditional story about the efficient incorporation of trade usage into commercial contracts, . . . Commercial parties, unable to specify every contingency with precision, can reduce transactions costs by incorporating default rules into their contracts; total contracting costs are minimized to the extent that those defaults reflect risk allocations that most parties would have adopted had they negotiated explicitly about the term,” and suggesting that “usages of trade. . .provide an alternative source of majoritarian defaults” that may be desirable for any of a number of reasons among them the fact that the application of even nonperfectly efficient custom “does serve the function of reducing the costs of contracting.”). See also, Steven Shavell, On the Writing and the Interpretation of Contracts, 22 J. Law, Econ. & Org. 289 (putting forth a specification cost saving justification for an approach to contractual interpretation that includes looking to usage based on a stylized model of contracting that does not take into account error costs or the ability of parties to engage in strategic behavior.).

8 Steven Walt, State of the Debate, at 274 (“A finding of a business norm requires some objective evidence; a pattern of behavior in the relevant trade.”)
Usage in the Courts

adjudication to the areas of contracting where it is likely to create the greatest benefits.

Part I explores the statutory framework and commonly articulated evidentiary standards for incorporating trade usages into commercial agreements. Part II presents the study of usage in the courts and discusses the limitations of the study’s methodology. Part III draws on the study’s findings to reevaluate the theoretical justifications for the claim that the incorporation strategy is likely to decrease specification costs without unduly increasing interpretive error costs. Part IV discusses the ways that the incorporation of trade usage affects motions for summary judgment and suggests that it might encourage strategic behavior. Part V identifies the areas of contract adjudication where incorporation is likely to create the largest benefits, identifies several small changes that could improve the operation of the strategy, and explores the desirability of moving the background rules of American commercial law in a more formalist direction for merchant-to-merchant transactions. Part VI concludes by identifying additional issues that need to be empirically resolved before the desirability of incorporation can be definitively assessed.

I. THE DOCTRINAL FRAMEWORK

Articles 1 and 2 of the Uniform Commercial Code and their Official Comments require or permit courts to make frequent recourse to usages of trade in deciding contract disputes. A usage is defined as “any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question.”9 Usages are considered part of the transactors’ legally enforceable agreement.10 The comments explain that “writings are to be read on the assumption that . . . usages of trade were taken for granted when the document was phrased.”11 Among other things, usages may also be looked to in an effort to interpret contract terms; fill contractual gaps; determine the reasonable time for the taking of an action when

---

9 UCC 1-205(2).
10 UCC 1-201(3) (defining “Agreement” as the “bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance.”).
11 UCC 2-202 cmt 2.
the written contract is silent;\(^\text{12}\) determine if a contract or a contract provision is unconscionable;\(^\text{13}\) define the contours of the actions that can be taken by a party given an option to act at his discretion;\(^\text{14}\) define the meaning of commercial unit;\(^\text{15}\) determine when it is reasonable to conclude that the tender of nonconforming goods with a price adjustment will be acceptable;\(^\text{16}\) create or exclude implied warranties;\(^\text{17}\) exclude consequential damages;\(^\text{18}\) define conforming tender;\(^\text{19}\) and flesh out the contours of the implied warranty of merchantability.\(^\text{20}\) Usages are also relevant to discerning the terms of a contract concluded under UCC 2-207(3) and to determining which so-called “different” or “additional terms” in a battle-of-the-forms situation are included in a contract formed under UCC 2-207(2)(b).\(^\text{21}\)

Usage is also at the heart of the Code’s non-waiveable duties of “reasonableness” and “good faith between merchants,” which includes “the observance of reasonable commercial standards of fair dealing in the trade.”\(^\text{22}\) Usages of trade are not considered parol evidence. It is therefore unnecessary to demonstrate an ambiguity in a contract’s written terms before usage evidence can be properly introduced.\(^\text{23}\)

\(\text{12}\) UCC 2-309 cmt 1 (noting that the “criteria as to reasonable time,” depend upon, among other things, commercial standards, and that an agreement to a “definite time” may be implied by usage of trade.”)

\(\text{13}\) See e.g. Adcock v. Ramtreat Metal Tech., Inc., 44 UCC Rep. Serv. 2d 1026, 1032[unpublished] (2001) (“A party defending a limitation of liability clause may prove it is conscionable regardless of the surrounding circumstances if the general commercial setting indicates a prior course of dealing or reasonable usage of trade as to the exclusionary clause.”)

\(\text{14}\) See UCC

\(\text{15}\) See UCC

\(\text{16}\) See UCC 2-508 (2) cmt 2 (noting that in determining whether the seller has “reasonable grounds to believe,” that non-conforming goods would be acceptable with a price adjustment, reasonable grounds can be found in “usage of trade.”).

\(\text{17}\) See U.C.C. 2-316 (3)(c) (“[A]n implied warranty can also be excluded or modified by . . . usage of trade.”).

\(\text{18}\) See UCC

\(\text{19}\) See UCC

\(\text{20}\) See UCC

\(\text{21}\) Different or additional terms that are in accord with usages and that do not cause unfair surprise or hardship become part of the parties’ contract because they are not considered “material alterations” of their agreement

\(\text{22}\) See UCC

\(\text{23}\) See UCC 2-202 cmt 1(“This section definitely rejects . . . The requirement that a condition precedent to the admissibility of the type of evidence specified in
The Code sets out a hierarchy of authority that gives express terms priority over inconsistent usages of trade. In practice, however, courts rarely give effect to express terms over an adequately demonstrated trade usage. A usage is generally found to be “consistent” with a contrary express term unless the usage is deemed to “totally negate” the express term. This very rarely happens. As one court observed, “the trend has been for judges, looking beyond written contract terms to reach the ‘true understanding’ of the parties, to extend themselves to reconcile trade usage and course of dealing with seemingly contradictory express terms. They have permitted course of dealing and usage of trade to add terms, cut down or subtract terms, or lend special meaning to contract language.”

The usage component of the incorporation strategy is not a pure default rule. The Official Comments note that particular usages may be excluded from consideration if they are “carefully negated.” However, simply including a clear clause covering a paragraph (a) is an original determination by the court that the language used is ambiguous.

See U.C.C. 1-205(4) (“The express terms of an agreement and an applicable course of dealing and usage of trade shall be construed wherever reasonable as consistent with each other; but when such construction is unreasonable express terms control both course of dealing and usage of trade and course of dealing controls usage of trade.”); id. 2-208(2) (“Express terms shall control course of performance and course of performance shall control both course of dealing and usage of trade.”).

See e.g., Campbell Farms v. Wald, 578 NW2d 96 (1998) (“In cases governed by the Uniform Commercial Code, the courts have regarded the established practices and usages within a particular trade or industry as a more reliable indicator of the true intentions of the parties than the sometimes imperfect and often incomplete language of the written contract. The court have allowed such extrinsic evidence to modify the apparent agreement, as seen in the written terms, so long as it does not totally negate it.”)

American Machine v. Strite Anderson, [inset string cite].

UCC 2-202 cmt ___. Quinn, a leading form book, suggests that to exclude a usage, transactors should include a version of the following clause for each usage they wish to exclude: “Specific Trade Usages Negated This Contract was written with the understanding that the following usage of the trade would not affect the content, interpretation or performance of this Contract and is hereby expressly excluded. The trade usage excluded would normally require [Describe normal effect.] In substitution, the parties have agreed to the following [Describe alternate procedures or allocation of rights adopted].” Form 4, p 1-28. In addition, to the extent that incorporationists are correct that the strategy permits transactors to
subject is insufficient to negate inconsistent usages. The enforceability and effectiveness of a general clause opting out of all trade usages is at best unclear.28 Such a clause might keep some usages out. However, given the central role usage plays, not only in the Code’s overall jurisprudence, but also in defining the contours of the non-waiveable duties of good faith and reasonableness,29 it is unlikely that the influence of trade usage on contract interpretation

contract with reference to “specialized or context specific terms [that] carry with them an array of implications that might be difficult even to bring to mind let alone commit to paper” see infra text accompanying notes. These usages become, in effect, mandatory terms across the relevant vocation or trade.

28 See LEXSTAT 5-1 FORMS & PROCEDURES UNDER THE UCC P 21.06: Forms and Procedures under the UCC (Matthew Bender & Company, 2010) (“The structure of Section 2-202 appears to allow the admission of course of dealing, course of performance and trade usage even when a merger clause is effective to totally integrate the agreement. Indeed, some doubt exists of the ability of the parties to exclude parol evidence of a course of dealing, usage of the trade or course of performance.”); David V. Snyder, Language and Formalities in Commercial Contracts: A Defense of Custom and Conduct, 54 S.M.U L. Rev. 617, at 635-36 (2001) (“As custom and conduct are part of the agreement not only by the fiat of the UCC definition but also as a practical matter, the parties will have a rough time banishing them generally.”) Although there were no cases in the study in which courts either upheld or negated a clause attempting to opt of usage, some courts have mentioned the absence of such as an additional justification for giving great weight to usage evidence, See e.g., Columbia Nitrogen v. Royster. In one case, the court found that the Code did not apply, but noted in dicta that if the Code applied, it would have enforced a provision in the contract which stated that “No terms, conditions, prior course of dealings, course of performance, usage of trade, understandings, purchase orders, or agreement purporting to modify, vary, supplement or explain any provision of this Agreement shall be effective unless in writing, signed by representatives of both parties” Madison Ind. v. Eastman Kodak Co, 13 UCC Rep. Serv. 2d 325 (1990). In another case, a clause excluding usages was included in the written contract, but did not even merit mention in the court’s opinion. See e.g., Leighton v. Valley Steel, 41 UCC Rep Serv 2d 1128 (denying the plaintiff’s motion for summary judgment and explaining that “whether usage of trade in the pipe industry excluded the implied warranty of merchantability is a genuine issue of material fact,” despite both a standard integration clause and a clause in the contract stating that “no course of prior dealing between the parties and no usage of the trade shall be relevant to supplement or explain any term used in this agreement.”).

29 Although the Code does permit transactors to particularize the “standards by which the performance of such obligations [of good faith and reasonableness] is to be measured,” their ability to do so is constrained by the requirement that such attempts at particularization must not be “manifestly unreasonable,” a concept that is also given content, at least in part, by reference to usages of trade. See UCC[].
can be completely excluded. In practice, the usage component of the incorporation strategy lies somewhere between a pure mandatory rule and a pure default rule.

Despite the importance of the concept of trade usage to determining the scope and meaning of sales transactions governed by Article 2, the Code provides little guidance on how the “existence and scope” of usages are to be proven. It requires only that a party seeking to introduce usage evidence give the other party notice\footnote{UCC 1-205(6) (“Evidence of a relevant usage of trade offered by one party is not admissible unless and until he has given the other party such notice as the court finds sufficient to prevent unfair surprise to the latter.”)} and that “the existence and scope of . . . a usage are to be proved as facts.”\footnote{UCC 1-205(2).} The Official Comments provide some elaboration. They explicitly reject the strict English and common law standards for establishing the existence of a custom, create a presumption that usages that are commercially accepted are reasonable, and make the question of whether an extant usage has been incorporated one for the trier of fact.\footnote{UCC 1-205 cmt 9.} The comments also note that “[i]n cases of a well established line of usage . . . where the precise amount of the variation has not been worked out into a single standard the party relying on the usage is entitled, in any event, to the minimum variation demonstrated.”\footnote{UCC 1-205 cmt 9.} The Code and the Comments are both silent on the question of who has the burden of proving the existence and scope of a usage. However, the leading Code treatise and the case law suggest that the burden of proof rests, at least in the gap filling and interpretation contexts, on the party attempting to prove the usage exists.\footnote{See White and Summers, supra note _ at 128 n. 42 (“Generally the party who asserts the existence of a trade usage or the like and benefits from its proof has the burden of proving it.”) In some UCC 2-207(b) cases, if the additional term in an acceptance is not the type of term that the comments designate as a per se material alteration, a party who wants to exclude the term bears the burden of proving that it was a “material alteration.” However, in practice, it was the party arguing for the inclusion of the term who most often offered this evidence.}

Drawing on these statutory requirements, incorporation’s defenders (“Incorporationists”) have developed a fairly well-articulated view of the type and quantum of “objective” evidence that they assume will be submitted to establish the existence, scope,
and content of a usage. They maintain that “[u]nder Article 2, there are two principal methods of demonstrating the existence of an observable regularity of conduct,” namely “expert testimony and evidence about statistical regularity.” They surmise that “much of the evidence of commercial norms might consist simply in the presentation of evidence of statistic norms—mere frequencies of a given behavior in the trade.” The leading Code treatise takes the position that “to prove [a usage of trade], a party must usually call on an expert.” A leading practice manual presumes the same.

Despite their legal realist roots incorporation’s defenders have never explored the types of trade usage issues that arise in the real world or the ways that trade usages are actually established in court. Rather, they have been content to assume that transactors have been taking advantage of the specification cost savings the strategy affords by including large numbers of vague and standard-like clauses in their contracts and that courts and juries are following the directives of the Code as written. As a leading Code commentator put it, “without a thorough analysis of a large group of cases, why should we believe that courts are systematically ignoring or misapplying these clear and direct commands?”

In an effort to take up the challenge of looking at just such a large group of cases the next section presents the results of a study of the digested cases decided between 1970 and 2007 in which a trade

35 Kraus & Walt, In Defense, supra note __ at 213.
37 White and Summers, Treatise, supra note __ at 140. See also, E. Allen Farnsworth, Contracts, at 41 (Under the UCC, “[a] party commonly shows a usage by producing expert witnesses who are familiar with the activity or place in which the usage is observed.”).
38 See Travailo, Nordstrom on Sales & Leases of Goods, para 3.14[c] at 244 (“[P]resumably expert testimony will be necessary to establish a trade usage”).
39 See infra notes __ and accompanying text (noting that the incorporationists assume without any empirical data that the core terms of most commercial contracts are vague and standard like which indicates to them that transactors are taking advantage of the potential specification cost savings the strategy makes available and that in so doing they are signaling to courts a desire to have their agreements given their customary meaning.)
Usage argument was raised in an Article 2 sales dispute. Its goal is to provide data that can be used to revisit the claim that the incorporation strategy decreases specification costs without creating a large increase in interpretive error costs.

II. USAGE IN THE COURTS

In an effort to explore how the trade usage provision operates in practice, a data set of cases was constructed. It consists of information about all of the sale of goods cases decided between 1970 and 2007 that are digested in Callahan’s UCC Digest under the relevant sections of the Code’s trade usage provision. The cases were coded to explore the types of situations where trade usage arguments are made, the type and quantum of usage evidence that parties introduced, and the type and amount of evidence that was required to establish the existence of a usage at trial or to defeat a

---

41 The study looked at the digested cases rather than a random sample of the cases produced through a database search for two reasons. First, such a search returns over 3,000 results. Second, many of these results involve mentions of the phrases “usage of trade” or “trade usage” merely incidentally when quoting various Code provisions, so discretion would have to be exercised with respect to deciding what is and is not a real trade usage case. As a consequence the relatively small number of cases in the study does not necessarily mean that trade-usage issues are infrequent.

42 The cases were drawn from the UCC Case Digest (formerly Callahan’s now West) under the para.1205 “Course of Dealing and Usage of Trade,” omitting 1205.1(6) “As to security interests;” 1205.1(10) “As to acceleration;” 1-205.1 (11) “As to Ownership or Title” 1-205.1 (12) “As to banking practices;” 1205.2(3)-(7) “Bank Transactions;” 1205.3 (all) “Course of dealing;” 1205.4(1)(b) “Course of Dealing;” 1205.4(3)(a) “motor vehicles course of dealing;” 1205.4(7)(a)-(c) “Banking;” 1205.4(8)(b) “Clothing and fabric: Course of Dealing;” 1205.4(9)(b) “Construction materials: Course of Dealing;” 1205.4 (11) “Security interests;” 1205.4(12)(b) “Other: Course of dealing;” 1205.5 (1)(b) “Express terms of agreement control: Course of dealing;” 1205.5(1)(d) “Express terms of agreement control: Course of performance;” 1205.5(3)(b) “Machinery and equipment: Course of Dealing;” 1-205(4)(a)-(c) “Security agreements;” 1-205(5) (a)-(b) “Banking and lending;” 1205.6(2) (all) “Course of dealing;” 1205.8 (all). Of the cases in these sections of the digest were omitted for reasons noted individually in Appendix A. The most common reasons for exclusion were that the case did not deal with sales, that the case either made no mention of usage, or the court, in remanding or ruling, simply mentioned usage or the possibility of introducing usage evidence in passing. Individual cases dealing with warranty of title were also omitted regardless of where in the digest they appeared. About ten cases remain to be coded and full files for six cases have just arrived and have not been incorporated in the database used to produce these numbers.
motion for summary judgment.

To obtain detailed information about as many of the 180 cases as possible, a letter was sent to at least one attorney involved in each case. The letter asked for case documents relevant to the trade usage issues. The documents obtained were supplemented with case documents downloaded from Lexis and Westlaw. Additional information was also obtained from court files where this could be done at a cost under $150 per case.

Using these methods of data collection, a significant portion of the trade usage-related litigation record was obtained for 58 cases (the “detail group”). Another group of 44 cases (the “opinion-only group”) was coded using information gleaned solely from opinions available on Lexis and Westlaw. The remaining 67 cases in the digest were ones in which the opinion did not discuss the types of usage evidence that were introduced. These cases were coded separately and only to determine the type of trade usage issue they involved (the “issue only group”).

---

43 The number of cases in the digest seems strikingly small in light of the Code’s pervasive reliance on trade usage. The reasons for this are unclear. It might be that trade usage plays only a minor role in Article 2 commercial disputes (perhaps because lawyer’s consulting treatises and form books would be told that they cannot prove a usage without an expert witness). Alternatively, the small number of published decisions may be due to the fact that the postures of cases where usage issues are likely to arise, are unlikely to result in published opinions. For example, cases that pit one asserted usage against another, or cases where one party introduces evidence to prove and the other party introduces evidence to disprove, a usage are unlikely to result in written state trial court published opinion (as these are rare) or an appeal since they turn on factual findings that are unlikely to be reversed on appeal.

44 There were some cases in which the lawyers could not be located in Martindale-Hubble.

45 There were several cases where the case file turned out to be more expensive either because court personnel misestimated the cost, or because additional documents relevant to the issue had to be requested.

46 For a list of cases included in the “detail group” and the documents obtained and reviewed for each see Appendix B.

47 Cases were included in the “opinion-only” group where the opinion made explicit reference to the type of usage information introduced. In order to rule out the possibility that cases in this group underreported trade usage evidence a two sided Fischer’s exact test was run comparing the frequency with which key types of evidence appeared in the “opinion only” and “detail” groups. It found no statistically significant differences between them. See infra notes__ (reporting the p values for particular types of data).

48 Data from the “issue only group,” were included in the analysis only to
A. Case Characteristics

The cases in the study came from a variety of industries. With the exception of disputes over the extent of warranties, warranty limitations, several cases dealing with descriptions of animals’ breeding capacity, and limitations of remedies in seed and agricultural chemical transactions, there were no claims about the substance of a particular usage that appeared with any frequency across the cases studied.

Across the “detail” and “opinion only” groups [hereinafter the “Study Group”], __% of the cases were in federal court (of these _ were trial court decisions and _appeals) and __% in state court (of these _ were trial court decisions and _appeals). [Additional descriptive statistics such as the amounts at stake and whether the contracting relationships between the parties were discrete or repeat will be included here.49 ]

Across the Study Group 61% of the cases involved trials or appeals from a trial judgment, 30% motions for summary judgment, 4% motions to stay or compel arbitration and 3% other procedural postures.50

B. The Types of Issues That Arose

The study sought to identify the type of issue the usage was introduced to address.

Across the Study Group 6.7% of the cases involved gap filling.51
determine whether there were any statistically significant differences between the types of cases in this group and the types of cases in the “detail” and “opinion only” groups, in terms of the issue to which the usage or alleged usage was addressed.

49 Across the twenty-two cases in the detail group that went to trial on a usage-related interpretation issue, at least 58% (14) involved transactors who had dealt with one another before. Of these 14, cases a large price movement in the relevant market seemed to have precipitated the dispute in at least nine of them.


51 A case was coded as involving gap-filling if the written contract in question was silent on the issue the usage purported to cover. Technically, under the Code, usages are part of the transactors’ legally enforceable agreement so the
50% involved interpretation, 13.3% involved warranties, 15.6% involved limitations of remedies, 9% involved formation, and the rest involved other issues. There were no cases dealing with remote contingencies.\textsuperscript{52}

\begin{center}
\begin{tabular}{|c|c|c|c|c|}
\hline
 & FORMATION & GAP FILL & INTERPRETATION & WARRANTIES & LIMITATION REMEDY \\
\hline
\textbf{Most Common Types of Usage Issues} & & & & & \\
\hline
\end{tabular}
\end{center}

[The types of issues that arose will be further broken down here. Among other things the data will demonstrate that in almost all of the cases in the Study Group, the usage at issue related to a core or routine aspect of trade such as price, quantity, quality, payment, warranty, acceptance, rejection, delivery terms or limitations of damages]

[The interpretation cases will be broken down further to determine whether the usage was offered to give meaning to a written term (and whether that term was detailed or vague), to imply a condition precedent or a condition subsequent to the operation of a clear provision, to define an industry term of art that would have been difficult or complex to memorialize in a written provision, or to suggest that a clause should be applied more flexibly than its language dictates. This section will also provide data about the proportion of contracts that were standard form (and whether the controversy related to boilerplate or specifically negotiated terms) or detailed, and the proportion that were relatively vague and nomenclature of referring to a gap filled by a usage is inconsistent with the jurisprudential foundation of the Code.\textsuperscript{52}

\textsuperscript{52}The study defined a remote contingency as a low probability event that did not relate to the core terms of the deal.
informal. Preliminary coding suggests that most of the contracts involved in interpretation disputes were very detailed, and the clauses the usages sought to interpret were not standard-like but rather quite specific.

**Plaintiff and Defendant Behavior** [This section will eventually report whether or not there are meaningful differences in the behavior of plaintiffs and defendants with respect to the types of usage related issues they raise in litigation. For example, one marked difference is that in cases where the Plaintiff raised the trade usage issue, only 3% involved warranties and limitation of remedies, whereas in cases where the defendant raised the usage issue these subjects accounted for 45% of the cases. [the discussion here will continue]

C. The Types of Evidence Introduced

The chart below provides the percentage of cases in the Study Group in which the following types of evidence were introduced: testimony of plaintiffs or their employees, testimony of defendants or their employees, non-party testimony offered by defendant, non-party testimony offered by plaintiff and trade codes.

![Types of Evidence Introduced in Usage Related Disputes](chart.png)

These findings are broken down further in the discussion that follows.

**Party or Party Employee Evidence** Across the Study Group, the most common type of usage evidence introduced (or that was sought to be introduced) was the testimony of a party or a party’s own
Plaintiffs and/or their employees ("plaintiffs") testified or gave affidavits in 50.5% of the cases, while defendants and/or their employees ("defendants") did so in 48.5% of the cases. In 54% of these cases, this was the only type of usage evidence introduced.

Looking only at the cases where a trial was held, plaintiffs testified in 58.9% of the cases, while defendants did so in 46.6% of the cases. In 50% of these cases this type of party and party-employee witness testimony was the only type of evidence introduced on the usage issue.

Moreover, even in cases where a trial was held and a usage was found to exist, party testimony was the only usage-related evidence introduced in 52.6% of the cases. In 16.7 percent of these cases, however, the court found that a course of dealing or course of performance supported its finding on the usage issue.

**Non-party Witness Evidence** The study sought to examine how often expert testimony was introduced, the extent to which the introduction of this testimony was necessary to establish the existence of a usage, and the impact that such testimony had on the likelihood that a usage would be found to exist. However, even in cases for which full transcripts were available, it was often impossible to determine whether a particular witness was a fact witness, a lay opinion witness, or an expert witness. Given this limitation, all non-party or party-employed witnesses were coded together as non-party witnesses.

Across the Study Group, 20% of plaintiffs and 23.2% of defendants introduced nonparty testimony. Even in cases in which a trial was held and a usage was found to exist, plaintiffs introduced non-party witnesses only 16.2% of the time, while defendants did so...
28.2% of the time.\(^{57}\) Since only some of the nonparty witnesses would have qualified as experts, this data permits the conclusion that the introduction of non-party expert witness testimony is not required to establish the existence of a usage.\(^{58}\) The data cannot, however, be used to determine how often the testimony of party, or party-employed, expert witnesses was introduced.\(^{59}\)

**Trade Codes and Similar Writings** Parties attempted to introduce Trade Codes and other trade association publications in 11% of the cases. This type of evidence was admitted at trial in five cases; a usage was found to exist in three of these. The number of cases is, however, too small to make reliable inferences about the weight courts attribute to this kind of evidence.

**Regularity of Observance** The Code states that to be a “usage” a practice must be regularly observed. In most cases where a usage was found to exist, this doctrinal requirement was met (to the extent that it was addressed at all) by a mere assertion by a witness that a practice was common or that they had never seen things done differently. Across the gap filling and interpretation cases in the Study Group, there was not a single instance of a party trying to prove “regularity of observance” using statistical data about the frequency with which a practice is observed. Rather, the witness affidavits, testimony, and/or depositions, which were obtained for __witnesses across the cases studied in depth, reveal that to the extent the question of frequency is addressed at all, the person providing the evidence simply states that X is the practice of his firm and others he knows of, that X is widely followed, that X is a custom or usage of trade, or that he does not know anyone who does not do X.\(^{60}\) Even in the cases with the largest stakes, the best lawyers, and

\(^{57}\) In the cases that went to trial there was no statistically significant difference between the opinion only and the detail group (using a two sided Fishers exact test) in the rate at which either plaintiffs (p=.18) or defendants (p=.36) introduced non-party witness testimony.

\(^{58}\) However, the inability to distinguish expert witnesses from lay opinion witnesses makes it impossible to establish whether or not expert testimony, when introduced in a particular case, was or was not treated as conclusive by courts.

\(^{59}\) See infra notes _-_-and accompanying text discussing the reasons (apart from their incentive to lie) that the testimony of party employed experts as to trade usages should be viewed with skepticism.

\(^{60}\) In order to get a feel for the types of evidence that courts accept as fulfilling the statutory requirement that the usage be regularly observed, consider the testimony that was actually introduced in the following cases where a trial was
the testimony of witnesses with traditional expert qualifications, proof of statistical regularity was still a matter of assertion and opinion.

The only types of cases in which parties introduced evidence that the claimed usage had actually been observed in any specific transactions, were battle-of-the-forms cases. In six out of ___ of these cases, the party seeking to have an additional term in its acceptance included in a contract introduced a few contracts drafted by others in their industry in an effort to establish that there were at least some specific instances where similar written terms were used. There were, however, no cases where the proffered evidence came close to establishing the frequency with which the practice was observed in a place, vocation, or trade.

**Plaintiff and Defendant Behavior (Regarding Evidence)** [This section may eventually report whether or not there are meaningful differences in the behavior of plaintiffs and defendants with respect to the type and amount of usage evidence offered. A preliminary exploration of this question suggests that any differences that exist are slight.]

held and the court found the claimed usage to exist. In Spurgeon v. Jamison Motors, 521 P.2d 924 (1974) two of the defendant’s employees testified as to the usage of the used farm machinery trade. Ingeman Svendson, testified that he had worked with farm machinery for 40 years, and when asked whether it was customary to warrant used combines, he said “no.” That was the extent of his testimony on the scope of the usage. Spurgeon v. Jamison Motors, Transcript of Testimony, C.A. No. 6985 p. 41. Keith Jamison also testified to Jamison Motor’s policy of sharing repair costs 50-50 on newer used models and providing no additional warranties. He was then asked if this was “pretty much standard throughout the business in your trade,” and he replied that it was. Id. at 79.

61 M.A. Mortenson Co., Inc. v. Timberline Software, 37 UCC Rep. Serv. 2d 892 (1999); 998 P.2d 305 (2000) (where in a high profile case that attracted an amicus brief from the ___because it had huge potential ramifications for the software industry, the defendant introduced fifteen “true copies of personal software license agreements from 15 well known software developers,” that included the provision it claimed was a usage).

62 Across the detail and opinion-only groups, plaintiffs raised the trade usage issue in 42% of the cases and defendants raised it in 58% of the cases. Looking only at the cases that went all the way to trial, plaintiffs raised the issue 46.1% of the time and defendants 53.6% of the time. Plaintiffs succeeded in establishing the existence of a usage in 76% of the cases in which they raised the usage issue and defendants did so in 72% of the cases in which they raised the usage issue. In the cases where plaintiffs established the existence of the usage, they introduced
D. Case Outcomes

Trial  Across the Study Group, 58 cases went to trial on a usage issue. Courts/juries found usages to exist in 75% of them. In the 19.4% of cases that went to trial, and in which both sides introduced some usage-related evidence, a usage was found to exist 53.8% of the time. In cases that went to trial in which only one side introduced usage-related evidence, a usage was found to exist 80% of the time.

[Additional data on how the use of non-party witnesses affected outcomes will be reported here] Plaintiffs and defendants both introduced nonparty witness testimony in only 10% (10) of these cases. A usage was found to exist in only two. One was the casebook classic Columbia Nitrogen v. Royster.

Summary Judgment  Across the Study Group, 30% the cases involved motions for summary judgment on a usage-related issue. In 65% of these cases (seventeen cases), the usage argument was raised by the non-movant in an effort to defeat the motion. This tactic was successful 70.6% of the time. In the other 34% of the cases (nine cases), the movant asserted the existence of a usage and was granted summary judgment on the usage-related issue 88.9% of the time.

In 83.3% of the cases where a usage argument defeated a motion for summary judgment, the only evidence of the usage introduced nonparty witness testimony 30% of the time (defendants also introduced such evidence in 12% of these cases). In contrast, in cases where defendants established the existence of a usage, they introduced nonparty witness testimony 40% of the time (plaintiffs also introduced such evidence in 13% of the these cases).

In most jurisdictions a denial of summary judgment is not a final order and is hence not appealable. As a consequence, these decisions are less likely to show up in digested opinions. It is therefore not possible to know how frequently usage arguments are used to defeat motions for summary judgment. In addition, although courts sometimes publish opinions on this issue, there is no data available on the frequency of this practice.

Or, looked at from a different perspective, on motions for summary judgment plaintiffs raised the usage issue 28.6% of the time, while defendants did so 71.4% of the time.

37% of these cases were at the trial level and 62.5% at the appellate level.

In the five cases where a usage argument did not defeat a motion for summary judgment, the non-movant introduced only its own or its employees testimony in three of the cases. In one of these cases, the court explicitly noted the inappropriateness of relying on testimony of a party or a party’s employees to defeat a motion for summary judgment, see CoreStar v. LPB (__) In the remaining two cases, the parties sought to introduce additional types of evidence but the court excluded the evidence. See Golden Peanut v. Hunt 18 UCC Rep. Serv. 2d. 26
by the non-movant was an affidavit of one of its employees.\textsuperscript{67} This strongly suggests that courts do not, as a doctrinal matter, require the party asserting a usage to defeat a motion for summary judgment, to produce a great deal of evidence supporting their claim.\textsuperscript{68}

In cases where the party moving for summary judgment introduced a usage argument in support of its claim, summary judgment on the usage issue was granted 88.9\% of the time (eight cases). However, it is not possible to determine from these cases the type or amount usage evidence that courts require to grant summary judgment on a usage related issue. In 75\% of the cases where the motion was granted (six of eight cases), the usage-related issue was whether or not an additional \textit{written} term in a variant acceptance was customary in the relevant industry.\textsuperscript{69} In all of these

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{67} Insert a footnote with information from the eight detail cases where the motion was defeated giving a sense of just how cursory the assertions in the party employee affidavits were on the usage issue.
\item \textsuperscript{68} 50\% were primary court decisions and 50\% were appeals from a grant of summary judgment or a denial of summary judgment (one case on interlocutory appeal by leave of court).
\item \textsuperscript{69} See \textit{Bayway v. OMI}, 215 F. 3d 219 (2000) (where the movant-plaintiff introduced the testimony of two expert witnesses, and five industry contracts containing the disputed clause); \textit{MA Mortenson v. Timberline}, 970 P.2d 1228 (1999)(where the defendant movant introduced two expert witnesses and copies of personal software license agreements from 15 well known software suppliers); \textit{Gooch v. El Dupont De Nemours}, 40 F. Supp 2d. 863 (1999) (where movant-defendant introduced the deposition of the plaintiff’s employee which included eleven other herbicide contracts for products he purchased which also included the clause at issue and the court noted that similar clauses had been upheld in other agricultural chemical cases); \textit{Stirin v. El Dupont De Nemours}, 21 UCC Rep. Serv. 2d. 979 (1993) (where movant-defendant, albeit as an attachment to an employee’s affidavit introduced six labels from other chemical products some produced by DuPont and some by others, with a similar limitation of remedy clause); \textit{Suzy Philips v. Coville}, 939 F Supp 1012 (1996) Aff’d 1997 US App. Lexis (1997) (where the movant-defendant introduced the Worth Street Textile Rules to argue that a limitation of remedy clause in an acceptance was not a material alteration as it was standard in the textile industry and had been included in}
\end{enumerate}
\end{footnotesize}
cases the movant introduced evidence other than party and party employee testimony and the non-movant opposed the evidence only with legal arguments. In the remaining two cases, the court granted summary judgment based solely on the testimony of the parties or their employees. In neither of these cases did the party opposing the motion introduce any usage evidence of its own.  

There were only two cases where the parties presented conflicting evidence of usage. The court denied summary judgment in both of them.  

In sum, while Code commentators and academics have long expressed concern that courts might impose too high a requirement for establishing a trade usage, “for it is likely to be confused with ‘custom’ and the law has long encumbered proof of custom with stringent requirements,” precisely the opposite seems to be the case.

E. Methodological Issues and Limitations of the Study

The picture of the role played by usage in contract disputes that emerges from the study has certain limitations. Most importantly, it does not give us any direct information about how, if at all, the prospect that courts will apply the incorporation strategy influences primary contracting and dispute-related behavior—that is, the types of provisions transactors will include in their contracts and the ways they will behave when disagreements arise over their respective rights and duties. Indeed, it does not even tell us whether the law in fact influences behavior in its shadow, as there are many

---

70 Graaf v. Bakker Bros. 934 P.2d 1228 (1997) (where the court granted the defendant’s motion for summary judgment, finding the usage it asserted to exist, based only on an affidavit supplied by one of its employees); B/R Carpet Sales Inc. v. Krantor Corp., 226 AD2d 328 (1996) (where the court granted summary judgment for the plaintiff, finding that the defendant had not rejected the goods within a reasonable time, which the plaintiff’s employee testified was 48 hours under a usage of the trade)


72 White and Summers 3-3 at 127 3rd ed. Hornbook student series.
other considerations that might influence contracting behavior whose importance cannot be assessed on the basis of this data alone. The study is also limited in its ability to paint a complete picture of the evidence of usage that is introduced across all of the trials where a usage issue is raised, because the cases in the digest are disproportionately appeals relative to the underlying population of cases of real interest.

The findings may also have been influenced by the two types of selection effects that typically characterize case-based research that relies on cases decided by reported judicial opinions. In comparison to the entire population of cases that wind up in court, cases decided with a reported opinion tend to be disproportionately in Federal court (trial or appellate), one of the rare state trial court decisions memorialized in a published opinion, or a state cases that involved an appeal of some sort that resulted in a published decision. Given the origin of the data, a selection effect of the classic Priest-Klein\(^73\) variety may have introduced bias into some of the results relating to the types and quantum of evidence introduced. As a consequence, the study cannot rule out the possibility that more or different trade usage evidence was introduced in the cases that were decided without an opinion.

There are, however, several considerations that suggest that the selection effect problem does not entirely undermine the study’s findings. First, across the appellate cases in the Study Group, the usage-related issue was the only issue appealed in only 12.2% of the cases. In the remaining cases that were appealed, 20.4% involved 2 issues, 28.6% involved 3 issues, and 38.7% involved 4 or more issues.\(^74\) These data suggest that any selection effect that is introduced may be quite noisy with respect to the quantum of evidence introduced. Second, only a small percentage of the cases (for reasons discussed further below) were cases where the court was faced with one party’s evidence that the usage was A and another party’s evidence that the usage was B, and had to decide between them. This is classic situation in which the Priest-Klein selection effect with respect to the strength and quantum of evidence


\(^74\) These data are preliminary as they are based on a random sample of half of the appeals filed.
introduced would be the greatest. Rather, in approximately 75% of the cases in the Study Group, one party submitted evidence of usage while the other party claimed that the usage was inadmissible based on a legal argument other than that the evidence submitted was insufficient to meet the burden of proof. In these cases, there is no reason to think that a selection effect is operating to make cases with weaker evidence go to appeal. In fact, for cases in some postures, the selection effect might well lead to a bias in favor of cases with stronger evidence of usage making it into the published reports.75

The study’s results about the types of issues (gap filling, warranty, etc) that arise may also have been affected by a factual issue-based selection effect. This effect arises because cases that go to

75 To see why consider the following four situations: (1) Suppose that at trial the plaintiff seeks to introduce a usage, and the defendant seeks to exclude it. Suppose that the court admits the usage and it is found to exist and the plaintiff prevails, and the defendant is deciding whether to appeal. His decision will be based on his estimate of the strength of his legal argument on appeal, not on the strength of the plaintiff’s usage evidence. If, on the other hand, the court said the evidence did not establish a usage (meaning the evidence was weak), the defendant would not be likely to appeal since the fact that it was admitted did not effect the outcome. The plaintiff in such a situation is also unlikely to appeal, because appellate courts do not ordinarily reverse factual determinations of this sort except in egregious cases; (2) Now suppose that the court excludes the plaintiff’s evidence of usage and the plaintiff must decide whether to appeal. Holding constant the strength of the plaintiff’s legal argument on appeal, the more likely it is that if he prevails and the usage evidence is admitted, it will be found to establish a usage, the more likely he is to appeal. Thus, the selection effect here should be in favor of appeals occurring more often when the plaintiff’s evidence is strong then when it is weak; (3) Suppose that at trial the defendant seeks to introduce usage evidence, the plaintiff claims that it should be excluded, and the court admits the usage. If the usage is found to exist, the plaintiff’s decision on whether to appeal will be based on his evaluation of the strength of his legal argument. If the court finds that the usage does not exist, the plaintiff wont appeal and neither will the defendant, as reversals of finding of fact are rare. Since cases where the usage is found to exist should be ones where stronger rather than weaker evidence is admitted, there is no reason to think that cases with weaker evidence are being weeded out of the sample, and in fact the reverse seems to be true; (4) Now suppose that the defendant seeks to introduce usage and the court excludes it. Holding the strength of the defendant’s legal argument constant, the stronger his usage evidence the more likely that he is to appeal, since the greater is the likelihood that if he is successful on the legal appeal and the case is remanded that it will change the outcome. In sum, in cases that arise in this posture, the selection effect, if any, inclines towards cases with stronger evidence of usage being more likely to appear in the appellate courts than cases where usages are weak.
trial and turn on factual rather than legal issues, are far less likely to be appealed given the tremendous deference given to trial courts’ findings of fact. This selection effect might account, at least in part, for the small number of cases involving gap-filling or looking to usage to interpret standard-like provisions. In these types of cases, one party will typically claim the usage is A, and the other that the usage is B, so which ever way the court rules, an appeal, and with it a reported decision, is unlikely to occur since the probability of obtaining a reversal is very low. In an effort to explore the possibility that this type of selection bias is responsible for the infrequency of these types of cases, a data set was constructed that looked at the Westlaw Court Document Data base for Illinois State and Federal Court Filings. A search of the term “usage of trade” turned up 170 hits for the years 1999-2010, a total of 104 independent cases. After excluding the types of cases that the large study excluded, and cases that merely cited statutory language referring to usage, without asserting that a usage existed or suggesting that a usage-based argument was in the offing, 24 cases remained. Of these cases, one (4.2%) involved gap filling in the context of a contract by conduct, one (4.2%) involved filling a gap in a written contract, and one (4.2%) involved making a general clause more specific. These findings echo the results of the case study in terms of the type of trade usage issues that wind up in courts. Whether or not gap-filling or giving meaning to standard-like provisions by usage is occurring in the shadow of the law in disputes that arise, but do not result in legal filings, cannot be determined.

With these methodological limitations in mind, the next sections draw on the study’s findings, to revisit the core arguments used to justify the incorporation of trade usages and other commercial practices.

---

76 The database is IL-FILING-ALL and according to Westlaw it includes “documents filed with Illinois state and federal trial courts. Documents include the following civil trial court filings: pleadings, motions, memorandum, trial briefs, non-expert depositions and discovery, non-expert affidavits, proposed orders, agreements, verdicts, settlements and other trial filings.” See: https://web2.westlaw.com/scope/default.aspx?db=IL%2DFILING%2DALL&RP=/scope/default.wl&RS=WLW11.07&VR=2.0&SV=Split&FN=_top&MT=208&MS T=

77 See supra note _
II. REVISITING INCORPORATION ON ITS OWN TERMS

The study of usage in the courts identified significant differences between the way the incorporation strategy is assumed to work in theory and the ways that it works in practice. In order to fully evaluate the merits of the strategy and assess whether it is in fact a theoretically justifiable or judicially implementable approach to contract interpretation, it is useful to revisit the arguments used to justify the strategy against the background of this empirically-grounded picture of the types of trade usage disputes that arise and the ways the existence and content of usages are established in US courts.

Although the study was designed to empirically test the interpretive error cost aspect of the incorporation debate, its findings about the types of cases that arise, the ways that courts interpret and apply the Code’s hierarchy of authority, and the ease with which parties can establish the existence of a usage, also raise questions about the validity of the assertion (which has never been supported by any empirical evidence) that the strategy is likely to reduce specification costs.

A. Specification Costs

Incorporationists set forth two primary rationales for making trade usages part of commercial agreements and drawing on them to interpret contracts. The first is that a majority of merchant transactors want their contracts to be given their customary meaning, so that incorporating usages will best effectuate their contractual intent. The second is that when transactors are confident that courts will look to trade usages to fill gaps, interpret contracts, and deal with remote contingencies, they will choose to draft less detailed agreements and thereby realize significant specification cost savings.

The only way to even begin to directly test whether transactors are taking advantage of the specification cost savings the strategy

78 See e.g., Snyder, supra note __ at , 617 (2001)[hereinafter “Language and Formalities”] (giving “an assent-based justification for constructing contracts in light of custom and conduct”); Randy Barnett, Sounds of Silence, __U. Va. L. Rev. __(suggesting that looking to custom will best effectuate the intent of the parties, thereby reinvigorating consent as an essential element of contract.); Walt, State of the Debate, supra note _ at 262 (noting that historically “[t]he debate between incorporation and formalism. . .has turned on party intent.”).
may create would be to look at a representative sample of contracts from a cross-section of industries, data that was unavailable at the
time of this study and that would, even if available, be difficult to
definitively interpret.\textsuperscript{79} However, notwithstanding the selection
effects identified in the previous section, the data in the study
provides an indirect (and somewhat inconclusive) way to begin to
shed light on whether transactors are in fact taking advantage of the
specification cost savings the strategy makes available to them.

The theory behind the incorporation strategy suggests that when
drafting contracts in the shadow of incorporation, transactors will
choose to leave more gaps in their agreements and will incline
towards including vague, standard-like provisions, that have a clear
private meaning to them (although not necessarily to a court) and
are relatively inexpensive to draft.\textsuperscript{80} Transactors may also forgo
complex written provisions in favor of terse clauses that use
industry-specific short-hand phrases to implicitly reference complex
“terms that have a domain specific meaning that have evolved to
address the particularized needs and expectations of contractors with
in a given domain.”\textsuperscript{81} Some incorporationists suggest that the
strategy may also reduce specification costs by making it possible for
transactors to contract with respect to inchoate understandings that

\textsuperscript{79} In an attempt to learn what this type of data might reveal, a letter was sent
to fifty randomly selected mid-size manufacturing firms within a 50 mile radius of
Chicago Illinois asking them to share a copy of one of their typical supply
agreements with the researcher. Not a single firm agreed to supply a contract.
However, even this type of data might not settle the question. If the data revealed
that there were lots of vague and standard-like provisions relating to core terms, it
would make plausible the incorporationists’ claims that transactors include such
provisions intending that they be given their customary meaning. However, the
presence of such provisions might be equally compatible with the explanation that
transactors think that they will have more information by the time the clause will
become relevant and that this information will help them negotiate (or renegotiate)
a better provision than they could have constructed at the time of contracting.
Similarly, if the study revealed very detailed contracting about core matters this
would not necessarily indicate that transactors wanted to reject the incorporation
strategy, as there are many reasons for memorializing obligations in writing. It
might, nonetheless, be useful to do such a study to look for evidence of
contractual fortification or provisions of the Code that parties seek to
systematically opt out of.

\textsuperscript{80} A standard-like provision is one that by its wording invites a court to give it
contextual meaning, for example, a provision that delivery should be on
customary terms, or that the widgets need to function reasonably well.

\textsuperscript{81} Kraus and Walt, \textit{In Defense}, supra note \_at \_.

reflect “specialized or context specific terms [that] carry with them an array of implications that might be difficult even to bring to mind let alone commit to paper.” As a consequence, if the prospect that trade usage would be incorporated into written agreements were leading to the types of drafting choices incorporationists anticipate, a significant number of trade usage cases should deal with gap-filling and giving meaning to standard-like and weakly-specified contractual provisions. This is not, however, what the study found. However, along this dimension the study’s results are at best suggestive, because they might be strongly affected by the factual issue selection effect identified above. In addition, the number of cases in the pilot study of filings is too small to permit strong inferences about the types of contract provisions at issue across all cases filed, much less across all contracts governed by the Code.

Across the cases in the Study Group, only 11% involved gap-filling, a finding confirmed (albeit weakly due to the small number of cases) by the pilot study of the usage issues raised in Illinois case filings. There were no cases in the detail group in which usage evidence was introduced to give meaning to a standard-like term. While cases interpreting industry terms of art or industry short-hand were common, the clauses being interpreted and the usages being introduced were of roughly equivalent complexity and would have cost approximately the same amount to include in the parties’ written agreement. Finally, while it was impossible to tell for sure whether transactors were trying to establish the existence of complex customs that could only be articulated ex-post, none of the usages alleged in any of the cases seemed as if they would have been very complex or difficult to articulate at the time of contracting. Most interpretation cases in the detail group involved usages that were

82 If courts do incorporate usages of this description, these usages are in effect mandatory rules. Because these understandings cannot, by definition, be written down, they also cannot be specifically negated in commercial agreements. See Quinn, supra note ___ at ___ (noting that a contract provision that seeks to specifically negate a usage should include a statement describing the usage to be negated).

83 See e.g. Action Time Carpet v. Midwest Carpet Brokers, 271 NW2d 36 (1978) (where the contract called for delivery to be “at once,” and the alleged usage was that this meant “as soon as possible.”); U.S. Industries v. Semco, 562 F.2d 1061 (1977) (where the contract stated that delivery was to be on an “as needed” basis and the alleged usage was that it meant “until the job was finished”) [this footnote will include all of the cases in this category so the reader may judge relative specification costs for themselves].
introduced to “interpret” a detailed or highly specific clause embedded in a detailed agreement.84

The small number cases involving gap filling or the interpretation of standard-like provisions might also be viewed as an indication that the incorporation strategy is functioning extraordinarily well. It might be enabling transactors to avoid litigation by encouraging them to look to usages to cooperatively fill gaps or and give meaning to any under-specified provisions in their agreements.85 This explanation, however, is hard to reconcile with the large number of cases where parties are arguing about the existence, content, and admissibility of usages that are alleged to be relevant to interpreting industry quality specifications like “healthy, high-quality SEW pigs”86 or industry short-hand terms relating to core terms of the contract. That is, to believe that the shadow effect of the strategy was working so perfectly, it would be necessary to explain why the customary meaning of these types of written terms that were intended to be given a customary meaning, was less clear to the parties than the customary meaning of similar types of terms that were not written down.

Given the methodological limitations of the Study, it is useful to briefly explore some additional theoretical and doctrinal reasons that the strategy may not reduce specification costs to the extent incorporations defenders expect.

Even assuming that the incorporation strategy influences transactors’ drafting decisions in the way and for the reasons that incorporationists theorize, its effect on the content of commercial contracts might be much weaker than they anticipate.

84 Here the reasons a usage was offered will be broken down as follows: to suggest that the clause be applied more flexibly (__%), or to claim that there was an usage-based pre-condition to its application (__%), or to demonstrate that there was a usage that excused its observance(__%).

85 In addition, because the situations in which usages are most likely to exist—when transactors deal with one another on a repeat basis or within a well defined market where most participants are buyers one day and sellers the next—are also the situations in which transactors who want to continue to do business with one another in the future are likely to work out any rough edges in their relationship in a cooperative manner. As a consequence, they might well fill gaps and give meaning to standard like provision without recourse to court regardless of the interpretive approach that a court would apply.

Incorporationists overlook the fact that there are many reasons, wholly apart from signaling their desired contractual meaning to a court, that transactors include detailed written provisions in their contracts. In situations where transactors are dealing with one another for the first time, they might not have much information about one another’s understanding of the content of the relevant usages.\(^{87}\) As a consequence, to know what their agreement obligates them to do, and the type of return performance they can expect, they have to incur either the cost of investigating the other party’s understanding (perhaps by discussing the meaning of core terms or unwritten expectations and/or investigating the practices in his local market), or the cost of memorializing the relevant usages in writing. Although it is difficult to predict whether the cost of investigation or the cost of drafting is likely to be higher, the cost of investigation will have to be borne every time a new contracting partner is chosen (and, unlike drafting, will not make disputes more amenable to resolution on a motion for summary judgment), but the cost of drafting provisions reflecting the relevant usages will be incurred only once. Thereafter, the provisions can be used in subsequent transactions at little or no cost. Transactors, particularly those who enter into many contracts in a single market, may therefore find it advantageous to incur the one-time cost of memorializing usages in contract provisions (which they will implicitly prorate over all the future contracts in which they anticipate their use), rather than bear the cost of investigating the usage-related knowledge of all of their future contracting partners. This saving may be particularly large for transactors who sell their goods over the internet on click-to-buy websites. In these situations sellers typically do not know the identity or location of the buyer, making it especially important to

---

\(^{87}\) Even transactors who are familiar with one another’s understanding of the relevant usages might nonetheless choose to write the usages down out of concern that, should their interests become adverse and third-party adjudication become necessary, each side would be able to introduce at least facially plausible conflicting evidence about content of the usage (which can be created merely through the introduction of an affidavit from a party or a party’s employee), thereby making summary judgment unavailable. One form book takes this a step further and advises that “if investigation reveals that there is some course of dealing or usage which is advantageous, describe it specifically in the contract, rather than rely on interpretation,” explaining that “the penalty for lack of express language may be some uncertainty as to what is or will be the trade usage, course of performance, or course of dealing.” Nimmer, supra note __2010 supp 5-44.
specify all parameters of the deal in advance. Transactors might also decide to memorialize usages in writing simply for planning purposes—that is, to clarify between themselves, and for each of their many employees who will participate in the administration of the contract—what is to be done under the contract. By clearing up any ambiguities in the content of the relevant usages, these provisions will help to ensure that their deal runs smoothly and continues to do so even in the event of a change of control or personnel. At the time of contracting, transactors tend to be focused on performance. They may therefore find it worthwhile to spend time articulating and clarifying the details of the performance they expect to receive.

In sum, the many benefits to transactors of memorializing usages in written terms together with the paucity of cases where courts are in fact called upon to fill gaps or interpret standard-like provisions, suggests that the actual specification cost savings created by the incorporation strategy may turn out to be far smaller than incorporations’ defenders claim, even when transactors want their agreement to be subject to incorporationist interpretation.

A mere failure to produce specification cost savings as large as incorporation’s defenders claim would not, standing alone, necessarily undermine the desirability of the strategy. However, incorporationists have failed to recognize that the interpretive gloss that courts have given to the Code’s hierarchy of authority (which in practice privileges usages over express terms unless doing so would result in a “total negation,” of the express term), together with the fact that usage evidence is not parol and that usages can, in practice, be proved solely through the testimony of a party or their employees, raises the prospect that the incorporation strategy may actually increase specification costs.

When transactors who want to control the meaning of their contract through express terms are drafting in the shadow of the

88 These clauses could also be included in contracts with contracting partners who are either in different trades, or located in different localities that may or may not have different usages, thereby facilitating the creation of new contracting relationships.

89 See Stewart Macaulay, Non-Contractual Relations in Business: A Preliminary Study, Am. Soc. Rev. (196_).

90 UCC 1-205(4)
incorporation strategy as it operates in practice rather than in theory, they will have to include additional detail and/or additional provisions to fortify their contract’s terms against usage-based interpretation. The cost of this fortification will be particularly high if transactors’ preferred express terms actually conflict with or differ from either actual trade usages or any usages that one or the other of them might plausibly assert if a dispute arises. As a leading form-book explains, to ensure usages cannot be used to interpret a contract, the contract should include a provision specifically setting out, negating, and replacing each usage-based interpretation that the transactors wish to exclude.

A simple example can be used to get a feel for the specification costs that might be required to fortify even a simple transaction against incorporationist interpretation. Consider a contract for the sale of two hundred tons of fertilizer with a 22% nitrogen content to be delivered FOB seller’s place of business on March 1st for a price of $X. Suppose that the price of fertilizer rose after the contract had been signed, and the seller delivered one hundred and eighty tons of fertilizer with a 16% nitrogen content on March 7th. If the buyer sued for breach of contract and these facts were undisputed, he might nevertheless be unable to prevail on a motion for summary judgment. The seller could claim there was a usage that quantities were mere estimates, or that any quantity within twenty tons of the promised amount was considered good tender under a usage of trade. The seller might also claim that although the contract called for 22% nitrogen content, there was a usage that any nitrogen percentage within eight percent of the promised amount was considered good tender. The seller could also assert that the delivery dates were mere estimates or any of a

91 The fact that courts are so wedded to interpreting even very detailed contractual provisions in light of trade usage (thereby creating a regressing to the usage effect), increases the specification costs of transactional innovation and may therefore impede the development of more efficient contract provisions and structures across a market.

92 See Quinn, supra note _ (providing template clause for opting out of a trade usage).

93 See Columbia Nitrogen v. Royster, [insert cite] Hegblade-Marguleas-Tenneco, Inc. v. Sunshine Biscuit, inc., 19 U.C.C. Rep. Serv. 1067 (1976) (where a contract for delivery of a fixed number of bushels of potatoes, was interpreted as being a contract for an estimated number of potatoes due to a usage of the potato processing industry).
number of other usages under which its late delivery would be considered acceptable. Alternatively, he might also claim that he should be given additional time to cure because the usages outlined above made it reasonable for him to conclude that the nonconforming fertilizer would be accepted with a price adjustment. Conversely, if the price of fertilizer fell, the buyer could reject a portion of the delivery claiming that the two hundred ton number was merely an estimate or an upper bound.\textsuperscript{94} She might also claim that the stated price was merely an estimate. As a consequence, transactors who wanted to ensure that this simple agreement would be given its plain meaning would have to include provisions in their writing reciting and negating all of the above mentioned usages as well as all of the usages that their contracting partner might be able to plausibly assert in the event of a dispute. Although incorporationists claim that parties do not have to take steps to protect their writing,\textsuperscript{95} in practice, transactors who want the written terms of their contract to be strictly enforced will have to incur significant specification costs to fortify their written contracts against usage based interpretation.

[The section will then explore some other arguments related to specification costs. Among other things, it will note that importing usage based analysis into the 2-207(b) battle of the forms provision, cannot save specification costs in its shadow.]

Finally, it is important to note that in incorporationist regimes, specification costs are likely to remain stable rather than decrease over time.\textsuperscript{96} As the study demonstrated, it was very rare for parties

\textsuperscript{94} Michael Schiavone & Sons v. Securalloy Co., 312 F.Supp 801 (1970) (where the contract called for the delivery of 500 tons of steel, the court permitted evidence in the form of testimony by the defendants employee that there was a usage of trade whereby a fixed quantity term in a contract, meant an amount up to that quantity, explaining that such a usage did not contradict the term, and that summary judgment was therefore inappropriate.)

\textsuperscript{95} See Hillman, supra note ___ at ___

\textsuperscript{96} Since the content of most commercial customs is determined at the trial level, and most trial courts do not routinely produce published opinions, the types of industry specific sets of usage based understandings that Llewellyn predicted would emerge over time as the Code was interpreted and applied, have not in fact been created. Scott, [insert cite] This, is, however quite fortunate, as there is no reason to believe that the first parties to litigate the content of a custom would have the incentives to introduce the optimal amount of information to a court, and a system that crystallized usages through the evolution of judicial decisions might
or courts to rely on usages established by case law precedent. This means that the content of particular usages must be established anew each time they are relevant to a particular case. In contrast, in a more plain-meaning/formalist regime, specification costs are likely to decrease over time as industry members borrow provisions memorializing usages from one another’s contracts and industry associations step up— as they did when contracts were governed by the more textualist oriented Uniform Sales Act— to provide standard form contracts, phrase books, and term books to help reduce the cost of contracting.

B. Interpretive Error Costs

The desirability of the incorporation strategy depends, in large part, on its effects on interpretive error costs. Incorporationists maintain that interpretive error costs are unlikely to be significant in relation to the strategy’s benefits because to establish the existence and scope of a usage, a party will have to introduce “objective evidence of . . . a business norm.” In their view, to satisfy this evidentiary requirement a party seeking to establish the existence and scope of a usage will have to present some combination of expert witness testimony, industry trade codes, statistical evidence that a practice is regularly observed, or, at a minimum, some examples of actual commercial transactions in which the practice was followed. The study of usage in the courts demonstrated, however, that these types of “objective” usage-related evidence lead to the encrustation of usages that would undermine the very evolution of commercial practices that the code was designed to foster. See Goetz and Scott, The Limits of Expanded Choice, __U Va. L. Rev.__

97 The study found that judges rarely referred to prior cases as evidence of the content or existence of a usage. Across the Study Group, this occurred in four cases. One of these was a maritime case. [cite] Two related to the question of whether the statement that a horse was “sound” created an express warranty, a subject that did not garner a consensus, Compare Sessa v. Reigle, to Simpson v. Widger, 709 A2d 1366 (1998). The third dealt with the reasonable time for a grain merchant to send a written confirmation of an oral contract Bureau Service v. King 721 N.E. 2d 159 (19__).

98 Interpretive error costs include the costs of courts mistakenly finding usages to exist when they do not, the costs of courts making errors in defining the scope and content of usages, as well as the cost of courts mistakenly incorporating extralegal understandings into legally enforceable contracts.


100 Id. at __
were neither commonly introduced, nor required by courts to establish the existence of a usage.

Across the cases in the Study Group that went to trial, only 36% involved the introduction of any non-party witness testimony.\textsuperscript{101} Plaintiff’s alone introduced this kind of testimony in 20% of cases, defendants alone in 23%, and in both parties did so in ___%. Even in the cases where a trial was held and a custom was found to exist, non-party witness testimony was introduced in only ___% of them. [Additional data will be added here that explores the effect that non-party witness testimony has on outcomes when it is introduced.\textsuperscript{102}]

In cases decided on motions for summary judgment non-party witness affidavits were introduced in just 21% of the cases. In 83.3% of the cases where the party raising the usage issue succeeded in defeating the motion, an affidavit from a party and or its employees was the only usage-related evidence introduced. [Some additional data will be inserted here].

The introduction or attempted introduction of Trade Codes and other trade association standard form contracts and publications was also uncommon. It occurred in just 11% of the cases. This may be due, in part, to the fact that a large number of the industries that produce Trade Codes and association drafted contracts also provide arbitration services to those who contract under them.\textsuperscript{103}

\textsuperscript{101} But see text accompanying notes ___-___(explaining that the data could not rule out the possibility that party or party employed expert witnesses testimony was more commonly introduced).

\textsuperscript{102} When nonparty witness testimony was introduced, it led to a finding that a usage existed in 75% of the cases where the plaintiff introduced it and the defendant did not (4 cases), 100% of the cases where the defendant introduced it and the plaintiff did not (9 cases), and 40% of the cases where both parties introduced it (6 cases but one excluded the evidence). The small number of cases, however, makes it impossible to fully assess the impact non-party testimony has on outcomes.

\textsuperscript{103} Given that the theory behind incorporating unwritten usages is that they arise from the competitive selection of rules and practices and are presumptively efficient and reasonable given their wide-spread use by merchants, looking to trade codes and standard form contracts as proxies for usage is conceptually problematic. Although associations whose members are buyers one day and sellers the next and that also have well-constructed committee structures and voting rules may generate the types of trade rules and standard-form contract provisions that come close to meeting these criteria, see e.g., Lisa Bernstein, \textit{The NGFA Arbitration}
The study did not find a single case where statistical evidence of “regularity of observance” was introduced. There were only six cases where a party introduced any evidence that the usage had actually been followed in even a few transactions between other market participants. All of these cases involved a battle-of-the-forms situation under 2-207(b), in which the party attempting to rely on a “different” or “additional” term in their acceptance introduced a few contracts with similar provisions from other industry participants to show that the provision’s inclusion was customary. In the main, courts did not require the introduction of any evidence, beyond the mere conclusory assertions of a witness or affiant, to establish that a practice was widely observed. Court opinions rarely addressed the statutory requirement of “regularity of observance,” although there were a few cases where a court found a usage not to exist and noted that sufficient evidence of regularity of observance had not been introduced.

Although the reason that statistical information about “regularity of observance” was never introduced could not be determined from the study, one reason might be that even if such detailed statistical evidence were available, it would not, standing alone, necessarily enable courts to identify “such regularity of observance in a place, vocation or trade, as to justify an expectation that it will be observed,” in any particular transaction.

Consider a contract for the delivery of one hundred bales of hay on the first of the month over the calendar year 2011 for a price of $50 per bale. Suppose that the price of hay suddenly increased...
on April 20, 2011 and that the seller delivered only eighty-five bales, claiming that there was a usage in the hay business that quantity statements in contracts were only estimates and that delivering any amount plus or minus twenty bales was considered acceptable under a usage of trade.\textsuperscript{105} Suppose further that to establish that usage the seller introduced a study which found that in one hundred contracts that called for the delivery of one hundred bales of hay on the first of the month, under one-third of the contracts eighty bales were tendered and accepted, under another third one hundred bales were tendered and accepted, and under the final third one hundred and twenty bales were tendered and accepted. If courts looked at this data through the lens of the Code and the Official Comments, they would likely conclude that it established a usage that when a contract says one hundred bales, one hundred bales plus or minus twenty bales is considered proper or customary tender. Given the structure and operation of the hay trade, however, a more accurate interpretation of this behavior is that the one hundred contractual relations observed were among transactors who trusted one another and dealt with one another on a repeat basis, so that within any individual relationship where eighty were accepted one month, a look at the next months tender would show one hundred and twenty were tendered. Among parties who trust one another and have sufficient inventory, it might be much cheaper to take the level of precaution that results in an average of one hundred bales per month being delivered, rather than the level of precaution associated with delivering exactly one hundred bales each time. Yet if relations between these parties broke down and they did not anticipate dealing with one another in the future, and one party delivered eighty-five at a time when the price had gone way above the contract price, to excuse delivery of the additional fifteen bales on the basis of a usage would be far from implementing the parties’ intent.\textsuperscript{106}

As this example illustrates, courts face interpretive difficulties in these situations because transactors’ willingness to make the types of adjustments that look on their surface like behavioral regularities introduce trade usage evidence the defendant had not produced sufficient evidence of regularity of observance)\textsuperscript{105} [insert case]

Usage in the Courts

often depends on the existence or non-existence of conditions that are observable to them but are not verifiable by a court. These include: the degree of trust they have in one another, the expected benefit of future dealings, and the likelihood that the difference will be made up in a future deal even if the market price makes it non-advantageous to do so. As a consequence, when courts incorporate behavioral regularities into contracts as trade usages, some of the regularities they incorporate are likely to be the types of norms that transactors are willing to follow when they want to preserve their relationship (a “relationship preserving” or “informal norm”), but that they would have been unwilling to promise to follow in their written agreement for any of a number of reasons.\footnote{For a comprehensive discussion of the ways that relationship preserving norms and end game norms impact commercial behavior and the consequences of confusing them in adjudication, see Bernstein, Merchant Law, supra note __.} When courts incorporate informal norms into commercial agreements, they will therefore be acting directly contrary to the parties’ intent and will therefore be creating large interpretive error costs.

Incorporationists view the incorporation of informal norms as “simply another potential source of interpretive error costs,”\footnote{Kraus and Walt, In Defense, supra note __ at 209.} and one that is not likely to be large given their “speculation” unsupported by any data, “that observable patterns of commercial behavior more often than not reflect formal rather than informal norms.”\footnote{Kraus and Walt, In Defense, supra note __ at __. In defending this position, incorporationists explain that because “informal norms are more likely to develop in the context of relational rather than discrete contracts . . .and [m]any, perhaps a majority of the transactions governed by Article 2 are discrete,” informal norms will not be common in contracting relationships governed by the Code. However, the data show that a significant proportion of the interpretation cases arising under the Code involve transactors who have dealt with one another before, often over an extended period of time. Across the twenty-two cases that went to trial on an interpretation issue, for example, at least half involved transactors who had dealt with previous occasions. More, importantly, however, incorporationists overlook the fact that the existence or non-existence of the type of informal norms that will appear to be behavioral regularities across a market or industry, is not determined only by the characteristics of the parties to a particular dispute, but also by structural and interpersonal features of the relevant market. These sorts of norms are likely to arise when many transactions in the market are repeat and the same types of adjustments and/or contractual flexibility will benefit a large number of transactors. In such contexts, if a case goes to court, the regularity of behavior in the market, the supposed predicate for finding a usage, is independent}
types of transactions subject to the Code for two reasons. First, because “informal norms most commonly will develop in the context of relational rather than discrete contracts. . [and] many, perhaps a majority, of the transactions governed by Article 2 are discrete;”\textsuperscript{110} and, second, because if these norms existed and were important, transactors would not “typically use express terms with vague or ambiguous meaning.”\textsuperscript{111} However, while the data cannot tell us how many relationships in the shadow of the Code are discrete or repeat, it did demonstrate that across the cases in the Detail Group that dealt with interpretation and went to trial, at least half involved transactors who had done business with one another before. Moreover, the data did not reveal any cases where courts were confronted with standard-like provisions; although it did reveal the use of some short-hand industry terms of art, that might be taken as a signal that transactors wanted them to be given a contextual interpretation.

The consequences, in terms of strategy’s shadow effects on commercial transactions, of courts routinely incorporating informal norms into commercial contracts are, however, more significant than the consequences of their making occasional errors in filling gaps or determining the meaning of written contractual provisions. In contracting contexts where both formal and informal norms are common, transactors will often find it beneficial to structure their contracting relationship using a mix of legally enforceable promises that condition on verifiable information, and informal agreements (both express and tacit) that condition on information that may only be observable. By transforming all of transactors’ commitments reflected in both formal and informal norms into legally enforceable contract obligations, the incorporation strategy makes it impossible for parties to fully realize the significant efficiency gains often that come with using this two-tiered contractual structure. Transactors are forced to either bear the interpretive error costs that come with the mis-incorporation of informal norms, or structure their relationship using a set of second-best terms that they are willing to

\textsuperscript{110} See Kraus and Walt, In Defense, supra note __ at 210.
\textsuperscript{111} Id. at 211
follow in their work-a-day interactions and have courts enforce in the event of a dispute. Unlike other types of interpretive error, whose magnitude transactors can influence (though certainly not completely control) through the inclusion of various types of contract provisions, the only way for transactors to avoid this type of interpretative error and obtain the benefits of their preferred contracting structure, is to opt out of the court system and the Code.112

Incorporationists have dismissed the importance of this type of interpretive error on practical grounds. They point out that even if informal norms did exist in significant numbers, the Code's trade usage provision does not require courts to take them into account. There is nothing in the language of the Code or the interpretations advanced in the Official Comments, however, to suggest that courts have the authority to incorporate only formal norms. The Code defines the existence of a trade usage by the regularity of its observance and the reasonableness of the expectation that it will be observed in a particular contracting relationship. Applying these criteria, informal norms are often indistinguishable from formal norms,113 because transactors (particular those in repeat-dealing relationships) expect one another to abide by them. Moreover, even if the Code were interpreted, or explicitly amended, to give courts the authority to incorporate only formal norms, it is unlikely that such a rule could be implemented in practice. While any transactor in the relevant market could be called to testify about their own subjective beliefs about whether a usage was meant to be enforced in court, it is unclear how, absent a social scientific survey, anyone would be able to testify as to the general attitude across the market, since it would depend on an aggregation of subjective beliefs across a large number of people. Indeed incorporationists conclude that “the paradigm evidence of an informal norm is provided by trade-wide testimony that a practice is not intended to be given legal effect,” a type of evidence that, even if available, would likely be too

112 This is precisely what a large number of merchant industries in which informal understandings add tremendous value to contracting relationships have done.

113 In markets where such norms are common, they are often backed by an array of non-legal sanction that make them, in effect, self-enforcing over a range of typical market conditions. It is therefore quite likely that they will, in fact, be observed by a majority of transactors most of the time.
expensive for litigants to actually acquire.

This section will also discuss other reasons to suspect that interpretive error costs might be large, however the Coding of the results needed to substantiate the arguments has not yet been completed. One reason to suspect that interpretive error costs might be significant, stems from the context in which many interpretation cases reach the court, namely times of extreme price movements or an unusually large one sided loss where one suspects that the norm broke down or was never intended to apply.

Finally, it is important to note that the debate over the magnitude of the interpretive error costs introduced by the strategy has focused entirely on cases that go to trial. It has entirely ignored the effect of the strategy on motions for summary judgment. As the study demonstrated, however, a party opposing a motion for summary judgment can assert the existence of a usage based on nothing more than a cursory affidavit supplied by one of its own employees (an affidavit that is simply attached to the moving papers so the affiant’s assertions are not subject to cross examination), a finding which suggests that summary judgment determinations may be subject to significant interpretive error costs.

**Conclusion** In sum, the study of usage in the courts revealed that the evidentiary basis of trade usage arguments and findings is, in practice, quite thin and rarely includes either statistical evidence of a regularity of observance or even examples of actual commercial transactions in which the usage was observed. The reasons for this are unclear and the study sheds no light on them. Nevertheless, the study’s findings might give pause to even incorporation’s strongest defenders, who have taken the position that “an analysis counts as an interpretation of custom only if it adequately fits relevant commercial behavior and attitudes [demonstrated through actual instances of commercial behavior]. . .otherwise, the analysis is not an interpretation of anything. It instead serves as a

---

114 There may also be additional barriers to parties obtaining different types of usage evidence. For example, it may be quite difficult for a company to convince its similarly situated competitors to disclose the parameters of the flexibility they offer to their customers. Firms typically prefer to keep this type of information private. A company might also fear that undertaking a statistical study of the contracting behavior of its competitors would, even in the unlikely event that anyone would respond to the survey, raise antitrust concerns.
recommended decision rule.” Indeed, taken as a whole, the information in the study suggests that some of the evidence that parties introduce to demonstrate usages (along with the economic/business rationales they offer to explain them) may give courts valuable contextual information that helps them decide cases in a commercially sensible way. However, to say the types of usage evidence introduced in typical Article 2 cases frequently establishes a “usage of trade,” as that term is defined in the Code, is something of a legal fiction.

IV. THE INCORPORATION STRATEGY AND STRATEGIC BEHAVIOR

[To be added]

V. REFORMING COMMERCIAL LAW

[This section will begin by exploring that ways that the data support replacing the default interpretive approach in the Code with either (1) a more formalist/textualist approach\textsuperscript{115} or (2) a more limited contextual approach that looks to usages only for select purposes—such as gap-filling or fleshing out the meaning of “merchantable goods”-- but not for the purposes of interpretation (unless it would be admissible for this purpose under the parol evidence rule in the New York common law).

The section will situate this discussion of the study’s findings and arguments in the context of theoretical work done by Schwartz and Scott on the reasons businesses would prefer a more formalistic approach to contract interpretation;\textsuperscript{116} the work of Miller;\textsuperscript{117}

\textsuperscript{115} This section will defend making the default rule a textualist/formalist one, while giving parties the opportunity to opt into an incorporationist adjudicatory regime provided that their contract appoints an expert arbitrator to make binding determinations about the content of usages. In the course of defending the change, the section will argue that if such a rule is properly structured it can have desirable information forcing effects and may largely eliminate commonly litigated issues such as whether the parties are merchants (which they will have to recite or will be considered to have stipulated to by virtue of the opt in), whether they are part of the same commercial community, and, if not, which communities usages should govern (a choice of usage clause), and whether they should have been aware of relevant usages (their opt in would constitute their consent to be bound).


\textsuperscript{117} Geoffrey Miller, Bargains Bi-Coastal: New Light on Contract Theory, 31 Cardozo L. Rev. 1475 (2010).
Eisenberg and Miller\textsuperscript{118} on transactors’ clear preference for New York law (formalist) over California law (contextual); and the work of Bernstein showing that the private legal systems created by merchants to resolve merchant-to-merchant disputes adopt highly formalist approaches to adjudication that eschew incorporation for any purpose other than gap filling narrowly defined.\textsuperscript{119}

At present, however, as the history of the ALI’s most recent attempt to overhaul Article 2 suggests, large-scale reform of American commercial sales law is politically infeasible. In addition, the ALI is the type of private legislature that is particularly unlikely to be able to produce the types of clear and detailed menus of default provisions and clauses that would be required to turn American sales law into a working system of clear rules that could be interpreted in a relatively formalistic manner and used to predictably (and relatively inexpensively) resolve business disputes.\textsuperscript{120} As a consequence, the essay will consider narrower amendments to the Code that the data suggest have the potential to reduce or eliminate particular types of disputes that give rise to a lot of litigation.

[This section will then discusses a series of small, yet potentially high impact reforms, suggested by the study’s findings, including changes relating to limitation of remedy and limitation of warranty clauses under 2-207(b), and the Code’s hierarchy of authority as interpreted by US courts. It will also suggest that the Code’s parol evidence rule, which does not treat evidence of usage as parol evidence and thus exempts it from the rules reach, be changed so that usage evidence is subject to the rule (and not included in the Code’s definition of “agreement”). This would greatly lower fortification costs.]

\textbf{V. CONCLUSION}

In an attempt to explore the incorporation strategy on its own terms, this Essay has assumed that transactors in fact want

\textsuperscript{120} See Alan Schwartz and Robert Scott, \textit{The Political Economy of Private Legislatures}, __U. Pa. L. Rev. __
contractual gaps to be filled, and their contractual provisions interpreted, against the background of trade usages. It is important to note however that there is no empirical evidence to substantiate the claim that this is in fact the approach that is favored by any, much less a majority of, transactors whose sales agreements are subject to the Code. Indeed, the very limited empirical evidence available suggests that both mid-sized merchants and corporate transactors entering into high-value supply agreements might, in fact, be opposed to incorporation, at least for interpretive (as opposed to gap filling) purposes. The vast majority of contracts filed as Exhibit 10 material contracts in the SEC’s EDGAR system have a “total agreement,” clause and/or some sort of integration/merger clause. In addition, some of these agreements include provisions specifically opting out of usage of trade, course of performance or course of dealing. However, the vast majority of the agreements that have these specific opt-out clauses only exclude these factors with respect to interpretation. Similarly, in merchant industries in which trade associations have created private legal systems to resolve disputes among their merchant members, the industry-expert arbitrators who decide the cases submitted to these private tribunals, have not been directed to adopt the incorporation strategy. Rather, they have been directed to employ a highly formalistic

---

121 In drafting the Code, Karl Llewellyn simply assumed that merchants wanted the legal rules governing their transaction to reflect the practices they followed in their work-a-day interactions. He that such an approach would both result in the generation of efficient commercial rules and make it easier for merchants to conform their actions to the dictates of the law. Modern incorporationists have concluded that transactors prefer incorporationist adjudication based solely on their empirically unsubstantiated belief that “contractors often, even typically, use express terms with vague or ambiguous plain meaning, [from which] we infer that they intend these terms to be interpreted in light of commercial practices.” Kraus and Walt, In Defense, supra note __at __Although the logic of this claim is plausible in situations where transactors leave gaps in contracts or include standard-like provision solely because the transactions costs of memorializing them in a writing is too high (and incorporationist adjudication therefore simply replicates their hypothetical bargain), the current literatures on incomplete contracting and the behavioral economics of contract drafting and negotiation offer many alternative explanations for the use of standard-like provisions and the presence of contractual gaps that cannot plausibly be said to carry this implication. For an overview of the many reasons transactors leave gaps in contracts see George Triantis__[insert].

122 [This footnote will contain the EDGAR data to substantiate the assertions made in the text.]
adjudicative approach that looks to usages, if at all, only to fill contractual gaps narrowly defined.\textsuperscript{123}

The extent to which transactors whose contracts are subject to the Code want usages to be incorporated is an issue that must be definitively resolved before it is possible to reach fully thought out conclusions about the direction American commercial law should take. If incorporation does not accord with the preferences of business transactors, it can no longer be justified with the standard arguments for majoritarian defaults that have long been used to defend it; another theory for its continued use must be developed. In addition, if the approach does not accord with majoritarian preferences, the magnitude of the fortification costs it imposes on transactors (which depend on the extent to which parties preferred meanings and obligations diverge from any usage based meanings and obligations that might plausibly be attributed to them) are likely to outweigh any specification costs savings the strategy could possibly create.

Another fundamental assumption behind the incorporation strategy that needs to be empirically investigated before serious reform can be attempted is the assumption that usages of trade exist in business communities.\textsuperscript{124} Again, the limited empirical evidence available on the existence of customs suggests that they might not be anywhere near as common as the incorporationists suggest.\textsuperscript{125} This

\textsuperscript{123} See Bernstein, Merchant Law, supra note __(describing the formalist approach adopted by the grain industry	extquoteright s arbitration tribunals), and Bernstein, Creating Cooperation, supra note __(discussing the formalistic adjudicative approach adopted by cotton industry tribunals)

\textsuperscript{124} Incorporation	extquoteright s defenders do not view this question as important to assessing the desirability of the strategy because if they did not “[a]ttempts to employ the strategy would end in a vain attempt to identify relevant commercial practices.” In Defense, supra note __at 200. However, in light of the study	extquoteright s findings about the ease with which usages can, in fact, be established in court, the issue of whether or not usages exist must be squarely faced by any serious attempt to defend the strategy.

\textsuperscript{125} See Bernstein, See Lisa Bernstein, \textit{Questionable Empirical Basis}, supra note __ at __ (presenting historical evidence that in US merchant industries that sought to codify their customs around the turn of the century, a time when all of the pre-conditions generally associated with the emergence of unwritten commercial custom such as social or ethnic homogeneity, repeat smaller scale transactions among those who were buyers one day and sellers the next, were near perfectly met, usages of trade that were geographically coextensive with the scope of trade did not consistently exist.). See also White, \textit{Cooperative Antagonist} supra note 4 at
research also suggests that to the extent true commercial usages do exist, they may be far more geographically localized than the extent of trade in the relevant markets; and much simpler in form than the sorts of detailed practices that transactors allege when it is in their interest to do so in court.\textsuperscript{126}

Finally, if it is established that the types of usages that the incorporations strategy searches for actually exist, and merchant transactors both know their content (another unsubstantiated assumption of the strategy\textsuperscript{127}) and want them to be taken into account in contract disputes, attention has to paid to the best procedural mechanism for determining their content and scope. Indeed, in his defense of including a merchant jury provision in the Code, Karl Llewellyn correctly noted leaving these issues to a lay jury would waste large amounts of trial time and come down to a battle between the seller’s man and the buyer’s man.\textsuperscript{128} As the data presented here demonstrate, this is exactly what has happened.

\textsuperscript{685} (criticizing the incorporation of trade usage and “suggesting [albeit without any empirical documentation] that useful trade practice exists in only a minority perhaps a smaller minority, of all cases where one might search for one. And . . . the capacity of lawyers to find and present this trace practice and of the judge or jury to understand it is even more limited.”).

\textsuperscript{126} Emily Kadens, The Myth of the Customary Law Merchant, 90 Tex. L. Rev. __ (forthcoming 2012) (providing evidence that during the pre-modern period custom was viewed as a local phenomenon and where customs were supra-local, they were either regional, such as the customs of the Mediterranean shippers, or of a very high degree of generality with many local variations).

\textsuperscript{127} Not only is there no empirical evidence that transactors are generally aware of usages in the markets in which they operate, there is also no well developed theory of how transactors come to know the content of commercial customs in markets where they are not buyers one day and sellers the next, and therefore acquire this knowledge through experience.

\textsuperscript{128} See sources cited supra note __ at __.