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ARTICLES

BRIBERY AS A "REAL" DEFENSE AGAINST A HOLDER IN DUE COURSE

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I. INTRODUCTION

Bribery¹ is an ancient evil. Egypt's legal system, which goes back "beyond 4000 B.C.,"² has left relics of specific pronouncements by King Thutmose III dated about 1500 B.C.³ condemning partiality on the part of a judge.⁴ Egyptian King Harmhab's Edict for Judges,⁵ written about

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1. Bribery is an unusually complex molecule and involves careful and extensive separate study. *See generally*, E.A. ROSS, *SIN AND SOCIETY* (1907); W.M. REISMAN, *FOLDED LIES: BRIBERY, CRUSADES AND REFORMS* (1979) containing a bibliography of over 180 sources including United Nations and Congressional papers and law review articles; N.H. JACOBY, P. NEHEMKIS, and R. EELLS, *BRIBERY AND EXTORTION IN WORLD BUSINESS: A STUDY OF CORPORATE POLITICAL PAYMENTS ABROAD* (1977); R.L. SMITH, *THE TARNISHED BADGE* (1965); THE KNAPP COMMISSION REPORT ON POLICE CORRUPTION (1972); D. BOULTON, *THE GREASE MACHINE: THE INSIDE STORY OF LOCKHEED'S DOLLAR DIPLOMACY* (1978); R.W. GREENE, *THE STING MAN: INSIDE ABCAM* (1981); J. LEVY-CAEN, *DE LA CORRUPTION DES EMPLOYES: EN DROIT FRANÇAIS ET EN DROIT ANGLAIS* (1934); L.R. DRISCOLL, *The Illegality of Bribery: Its Roots, Essence, and Universality*, *CAPITAL U.L. REV.* (to be published February 1985).

2. J. WIGMORE, *A PANORAMA OF THE WORLD'S LEGAL SYSTEM* 11 (Library Ed. (1936).

3. *Id.* at 16.

4. "It is an abomination of the god to show partiality. This is the teaching: thou shalt act alike to all, shalt regard him who is known to thee like him who is unknown to thee, and him who is near to thee like him who is far . . ." *id.* at 16-17, quoting from instructions recorded on the tomb of chief judge Rekhmire purporting to have been pronounced by King Thutmose III, citing the translation from J.H. BREASTED, *2 ANCIENT RECORDS OF EGYPT* § 666-670 (1907), at 52, n.c., 53.

5. King Harmhab's Edict, set forth by Wigmore, *supra* note 2, at 15-16, in part inveighs: "I have sailed and traveled throughout the entire land. I have sought out two judges perfect in speech, excellent in character, skilled in penetrating the innermost thoughts of men, and acquainted with the procedure of the palace and the laws of the court . . . I have said to them, 'You shall not take money from one party and decide without hearing the other; for how could you sit as judges upon other men's deeds when one among you is himself committing an offense against justice? The penalty for such an offense shall be death.' And I the king have decreed this, that the laws of Egypt be bettered, and that suitors may not be oppressed. For I

1300 B.C.,⁶ on penalty of death, even more expressly and absolutely prohibits a jurist from taking money from a party to a lawsuit.⁷

Almost as old as bribery itself is the law of commercial paper. The first known negotiable instrument dates back to about 2100 B.C., around the time of the reign of King Hammurabi.⁸

The laws pertaining to bribery and commercial paper are not only ancient, but each is an integral part of our present everyday lives. On a single average business day recently in the United States, it is reported that over 100 million checks valued at over \$50 billion were written.⁹ As for the prevalence of bribery today, the post-Watergate scandals involving Lockheed Aircraft's countless millions of dollars in payment abroad,¹⁰ and the incredible videotaped "Abscam"¹¹ operations at home, depict bribery as quotidian today as garden weeds, the common cold and TV soap operas.

1. *Bribery Laws*

Although they apparently have very little deterrent effect, we have anti-bribery laws aplenty¹² on the books. The founding fathers

Id. (citing at 52, n.b., 53, the translation in BREASTED, *supra* note 4, Vol. 3 § 23.)

6. *Id.* at 18. Harmhab is said to have married the aunt-in-law of King Tutankhamen. *Id.*

7. *See supra* note 5.

8. The bearer note reads, "5 shekels of silver, at the usual rate of interest, loaned by the Temple of Shamash and by I. Company, to Idin and his wife, are payable with interest on sight of the payors at the market-place to the bearer of this instrument." WIGMORE, *supra* note 2 at 69 (citing the German translation in M. SCHORR, URKUNDEN DES ALTABABYLONISCHE ZIVIL-UND PROZESSRECHTS, (No. 58) at 88 (1913). *Id.* at 95, n.e.

9. REILING, THOMPSON, BRADY and MACCHIAROLA, BUSINESS LAW TEXT AND CASES 393 (1981).

10. BOULTON, *supra* note 1 at xiv. Senator Church, investigating Lockheed Aircraft, is quoted as stating, "The bribes and the payoffs associated with doing business abroad represent a pattern of crookedness that would make, in terms of its scope and magnitude, crookedness in politics look like a Sunday school picnic by comparison." *Id.* at 266.

11. "Abscam" was short for Abdul scam and involved a two-year investigation operated through a dummy corporation on Long Island called Abdul Enterprises, Ltd. which resulted in bribery indictments of, among others, Philadelphia Congressman Michael J. Myers; Representative Raymond F. Lederer (D-Pa.), a member of the House Ways and Means Committee; Representative John W. Jenrette, Jr. (D-S.C.), a member of the House Appropriations Committee; Representative Richard Kelly (R-Fla.); Representative Frank Thompson, Jr. (D-N.J.), Chairman of the House Administration Committee and the subcommittee on Labor-Management Relations; and Representative John M. Murphy (D-N.Y.). GREENE, *supra* note 1, at 5-6.

12. "There is law aplenty on the books," but the real question is the extent of "commitment to consistent and vigorous enforcement, which is, of course, the key to the enforcement of antibribery laws and indeed to any meaningful response to white-collar crime." REISMAN, *supra* note 1 at 160.

so deplored bribery that, except for treason, it is the only crime specified in the Constitution as an impeachable offense.¹³ Bribing another's employee to influence him to perform his duties improperly ("commercial bribery"¹⁴) is a common law offense,¹⁵ is prohibited by specific criminal statutes in at least half our states¹⁶ and, in the rest, may constitute wrongful conduct under the common law, or under one or a combination of those states' various general criminal

13. U.S. CONST., art. II, § 4 provides for impeachment of the president, vice-president, and all civil officers for "Treason, Bribery, or other high Crimes and Misdemeanors." As to this provision, Prof. Reisman says, "It should be no surprise that the first modern experiment in popular government fixed so sharply on bribery as a fundamental violation of the trust the people were putting in an elected leader. In this constellation of expectations, bribery is a form of treason." *Id.* at 3-4.

14. Commercial bribery has been defined as the "bribing of another's employees for the purpose of inducing the employees to act in their employment in some way favorable to the briber's interest." D.B. DOBBS, HANDBOOK OF THE LAW OF REMEDIES 700 (1973). It has also been described as "an offense of bribing an employee, servant, or agent, with the intent to influence him in his relation to his employer, master or principal." 1 A.L.R. 3d 1350, 1352-53 (1965). 12 AM. JUR. 2d 759 (1964) defines it as "the act of giving or receiving a gift for the purpose of influencing any agent to improperly discharge a duty entrusted to him by a private individual or corporation." The history of various statutes prohibiting commercial bribery is described in *Perrin v. United States* 444 U.S. 37 (1979). "Commercial bribery was generally treated under the rubric of the law of 'master and servant' since it involved deceit of the employer practiced jointly by the external briber and the employee as well as contractual violations by the employee. But the Federal Trade Commission viewed commercial bribery as an unfair trade practice." REISMAN, *supra* note 1 at 176, n.3. *See also* *United States v. Pomponio*, 511 F.2d 953 (4th Cir. 1975).

15. "The common law offense of bribery has been defined as follows: 'whenever a person is bound by law to act without any view to his own private emolument, and another by a corrupt contract engages such person on condition of the payment or promise of money or other lucrative consideration to act in a manner which he shall prescribe, both parties are by such contract guilty of bribery' (14 Halsbury's Laws (3rd Ed.) 213; 2 Douglas Election Cases 400)." I WORDS AND PHRASES, *Bribery* 185 (2d ed. 1969).

16. *See, e.g.*, ARIZ. REV. STAT. ANN. § 13-2605 (Supp. 1983-84); ARIZ. GEN. CORP. LAW § 10-136 (1977); COLO. REV. STAT. § 18-5-401 (1978); CONN. GEN. STAT. §§ 53a-160, 53a-161; HAWAII REV. STAT. § 708-880; ILL. REV. STAT. Ch. 28 §§ 29A-1 - 20A-3; KAN. STAT. ANN. § 21-4405; KY. REV. STAT. §§ 518.030; LA. REV. STAT. ANN. 14:73; MASS. GEN. LAWS, Ch. 271 § 39; MICH. STAT. ANN. § 750-150; MO. REV. STAT., title 38 § 570.150; NEB. REV. STAT. § 28-710; NEV. REV. STAT. §§ 613.110, 613.120; N. H. REV. STAT. § 638.7; N.J. STAT. ANN. §§ 2C:21-10 through 2C:21-15; 2C:41-1 through 2C:41-6.2 (1979); N.Y. PENAL LAW §§ 180.00 - 180.08; N.C. GEN. STAT. § 14.353; PA. CONS. STAT. ANN. title 18 § 4108; R.I. GEN. LAWS §§ 11-7-3 - 11-7-5; S.C. CODE § 16-17-540; TEX. PENAL CODE ANN. § 32.43 (1974 and Supp. 1984); UTAH CODE ANN. § 76-6-508 (1978); VA. CODE § 18.2-444 (1982); WASH. REV. CODE ANN. §§ 49.44.060, 49.44.070 (1962); WIS. STAT. § 134.05. Commercial bribery may also violate other criminal statutes in these states, and their common law; furthermore, in other states, it may violate the common law and various of their other criminal statutes. *See infra* note 17.

Arizona, Colorado, Kansas, New Hampshire, New York and Texas provide for felony violations under certain circumstances. In other states, commercial bribery violations constitute misdemeanors.

statutes.¹⁷ Federal statutes providing a second layer of enforcement supplementing state authority to prosecute commercial bribery have recently proliferated.¹⁸

The earliest commercial bribery¹⁹ statutes passed in the United States were enacted just after the turn of the century.²⁰ They represented a legislative response to the then alarming spread of commercial bribery and its viciousness, dishonesty, and "demoralizing tendencies."²¹ New York's first commercial bribery statute, passed in 1905,²² was expanded

17. See, e.g., CAL. PENAL CODE §§ 484, 504, 506, 508, 639 and 639a; IDAHO CODE ANN. § 18-2402; MONT. CRIM. CODE §§ 94-2306 - 2309; N.M. CRIM. CODE § 30-16-6 (general criminal fraud statute); OHIO REV. CODE §§ 2913.02, 2921.13, 2913.43(A), 2921.21(A), 2923.03, 2921.22(A), 2905.12(C), 2905.11; OR. REV. STAT. § 165.080 (falsifying business records); OKLA. REV. STAT. 21 § 421 (conspiracy), 21 § 1640; WYO. REV. STAT. § 6-7-315.

18. See *Perrin*, *supra* note 14; the Federal Trade Commission Act, as amended, 15 U.S.C. § 45(a)(1)(2) (1982); the Mail Fraud statute, 18 U.S.C. § 1314 (1982); the Robinson-Patman Act, 15 U.S.C. § 13 (1982); the Travel Act, 18 U.S.C. § 1952 (1982); the Hobbs Act, 18 U.S.C. § 1951 (1982); the Racketeer Influenced Corrupt Organization Act ("RICO"), 18 U.S.C. § 1962 (1982); the Bank Secrecy Act, 31 U.S.C. § 1059(2) (1982); the Wire Fraud statute, 18 U.S.C. § 1343 (1982). There are also a large number of federal statutes prohibiting not only such activities as bribing a Congressman (18 U.S.C. §§ 204-205), a bank examiner (18 U.S.C. §§ 212-213) or any other federal "public official" (see 18 U.S.C. § 201(a)), but criminalizing "graft" and "conflict of interest" (18 U.S.C. §§ 201-211) even as to former employees (*id.*) and partners of employees (*id.*). As to what commissions or fees are unlawful under the Robinson-Patman Act, see 42 A.L.R. FED. 276 (1979). See also 55 AM. JUR. 2d *Monopolies* §§ 17, 162, 163, 800, 801 (1971); as to cases dealing with federal kick-back statutes (41 U.S.C. §§ 51-54 (1982)), see 17 L.Ed.2d 919 (1967). Any consignee or consignor of property delivered for interstate transportation may not receive money or any valuable consideration as a rebate or offset against regular charges for transportation. See § 1(3) of the Elkins Act, 49 U.S.C. § 41(3). A briber may be prosecuted for his activities in aiding a bank officer who violates 18 U.S.C. §§ 371 and 215. *U.S. v. Michael*, 456 F. Supp. 335 (D.C.N.J. 1978). See also *Continental Management, Inc. v. U.S.*, 527 F.2d 613 (Ct. Cl. 1975) as to civil sanctions, and cases collected at 12 AM. JUR. 2d 750, *Bribery, Under Federal Statutes* § 4 (1964).

As to the Foreign Corrupt Practices Act (15 U.S.C. §§ 78a, 78m) see ARKIN, DUDLEY, EISENSTEIN, RAKOFF, RE AND SIFFERT, 5 BUSINESS CRIME: CRIMINAL LIABILITY OF THE BUSINESS COMMUNITY, ch. 18 and, generally, JACOBY, NEHEMKIS AND EELLS, *supra* note 1; BOULTON, *supra* note 1.

19. See *supra* note 14.

20. See 1 A.L.R.3d 1353 (1978). As to the constitutionality of commercial bribery statutes generally, see Annot., 1 A.L.R.3d 1350, 1357 (1978); *State v. Brewer*, 375 U.S. 9 (1963).

21. The words of *Sirkin v. Fourteenth St. Store*, 124 App. Div. 384, 387, 108 N.Y.S. 830, 832 (1st Dept. 1908).

22. New York's original commercial bribery statute was Sec. 384r of its then Penal Code, which provided: "*Corrupt influencing of agents, employees or servants.*—Whoever gives, offers or promises to an agent, employee or servant, any gift or gratuity

in 1909²³ and became § 439 of the former New York Penal Law, which thereafter was pared down²⁴ and cast into two separate statutes.²⁵ A further 1976 amendment bifurcated the crime into degrees, rendering the first degree a class A misdemeanor.²⁶ The most recent amendments raised the penalties in all four commercial bribery statutes, so that commercial bribing and bribe receiving in the first degree for the first time in New York's history may constitute class E felonies.²⁷

whatever, without the knowledge and consent of the principal, employer or master of such agent, employee or servant, with intent to influence his action in relation to his principal's, employer's or master's business; or an agent, employee or servant who without the knowledge and consent of his principal, employer or master, requests or accepts a gift or gratuity or a promise to make a gift or to do an act beneficial to himself, under an agreement or with an understanding that he shall act in any particular manner to his principal's, employee's or master's business; or an agent, employee or servant, who, being authorized to procure materials, supplies or other articles either by purchase or contract for his principal, employer or master, or to employ service or labor for his principal, employer or master, receives directly or indirectly for himself or for another, a commission, discount or bonus from the person who makes such sale or contract, or furnishes such materials, supplies or other articles, or from a person who renders such service or labor; and any person who gives or offers such an agent, employee or servant such commission, discount or bonus shall be guilty of a misdemeanor and shall be punished by a fine of not less than ten dollars nor more than five hundred dollars, or by such fine and by imprisonment for not more than one year." 1905 N.Y. Laws 225.

23. N.Y. PENAL LAW § 439 (1909), amended 1930 N.Y. Laws 882, c. 409. 1953 N.Y. Laws 2455 c. 891, § 7 was from Penal Code 1881, § 384r, added 1905 N.Y. Laws 225 c. 136, § 1.

24. N.Y. PENAL LAW §§ 180.00, Commercial bribing, and 180.05, Commercial bribe receiving were passed by 1965 N.Y. Laws 2343 c. 1030. *Id.* at 326, 330. The new statutes deleted the former § 439 penalties which rendered a seller who gave a present to a purchasing agent and the agent both guilty of a crime even in the absence of any intent or agreement that the agent's conduct would thereby be influenced.

25. *See supra* note 24.

26. Effective September 1, 1976, pursuant to 1976 N.Y. Laws, c. 458, §§ 1 and 5. Prior to that time, both commercial bribing and commercial bribe receiving were class B misdemeanors not split into different degrees. *See* 1965 N.Y. Laws 2420, c. 1030.

27. The most recent amendments were effective September 1, 1983, and were passed by 1983 N.Y. Laws 2048, c. 577 § 1. N.Y. PENAL LAW § 180.08 entitled "Commercial bribe receiving in the first degree" provides:

An employee, agent or fiduciary is guilty of commercial bribe receiving in the first degree when, without the consent of his employer or principal, he solicits, accepts or agrees to accept any benefit from another person upon an agreement or understanding that such benefit will influence his conduct in relation to his employer's or principal's affairs, and when the value of the benefit solicited, accepted or agreed to be accepted exceeds

2. Definition of Bribery

Bribery has almost as many definitions as does the word "evil" or "immorality." The subject requires separate and extensive study, not here undertaken. For our purposes, we must keep in mind that bribery is always associated with gross corruption.²⁸

The verb "to bribe" is derived from and originally was defined as "to steal."²⁹ Bouvier's 1914 Law Dictionary defines a briber simply as "a thief."³⁰ One workable modern definition of bribery is "the act or practice of giving, offering, or taking rewards for corrupt practices."³¹ It is applied both to the one who gives and to the one who receives.³²

The difference between "commercial bribery"³³ and the bribery of public officials has to do with the position held by the bribe-receiver. In commercial bribery, he works for a private, rather than a public, employer. The bribery of public officials is far graver, since it involves the prostitution of a public trust.

The essence of the act of bribery is the giving of a gift or benefit *for the purpose of corruptly influencing an agent to discharge his duties improperly.* In that sense, it is the antithesis of honest pay received for an honest day's work. It is dishonest pay received secretly to perform the dishonest bidding of the briber, in breach of the bribe-receiver's duty toward his principal or employer, be such principal or employer a public or private commercial entity.

When a briber gets "his man" (the bribe-receiver) within a system of justice, politics, some branch of commerce, or within another's

one thousand dollars and causes economic harm to the employer or principal in an amount exceeding two hundred fifty dollars. Commercial bribe receiving in the first degree is a class E felony.

N.Y. PENAL LAW § 180.08 (McKinney 1975 and Supp. 1983-84). *See also* New York companion statutes: § 180.00 Commercial bribing in the second degree; § 180.03 Commercial bribing in the first degree; § 180.05 Commercial bribe receiving in the second degree; related statutes in Article 180, N.Y. PENAL LAW.

28. *See* McConnell v. Commonwealth Pictures Corp., 7 N.Y.2d 465, 199 N.Y.S.2d 483, 166 N.E.2d 494 (1960); DRISCOLL, *supra* note 1.

29. THE CENTURY DICTIONARY AND CYCLOPEDIA, AN ENCYCLOPEDIA LEXICON OF THE ENGLISH LANGUAGE, Vol. 1 (1911).

30. The definition, in its entirety, reads: "BRIBOUR. One who pilfers other men's goods; a thief. *See* 28 Edw. II. c.1." BOUVIER'S LAW DICTIONARY 3d rev. 8th ed. 395 (1914).

31. THE WEBSTER'S NEW ENCYCLOPEDIA DICTIONARY OF THE ENGLISH LANGUAGE, UNABRIDGED 226 (1977); *see also* DRISCOLL, *supra* note 1.

32. *Id.*

33. *See supra* note 14 and 27.

business, "his man" has been "bought" and is thus "owned" by the briber, although he officially works for another. What follows is a boring-from-within betrayal process. Through "his man" the briber gets what he wants from the employer and, to that extent, secretly controls and thereby also "owns" the employer. The briber thus "steals" the services and loyalty of the agent or employee from the employer. Viewed in this light, bribery has been characterized not only as different from, but possibly worse³⁴ than any other species of crime, and has been described as a form of "treason."³⁵

II. SCOPE OF ARTICLE

One recent case required the superimposing of the complex legal problems involved with bribery onto the clockwork of the law of commercial paper. The case was *Bankers Trust v. Litton Systems, Inc.*,³⁶ decided in 1979 by the United States Court of Appeals for the Second Circuit, applying New York law. There, apparently for the first time, a court was asked to decide whether bribery was a "real"³⁷ defense against a holder in due course.³⁸ The court found it was not a "real" but a "personal"³⁹ defense, to be treated the same as fraud in the inducement.⁴⁰

This article analyzes the *Bankers Trust* decision and suggests, in the interests of justice and in furtherance of the general public

34. "Bribery is thus different from other species of crime—worse, if you like—but there is no reason to assume that bribery does not have its operational code." REISMAN, *supra* note 1, at 2.

35. *See supra* note 13. Bribery is offensive and antithetical to our basic economic philosophy insofar as it interferes with our need to maintain competitive conditions. *See, e.g., Continental Management, supra* note 18. Since maintenance of competition "is not viewed as a tampering with nature in favor of one class or another but as a type of conservation, a fidelity to an essentially necessary state of nature," bribery is the antithesis of our most fundamental policies and goals. REISMAN, *supra* note 1, at 41. In contrast to American economic philosophy which is founded upon the maintenance of free competition, consider Joe Bonanno's description of the economic philosophy of organized crime. As a main objective, it seeks to establish and maintain a strict system of monopolies. In his words, "If two Family members are bakers, they are not allowed to own bakeries on the same block, for that would be bad for both their businesses. They would be competing against each other." J. BONANNO with S. LALLI, *A MAN OF HONOR, THE AUTOBIOGRAPHY OF JOSEPH BONANNO* 79 (1983).

36. 599 F.2d 488 (2d Cir. 1979).

37. *See infra* note 80 as to "real" defenses.

38. *See infra* Part III.

39. *See infra* note 80 as to "personal" defenses.

40. 599 F.2d at 493. Fraud in the inducement is fraud as to the nature of the transaction as contrasted to fraud in the execution (or "essential" fraud) which is fraud as to the nature of the instrument.

policy interest which New York has always had in condemning criminal bribery, the court could and should have gone the other way. In any event, the analysis clarifies that even if *Bankers Trust* is applicable to the particular facts of that case, it does not purport to, nor should it be construed as standing for the general principle that bribery is not a "real" defense good against the holder in due course of a negotiable instrument.⁴¹

III. HOLDER IN DUE COURSE IN THE LAW OF COMMERCIAL PAPER: PHILOSOPHY AND TECHNICAL PREREQUISITES

To cope with the issue of whether bribery is a good defense in a civil action by a holder in due course, a basic understanding of the underlying doctrines and the technical requirements of attaining holder in due course status is necessary.

1. *Philosophy*

The holder in due course has been said to be the "emperor of bona fide purchasers."⁴² The precursor of the concept of bona fide or good faith purchaser appears primitively and as an ungerminated seed, as early as 2250 B.C. in the Code of Hammurabi.⁴³ The first known

41. See *infra* note 83 as to the definition of "instrument."

42. WHITE AND SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE 456 (1972). The holder in due course is "one of the few purchasers in Anglo Saxon jurisprudence who may derive a good title from a chain of title that includes a thief in its links." *Id.* at 459.

43. Sections 9-12 of this earliest Code provide:

9. If any one lose an article, and find it in the possession of another: if the person in whose possession the thing is found say "A merchant sold it to me, I paid for it before witnesses," and if the owner of the thing say "I will bring witnesses who know my property," then shall the purchaser bring the merchant who sold it to him, and the witnesses before whom he bought it, and the owner shall bring witnesses who can identify his property. The judge shall examine their testimony—both of the witnesses before whom the price was paid, and of the witnesses who identify the lost article on oath. The merchant is then proven to be a thief and shall be put to death. The owner of the lost article receives his property, and he who bought it receives the money he paid from the estate of the merchant.

10. If the purchaser does not bring the merchant and the witnesses before whom he bought the article, but its owner bring witnesses who identify it, then the buyer is the thief and shall be put to death, and the owner receives the lost article.

11. If the owner do not bring witnesses to identify the lost article, he is an evil-doer, he has traduced, and shall be put to death.

12. If the witnesses be not at hand, then shall the judge set a

negotiable instrument⁴⁴ is likewise of Hammurabian vintage, although the fertile idea⁴⁵ of transferability and negotiability did not appear in European law until thousands of years later in the late middle ages.⁴⁶

By the mid-1700's, however, our current basic principles of the law of commercial paper were clearly laid down in the decisions of English courts.⁴⁷ In 1758, Lord Mansfield in the seminal case of *Miller v. Race*⁴⁸ set forth the essential elements of the holder in due course doctrine.⁴⁹

The theory enunciated in *Miller v. Race* was that if *T* steals money from victim *V*, *V* has a good cause of action against *T* to recover the money. But if *T* has used the money and it eventually finds its way into the hands of, for example, merchant *M*, who took it for goods sold, *V* cannot recover the money from *M*.

Substituting bearer paper⁵⁰ for cash, if *T* steals bearer paper from *V*, *V* cannot recover the instrument if it passes through commerce

limit, at the expiration of six months. If his witnesses have not appeared within the six months, he is an evil-doer and shall bear the fine of the pending case. Code of Hammurabi, B.C. 2250, Pamphlets, V1421, 12182. Association of the Bar of the City of New York Library.

44. See *supra* note 8.

45. WIGMORE, *supra* note 2, at 69.

46. *Id.*

47. W. BRITTEN, *BILLS AND NOTES* 9 (2d ed. 1961).

48. 1 Burr. 452, 97 Eng. Rep. 398 (K.B. 1758).

49. In *Miller*, *supra*, note 48 a demand promissory note in the amount of 21 pounds 10 shillings was made payable to William Finney or bearer. Finney mailed the note to one Bernard Odenharty on December 11, 1756, but it was lost in a mail robbery. Miller was an innkeeper who took the note for value on December 12th, in the usual course of his business; but when he applied to the bank for payment, Race, the bank clerk, refused either to pay the note or to redeliver it to Miller, because the bank had been asked to stop its payment. Miller sued in trover for wrongful conversion. Because he had taken the instrument for full and valuable consideration, and in the usual course of his business and without any notice or knowledge that it had been stolen, Miller prevailed. He was, although that term was not specifically coined, a "holder in due course."

50. The law of commercial paper in the United States is embodied in the Uniform Commercial Code (UCC). Louisiana has adopted only Articles 1, 3, 4, 5, 7 and 8 of the UCC. UCC 1978 Official Text with Comments, Table 1, XLIII, n.3. The New York UCC statutes are referred to as "UCC" followed by a section number. All quotes of the text of the UCC statutes have been taken from the UCC 1978 Official Text, *supra*. The UCC has been applied in bankruptcy proceedings (In re United Thrift Stores, 363 F.2d 11, 14 (3rd Cir. 1966)) and "is generally considered to be the federal law of commerce." In re Quantum, 397 F. Supp. 329, 336, n.2 (D.C. Virgin Islands D. St. Croix 1975), citing In re King-Porter Co., 446 F.2d 722, 732 (5th Cir. 1971).

As to "bearer paper," UCC § 3-111 provides, "An instrument is payable to

and finds its way into the hands of one we now call a holder in due course;⁵¹ also, the issuer⁵² should ordinarily be liable to pay the holder in due course if sued for the amount of the instrument.

Put another way, we have a general rule of law that "no one can transfer a better title than he himself possesses."⁵³ *Nemo dat quod non habet.*⁵⁴ But one of the exceptions to this rule arises out of the law merchant as to negotiable instruments.⁵⁵ If such an instrument passes to that "highly refined species of bona fide purchaser"⁵⁶ known as a holder in due course, he will take the instrument "free of conflicting title claims to the instrument itself"⁵⁷ and, more importantly for our purposes, free of almost all defenses of prior parties with whom he has not dealt.⁵⁸ The holder in due course is accorded this extraordinary protection not because of his "praiseworthy character"⁵⁹ but to facilitate all commercial transactions and encourage and assure the free flow of negotiable instruments in commerce. The law desires unfettered negotiability of instruments and to that end assures that a holder in due course acquires the right to collect on instruments he buys on the market without the need for any "elaborate investigations"⁶⁰ of the process and background leading up to the

bearer when by its terms it is payable to (a) bearer or the order of bearer; or (b) a specified person or bearer; or (c) 'cash' or the order of 'cash,' or any other indication which does not purport to designate a specific payee." See also UCC § 3-805.

51. See UCC § 3-302.

52. "Issue" means the first delivery of an instrument to a holder or remitter. UCC § 3-102(1)(a). "Issuer" is not used in the UCC. The issuer of a draft or check (see UCC § 3-104(2)(b)) is denominated a "drawer" (see, e.g., UCC §§ 3-104(1)(b), 3-110(1)(a)), and the issuer of a note is denominated a "maker." *Id.* "Issuer" is used throughout to encompass either a "drawer" or "maker."

53. *Whistler v. Foster*, 14 Common Bench (N.S.) 248, 257-258, 43 Eng. Rep. 441, 444-45 (1863).

54. *Id.*

55. *Id.* Since negotiable instruments are "part of the currency," they "are subject to the same rule as money: and if such instrument be transferred in good faith, for value, before it is overdue, it becomes available in the hands of a holder, notwithstanding fraud which would have rendered it unavailable in the hands of a previous holder." *Id.* The law of "negotiable instruments" in the United States today is known as the law of Commercial Paper and is embodied for the most part in UCC Article 3. See also UCC § 1-103.

56. WHITE AND SUMMERS, *supra* note 42, at 456.

57. *Id.*

58. The holder in due course takes free of all defenses of a party with whom he has not dealt except those potent defenses (commonly known as the "real" defenses) described in the UCC. See UCC § 3-305(2).

59. *Supra* note 36, *Bankers Trust* at 599 F.2d at 494 citing Gilmore, *The Commercial Doctrine of Good Faith Purchase*, 63 YALE L.J. 1057 (1954).

60. *Id.*

issuance of those instruments. Any requirement to look beyond the face of the instruments would be time-consuming and would thereby impede their free flow.⁶¹ Protection of the holder in due course traditionally has been likened to keeping "oil in the wheels of commerce."⁶² Without the lubrication afforded by the holder in due course doctrine, it is said that "those wheels would grind to a quick halt."⁶³

2. Some Basic Technical Prerequisites

To be a "holder in due course" of an instrument,⁶⁴ a person must at least be a "holder" as defined in UCC § 1-201:⁶⁵ he must not only be in possession of the instrument, but it must have been properly issued⁶⁶ or negotiated⁶⁷ to him. An instrument payable to order⁶⁸ and delivered to a transferee cannot be further negotiated or enforced by the transferee without indorsement.⁶⁹ Without such an indorsement, there is an incomplete negotiation. One given unindorsed order paper is a mere contract assignee. He stands in the shoes of his assignor and is incapable, until he attains the status of a "holder"⁷⁰ of acquiring the rights accorded to holders under UCC § 3-301.⁷¹ *A fortiori*, such a transferee, because he is not a holder, cannot attain the rights of a holder in due course. One to whom order paper has been delivered without indorsement has the specifically enforceable right to have the

61. The holder in due course is entitled to rely "on the contract rights of one who offers [the contract or instrument] for sale or to secure a loan." *Id.*

62. WHITE AND SUMMERS, *supra* note 42, at 457.

63. *Id.*

64. *See infra* note 83 as to the definition of "instrument."

65. "Holder" is "a person who is in possession of a document of title or an instrument or a certificated investment security drawn, issued, or indorsed to him or his order or to bearer or in blank." UCC § 1-201(20). *See also* UCC § 1-201(5) as to definition of "bearer."

66. *See supra* note 52 as to the definition of "issue."

67. "Negotiation is the transfer of an instrument in such form that the transferee becomes a holder. If the instrument is payable to order it is negotiated by delivery with any necessary indorsement; if payable to bearer it is negotiated by delivery." UCC § 3-202(1).

68. UCC § 3-110(1) in part provides: "An instrument is payable to order when by its terms it is payable to the order or assigns of any person therein specified with reasonable certainty, or to him or his order, or when it is conspicuously designated on its face as 'exchange' or the like and names a payee. . . ." *See also* UCC § 3-805.

69. The right of indorsement is covered in UCC § 3-201. The types of indorsements and their effect are important throughout Article 3 of the UCC, and are treated in detail, especially in UCC §§ 3-202 through 3-206.

70. *See supra* note 64.

71. Whether or not he is the owner, a holder of an instrument may transfer or negotiate it and, except as otherwise provided in UCC § 3-603, discharge it or enforce payment in his own name. *See* UCC § 3-301(3).

unqualified indorsement of his transferor:⁷² he may demand the indorsement and, should it fail to be forthcoming, apply to a court of equity for a decree directing the transferor unqualifiedly to indorse.⁷³ Negotiation is complete only when the indorsement is made, until which time the law provides no presumption even that the transferee owns the instrument.⁷⁴ Upon receiving the indorsement, the transferee becomes a holder and thereby may be able to achieve the status of holder in due course.

Bearer paper,⁷⁵ in contrast to order paper,⁷⁶ may be properly and completely negotiated by delivery alone,⁷⁷ and is the closest thing to cash in the world of commercial paper. As we saw in *Miller v. Race*,⁷⁸ it can move from hand to hand without so much as the tip of a pen touching it.

UCC § 3-305 provides that a holder in due course will take the instrument free from claims to it on the part of any person⁷⁹ and free from what we commonly call "personal defenses"⁸⁰ of any party with whom he has not dealt.

72. UCC § 3-201(3).

73. *Id.*

74. *Id.* A recent British case shows the broad general correlation of the UCC provisions to long-standing English law. To attain the rights of a holder or holder in due course, the court explains, "the holder of the bill must, if it be payable to order, obtain an indorsement and . . . he is affected by notice of a fraud received before he does so. Until he does so, he is merely in the position of the assignee of an ordinary chose in action, and has no better right than his assignor. When he does so, he is affected by fraud which he knew of before the indorsement." *Bank of Cyprus v. Jones, Q.B.*, February 24, 1984 (12th para. of decision) quoting *Whistler v. Foster*, *supra* note 53.

75. *See supra* note 50 as to "bearer paper."

76. *See supra* note 68.

77. *See* UCC § 3-202(1) at *supra* note 67.

78. *Supra* notes 48, and 49.

79. UCC § 3-305(1).

80. Some of the "personal defenses" are set forth in UCC § 3-306. By "personal" defenses we mean all those which are not "real" defenses. UCC § 3-305 sets forth the real defenses, as follows:

To the extent that a holder is a holder in due course he takes the instrument free from (1) all claims to it on the part of any person; and (2) all defenses of any party to the instrument with whom the holder has not dealt except (a) infancy, to the extent that it is a defense to a simple contract; and (b) such other incapacity, or duress, or illegality of the transaction, as renders the obligation of the party a nullity; and (c) such misrepresentation as has induced the party to sign the instrument with neither knowledge nor reasonable opportunity to obtain knowledge of its character or its essential terms; and (d) discharge in insolvency proceedings; and (e) any other discharge of which the holder has notice when he takes

There are five elements required for a "holder" to be a holder in due course, all of which are set forth in UCC § 3-302.⁸¹ One must be

1. A holder⁸² of a
2. Negotiable instrument,⁸³ who takes it for
3. Value⁸⁴ and in
4. Good faith⁸⁵ and
5. Without notice⁸⁶ that it was overdue or has been dishonored or of any defense or claim to it on the part of any person.⁸⁷

One who is not himself a holder in due course because he cannot fulfill all the substantive (and substantial⁸⁸) requirements of UCC § 3-302 may nevertheless attain the rights of a holder in due course if he took the instrument from a holder in due course.⁸⁹ In that way, for example, an instrument transferred as a gift may give an eligible donee⁹⁰ the same rights the donor had.⁹¹ If the donor was a holder in due course, the donee normally attains his rights. There is yet one

the instrument.

81. UCC § 3-302 provides: "A holder in due course is a holder who takes the instrument (a) for value; and (b) in good faith; and (c) without notice that it is overdue or has been dishonored or of any defense against or claim to it on the part of any person." UCC § 3-302(1). *See also* UCC § 9-206.

82. UCC § 3-302(1); *see also* UCC § 1-201(20), UCC §§ 3-305, 3-306, 3-202(1). *Cf.* UCC § 9-206 where this term is inapplicable.

83. For UCC Article 3 purposes "instrument" means negotiable instrument. UCC § 3-102(1)(e). *Cf.* UCC § 9-206 at text corresponding to note 93 *infra*. *See also infra* note 97.

84. UCC § 3-302(1)(a); *see also* UCC §§ 3-303, 9-206, 1-201(44), 4-208, 4-209 and WHITE AND SUMMERS, note 42 *supra*, at 465-71.

85. *Id.* at 471-72; UCC § 3-302(1)(b); UCC § 9-206.

86. UCC § 3-302(1)(c); UCC § 9-206; *see* UCC §§ 1-201(25), 3-304; WHITE AND SUMMERS, *supra* note 42, at 472-77.

87. UCC § 3-302(1)(c). *See also* UCC §§ 3-305, 3-306. UCC § 9-206 requires only that the assignee take his assignment "for value, in good faith, and without notice of a claim or defense"

88. At first blush the requirements listed in UCC § 3-302(1) may seem straightforward. Several of these elements, however, "are but doors which open onto breath-taking vistas of complex statutory and decisional law." WHITE AND SUMMERS, *supra* note 42 at 458.

89. *See* UCC § 3-201 as to the Code's "shelter" provisions.

90. *Id.* *See infra* note 91.

91. A transferee who has himself been a party to any fraud or illegality affecting the instrument or who had notice of a defense or claim against it as a prior holder cannot improve his position and benefit by the shelter provisions. *See* UCC § 3-201(1). Otherwise, the transferee obtains holder in due course rights if the transfer was by a holder in due course. Official Comment 2, UCC § 3-201.

more way of acquiring the rights of a holder in due course, and that is covered by UCC § 9-206 which pertains to assignees of certain buyers or lessees of non-consumer goods.⁹² UCC § 9-206 in part provides:

Subject to any statute or decision which establishes a different rule for buyers or lessees of consumer goods, an agreement by a buyer or lessee that he will not assert against an assignee any claim or defense which he may have against the seller or lessor is enforceable by an assignee who takes his assignment for value, in good faith and without notice of a claim or defense, except as to defenses of a type which may be asserted against a holder in due course of a negotiable instrument under the Article on Commercial Paper (Article 3). A buyer who as part of one transaction signs both a negotiable instrument and a security agreement makes such an agreement.⁹³

In the *Bankers Trust*⁹⁴ case, we therefore see the term "holder in due course" applied to the assignee of a lease⁹⁵ (meaning one coming under the provisions of UCC 9-206). "Holder in due course" under Article 3 of the Uniform Commercial Code speaks only to a holder of a negotiable instrument. "Instrument" itself, under Article 3, means a "negotiable instrument;"⁹⁶ and "holder in due course" in both UCC §§ 3-302 and 3-305 speaks to holders of an "instrument," meaning a negotiable instrument.⁹⁷ The holder in due course, under current law,⁹⁸ is a bona fide purchaser of a negotiable instrument, or one having those rights by virtue of the shelter provisions of UCC § 3-201,⁹⁹

92. Goods are "consumer goods" if they are bought or used primarily for household, family or personal purposes. See UCC § 9-109(1); *Laurel Bank & Trust Co. v. Mark Ford, Inc.*, 182 Conn. 437, 438 A.2d 705, 707 (1980).

93. UCC § 9-206(1). Note that Louisiana has not adopted Article 9 of the UCC. See *supra* note 50.

94. *Supra* note 36.

95. 599 F.2d 491.

96. *Supra* note 83.

97. Under Article 3 of the UCC the most acute of preliminary questions in determining whether one should be accorded the exalted status of a holder in due course is whether he holds a negotiable instrument. See definitions in UCC §§ 3-104(1) and 3-105, 3-112. The presumption is against negotiability, since all technical statutory requirements must be met before an instrument will be deemed "negotiable." Under Article 3, one can be a holder in due course only of a negotiable instrument; however, an assignee may also attain the rights of holder in due course under UCC § 9-206.

98. Governed in all states in the United States by the UCC. Louisiana, however, has not passed UCC Article 9. See *supra* note 50.

99. See *supra* note 91.

but he may also acquire the rights of a holder in due course as an assignee of a contract or lease of non-consumer goods, under the supplementary provisions of UCC § 9-206.¹⁰⁰

The key import of the holder in due course doctrine, for our purposes, is that one with holder in due course status takes free of all defenses of any party with whom he has not dealt except "real" defenses. These "real" defenses are only those few rare and potent ones described in UCC § 3-305(2)(a) through (e).¹⁰¹ The "personal" defenses are all others.¹⁰²

Most of the litigation involving holders in due course has nothing to do with the claims or defenses to which they are subject. Rather, the cases pivot on whether holder in due course status has been established. Once it is shown that a defense exists, the person claiming the rights of a holder in due course has the burden of establishing all the elements set forth in UCC § 3-302.¹⁰³ Only if he sustains this often weighty burden does he attain the rights of a holder in due course; and only then does the question of whether the defense is "real" or "personal" become an issue.¹⁰⁴

IV. ILLEGALITY AS A "REAL" DEFENSE

UCC § 3-305 provides that any holder in due course is subject to the real defense of illegality, but only "such . . . illegality of the transaction, as renders the obligation of the party a nullity."¹⁰⁵ Whether the "illegality" is or is not of such a degree of severity as to render the obligation of the party a nullity and void is "primarily a matter of local concern and local policy."¹⁰⁶ It is therefore left to "the local

100. See *supra* text corresponding to note 93.

101. See *supra* note 80.

102. *Id.* See also UCC § 3-306; Official Comment 5 to UCC § 3-306.

103. UCC § 3-307(3).

104. See *supra* note 80. The term "real" defense is pre-Code in origin, is not used in the UCC, but connotes those defenses set forth in UCC § 3-305(2)(a) through (e).

105. UCC § 3-305(2)(b). See text of statute *supra* note 80.

106. Official Comment 6 to UCC § 3-305 states:

Duress is a matter of degree. An instrument signed at the point of a gun is void, even in the hands of a holder in due course. One signed under threat to prosecute the son of the maker for theft may be merely voidable, so that the defense is cut off. Illegality is most frequently a matter of gambling or usury, but may arise in many other forms under a great variety of statutes. The statutes differ greatly in their provisions and the interpretations given them. They are primarily a matter of local concern and local policy. All such matters are therefore left to the local law. If under that law the effect of the duress or the illegality is to make the

law"¹⁰⁷ to resolve. If under local law the effect of the illegality is "to make the obligation entirely null and void, the defense may be asserted against a holder in due course. Otherwise it is cut off."¹⁰⁸ The example proffered by the Official Code Commentators is, "Illegality is most frequently a matter of gambling or usury, but may arise in many other forms under a great variety of statutes."¹⁰⁹

When we deal with such illegality as renders the obligation of the party a nullity,¹¹⁰ it is well to keep in mind that an instrument normally is given for an "underlying obligation."¹¹¹ That is, the issuer most frequently uses it to pay for some obligation. Ordinarily,¹¹² unless otherwise agreed, the obligation to pay is *suspended* until the instrument is due or presented.¹¹³ If it is dishonored, an action may be maintained *either* on the instrument or the obligation.¹¹⁴

1. "Illegally Void": Definitions and Difficulties

The word "illegality" does not refer to the violation of criminal statutes alone. A contract is "illegal," the Restatement tells us, "if either its formation or its performance is criminal, tortious, or otherwise opposed to public policy."¹¹⁵ The word "illegality" in UCC §

obligation entirely null and void, the defense may be asserted against a holder in due course. Otherwise it is cut off.

107. *Id.*

108. *Id.* See also the broad scope provisions of UCC § 1-103.

109. *Id.*

110. UCC § 3-305(2)(b).

111. See UCC § 3-802.

112. But not if a bank is a drawer or primarily liable on the instrument: see UCC § 3-802(1) and (1)(a).

113. See UCC § 3-802(1)(b). The word "suspended" is intended to include suspension of the running of the statute of limitations (UCC § 3-122). Official Comment 3 to UCC § 3-802.

114. UCC § 3-802(1)(b). See UCC § 3-601 and Official Comment 3 to UCC 3-802 as to discharge of the obligor.

115. RESTATEMENT OF CONTRACTS § 512 (1932). See also *Hanley v. Savannah Bank & Trust Co.*, 208 Ga. 585, 68 S.E.2d 581 (1952) (agreement by mother to surrender possession of her infant to get a benefit under a will void); cf. *Andrews, The Stork Market: The Law of the New Reproduction Technologies*, 70 A.B.A.J. 50 (1984); *Coleman, Surrogate Motherhood: Analysis of the Problems and Suggestions for Solutions*, 50 TENN. L. REV. 71 (1982); *Randon v. Toby*, 52 U.S. (11 How.) 493 (1850) (in state where slavery tolerated, buying and selling of slaves not illegal.) "It is impossible to define with accuracy what is meant by public policy for an interference and violation of which a contract may be declared invalid. It may be understood in general that contracts which are detrimental to the interests of the public as understood at the time fall within the ban." *Pope Manufacturing Co. v. Gormully*, 144 U.S. 224, 233-234 (1892). "We are not required to look exclusively to statutory enactments in determining questions of public policy. Constitutions and statutes are evidence of the general public

3-305(2)(b), therefore, is broader than it may first appear, but at the same time narrower: it is wide enough to encompass contracts which are not only criminal but merely tortious¹¹⁶ or "contrary to the best interests of citizens as a matter of public policy"¹¹⁷ whether or not there has been any proper expression about it;¹¹⁸ but the illegality under UCC § 3-305 must be such as renders the obligation of the party, under local law, void.

There does exist a general rule that an illegal contract is "void."¹¹⁹ But, not surprisingly, the rule has a vast number of exceptions.¹²⁰ Furthermore, many statutes which use the word "void" permit a court to refuse enforcement of an entire contract, but also permit excision of an offensive clause and enforcement of the remainder of the contract.¹²¹ Hence, although these statutes contain the word "void,"

policy of a state; but when confronted with questions of general public policy, as defined in the books, the courts go beyond express legislation and look to the whole body of law—statutory, common, and judicial decisions." *Holland v. Sheehan*, 108 Minn. 362, 367, 122 N.W. 1, 3 (1909).

116. For example, it has been held in New York that to bargain to commit a tort is illegal. *Reiner v. North American Newspaper Alliance*, 259 N.Y. 250, 257 (1932).

117. *Anaconda Federal Credit Union No. 4401 v. West*, 157 Mont. 175, 178, 483 P.2d 909, 911 (1971).

118. *Id.* For example, it might be against public policy to enforce a contract provision providing that a party will not interpose the defense of usury, the statute of limitations, or failure of consideration. *Pope Manufacturing*, *supra* note 115 at 235. See also Gellhorn, *Contracts and Public Policy*, 35 COLUM. L. REV. 679 (1935).

119. RESTATEMENT OF CONTRACTS §§ 598, 607 (1932).

120. See *id.*, § 236(a); RESTATEMENT OF (SECOND) CONTRACTS § 229(a) (1973); 4 WILLISTON ON CONTRACTS (3d ed. 1961) § 620; J. CALAMARI AND J. PERILLO, THE LAW OF CONTRACTS (2d ed. 1977) 785-799; *Symcox v. Zuk*, 221 Cal. App. 2d 383, 34 Cal. Rptr. 462 (1963). Usury, "Blue Sky" or other remedial statutes passed to protect a certain class of people sometimes give the plaintiff within the protected class a valid cause of action against a defendant who, by statute, is deemed the wrongdoer. 15 WILLISTON ON CONTRACTS (3d ed. 1972) §§ 1754, 1755, 1756; 6A CORBIN ON CONTRACTS § 1540 (1963). An agreement illegal because of its wrongful purpose may nevertheless give rise to a valid cause of action by an innocent party if only one of them had an illegal purpose. RESTATEMENT OF (SECOND) CONTRACTS § 602. See also *infra* note 121.

121. See, e.g., UCC § 2-302 as to unconscionable contracts or clauses. New York also has a large number of statutes which declare a covenant, promise, agreement or understanding in, or in connection with or collateral to a contract or agreement to be void: See N.Y. GEN. OBLIG. LAW § 5-322.1 (McKinney 1978) entitled, "Agreements exempting owners and contractors from liability for negligence void and unenforceable; certain cases;" § 5-321 entitled, "Agreements exempting lessors from liability for negligence void and unenforceable;" § 5-311 entitled, "Certain agreements between husband and wife void;" § 5-301 entitled, "Certain employment contracts void;" § 5-322 entitled, "Agreements exempting caterers and catering establishments from liability for negligence void and unenforceable;" § 5-323 entitled, "Agreements exempting building service or maintenance contractors from liability for negligence void and unenforceable;" § 5-325 entitled, "Garages and parking places;" § 5-326 entitled, "Agreements exempting

whether the illegality would be such as to render the obligation of the party a nullity would be left to judicial interpretation.¹²²

For example, one of New York's¹²³ most encompassing statutes of frauds¹²⁴ starts, "Every agreement, promise or undertaking is void, unless it or some note or memorandum thereof be in writing. . . ."¹²⁵ Yet the term "void" here means only unenforceable (rather than even avoidable). The lack of a writing if not timely pleaded as an affirmative defense is waived.¹²⁶ It is equally clear everywhere else outside New York¹²⁷ that an oral contract within the purview of a given statute of frauds is not "illegal"¹²⁸: it is neither "criminal nor offensive to general policy"¹²⁹ but at worst a contract "lacking a couple of legal chromosomes."¹³⁰ This, despite the fact that "void" or "no action shall be brought"¹³¹ habitually appear in these various statutes of fraud.

Corbin cautions that the common meaning of "void" is "total absence of legal effect,"¹³² but that even in the term "void contract"

pools, gymnasiums, places of public amusement or recreation and similar establishments from liability for negligence void and unenforceable;" § 5-324 entitled, "Agreements by owners, contractors, subcontractors or suppliers to indemnify architects, engineers and surveyors from liability caused by or arising out of defects in maps, plans, designs and specifications void and unenforceable;" § 5-511 entitled "Usurious contracts void;" § 5-331 entitled, "Certain covenants and restrictions in conveyances and other agreements affecting real property void as against public policy;" § 5-415 entitled, "Certain transfers of property in pursuance of lottery, void;" § 5-501 entitled, "Rate of interest, usury forbidden;" § 5-413 entitled, "Securities for money lost at gaming, void;" § 5-401 entitled, "Illegal wagers, bets and stakes;" § 5-417 entitled, "Contracts, agreements and securities on account of raffling, void;" § 5-331 entitled, "Certain covenants and restrictions in conveyances and other agreements affecting real property void as against public policy."

122. It has been said, for example, that "An act or contract neither wrong in itself nor against public policy which has been declared void by statute for the protection or benefit of a certain party, or class of parties, is voidable only. U.S. v. New York & Porto Rico S.S. Co., 239 U.S. 88, 36 S. Ct. 41, 42, 60 L. Ed. 161; Weede v. Iowa Southern Utilities Co. of Delaware, 231 Iowa 784, 2 N.W.2d 372, 397, 398." BLACK'S LAW DICTIONARY, 1745 (4th ed. 1968).

123. There is "no common law statute of frauds. Each state has its own statute." J. DAWSON, W. HARVEY AND S. HENDERSON, CASES AND COMMENTS ON CONTRACTS, 951 (4th ed. 1982).

124. N.Y. GEN. OBLIG. LAW § 5-701 (McKinney 1978).

125. *Id.* § 5-701(a).

126. Sanger v. French, 157 N.Y. 213, 51 N.E. 979 (1898).

127. DAWSON, HARVEY AND HENDERSON, *supra* note 123, at 967.

128. *Id.*

129. *Id.* at 968.

130. *Id.*

131. Section 4 of the original 1677 statute of frauds uses the words "no action shall be brought." See *id.* at 952 setting forth the statute.

132. I CORBIN ON CONTRACTS (1963) § 7 p. 15. "One who says that an agreement

there is an intrinsic self-contradiction.¹³³ "Contract" by definition always includes "some element of enforceability."¹³⁴ He thus prefers "void agreement" to "void contract."¹³⁵

As to voidness, Corbin emphasizes the cruciality of judicial interpretation stating, "Even if a statute expressly declares an agreement to be illegal or void, justice requires and the courts have continually decided that the effect of such a statute upon a particular case must depend upon the circumstances of that case. The words of the statute will be interpreted in the light of the purpose of the statute, with due regard to the result that will be reached by the interpretation."¹³⁶

Thus, as the *New Howard*¹³⁷ case emphasizes: "An instrument which a statute, *expressly or through necessary implication declares void*, strictly speaking is a simulacrum only. It is without legal efficacy. It cannot obligate a party or support a right."¹³⁸ So that even though the word "void" is not used, an agreement may be void by statutory *implication*.

Most criminal statutes ordinarily stick to the knitting of describing what conduct they prohibit. Hence, most never get to "void" or "voidable" at all, words which languish in the more civilized world of contracts. Taking one example at random, "Robbery" in § 160.10 of the N.Y. Penal Law¹³⁹ sets forth the elements of the crime and then affixes its statutory classification: "Robbery in the second degree is a class C felony."¹⁴⁰ There the statute ends. It does not speak to

or promise is 'void' usually supposes that it has no legal operation whatever, being in many cases quite unaware that a number of important legal relations have been created." *Id.*

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.* at 17.

137. *New Howard Mfg. Co. v. Cohen*, 207 A.D. 588, 202 N.Y.S. 449 (1st Dept. 1924).

138. *Id.* at 202 N.Y.S. 451, emphasis added. The *New Howard* court explains why an instrument issued in defraud of creditors was not void, although a crime was involved under the then Bankruptcy Law, because the statute did not specify the instrument was to be treated as void. The holding is unremarkable because the crime involved was criminal fraud in the inducement, rather than the real defense of fraud in the execution; the statute had been amended to excise a previously included "void" provision; and bankruptcy laws are not a matter of local state public policy. All *New Howard* holds is that fraud in the inducement may be criminal, but still not a real defense against a holder in due course.

139. McKinney's *supra* note 23, at Book 39, 201-202.

140. *Id.* at 202.

whether a contract to commit robbery, or one induced by, tainted with, connected to, or resulting from such robbery is "void" or "voidable." The same applies to almost all other criminal statutes, including New York's commercial bribery statutes.

2. Criminal Illegality as "Penalized" in a Civil Action

Ultimately, determining whether the obligation under UCC § 3-305 is "illegally void" is a judgmental and labeling challenge. It is a buck envisioned to be passed to the local court, where it stops. It is the local court's function to perceive and implement local public policy. Thus, in a civil action, the court has inherent power to control the interpretation and application of criminal statutes, insofar as it expounds upon and teaches both the litigants and the public as to the meaning and impact of criminal statutes. And, by the very nature of a civil proceeding, it does so in a swift and effective manner, unimpeded by the constrictions inherent in criminal prosecutions. This power is especially effective in the sphere of commercial bribery. Bribery is all about money, and money is what the civil court has the power to give or not to give.

Thus, what is crucial to the vortex of our topic is that the punishment set forth in any penal statute is not the exclusive or even most effective "price" or penalty for that crime. Irrespective of any fines or sentences imposed upon a conviction beyond a reasonable doubt in a criminal case, in a civil action the court can find the illegal conduct mandates a forfeiture of property.

This was the jurisprudential feat performed in *Riggs v. Palmer*,¹⁴¹ now a legend in American legal folklore. In his dissent¹⁴² in *Riggs*,

141. The *Riggs* maxim set forth, "No one shall be permitted to profit by his own fraud, or to take advantage of his wrong, or to found any claim upon his own iniquity, or to acquire property by his own crime. These maxims are dictated by public policy, have their foundation in universal law administered in all civilized countries and have nowhere been superseded by statutes." *Riggs v. Palmer*, 115 N.Y. 506, 511-512 (1889). Although *Riggs* is frequently cited by American courts as the source of these maxims, their origin is much older. That one may not profit from his own wrong has been found to be one of some 214 maxims of Edmund Wingate published in London in 1658. Simpson, *The Rise and Fall of the Legal Treatise: Legal Principles and the Forms of Legal Literature*, 48 U. OF CHIC. L. REV. 632, 645 (1981). But their ultimate source has been traced back to "Ulpian in *Digest* 50.17.134.1 where it appears as *nemo ex delicto meliorem suam conditionem facere potest*." *Id.* This *Digest* was compiled by Domitius Ulpianus, a Phoenician born about A.D. 170. J. MUIRHEAD, *THE INSTITUTES OF GAIVS AND RULES OF ULPIAN* xiii (1880).

142. 115 N.Y. at 519.

Judge Gray anguished, "What power or warrant have the courts to add to the respondent's penalties by depriving him of property? The law has punished him for his crime and we may not say that it was an insufficient punishment."¹⁴³ In a superb exposition of advanced justiciary, the majority exhibited just what power the civil court had. The power to do justice, as *Riggs* demonstrates, is almost boundless.

That the Legislature understood civil courts would and should exact penalties in addition to those imposed by criminal statutes is evidenced by rarely cited language contained in the criminal statutes themselves. Present N. Y. PENAL LAW § 5.10, derived from an 1881 statute¹⁴⁴ predating *Riggs* specifically provides:

(3) This chapter does not bar, suspend, or otherwise affect any right or liability to damages, penalty, forfeiture or other remedy authorized by law to be recovered or enforced in a civil action, regardless of whether the conduct involved in such civil action constitutes an offense defined in this chapter.¹⁴⁵

Riggs never cited this statute's predecessor. A civil court does not need statutory language as authority for its power to "penalize" persons seeking to take advantage of illegal bargains.

From the 1889 Adam's rib holding in *Riggs*, over 70 years later was wrought the Eve we see in *McConnell v. Commonwealth Pictures Corporation*.¹⁴⁶ Both cases are cited in *Bankers Trust*.¹⁴⁷

When Elmer Palmer murdered his grandfather, *Riggs* held he forfeited his legacy under his grandfather's will.¹⁴⁸ When Fred McConnell allegedly bribed a producer's agent to get the film distribution contract for Commonwealth, he forfeited his right to collect under his commissions contract.

In McConnell's suit for an accounting, the defense was that he should not be permitted access to the court because he had bribed an agent of Universal Pictures to obtain the contract for Commonwealth. The court held the issue was not "whether the acts alleged in the defenses would constitute the crime of commercial bribery."¹⁴⁹

143. *Id.*

144. N.Y. PENAL LAWS § 5.10(3) (McKinney 1975) is derived from N.Y. PENAL LAW 1909 §§ 23, 24, 37, all of which were derived from the Penal Code of 1881. See *supra* Historical Note, McKinney's note 23, Book 39, p. 15.

145. *Id.* at 14-15.

146. See *supra* note 28.

147. 599 F.2d at 491, 492.

148. *Riggs v. Palmer*, *supra* note 141.

149. 7 N.Y.2d at 470.

McConnell's motion to strike the defenses for insufficiency was treated as his constructive admission¹⁵⁰ of those facts. McConnell thereby was deemed an unworthy plaintiff, seeking to take advantage of his own wrong, and to acquire property by his own crime. He could not recover commissions for having obtained a bribery-induced contract. The power of *Riggs* was upon him. But the court said "all" they were doing was "labeling the conduct described in these defenses as gross corruption depriving plaintiff of access to the courts of New York State."¹⁵¹ McConnell may not have been indictable, no less "convictable" beyond a reasonable doubt in a criminal case. It made no difference. He nevertheless was heavily penalized by the judgment in the civil case. Commonwealth was left with its bountiful windfall, enjoying the fruits of the contract McConnell had brought to them. McConnell wound up with nothing for all his efforts.¹⁵²

And it was the *McConnell* decision which barred one of the plaintiffs from summary judgment in the *Bankers Trust* case,¹⁵³ which we now examine.

V. FACTS AND RATIONALE OF *BANKERS TRUST V. LITTON*¹⁵⁴

Litton, the defendant, had decided to buy some photocopiers.¹⁵⁵ Angelo Buquicchio, a salesman who worked for Royal, a division of one of Litton's subsidiaries, recommended Litton lease the photocopiers from Regent Leasing, an outside entity.¹⁵⁶ Regent was to buy the equipment from Royal and then lease it to Litton. Neither Royal nor Litton knew Buquicchio would be making money in this transaction.¹⁵⁷ Regent's president when later deposed admitted that he paid money

150. Words used in *Flegenheimer v. Brogen*, 284 N.Y. 268, 272 (1940).

151. 7 N.Y.2d 471.

152. McConnell originally got \$10,000 from Commonwealth. Taking the defenses as true, he gave the producer's agent \$10,000. He was to get 20% of certain recouped gross receipts realized on the distribution of 40 Western and four serial motion pictures, simultaneously with further payments Commonwealth was obliged to make to the producer. Lower court in *McConnell* at 1 Misc.2d 751, 752 (Sup. Ct. 1955). Commonwealth had originally counterclaimed for the return of this \$10,000 but never appealed its being brushed aside in the lower court. McConnell never received anything other than the first \$10,000 which he allegedly used for the bribe.

153. Motion for summary judgment by plaintiff Regent denied, in reliance on *McConnell*, 599 F.2d at 491.

154. See *supra* note 36.

155. 599 F.2d at 490.

156. Regent was entirely independent of either Litton or Royal. *Id.*

157. *Id.*

to several Royal people, "particularly Buquicchio, so they would push leases generally and Regent's leases specifically."¹⁵⁸ To finance its purchases, Regent had borrowed money from the plaintiff banks, assigning the Litton leases as security.¹⁵⁹ The leases contained a provision allowing assignment and a clause providing the assignees' rights would be independent of any claims or offsets of Litton as against Regent.¹⁶⁰ When Litton defaulted, a suit was started by the banks and Regent, followed by motions for summary judgment. The heart of the defense was that the bribery of Royal's employees rendered Litton's obligation null and void. The Second Circuit affirmed the District Court's holding that the payments to Buquicchio "could constitute a defense against Regent."¹⁶¹ However, it was not a good defense against the banks as UCC § 9-206 holders in due course. Under New York law, the court concluded, "a holder in due course may treat a contract inducted by illegal bribery as merely voidable."¹⁶² To analyze the court's reasoning, the argument of the court has been broken down into three tiers, to show its progression, then each tier is separately treated, *infra*.

The substance of the court's reasoning was as follows:

TIER 1. In using the word "nullity" in UCC § 3-305, the "Legislature intended to provide a defense against a holder in due course only in cases where the obligation sued upon is void on its face (*e.g.* a wagering contract or a contract to perform an illegal act). . . ."¹⁶³

TIER 2. "An examination of bribery-induced contracts suggests that New York holds such contracts to be 'void.'"¹⁶⁴ "Confusion in the use of the words 'void' and 'voidable' is common."¹⁶⁵ Chiefly the difference becomes important only where property is transferred to a holder in due course.¹⁶⁶ Since the New York cases on illegal contracts induced by commercial bribery do not involve holders in due course, one may assume "void" was used loosely, "without regard to its importance

158. *Id.*

159. *Id.* This was not the usual "leveraged" lease transaction. Had it been, query as to whether plaintiffs would have been denied holder in due course status, having "dealt" with Litton. UCC § 3-305(2).

160. *Id.*

161. *Id.* at 491 relying on *McConnell*, *supra* note 28.

162. *Id.* at 492.

163. *Id.* at 491. These were the observations of the court below which were quoted with approval.

164. *Id.*

165. *Id.*, quoting from RESTATEMENT OF CONTRACTS § 475, comment b (1932).

166. *Id.*

when a holder in due course enters the picture."¹⁶⁷ A voidable contract may be ratified, while a void transaction cannot.¹⁶⁸ "*Sirkin v. Fourteenth Street Store* . . . suggests that the court meant the contract to be truly 'void' because it "could not be ratified. . . ."¹⁶⁹ TIER 3. However, the policy supporting the New York cases is one precluding recovery to a wrongdoer.¹⁷⁰ Where an innocent holder in due course "is suing upon an illegal contract, the policy argument is inapplicable because the plaintiff has done no wrong for which it should be penalized."¹⁷¹ "Bribery which induces the making of a contract is much like fraud which has the same result . . ."¹⁷² Since fraud in the inducement is a personal, not a real, defense under UCC § 3-305(2), "the same treatment should be given to a contract induced by bribery."¹⁷³ Denying recovery to holders in due course would probably

167. *Id.*

168. *Id.* at 492 quoting from RESTATEMENT OF CONTRACTS § 475, comment b (1932).

169. *Id.*, referring to *Sirkin*, *supra* note 21.

170. *Id.*, citing *inter alia*, RESTATEMENT OF CONTRACTS § 598, comment a, (1932); 14 WILLISTON ON CONTRACTS § 1630A (3d ed. 1972); *Riggs v. Palmer*, *supra* note 141, *McConnell*, *supra* note 28; *Riener*, *supra* note 116.

171. *Id.* at 492-93.

172. *Id.* at 493.

173. *Id.* Here the court refers to RESTATEMENT OF CONTRACTS § 577, "Illustrations 4 & 11 (1932)." *Id.* Referring to this authority, one sees § 577 is entitled, "Bargains to Defraud or Harm Third Persons." The following rule is then set forth: "A bargain performance of which would tend to harm third persons by deceiving them as to material facts, or by defrauding them, or without justification by other means is illegal." The RESTATEMENT continues:

Comment: a. Cases falling within the rule stated in the Section would generally, but not always involve the commission of a tort and therefore fall within the rule stated in § 571.

b. The tendency of the performance to deceive or otherwise harm others sometimes necessarily follows from the character of the performance promised, but in other cases the performance promised may be used innocently or may be used in such a way as to harm or defraud others. In such cases it is the purpose so to use the performance that makes the bargain illegal. The purpose may be entertained by one or by both parties to the contract. If entertained by one only, the other party may recover for a breach of the contract (see § 602). If an improper purpose is entertained by both parties to the contract, neither can recover. Illustrations 4 and 11 cited by *Bankers Trust* set forth:

4. A desires to buy land from B at a low price. C is aware of facts which, if told B, will induce him to refuse to sell for such a price. A promises C \$500 if C will not tell B the facts in question. C does not tell B. The agreement is illegal.

11. A agrees with B to pay B \$500 if B causes a legislative investigation of the affairs of a corporation. A's purpose is to depress

not "have an appreciable effect on the frequency of commercial bribery. Moreover, the holder in due course concept embodies important policies which must be weighed against the policy of holding void, contracts induced by bribery."¹⁷⁴

Taking these three points in order:

COMMENT AS TO TIER 1. This statement appears misleading. If the obligation sued upon is void on its face (*e.g.*, indicates it is a wagering contract or a contract to perform an illegal act, the examples proffered by the court), there could not be a holder in due course. The holder would take with "notice"¹⁷⁵ that the obligation is illegal and, having notice of a defense, he would be unable to establish his status under UCC § 3-302(1)(c). He might also have trouble in sustaining his burden of establishing his good faith.¹⁷⁶

Even a "small" irregularity which should have been spotted on the face of an instrument will bar establishment of holder in due course status. Thus, in a typical "notice" case, a man had signed both his name and his wife's name, placing his initials after the wife's signature on a note. When the purchasing bank sued on it, failure of consideration was raised as a defense. The bank could not establish it was a holder in due course because of the "irregularity" of the initials next to the one signature. On appeal, the finding was affirmed.¹⁷⁷

UCC § 3-304 itself specifies that the purchaser has notice of a claim or defense if "(a) the instrument is . . . so irregular as to call into question its validity, terms or ownership or to create an ambiguity as to the party to pay; or * * * (2) the purchaser has notice that the obligation of any party is voidable in whole or in part, or that all parties have been discharged."¹⁷⁸ It thus appears that any contract illegal on its face could not, by definition, pass to a holder in due course.

the value of the shares and to obtain profit from selling short. B causes the investigation and produces the desired result. The bargain is illegal.

Neither of these illustrations seems apposite to acts prohibited under the New York Commercial Bribery statutes in that the parties to whom money is offered in these examples is not an employee or agent of the victim of the fraud. The crime of commercial bribery has at its heart the necessary element that the bribe-receiver is an employee or agent. Thus, commercial bribery is a far graver act than fraud. Its "treason" element (*see n. 13 supra*) is the essence of the crime, and that element is missing in both these illustrations.

174. 599 F.2d at 493.

175. *See* UCC §§ 3-302, 3-304, 9-206; *see also* UCC § 1-201(25) as to when a person has "notice" of a fact.

176. "Notice" and "good faith," although hardly identical, "appear in the cases and in the flesh as first cousins." WHITE AND SUMMERS, *supra* note 42, at 471.

177. *Arcanum National Bank v. Hessler*, 69 Ohio St.2d 549, 433 N.E.2d 204 (1982).

178. UCC § 3-304 (emphasis added).

The concept makes good sense. The "would-be holder in due course"¹⁷⁹ simply "does not deserve to take free of such defenses, for he could have refused to take"¹⁸⁰ the instrument or proffered transaction.

More importantly, as to Article 3 instruments, a check or simple promissory note might be issued by A, a debtor, payable to L, a loan shark, as follows:

July 27, 1984

FOR VALUE RECEIVED, I promise to pay to the order of
L the sum of \$5,000.00
payable in 30 days.

(Signed) A

If this instrument were given in return for a \$4,000 loan made by L to A on July 27, 1984, in New York the note could be truly void as criminally usurious¹⁸¹ and the usury defense would be a real defense against a holder in due course.¹⁸² Furthermore, the note could also be usurious and truly void in New York were it given for a loan at interest in excess of 16% per annum (although it would not be criminally usurious¹⁸³). Thus, it would be void in the hands of a holder in due course, even though no criminal statute was violated.¹⁸⁴ To boot, in New York a usurious transaction is "not so utterly void"¹⁸⁵ that it

179. White and Summers explain the rationale of UCC § 3-304: A party can acquire notice of a defense in a variety of ways. He can observe that the instrument is crudely altered; he can see that its date for payment has already passed; he can note that it has been stamped 'paid,' or he may even have actual knowledge of a contract defense of the drawer or maker. In all such cases a would-be holder in due course does not deserve to take free of such defenses, for he could have refused to take the instrument.

Id., *supra* note 42, at 471.

180. *Id.*

181. N.Y. PENAL LAW §§ 190.40, 190.42. This would not apply to certain exempt transactions, such as any loan or forbearance in the amount of \$2,500,000 or over as provided in GOL 5-501(6)(b) and would not apply in several other exceptions outlined in the GEN. OBLIG. *See* GEN. OBLIG. §§ 5-501 through 5-531.

182. *Sabine v. Paine*, 223 N.Y. 401, 119 N.E. 849 (1918), cited by *Bankers Trust*, 599 F.2d at 493.

183. GEN. OBLIG. §§ 5-501, 5-511.

184. *Sabine v. Paine*, *supra* note 182.

185. *Smith v. Marvin*, 27 N.Y. 137, 143 (1863); *Graham v. Weiss*, 3 Misc. 2d 28, 30, 149 N.Y.S.2d 676, 678 (Sup. Ct. 1958).

cannot be ratified. To the extent that a debtor repays any portion of the loan, he is deemed to have ratified¹⁸⁶ the transaction and cannot recover, except to the extent of any amount in excess of the legal rate of interest.¹⁸⁷ If he had paid nothing and was sued, the defense of usury would be good, even as against a holder in due course, who could not collect on such a void instrument.

What is important is that, as the illustration of the note indicates, there is nothing "on its face" to show its void nature. If the same note in New York were issued in payment of an illegal gambling debt,¹⁸⁸ the illegality would be a good defense against a holder in due course since the instrument, although it has no remarkable facial defects, is void.

It is also clear that while UCC § 9-206¹⁸⁹ validates the type of waiver of defense clause involved in *Bankers Trust*, the statute works only when the assignment is taken for value, in good faith, and without notice of a claim or defense.¹⁹⁰ The assignment remains subject to the same defenses as may be asserted against a holder in due course of an instrument under UCC Article 3.¹⁹¹

The statement that the word "nullity" in UCC § 3-305(2)(b) was intended "to provide a defense against a holder in due course only in cases where the obligation sued upon is void on its face," hence seems unsupportable.

186. *Id.*

187. GEN. OBLIG. § 5-513.

188. See GEN. OBLIG. Title 4 and, e.g., GEN. OBLIG. § 5-413. As to the illegal voidness of instruments issued for gambling purposes, see *Hotel Riviera, Inc. v. First National Bank and Trust Company of Oklahoma*, 580 F. Supp. 122 (W.D. Okla. 1983); *Gulf Collateral, Inc. v. Morgan*, 415 F. Supp. 318, 322 (S.D. Ga. 1976); *National Recovery Systems v. Mazzei*, 123 Misc.2d 780, 475 N.Y.S.2d 208 (Sup. Ct. 1984) (a gambling debt will not be enforced in New York unless it was valid where incurred). See also: *Hendrix v. McKee*, 281 Or. 123, 575 P.2d 134 (1977); *Miller v. Radikopf*, 394 Mich. 83, 228 N.W.2d 386 (1975) (agreement to split proceeds of winning Irish Sweepstakes ticket enforced as non-offensive to public policy).

189. See *supra* text corresponding to note 93.

190. UCC § 9-206. *United Counties Trust Co. v. Mac Lum, Inc.*, 643 F.2d 1140 (5th Cir. 1981) (assignee found to have had "notice" was subject to defense of failure of consideration); *First National Bank of New Jersey v. Reliance Elec. Co.*, 668 F.2d 725 (3d Cir. 1981) (assignee did not meet good faith and absence of notice requirements and could not benefit from waiver of defense clause); *Personal Finance Co. v. Meredith*, 39 Ill. App. 3d 695, 350 N.E.2d 781 (1976) (if plaintiff had actual notice of complaints it would not have been holder in due course); *Laurel Bank & Trust Co. v. Mark Ford, Inc.*, 438 A.2d at 105, *supra* note 92 (assignment is subject to all defenses of a type assertable against a holder in due course under UCC Article 3).

191. *Laurel Bank*, 438 A.2d at 705, *supra* note 92.

COMMENT AS TO TIER 2. As to whether a bribery-induced contract is truly void in New York in that it may not be ratified, the *Sirkin*¹⁹² wording adverted to by the court is as follows:

. . . this is not a case in which the rule of ratification, applicable to ordinary contracts induced by fraud, should be applied. The public policy of our state forbids the ratification, as well as the making of such a contract. Usually private contracts concern only the parties thereto, and it is optional with a person who has discovered that he has been defrauded whether to ratify the contract or to rescind it. There is ordinarily, at least, no general public policy involved in such cases.¹⁹³

Sirkin is New York's classic commercial bribery case. It was a simple action to recover some \$1,500 for hosiery and wrappers sold to the defendant, a Manhattan department store. The defense was that *Sirkin* had paid a bribe to the store's purchasing agent; hence, the store should not have to pay for the goods delivered and accepted under the bribery-induced contract. The court found the defense sufficient.¹⁹⁴ The store was able to keep the goods without having to pay for them. The moral was simple: One who commits commercial bribery forfeits his right to collect on the business he bribed to get. The civil judgment had a remarkable penalty; and there was no problem about establishing guilt beyond a reasonable doubt.¹⁹⁵ *Sirkin* held the bribery-induced contract illegally void because it was induced by the commission of a crime. (The Penal Law's first stated general purpose in New York is to "proscribe conduct which unjustifiably and inexcusably causes or threatens substantial harm to individual or public interests."¹⁹⁶)

A litmus test of voidness has to do with whether a given contract may be ratified.¹⁹⁷ *Sirkin* finds the bribery-induced contract may

192. See *supra* note 21.

193. *Id.* 124 App. Div. at 391, 108 N.Y.S. at 835.

194. The *Sirkin* dissent insists New York's then commercial bribery statute (§ 384r, text *supra* note 22) failed to set forth the contract was void (*Bankers Trust* also so states); that it was voidable only, since it was a legal contract merely bribery-induced (*Bankers Trust* also so states); and that (echoing the Gray dissent in *Riggs*) the criminal statute fixed a penalty and the court may not impose additional punishment for its violation. See 124 App. Div. at 395, 108 N.Y.S. at 838. Cf. N.Y. PENAL LAW § 5.10(3).

195. See *McConnell*, *supra* note 28. The same general notion is seen in the New York statute allowing one who receives unsolicited goods to treat them as an "unconditional gift." N.Y. GEN. OBLIG. LAW § 5-332(1).

196. See N.Y. PENAL LAW § 1.05(1).

197. See *Bankers Trust* at 599 F.2d 492.

not be ratified because it involves criminal conduct. The general rule is if the act done was a civil act, it may be ratified; "but no authority is to be found that an act which is itself a criminal offense is capable of ratification."¹⁹⁸ Ratification is a doctrine which applies when the following four elements are present: (1) the *principal is disclosed* sufficiently to be capable of later identification and (2) the agent acts without or in excess of his authority and (3) the ratification is of the entire act and not of a part and (4) the principal knows all the facts of importance when he ratifies.¹⁹⁹ Ratification is generally a contracts and torts doctrine.²⁰⁰

Although a forgery may be "ratified,"²⁰¹ the Official Code Commentators make clear that what is meant is "adopted" and, if that is done, the word "ratified" is merely used to indicate the adoption of retroactive.²⁰² They further caution that, "While the ratification may be taken into account with other relevant facts in determining punishments, it does not relieve the signer of criminal liability."²⁰³

Note that in forgery, by the forger's very act of passing off the signature as the principal's, the forger purports to act as, and therefore for, a principal; furthermore, ratification of the forgery is never forced, but voluntary. One of the necessary elements of ratification is that the agent purport to act for a principal. In the criminal bribery agreement, the agent does not purport to act for the principal. As to this, Corbin says "an agreement by two parties for the doing of acts that both know to be a felony would have no legal operation and be 'void' although the acts themselves, when performed, would have very important legal effects indeed."²⁰⁴ (If the resulting bribery-induced contract is illegally void,²⁰⁵ forcing a ratification down the throat of the already victimized principal seems incongruous. If he cannot ratify

198. *Brook v. Hook*, L.R. 6 Ex. 89 (Exchequer 1871). Since one cannot commit a crime by ratifying what is already done, the rule that subsequent ratification is equivalent to prior authorization cannot be applied to criminal cases. *Cook v. Commonwealth*, 141 Ky. 439, 132 S.W. 1032 (1911).

199. A.L. SAINER, *THE SUBSTANTIVE LAW OF NEW YORK* 6 (1972).

200. *Id.* at 7; W. SEAVEY AND L. HALL, *CASES ON THE LAW OF AGENCY* 314 (1956).

201. UCC § 3-404. *See also* *United States v. Davis*, 125 F. Supp. 696 (W.D. Ark. 1954) (making payments on a note which the makers denied they signed not deemed a "ratification").

202. Official Comment 3 to UCC § 3-404.

203. *Id.*

204. I CORBIN ON CONTRACTS § 7 p. 16.

205. *Sirkin*, *supra* note 21; ". . . an agreement to divide the profits of a fraudulent scheme, or to carry out some object, in itself not unlawful, by means of an apparent trespass, breach of contract or breach of trust, is unlawful and void. (POLLOCK ON CONTRACTS, 342; SALMOND & WINFIELD, CONTRACTS p. 145); *Harrington v.*

voluntarily, passing the transaction to a holder in due course cannot coerce ratification.)

Under the general doctrine of *respondiat superior*, a principal has been held criminally liable for a slander committed when a manager of its store accused a customer of stealing.²⁰⁶ One thus easily discerns that the rule which prevents "ratification" of criminal acts is founded not only on public policy considerations, but on a concern for protecting a principal from being ensnared into liability for an unauthorized criminal act.

There is also to be considered where a person harmed by the crime has power to control whether prosecution for the crime shall or shall not be brought. As *Sirkin*²⁰⁷ had implied "Insofar as an act constitutes a private wrong the injured individual is free to make a settlement with the wrongdoer, or to forgive him entirely without any reparation. But the general rule is that a private individual has no power to ratify, settle or condone a public wrong even if it was a wrong which injured his person or harmed his property."²⁰⁸ Any ability he has to ratify would come only if there is a specific exception to the general rule and only in the exact manner provided by that exception.²⁰⁹ For example, in New York, the owner of property cannot, by accepting complete restitution, forgive the crime of larceny or embezzlement.²¹⁰ A larceny victim may contract with the thief for repayment of his loss, but not if the contract includes an express or implied promise that the victim will refrain from initiating a criminal prosecution: A person commits the crime of compounding a crime if

Victoria Graving Dock Co., 3 Q.B.D. 549.)" *Reiner*, *supra* note 116 at 260-261; emphasis added.

206. *Gillis v. Great Atlantic & Pacific Tea Co.*, 223 N.C. 470, 27 S.E.2d 283 (1943).

207. *Supra* note 21.

208. R. PERKINS, CASES AND MATERIALS ON CRIMINAL LAW AND PROCEDURE 517-18 (1952).

209. *Id.*, citing *Commonwealth v. Heckman*, 113 Pa. Super. 70, 172 Atl. 28 (1934). Without the specific exception, a rape victim could not "ratify" the rape by forgiving the act. *Id.*, citing *Commonwealth v. Slattery*, 147 Mass. 423, 18 N.E. 399 (1888). It was "even beyond the power of mother's love to wipe out the criminal guilt of a son who maliciously burned her barn." *Id.*, citing *State v. Craig*, 124 Kan. 340, 259 Pac. 802 (1927). *Cf. People v. Gould*, 70 Mich. 240, 38 N.W. 232 (1888) (prosecution for seduction by false promise of marriage discharged after parties' marriage).

210. N.Y. PENAL LAW § 215.45 (McKinney 1975). *See also Breaker v. State*, 103 Ohio St. 670, 134 N.E. 479 (1921); *Fleener v. State*, 58 Ark. 98, 23 S.W. 1 (1893). In New York, it is an affirmative defense to the crime of compounding a crime that acceptance of restitution was in the reasonable belief that the amount was not in excess of the amount due. *Id. See*, however, *infra* note 211.

he agrees to accept any benefit upon an understanding that he will refrain from initiating prosecution for a crime.²¹¹

These, then, are some of the broad and complex concepts underlying the statement in *Sirkin* that a bribery-induced contract may not be ratified. If that statement is true, it would give the bribery-induced contract what *Bankers Trust* calls "a characteristic of true voidness."²¹²

One case not cited by *Bankers Trust* is *Babcock v. Warner*,²¹³ which squarely faced the question of whether a bribery-induced contract may be ratified. The court held the contract was not capable of such ratification as to enable one to recover under it. However, this decision did not involve a holder in due course, and thus may not have affected the last and most crucial step of the court's reasoning in *Bankers Trust*.

COMMENT AS TO TIER 3. The turning point of the *Bankers Trust* holding occurs when the court stops examining the character of the bribery-induced contract (after finding New York law holds such contract to be void), and then turns away to examine the character of the plaintiff. It is here the decision appears to run two different reasons together, perhaps "even reasons of different types."²¹⁴ A holder in due course of an instrument issued for an illegal gambling debt, or of a usurious instrument (even one not criminally usurious) in New York is an innocent non-wrongdoer;²¹⁵ yet he is precluded from recovery precisely because these instruments are treated as illegally void. A holder in due course for the same reason may not recover if there was such fraud in the execution as to constitute a real defense under UCC § 3-305.²¹⁶ In applying UCC § 3-305 to real defenses such as illegal gambling, usury, or fraud in the execution, the policy of New York has not at all been concerned with the preclusion of wrongdoers from recovery. Holders in due course by definition are not wrongdoers as to the instrument or obligation.

The Williston rules relied on by *Bankers Trust*²¹⁷ that "An innocent plaintiff may recover on an illegal agreement which is not

211. N.Y. PENAL LAW § 215.45(1) (McKinney, 1975); *Davis v. Mathews*, 361 F.2d 899, 902 (1966).

212. 599 F.2d at 492.

213. *Babcock v. Warner Bros. Theatres, Inc.*, 240 App. Div. 466, 270 N.Y.S. 765 (1934).

214. Summers, *Two Types of Substantive Reasons: The Core of a Theory of Common-Law Justification*, 63 CORNELL L. REV. 707, 715 (1978).

215. See, e.g., requirements of UCC §§ 3-302, 3-303, 3-304, 3-201, 3-307(3) and 9-206(1).

216. See UCC § 3-305(2)(c) and Official Comment 7 to UCC § 3-305.

217. See *supra* note 36, *Bankers Trust*, 599 F.2d at 493, n.2.

declared void by statute"²¹⁸ and that "a holder in due course may recover on a negotiable instrument originally given as part of an illegal transaction"²¹⁹ hardly dispose of the illegality complications under UCC § 3-305. The holder in due course indeed may recover—if the illegality is not such as to render the obligation void. But if the obligation is void, he may not. Williston does not mandate anything to the contrary, and that is the only possible interpretation to be given his rules; otherwise, the letter and philosophy of UCC § 3-305(2)(b) codifying illegality as a real defense would itself be a nullity.

In denying recovery to holders in due course of illegally void instruments, the New York courts refuse to validate void *transactions*, notwithstanding the innocence of the *party* seeking their enforcement. *Sirkin*²²⁰ is clear that the court would not lend its aid to the "enforcement of this *contract*,"²²¹ stating:

The Legislature has not expressly declared either that the contract to pay the bribe or the contract induced by the bribe is void or unenforceable. A contract, however, made in violation of a penal statute, although not expressly prohibited or declared to be void, is prohibited, void, and unenforceable, whether executory or executed (*Griffith v. Wells*, 3 Denio, 226; *Barton v. Port Jackson and N.T.P.R. Co.*, 17 Barb. 397).²²²

In order to focus on the voidness issue in *Bankers Trust*, it is necessary to examine the transactions involved in that case, since there were three different contracts which need to be separated out.

V. BRIBERY AND ITS THREE BASIC CONTRACTS

The three basic contracts involved in *Bankers Trust* are typical of all commercial bribery contracts. They are as follows:

A. *The Employment Contract*: The contract between the employer or principal and the bribe-receiver who is an employee, agent, or fiduciary.²²³ [In *Bankers Trust* this was the contract between

218. *Id.*

219. *Id.*

220. *Supra* note 21.

221. 124 App. Div. at 388, 108 N.Y.S. at 834; emphasis added.

222. *Id.* See also *State ex rel Bradford v. Cross*, 38 Kan. 696, 17 P. 190 (1888) (if the state could prove bribery at the trial, a contract for the sale of school lands would be declared void and the state would not be required to return the bribe money).

223. N.Y. PENAL LAW §§ 180.00, 180.03, 180.05 and 180.08 (McKinney 1975). The employment contract in connection with bribery involving public servants would be

Royal and Buquicchio and the other employees who were bribed.^{224]}

B. *The Bribery Contract*: The bribery agreement between the bribe-receiver and briber,²²⁵ made in breach of the fiduciary duty owed under the Employment Contract. Its purpose is to obtain the Resulting Contract. [In *Bankers Trust* this was the agreement between Regent and the Royal employees, particularly Buquicchio.^{226]}

C. *The Resulting Contract*: The bribery-induced contract between the principal and the briber or a third party.²²⁷ [In *Bankers Trust*, this was the lease entered into between Litton and Regent.^{228]}

ANALYSIS

A. Under the Employment Contract, the employee, agent or fiduciary owes a duty of loyalty and good faith to the employer or principal.²²⁹

B. The Bribery Contract itself is illegal and surely absolutely void in New York. Whether the employer or principal is a public

the government instrumentality. See N.Y. PENAL LAW § 10(15) (McKinney 1975) definition of "public servant." See also § 200.40 as to "party officer," and §§ 200.45, 200.50 as to bribe giving and bribe receiving for public office.

224. See 599 F.2d at 490.

225. Extortion is not per se denominated as a defense to commercial bribery, as it is in the bribery of either public or labor officials. No cases have been found involving the use of extortion, duress or coercion as a defense to a civil action involving bribery or commercial bribery. If coercion is employed by one of the parties, however, such conduct would itself be criminal in New York. See N.Y. PENAL LAW §§ 135.60, 135.65, 135.70, 135.75 (McKinney 1975).

226. 599 F.2d at 490.

227. New York has held such contracts to be void. "An examination of the language in the New York decisions on the enforceability of bribery-induced contracts suggests that New York holds such contracts to be 'void.' *Sturm v. Truby*, 245 App. Div. 357, 361, 282 N.Y.S. 433, 437 (4th Dept. 1935); *Sirkin v. Fourteenth Street Store*, 124 App. Div. 384, 393, 108 N.Y.S. 830, 837 (1st Dept. 1908), cited with approval in *McConnell v. Commonwealth Pictures Corp.*, 7 N.Y.2d 465, 470, 166 N.E. 494, 497, 199 N.Y.S.2d 483, 486 (1960); and *Shemin v. A. Black & Co.*, 32 Misc.2d 1046, 225 N.Y.S.2d 805 (Sup. Ct. N.Y. Co. 1962), *rev'd on procedural grounds*, 39 Misc.2d 354, 240 N.Y.S.2d 622 (1st Dept. 1963)." *Bankers Trust*, 599 F.2d at 492.

228. 599 F.2d at 490.

229. *Continental Management*, *supra* note 18; *Levy-Caen*, *supra* note 1 at 107-09, citing *Rothschild v. Brookman*, 2 Dow & C1, 188 (1831); *Pariente v. Lubbock*, 20 Beav. 588 (1885); *Andrew v. Ramsay*, 2 K.B. 635 (1903). This is implicit in the agreement between them, "since the undertaking is to advance the interests of the principal in accordance with the principal's desires. It is not the agent's business that is carried on, but that of the principal . . ." *Seavey and Hall*, *supra* note 200 at 3; see generally, *Muris, Opportunistic Behavior and the Law of Contracts*, 65 MINN. L. REV. 521 (1981); *Summers, The General Duty of Good Faith—Its Recognition and Conceptualization*, 67 CORNELL L. REV. 810 (1982).

institution or a private entity, both parties are engaging in criminal conduct and are *in pari delicto*.²³⁰ There is no "victim" in this two-party agreement; hence, there is no possibility of "ratification." Since both parties' conduct is criminal and they are equally at fault, we do not have a "voidable" contract such as one resulting from fraud in the inducement, where the victim is allowed time to decide whether he wishes to elect to ratify or rescind. Instead, we have a situation like *The Highwayman's case*:²³¹ two criminals engaged in an illegal agreement, neither having a cause of action against the other for breach of their void agreement.

If the characterizing of this Bribery Contract is not excessive, assume a \$10,000 check were issued by *B*, a bribe-giver payable to the order of *A*, a bribe-receiver. Were this check negotiated to a holder in due course who sued *B*, and *B* claimed such illegality of the instrument as to render his obligation a nullity (the "real" defense of illegality), this defense should be good.²³²

No cases have been found on this point either in the United States or, going as far back as 1945, in Great Britain. The holding in *Bankers Trust* might be improperly misconstrued as authority for

230. *Clark v. United States*, 102 U.S. 322 (1880); RESTATEMENT OF CONTRACTS § 598 (1932). Generally if a contract is illegal, neither party may recover on it and the parties are left where they stand on the theory that the court will not grant aid to either wrongdoer. *Id.*; *Hedla v. McCool*, 476 F.2d 1223 (9th Cir. 1973) (collecting general illegality cases). One who bribes or attempts to bribe a judge or other public official or agent is guilty of moral turpitude. See *United States v. Manton*, 107 F.2d 834 (2d Cir. 1938), *cert. den.* 309 U.S. 664 (1940); *In re McNally*, 252 App. Div. 550, 300 N.Y.S. 459 (1938) (attorney convicted of commercial bribery disbarred because acts involved moral turpitude). *Cf. Singleton v. Foreman*, 435 F.2d 962 (5th Cir. 1970) (complaint seeking return of jewelry deposited to secure illegal contingency fee agreement in divorce case stated a valid claim); *Liebman v. Rosenthal*, 185 Misc. 837, 57 N.Y.S.2d 875, *aff'd* 269 App. Div. 1062, 59 N.Y.S.2d 148 (2d Dept. 1945) (jewelry given in France to one purporting to be a friend of Portuguese Consul to be used as bribe for visas to help plaintiff and his family escape Nazis during World War II: complaint for return of jewelry withstood motion for summary judgment, since plaintiff was defrauded, not *in pari delicto*, and not guilty of moral turpitude); *Aikman v. City of Wheeling*, 120 W. Va. 46, 195 S.E. 667 (1938) (recovery allowed although restitution check proffered on condition that payee suppress criminal prosecution). See also, generally, *Gellhorn, Contracts and Public Policy*, 35 COLUM. L. REV. 679 (1935).

231. See *McMullen v. Hoffman*, 174 U.S. 639 (1899) which refers to this as a "real" case. *Id.* at 654.

232. Lord Mansfield cautions that this is true even though illegality "sounds at all times very ill in the mouth of the defendant." *Holman v. Johnson*, 1 Cowp. 341, 343 (1775). Also a "person who is guilty of illegality or fraud, and knows that he cannot sue himself, is likely to hand over the instrument to some other person to sue for him." *Bank of Cyprus*, *supra* note 74.

the proposition that bribery would be a personal and not a real defense against the holder in due course of such an instrument. *Bankers Trust* does not so hold and in any event should not be so construed.

The following examples are proffered to indicate why bribery should be a "real" defense if an instrument is issued in payment of the bribe, although it has passed to a holder in due course:

EXAMPLES

Dramatis Personae:

B: Briber

J: Dishonest Judge who agrees to accept bribe

A: Dishonest Agent who agrees to accept bribe

H: Holder, or possible Holder in Due Course

V: Victim of fraud in the inducement

1. *B* promises to pay Judge *J* \$25,000 if *J* will decide a case to be heard tomorrow in *B*'s favor. *J* decides the case in *B*'s favor, but never receives the \$25,000 and sues *B* for breach of contract. *J* cannot recover if *B* pleads illegality. The parties are *in pari delicto* and the agreement is illegally void.²³³

2. *B* pays *J* \$25,000 cash in return for *J*'s agreement to decide a case to be heard tomorrow in *B*'s favor. *J* accepts the money but decides the case against *B*. *B* sues *J* for return of his money. *B* is denied access to the courts and cannot recover.²³⁴

233. See *supra* notes 230-32.

234. *Womack v. Maner*, 227 Ark. 789, 301 S.W.2d 438 (1957) (no recovery of bribe money paid to a county judge to prevent plaintiff from being punished for gambling); *Riggs v. Palmer*, *supra* note 141; *McConnell*, *supra* note 28. Query as to what effect a claim of extortion would have on the plaintiff's rights in such a case. The Reviser's Notes to the Revision of the N.Y. PENAL LAW explain:

Even though the victim of an extortion, he [the briber] is still guilty of bribery by virtue of conferring a benefit upon a public servant or a labor official 'upon an agreement or understanding that' the latter's decision or action will thereby be influenced' (N §§ 180.15, 200.00). Out of obvious equitable considerations, the new bill arbitrarily restores the coerced 'bribe giver's' defense (N §§ 180.20, 200.05).

Fourth Interim Report of the State of New York Temporary Commission on Revision of the Penal Law and Criminal Code, Leg. Doc. (1965) No. 25 at 43. Extortion might conceivably throw the case into a Liebman-type situation (see *Liebman v. Rosenthal*, *supra* note 230) allowing recovery if plaintiff were not deemed guilty of moral turpitude. See generally, N.Y. PENAL LAW §§ 35.05 (McKinney 1975); *William J. Davis, Inc. v. Slade*, 271 A.2d 412 (1970) (landlord under illegal lease deemed not guilty of moral

3. *B* pays *J* \$25,000 cash in return for *J*'s agreement to decide a case to be heard in *B*'s favor. *J* accepts the money and decides the case in *B*'s favor. *B* sues *J* to get his money back. *B* is denied access to the courts and cannot recover.²³⁵

4. *B* gives *J* his personal check for \$25,000 made payable at *J*'s request to the order of "Cash," in exchange for *J*'s promise to decide a case to be heard tomorrow in *B*'s favor. An hour later, *J* takes the check and gives it to *H*, in payment for a good used car. *H* gives *J* the car. The check is dishonored. (*B* may have stopped payment because he has decided to abandon his crime; or he does not trust *J*; or he just does not have that much money in his checking account.) *H* sues *B* on the instrument. *B* pleads illegality as a defense. Assuming *H* can prove his holder in due course status, *B*'s defense should nevertheless be good. The transaction, bribing a judge, is a felony and void.²³⁶

(a) *If the defense is not good against a holder in due course: H* could recover from *B* on the instrument, leaving *J* with the car. The dishonest judge will profit from his crime. If *B* sues *J*, he cannot as a wrongdoer have access to the courts to get his money back.²³⁷ As between *B* and *J*, we have more of an interest in having the bite of the law felt by *J*, who is in a position of public trust and who may again be encouraged to accept bribes; but the result instead is that *B*, the briber is forced to carry out a crime and to pay; and *J*, the corrupt judge, keeps the benefit of his illegal bargain.

(b) *If the defense is good against a holder in due course: H* could not collect from *B* if *B* pleads illegality as a defense. This would not

turpitude entitled to recover in quasi-contract); see also Aikman, *supra* note 230; Singleton v. Foreman, *supra* note 230.

235. See *supra* note 234.

236. *Id.*

237. The obligation to pay a bribe to a judge cannot but be a nullity. The original agreement was by two parties for doing of acts that both knew to be a felony and would have no legal operation and be void. See text corresponding to *supra* note 204 ". . . no man may be permitted to profit from his own wrongdoing in a court of justice." Glus v. Brooklyn Eastern Terminal, 359 U.S. 231, 232 (1959); Stone v. Freeman, 298 N.Y. 268, 82 N.E.2d 571 (1948); Womack v. Maner, *supra* note 234. Courts are closed "to one who would prove his own wrongdoing as a basis for his supposed 'rights.'" Carr v. Hoy, 2 N.Y. 2d 185 (1957); Sirkin, 108 N.Y.S. 830; McConnell, 7 N.Y. 2d 465; Reiner, 259 N.Y. 250; Riggs, 115 N.Y. 506; Holman, 1 Cowp. 341; Certa v. Wittman, 35 Md. App. 364, 370 A.2d 573 (1977); Androws v. Coulter, 163 Wash. 429, 1 P.2d 320 (1931); Lanley v. Devlin, 95 Wash. 171, 163 P. 395 (1917).

leave *H* without remedy. He has two perfectly valid causes of action against *J*:

[1] *An action for goods sold and accepted in the amount of \$25,000;*²³⁸ and

[2] *An action on the instrument for breach of warranty.*²³⁹ In this case, *J* breached his warranty on transfer that there would be no defense good against him. If *B* had a good defense of illegality, *H* could collect the \$25,000 from *J* for breach of this warranty. This result leaves *B* not having to pay the bribe money and complete the crime, and *J*, feeling the bite of the law, having to pay for his car with his own money.

*If, as is customary, H had asked for J's indorsement, albeit no indorsement is necessary to transfer bearer paper:*²⁴⁰ *J* would have made this warranty that there was no defense good against him to *H* and any subsequent holder taking in good faith.²⁴¹ Even if *J* had given a "without recourse" indorsement, *H* (and any subsequent holder taking in good faith)²⁴² would still have a good breach of warranty cause of action against *J*: the "without recourse" indorsement merely narrows the no defense warranty²⁴³ to a warranty that *J* had "no knowledge of" a defense good against him. In the example proffered, *J* had actual knowledge of a defense good against him, having taken the instrument in payment of a bribe, and would thereby be liable for breach of this warranty.

5. Same facts as in 4, except that *J* has extorted²⁴⁴ the money from *B*, who gave *J* the same \$25,000 check made out to "Cash" at *J*'s behest. *J* uses it to pay for the car and, when the instrument is dishonored for any of the reasons suggested in 4 above, *H* sues *B*.

(a) *If the defense of bribery is not good against a holder in due course:* the victim of the extortion would have to pay *H*. *J* might keep his car and profit from his crime. Although in New York extortion is a defense to a criminal bribery charge involving a public servant

238. "Unless otherwise agreed where an instrument is taken for an underlying obligation . . . the obligation is suspended. . . . If the instrument is dishonored action may be maintained on either the instrument or the obligation . . ." UCC § 3-802.

239. "Any person who transfers an instrument and receives consideration warrants to his transferee" *inter alia* that "no defense of any party is good against him." UCC § 3-417(2)(d).

240. UCC § 3-202(1).

241. UCC § 3-417(2).

242. *Id.*

243. UCC § 3-417(3).

244. *See supra* note 234.

or labor official, *B*'s case against *J* is not clear cut. Equitably, he should recover. But no case has been found holding *B*, as a briber, would not be denied access to the courts and precluded from recovering against *H*.

(b) *If the defense of bribery is good against the holder in due course: H can collect against J on either of his two causes of action set forth in 4(b)[1] and [2] above.*

6. Same facts as in 4, except that the bribe-taker is not a judge but *A*, an employee who has accepted the \$25,000 check made out to "Cash" in exchange for his promise to have his employer give a contract to *B*. *A* now goes to *H* and buys the same car, giving *H* the check. *B* has second thoughts and stops payment, maybe because he does not trust *A*, has decided to abandon his crime, or maybe because he just does not have that much money in his checking account. In any event, the check is returned to *H* dishonored. *H* sues *B* on the instrument.

(a) In states where commercial bribery under these circumstances is a felony,²⁴⁵ *B*'s defense without doubt should be a real defense against *H*. The defense should also be good in all other states because (1) The instrument is issued in direct contravention of those states' commercial bribery statutes and thus is criminal in nature. The underlying obligation (to pay a bribe) must be regarded as void. Both parties are guilty of moral turpitude and are *in pari delicto*. Neither is capable of ratifying his void agreement or criminality; or (2) The instrument is issued in direct contravention of those states' other criminal statutes, or is a common law offense or repugnant to the public policy of these states. This would again leave *H* with his two good causes of action set forth in 4(b)[1] and [2] above against *A*, the bribe-taker.

(b) *If the illegality is not a good defense against H: B would have to pay H and again A, the bribe-taker, profits from his crime or takes advantage of his own wrong and keeps the car. (Should B sue A, he would be denied access to the courts as a wrongdoer, since courts will ordinarily not assist a briber to recover bribe money paid.²⁴⁶)*

Contrast the following fraud in the inducement example:

7. Victim *V* gives *A* his personal check for \$25,000 made payable at *A*'s request to the order of "Cash" in exchange for an emerald ring which *A* has represented to be "worth over \$30,000." *A* transfers

245. See, e.g., *supra* note 16.

246. *Womack v. Maner*, *supra* note 234.

the check to *H* in return for a good used car which *H* delivers to *A*. *V* finds out from an appraiser that the ring is "a nice ring worth about \$500," and immediately stops payment on his check. *H* sues *V*. *V* shows he has a defense of fraud in the inducement. *H* establishes he is a holder in due course. *V* will have to pay *H*, since fraud in the inducement is a personal defense. *V*'s obligation to pay is voidable only, not void. However, *V* has a good cause of action against *A*. He is not denied access to the court because he is guilty of a crime, moral turpitude, or is trying to profit from his own crime or take advantage of his own wrong. As a victim of a fraud, in New York *V* is entitled either to ratify or rescind the voidable contract and, to fraud damages.²⁴⁷ Thus, the wrongdoer is not left with the fruits of his misdeed.²⁴⁸

In *McConnell v. Commonwealth*,²⁴⁹ had the alleged bribe to the producer's agent been in the form of McConnell's \$10,000 check eventually taken by a holder in due course, it is inconceivable to the writer that New York courts would not have held bribery to be a real defense, if McConnell had pleaded illegality in an action by the holder in due course.²⁵⁰

Because the Uniform Commercial Code has built in warranties on transfer and presentment,²⁵¹ the instrument issued to pay a bribe should be treated as truly void, coming from an illegally void, unratifiable two-party agreement, with no redeeming features between parties to a crime who are *in pari delicto*. Otherwise, for the first time, bribe-takers could accept instruments and, by merely negotiating to a holder in due course, the instrument would metamorphose into a legal obligation to commit a crime and pay a bribe.

If bribery is treated as a real defense, the illegal Bribery Contract is left to unwind, so that no money is paid out on it.

C. The Resulting Contract, of the type involved in *Bankers Trust*, is more complex. It is, however, the *raison d'être* of the Bribery Contract. In that sense, it is also the *corpus delicti* of the criminal bribe. The Resulting Contract is the bag of loot The Highwayman²⁵² sought

247. See N.Y. CIV. PRAC. LAW § 3002(e).

248. The opposite result occurs if bribery is not a real defense. See *supra* examples 4(a), 5(a), 6(b).

249. *Supra* note 28.

250. It is black letter law that one who has timely withdrawn from his wrongful act stands clear. McConnell would have been allowed to say he turned back from his wrongful intentions. If he so pleaded, the reason would not be important; the turning back is paramount. See *Aikman v. City of Wheeling*, *supra* note 230.

251. UCC § 3-417.

252. See *supra* note 231.

to have apportioned, or the body of the poisoned grandfather in *Riggs v. Palmer*²⁵³—the entity which will give the criminal the fruits of his crime.

Like a check given in payment of a bribe, the Resulting Contract is legal on its face. But under its gloss is a dough composed of breach of fiduciary duty, corruption, crime, some larceny, conspiracy, theft, betrayal, embezzlement, mendacity and "treason,"²⁵⁴ held together by the grease of the briber's lubrication payments and droplets of fraud. Its flavor is different from a transaction resulting from fraud in the inducement because of the existence of the Employment Contract. At the moment of making the criminal Bribery Contract, there simultaneously occurs a breach of fiduciary duty under the Employment Contract. Those two misdeeds then merge with the briber's crime. The Resulting Contract is thus born with two bad genes coming from the bribe-receiver, linked with the bad gene of the briber's crime. Is it void or voidable? *Sirkin*²⁵⁵ said it was void; *Bankers Trust*, voidable only, in the hands of a holder in due course.

Since a holder in due course, by definition, is a non-wrongdoer as to the obligation or transaction, that cannot be a reason for treating as voidable a bribery-induced contract which for over 75 years in New York has been condemned as illegally void.

As *Sirkin* observed, quoting Chief Justice Marshall: "Where the contract grows immediately out of, and is connected with, an illegal

253. *Supra* note 141.

254. *See supra* note 13.

255. *See supra* text corresponding to note 222. If it is void, how many void contracts are there floating around which parties abide by? The validity of the contract which McConnell allegedly bribed to get for Commonwealth was never questioned. Query as to what would have happened if Universal, whose agent was bribed, breached and pleaded the illegality.

In 1981, the *McConnell* case was invoked in a landlord's summary proceeding for some \$27,000 in unpaid rent under the lease of a Brooklyn warehouse. The tenant, Prudential Lines, Inc., pleaded the landlord had bribed its vice-president and board member to obtain the lease. It took the position, therefore, that although the lease had four more years to run, it should not have to pay anything and should be permitted to collect rents from its subtenant for the balance of the lease. The court disagreed, stating (1) neither *Sirkin* nor *McConnell* required the wrongdoer without compensation to provide goods or services *in futuro*; and (2) since the bribe-taker was their own agent, the parties were *in pari delicto*. As to where this would leave the parties, the court sidestepped. Prudential had adverted to pending actions it had commenced against the landlord in State and Federal courts. In view of the nature of summary proceedings, the court found Prudential should pay its rent and be relegated to having its commercial bribery problems resolved in the pending plenary actions. *McKeon v. Prudential Lines, Inc.*, 108 Misc.2d 873, 438 N.Y.S.2d 960 (N.Y. City Civ. Ct., Kings Co. 1981).

or immoral act, a court of justice will not lend its aid to enforce it. And if the contract be, in fact, one connected with the illegal transaction, and growing immediately out of it, though it be, in fact, a new contract, it is equally tainted by it."²⁵⁶

Under New York law, the bribery-induced contract has been held and appears to be truly, not loosely, illegally void. If it cannot be perceived as truly void, however, one might consider treating it like an instrument which is fraudulently taken prior to issuance. The "voidness" issue is thereby avoided. The defense in that case would be that because the instrument or assignment was bribery-induced, it was never voluntarily delivered or issued into commerce. Hence, there cannot be a holder in due course. The same occurs where the payee's signature on order paper is forged. There can be no holder, and hence no holder in due course.²⁵⁷ This principle has not impeded commerce; nor has the law that fraud in the execution or other illegally void transactions²⁵⁸ may be asserted as real defenses against a holder in due course.

Infancy, or such duress or incapacity as renders the obligation a nullity, and discharge in insolvency proceedings are all real defenses under UCC § 3-305.

Had *Bankers Trust* held bribery to be a real defense, the plaintiff banks would have had a good cause of action against their assignor for breach of the implied warranty that the assignment was valid and that there would be no defense which would impede their obtaining a judgment on it.²⁵⁹

Much of the mystique surrounding the sacred rights of a holder in due course has recently been dispelled. In consumer sales, even prior to the Federal Trade Commission Act mandates²⁶⁰ the holder in due course doctrine had ceded to the reality that consumer notes

256. 124 App. Div. 394, 108 N.Y.S. at 837.

257. "No party can ever be a holder of an order instrument stolen prior to indorsement by the owner of the instrument." WHITE AND SUMMERS, *supra* note 42 at 459.

258. For example, in Alabama a contract to issue stock in exchange for a promissory note was held truly void and it was found that "the illegality voids the instrument, even in the hands of a holder in due course." *General Beverages v. Rogers* 216 F.2d 413, 417 (10th Cir. 1954).

259. See *Friedman v. Schneider*, 238 Mo. App. 778, 186 S.W.2d 204 (1945); RESTATEMENT OF CONTRACTS 2d § 333(2); *Lonsdale v. Chesterfield*, 99 Wash.2d 353, 662 P.2d 385 (1983).

260. Thereunder, contracts must carry a ten-point bold face notice that the holder takes subject to the consumer's claims and defenses. See 16 C.F.R. § 433.2 (1976).

ordinarily did not course through the long and fast streams of commerce. They rarely went beyond their first transferee. Institutions like the plaintiffs in *Bankers Trust* which finance the purchase of non-consumer goods likewise tend to be first and last transferees. Hence, the overriding necessity for enveloping the holder in due course in his traditional protective mantel does not exist to the same degree under UCC § 9-206 as it does for negotiable instruments.

As one with the rights of an Article 3 holder in due course, however, it seems clear that the UCC § 9-206 assignee remains subject to any real illegality defense under UCC § 3-305, whether or not the assigned transaction is "void on its face."²⁶¹

CONCLUSION

Although a holder in due course may take a good title from a chain which has a thief in its links,²⁶² the bearer instrument which passed via a thief to the holder in due course in *Miller v. Race*²⁶³ was legally issued.²⁶⁴ It is only such legally issued instruments which the law need seek to protect. Instruments or agreements growing out of such criminality as would render them void require condemnation as a transaction—regardless of whether the plaintiff is a holder in due course. That is the *raison d'être* of the real illegality defense under UCC § 3-305.

In *Bankers Trust* the court was invited not to aid illegality but to condemn it.²⁶⁵ The court, however, sent its regrets. It may thus have left the impression that in New York bribery is not as bad—since it is not as illegally void—as usury or gambling, which are real defenses. Yet usury is a real defense even in instances where the amount charged does not attain the level of criminality; and gambling run by the state is not illegal. Hence, they do not appear to be more serious in nature than illegal commercial bribery.

From time to time, the legalization of capital punishment, and of various crimes such as the sale of addicting drugs, prostitution, pornography and adultery is discussed and considered. Usury and gambling are included in those discussions. Bribery is not. It cannot

261. See *Bankers Trust*, 599 F.2d at 491; and *supra* text corresponding to notes 175-91.

262. See *supra* note 42.

263. See *supra* note 49.

264. See *supra* note 52. *Contra* UCC § 3-207(1)(c) as to illegal negotiation.

265. *Selango United Rubber Estates, Ltd. v. Cradock*, 2 All. E.R. 1073 (1968), at text of decision corresponding to court's n.185.

be legalized precisely because its essence is antithetical to structure. It does to legal, commercial, or societal fiber what termites do to wood, consuming and destroying from within.²⁶⁶ If bribery is to be deterred, it is the decisions of civil courts which have great influence as a deterrent. Principals who are victimized by commercial bribery require, especially in a UCC § 9-206 case, as much, if not more protection from courts, as the holder in due course.

It may be true, as *Bankers Trust* opined, that its holding will not have "an appreciable effect on the frequency of commercial bribery."²⁶⁷ One could also speculate that had the court seen fit to hold the other way, such a decision might have had an appreciable effect on reducing commercial bribery—how much of an effect is impossible to guess, since all bribery arrangements are always made and kept completely shrouded in secrecy.

266. A handbook written by an 18th Century Ottoman statesman observed: "Bribery is the beginning and root of all illegality and tyranny, the source and fountain of every sort of disturbance and sedition, the most vast of evils, and the greatest of calamities. It is the mine of corruption than which there is nothing whatever more calamitous . . ." JACOBY, NEHEMKIS AND EELLS, *supra* note 1, at 254 n.4; DRISCOLL, *supra* note 1.

267. 599 F.2d at 493.

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