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## A SUMMARY OF ARTICLES 3 AND 4 AND THEIR IMPACT IN NEW YORK\*

*Norman Penney*†

This article on articles 3 (Commercial Paper) and 4 (Bank Deposits and Collections) is written for publication in a New York oriented symposium on the Uniform Commercial Code. Symposia of this type are directed primarily toward practitioners who must cope with a new and far-reaching statute. Page limitations impel the writer to cast such a paper in the form of a survey highlighting the more significant innovations. The literature abounds in such articles, annotated to the law of one state or another.<sup>1</sup> This article will not vary significantly from the familiar format. Assuming that the draftsmen devoted considerable time to organizing and ordering the parts and sections of the Code being discussed, this article will deal with each part consecutively, discussing those provisions worthy of mention in a paper of this character. The

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<sup>1</sup> Andrews, "Should Article 3 of the Uniform Commercial Code Be Adopted in Ohio?" 14 Ohio St. L.J. 32 (1953); Finkelstein, "Article Three—Commercial Paper," 22 Tenn. L. Rev. 812 (1953); Arnesen, "Illinois Uniform Commercial Code: A Comparison of Article III—Commercial Paper—and the NIL," 50 Ill. B.J. 216 (1961); Hill, "How the Adoption of the Uniform Commercial Code Would Affect the Law of Negotiable Instruments in Oregon," 32 Ore. L. Rev. 97 (1953); Jacobs, "The Effect of the Adoption of the Proposed Uniform Commercial Code on the Negotiable Instruments Law of Louisiana—Rights of a Holder," 15 La. L. Rev. 419 (1955); Leary, "Commercial Paper: Article III," 16 Ark. L. Rev. 33 (1961); Marsh, "How the Adoption of the Uniform Commercial Code Would Affect the Law of Negotiable Instruments in Oregon," 34 Ore. L. Rev. 33 (1954); Re, "Some Effects of the Uniform Commercial Code on New York Law—Symposium," 26 St. John's L. Rev. 1, 26 (1951); Steinheimer, "Impact of the Commercial Code on Liability of Parties to Negotiable Instruments in Michigan," 53 Mich. L. Rev. 171 (1954); Tyler, "How the Adoption of the Uniform Commercial Code Would Affect the Law of Negotiable Instruments in Oregon," 33 Ore. L. Rev. 41 (1953).

Clarke, "Bank Deposits and Collections: Article IV, Letters of Credit: Article V," 16 Ark. L. Rev. 45 (1961); Dehner, "Article Four—Bank Deposits and Collections," 22 Tenn. L. Rev. 832 (1953); Iuthwaite, "Bank Deposits and Collections Under the Uniform Commercial Code," 40 Mich. St. B.J. 17 (August 1961); Love, "How the Adoption of the Uniform Commercial Code Would Affect the Law of Bank Deposits and Collections in Oregon," 32 Ore. L. Rev. 25, 156, 288 (1952-53); Sneed & Morrison, "Bank Collections—A Comparative Study," 29 Texas L. Rev. 713 (1951); Trumbull, "Bank Deposits and Collections in Illinois Under the Proposed Uniform Commercial Code," 55 Nw. U.L. Rev. 253 (1960); Wilson, "How the Adoption of the Uniform Commercial Code Would Affect the Law of Bank Deposits and Collections in Oregon," 30 Ore. L. Rev. 359 (1951); Comment, 18 Wash. & Lee L. Rev. 350 (1961).

Bibliographies containing additional law review commentaries may be found in Goodrich & Wolkin, *The Story of the American Law Institute, 1923-1961* at 48-66 (1961) and throughout the annotations to articles 3 and 4 in 1 *Uniform Commercial Code (Unif. Laws Ann.)* 359-568; 2 *Uniform Commercial Code (Unif. Laws Ann.)* 1-100 (1962).

reader may follow the discussion by turning the pages of the new statute as he proceeds through the article. The author has attempted to annotate the discussion to present law, particularly the law of New York. References are also made to the most helpful periodical and textual literature in the field. Readers wishing to pursue any particular problem in depth should consult the vast body of discussion and reference material found in the Reports of the New York Law Revision Commission.<sup>2</sup> Though some of this material is obsolete because of changes made in the 1957 official text, the use of the New York Annotations to the Commercial Code<sup>3</sup> as a supplement to the Law Revision Commission studies should make the commentaries and references extremely valuable. New York is unique in having such a thorough body of transitional literature.

### ARTICLE 3

Article 3 is largely a modern-day revision of the Negotiable Instruments Law. There are relatively few changes. In many instances the language employed in the Negotiable Instruments Law is used verbatim. In most cases negotiable instruments problems will be resolved in exactly the same manner as they were under the N.I.L. Article 3 will produce relatively few redrafting projects.

One might well question the necessity of revising the N.I.L. The Negotiable Instruments Law has received its fair share of criticism. This first effort at uniform legislation was subjected to heavy attack almost from the outset<sup>4</sup> and has accumulated a great body of criticism since the turn of the century.<sup>5</sup> The character of the criticisms prompting a revision of the N.I.L. fall into four general categories. First, the Nego-

<sup>2</sup> Mulvaney, "Checklist of New York Law Revision Commission Materials on the Uniform Commercial Code," 53 L. Lib. J. 29 (1960).

<sup>3</sup> Hogan & Penney, "Annotations of the Uniform Commercial Code to the Statutory and Decisional Law of New York State," New York Annotations to Uniform Commercial Code and Report of Commission on Uniform Commercial Code (N.Y. Comm'n on Uniform State Laws 1961). See also N.Y. Comm'n on Uniform State Laws, Supplementary Report on the Uniform Commercial Code (1962) (describing and commenting upon the variations in the New York enactment of the UCC); Comm'n on Uniform State Laws of the Ass'n of the Bar of the City of New York, Report on the Uniform Commercial Code (1962) (assessing the extent to which the UCC (1958) meets the recommendations and criticisms of the New York Law Revision Commission).

<sup>4</sup> The earliest and most influential critic was Dean Ames of the Harvard Law School, a party to the famous "Ames-Brewster Controversy." McKeehan, "The Negotiable Instruments Law (A Review of the Ames-Brewster Controversy)" (pts. 1-3), 50 Am. L. Register 437, 499, 561 (1902).

<sup>5</sup> See, e.g., Beutel, "The Negotiable Instruments Act Should Not Be Amended," 80 U. Pa. L. Rev. 368 (1932); Brannan, "Some Necessary Amendments of the Negotiable Instruments Law," 26 Harv. L. Rev. 493, 588 (1913); Britton, "Proposed Amendments to the Uniform Negotiable Instruments Law," 22 Ill. L. Rev. 815 (1928); Hening, "The Uniform Negotiable Instruments Law. Is It Producing Uniformity and Certainty in the Law Merchant?" 59 U. Pa. L. Rev. 471, 532 (1911). A host of other articles containing commentaries and criticisms may be found in the bibliography to the fourth edition of Professor Britton's casebook, Britton, Cases on Bills and Notes xix-xxxi (4th ed. 1951).

tiable Instruments Law has suffered by virtue of strained judicial interpretations attempting to bring too many types of instruments within the statute.<sup>6</sup> Second, the Negotiable Instruments Law has been criticized as poorly organized.<sup>7</sup> There are some antiquated provisions which have never been utilized.<sup>8</sup> Third, the courts of the various states have taken different approaches in interpreting certain sections of the N.I.L.<sup>9</sup> and many legislatures have adopted nonuniform amendments<sup>10</sup> so that the law as now applied is anything but uniform. Finally, there are many technical flaws or open questions arising under the N.I.L. which the Code draftsmen have sought to correct and answer. Among these questions, are:

1. Is it possible to convert bearer paper to order paper by indorsement?<sup>11</sup>
2. Are both acceptance and payment within the finality rule of *Price v. Neal*?<sup>12</sup>
3. May a payee be a holder in due course?<sup>13</sup>

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<sup>6</sup> Hawkland, *Cases on Bills and Notes* 25-28 (1956); Cosway, "Innovations in Articles Three and Four of the Uniform Commercial Code," 16 *Law & Contemp. Prob.* 284, 285-86 (1951); Leary, "Some Clarifications in the Law of Commercial Paper Under the Proposed Uniform Commercial Code," 97 *U. Pa. L. Rev.* 354, 355-57 (1949).

<sup>7</sup> Sutherland, "Article 3—Commercial Paper," *Uniform Commercial Code of Massachusetts* 153, 156-57 (1958).

<sup>8</sup> N.I.L. §§ 161-77 (N.Y. Negotiable Instr. Law §§ 280-306) (acceptance and payment for honor). A search for cases annotated to these sections will readily demonstrate the few times that these provisions have been involved in commercial litigation. The writer recognizes, but questions, the argument that this is merely indicative of the clarity and comprehensiveness of these sections.

<sup>9</sup> Cosway, *supra* note 6, at 287; Hening, *supra* note 5.

<sup>10</sup> Brannan, *Negotiable Instruments Law* 110-208 (Beutel 7th ed. 1948) (statutory variations are annotated to the portion of this book setting forth "The Original Negotiable Instruments Act and Commissioners' Notes").

<sup>11</sup> This is the dilemma produced by the conflict between N.I.L. §§ 9(5) and 40. See Britton, *Bills and Notes* 146-49 (2d ed. 1961). Leary, *supra* note 6, at 380-81 (1949); See discussion of UCC § 3-204 in text following note 58, *infra*.

<sup>12</sup> Britton, *supra* note 11, at 380-81. Aigler, "Two Significant Recent Decisions in Negotiable Instruments," 2 *Ariz. L. Rev.* 1, 7-16 (1960). See discussion of UCC § 3-418 in text following note 174, *infra*.

<sup>13</sup> Aigler, "Payees as Holders in Due Course," 36 *Yale L.J.* 608 (1927). Britton, "Holder in Due Course—A Comparison of the Provisions of the Negotiable Instruments Law with those of Article 3 of the Proposed Uniform Commercial Code," 49 *Nw. U.L. Rev.* 417, 442-43 (1954); Britton, "The Payee As A Holder In Due Course," 1 *U. Chi. L. Rev.* 728 (1934); Feezer, "May the Payee of a Negotiable Instrument Be A Holder in Due Course?" 9 *Minn. L. Rev.* 101 (1925); Palmer, "Negotiable Instruments Under the Uniform Commercial Code," 48 *Mich. L. Rev.* 255, 276 (1950).

UCC § 3-302(2) clearly permits payees to qualify as holders in due course. Although the Court of Appeals has not passed directly on this point, the Code provision seems to accord with the weight of lower court authority in New York. *Zanetti v. Malanga*, 19 *Misc. 2d* 862, 190 *N.Y.S.2d* 185 (Sup. Ct. Sullivan County 1959); *South Shore Sec. Co. v. Goode*, 5 *Misc. 2d* 972, 162 *N.Y.S.2d* 962 (Sup. Ct. Kings County 1957); *Yokohama Specie Bank v. Millbert Importing Corp.*, 182 *Misc. 2d* 281, 44 *N.Y.S.2d* 71 (Sup. Ct. New York County 1943); *First Nat'l Bank & Trust Co. v. Conzo*, 169 *Misc. 2d* 268, 7 *N.Y.S.2d* 334 (Sup. Ct. Chemung County 1938). *Contra*, *Alpert v. City Motor Sales*, 194 *Misc. 2d* 479 (Albany City Ct. 1949).

4. Shouldn't a rule governing the imposter payee problem be codified?<sup>14</sup>

5. Why should a bank suffer a loss on an undelivered incomplete instrument in the case where a customer has signed a blank check and left it on his desk top?<sup>15</sup>

*Part 1: Form and Interpretation*

*A. Types of Paper Covered and Excluded (3-103, 3-104)*

Article 3 is limited to commercial paper. Bank collections, letters of credit, investment securities and secured transactions are dealt with elsewhere.<sup>16</sup> Although comment 5 to section 3-104 makes clear that the Code does not require the presence of particular words in instruments to make them negotiable, the elimination of N.I.L. section 10<sup>17</sup> and the language of 3-104(1)(b)<sup>18</sup> do appear to make the Code more stringent than the N.I.L. on the question of negotiability.

*B. Negotiability: Unconditionality (3-105, 3-112)*

Under present law a note payable only out of a particular fund is non-negotiable;<sup>19</sup> no exception is made in the case of instruments issued by governmental agencies or units.<sup>20</sup> The Code creates an exception to the decisional law rule as to governmental paper and conforms with statutes conferring negotiability upon certain municipal obligations.<sup>21</sup> Many of

<sup>14</sup> Palmer, *supra* note 13, at 284-88; Britton, *supra* note 11, at 440-47. See discussion of UCC § 3-405 in text following note 126, *infra*.

<sup>15</sup> Britton, *supra* note 11, at 204-09. See discussion of UCC § 3-115 in text following note 39, *infra*. Britton, "Defenses, Claims of Ownership and Equities—A Comparison of the Provisions of the Negotiable Instruments Law with Corresponding Provisions of Article 3 of the Proposed Commercial Code," 7 *Hastings L.J.* 1, 11-12 (1955); Cosway, *supra* note 6, at 268; Palmer, *supra* note 13, at 265-67.

<sup>16</sup> These are dealt with in articles 4, 5, 8, and 9, respectively.

<sup>17</sup> N.I.L. § 10 (N.Y. Negotiable Instr. Law § 29) Terms, when sufficient.

The instrument need not follow the language of this chapter, but any terms are sufficient which clearly indicate an intention to conform to the requirements hereof.

<sup>18</sup> Section 3-104(1)(b) states:

Any writing to be a negotiable instrument with this Article must . . . (b) contain an unconditional promise or order to pay a sum certain in money and no other promise, order, obligation or power given by the maker or drawer except as authorized by this Article; and . . .

<sup>19</sup> N.I.L. § 3 (N.Y. Negotiable Instr. Law § 22). Accord, UCC § 3-105(2)(b).

<sup>20</sup> *Bull v. Sims*, 23 N.Y. 570 (1861) (pre-N.I.L. case assessing negotiability of municipal warrants by same standards as applied to ordinary makers). *Kohn v. Sacramento Elec. Gas & Ry.*, 168 Cal. 1, 141 Pac. 626 (1914); cf. *County Comm'r v. Bank of Gastonia*, 157 N.C. 191, 72 S.E. 996 (1911). *Hawkland*, *supra* note 6, at 35-36. See also the critical comment with respect to greater liability being assumed by indorsers of such instruments in *Hill*, *supra* note 1, at 112; *Benton v. Freedom Township Supervisors*, 118 Pa. Super. 229, 178 Atl. 520 (1935); *Bank of California, N.A. v. National City Co.*, 141 Wash. 243, 251 Pac. 561 (1926). See also *Manker v. American Sav. Bank & Trust Co.*, 131 Wash. 430, 230 Pac. 406 (1924).

<sup>21</sup> See, e.g., N.Y. Local Fin. Law § 161.00 and the many sections of the N.Y. Pub. Auth. Law cited in the N.Y. annotation to this subsection, *Hogan & Penney*, *supra* note 3, at 94-95.

the instruments issued by governmental entities would probably qualify as "investment securities" under article 8.<sup>22</sup> The Code also broadens the present rule affording negotiability to instruments payable only out of the assets of unincorporated associations by permitting payment to be limited to the assets of a partnership, trust or estate.<sup>23</sup>

In addition to continuing the rule permitting a statement of the transaction giving rise to the instrument, the Code permits inclusion of some of the common provisions found in so-called "long form" notes. The most important of these new provisions are found in the subsection permitting reference to a separate agreement.<sup>24</sup> In New York this provision has been further extended by the addition of language permitting reference to a "separate agreement for rights as to prepayment or acceleration."<sup>25</sup> This section describing when a promise or order is unconditional also includes a specific subsection stipulating that language in instruments providing for maturity in accordance with or "as per" certain transactions does not render them unconditional.<sup>26</sup> A later subsection denies negotiability to instruments made "subject to or governed by" other agreements.<sup>27</sup> While these provisions have been criticized as overly concerned with detail, the empirical and arbitrary criteria have been supported as the only realistic way to sort out or distinguish phrases rendering promises either conditional or unconditional.<sup>28</sup>

In conjunction with section 3-105, one should read the section setting forth the "terms and omissions not affecting negotiability."<sup>29</sup> Of par-

<sup>22</sup> See the broad, functional definition of a "security" in UCC § 8-102(1)(a).

<sup>23</sup> UCC § 3-105(1)(h). In accord as to instruments payable only out of the assets of an unincorporated association is *Hibbs v. Brown*, 190 N.Y. 167, 82 N.E. 1108 (1907), 8 Colum. L. Rev. 215, 216, 233 (1908). Permitting payment to be limited to the assets of a partnership, trust or estate may change the law of New York. See *Hibbs v. Brown*, supra, at 178, 82 N.E. at 1111, 1112, distinguishing partnerships from unincorporated associations. See also *Schmittler v. Simon*, 101 N.Y. 554, 5 N.E. 452 (1886), which implies that a draft payable only out of the assets of an estate is nonnegotiable. See generally, Britton, supra note 11, at 36-37.

<sup>24</sup> UCC § 3-105(1)(c).

<sup>25</sup> N.Y. Sess. Laws 1962, ch. 553 § 3-105(1)(c) (effective Sept. 27, 1964).

(1) A promise or order otherwise unconditional is not made conditional by the fact that the instrument . . .

(c) refers to or states that it arises out of a separate agreement *or refers to a separate agreement for rights as to prepayment or acceleration . . .* (Italicized portion added in N.Y.)

For a brief discussion of this and other New York variations, see Penney, "New York Revisits the Code—Some Variations in the New York Enactment of the Uniform Commercial Code," 62 Colum. L. Rev. 992, 994-96 (1962).

<sup>26</sup> UCC § 3-105(1)(h). This seems to accord with present law. *Public Nat'l Bank & Trust Co. v. Garcia Sugars Corp.*, 173 Misc. 364, 16 N.Y.S.2d 914 (Sup. Ct. N.Y. County 1939), aff'd, 259 App. Div. 878, 20 N.Y.S.2d 1015, motion for leave to appeal denied, 259 App. Div. 1001, 21 N.Y.S.2d 395 (1st Dep't 1940), aff'd, 285 N.Y. 661, 33 N.E.2d 867 (1941); *Hawkland*, supra note 6, at 18-19. See Note, 32 Harv. L. Rev. 560, 565 (1919).

<sup>27</sup> UCC § 3-105(2)(a). Accord, *Old Colony Trust Co. v. Stumpel*, 247 N.Y. 538, 161 N.E. 173 (1928). For further cases see *Hawkland*, supra note 6, at 18-19.

<sup>28</sup> Compare *Hawkland*, supra note 6, at 18-19 (approving), with *Cosway*, supra note 6, at 295 (critical).

<sup>29</sup> UCC § 3-112.

ticular importance in the latter section is the provision that "the negotiability of an instrument is not affected by . . . a promise or power to maintain or protect collateral or give additional collateral. . . ."<sup>30</sup> This new provision, reflecting the dictum of *First Nat'l Bank v. Blackman*,<sup>31</sup> has been further modified in New York by the addition of language permitting covenants to "furnish financial information or to do or refrain from doing any other act for the protection of the obligation. . . ." This added language was apparently designed to support covenants to maintain working capital, to restrict dividends, to provide a sinking fund, not to raise salaries, and the like.<sup>32</sup>

### C. *Negotiability: Definite Time* (3-109)

There are two notable provisions relating to the requirement that a negotiable instrument be payable at a definite time. N.I.L. section 4(3),<sup>33</sup> permits instruments payable at death or at a fixed period after death<sup>34</sup> to qualify as payable at a determinable future time. The Code reverses this rule.<sup>35</sup> Secondly, and more important, the Code solves the much litigated question of when instruments subject to acceleration are negotiable.<sup>36</sup> A note subject to acceleration at the sole option of the holder, as for example upon the holder's "deeming himself insecure," is nevertheless negotiable; an instrument may be subject to "any acceleration."<sup>37</sup> The

<sup>30</sup> UCC § 3-112(1)(c).

<sup>31</sup> 249 N.Y. 322, 164 N.E. 113 (1928).

<sup>32</sup> This amendment represents a partial retreat from the attempt of the Code draftsmen to "bring the note back . . . to its original concept of being . . . 'a courier without luggage.'" 1954 N.Y. Law Rev. Comm'n Rep. 506 (testimony of Professor Mentschikoff in Law Revision Commission hearings). This same subsection was changed as a result of the deliberations between the 1952 and the 1957 official text in order to meet the very same points advanced by the New York Clearing House Association in the 1954 hearings. Compare 1954 Law Rev. Comm'n Rep., 505 with ALI Recommendations on UCC 93 (1956) [hereinafter cited as 1956 Recommendations]. See also Penney, *supra* note 25, at 996. The banking lawyers, however, apparently felt that the 1957 draft did not go far enough. Although the liberalized New York variation may accord with present New York law this does not justify adoption of this variation on a national basis unless the practice and demands elsewhere require this additional "luggage." Many instruments with this type of provision will probably be controlled by article 8. See UCC § 8-102(1)(a).

<sup>33</sup> N.I.L. § 4 (N.Y. Negotiable Instr. Law § (23)). Determinable Future Time: What Constitutes.

An instrument is payable at a determinable future time, within the meaning of this act, which is expressed to be payable . . .

(3) On or at a fixed period after the occurrence of a specified event, which is certain to happen, though the time of happening be uncertain. . . .

<sup>34</sup> *Hegeman v. Moon*, 131 N.Y. 462, 30 N.E. 487 (1892); *Carnwright v. Gray*, 127 N.Y. 92, 27 N.E. 835 (1891). See, however, dictum in *Kerr v. Smith*, 156 App. Div. 807, 142 N.Y. Supp. 57 (1st Dep't 1913). See *Cosway*, *supra* note 6, at 296.

<sup>35</sup> UCC § 3-109(2):

An instrument which by its terms is otherwise payable only upon an act or event uncertain as to time of occurrence is not payable at a definite time even though the act or event has occurred.

<sup>36</sup> See *Palmer*, *supra* note 13, at 262-64; *Britton*, "Formal Requisites of Negotiability—the Negotiable Instruments Law Compared With the Proposed Uniform Commercial Code," 26 *Rocky Mt. L. Rev.* 1, 11-15 (1953); *Chafee*, "Acceleration Provisions in Time Paper," 32 *Harv. L. Rev.* 747, 775 (1919); *Note*, 101 *U. Pa. L. Rev.* 835 (1953).

<sup>37</sup> UCC § 3-109(1)(c).

maker of a note is protected from an arbitrary and unreasonable acceleration by the provision in section 1-208, which requires that the holder "in good faith believe[s] that the prospect of payment or performance is impaired."<sup>38</sup>

#### D. *Incomplete Undelivered Instruments* (3-115)

As mentioned above, negotiable instruments students have long been troubled that nondelivery and unauthorized completion together constitute a real defense.<sup>39</sup> Certainly the remote holder in due course cannot better protect himself in the taking of such paper and has no fewer equities than a holder of delivered but unauthorizedly completed paper or nondelivered but properly completed paper. The drawer of a check signed in blank and left where it can be easily pilfered should not be protected as against the payor bank which innocently pays a stolen, completed and cashed check. The Code reverses the N.I.L. and case law by making nondelivery of an incomplete instrument a personal defense.<sup>40</sup> This is the more equitable rule and is extended to payor banks by a comparable provision in article 4.<sup>41</sup> At the suggestion of the New York Law Revision Commission, a qualification to the counterpart rule in article 4 was added denying protection to a bank with notice that the completion was improper.<sup>42</sup>

<sup>38</sup> As so limited, the Code appears to accord with present New York Law. N.Y. Negotiable Instr. Law § 23(1)(2)(3); *Higgins v. Hocking Valley R.R.*, 188 App. Div. 684, 177 N.Y. Supp. 444 (1st Dep't 1919); *Lincoln Nat'l Bank & Trust Co. v. Marsh*, 24 N.Y.S.2d 281 (Sup. Ct. Onondaga County 1940); *Glide v. Sheridan*, 173 Misc. 542, 18 N.Y.S.2d 339 (Sup. Ct. N.Y. County 1939). But see *Old Colony Trust Co. v. Stumpel*, 126 Misc. 375, 379, 213 N.Y. Supp. 536, 539-40, aff'd, 219 App. Div. 771, 220 N.Y. Supp. 893 (1st Dep't 1927), aff'd on other grounds 247 N.Y. 538, 161 N.E. 173 (1928) (that an instrument accelerable upon the holder's deeming himself insecure is nonnegotiable). See generally Britton, supra note 11, at 63-67, and cases cited therein.

<sup>39</sup> N.I.L. § 15 (N.Y. Negotiable Instr. Law § 34) provides:

Where an incomplete instrument has not been delivered it will not, if completed and negotiated, without authority, be a valid contract in the hands of any holder, as against any person whose signature was placed thereon before delivery.

See *Holzman, Cohen & Co. v. Teague*, 172 App. Div. 75, 158 N.Y. Supp. 211 (1st Dep't 1916); *Linick v. A. J. Nutting & Co.*, 140 App. Div. 265, 125 N.Y. Supp. 93 (2d Dep't 1910). For criticisms of this rule and citations to many cases, see Britton, supra note 15, at 11-12. *Palmer*, supra note 13, at 265-67; *Sutherland*, "Article 3—Logic, Experience and Negotiable Paper," 1952 Wis. L. Rev. 230, 245-46. See generally, Britton, supra note 11, at 204-09; *Brady, Bank Checks 70-71* (Bailey ed. 1962), reprinted from 78 *Banking L.J.* 737, 750-53 (1961).

<sup>40</sup> UCC § 3-115(2). See also UCC § 3-305(2) which provides that a holder in due course takes free of all but certain enumerated defenses (not including incompleteness combined with failure of delivery), and UCC § 3-407(3) which permits a subsequent holder in due course to enforce as completed, an incomplete instrument which has been completed.

<sup>41</sup> UCC § 4-401(2)(b).

<sup>42</sup> UCC § 4-401: When Bank May Charge Customers Account.

(2) A bank which in good faith makes payment to a holder may charge the indicated account of its customer according to . . .

(b) the tenor of his completed item, even though the bank *knows the item has been completed unless the bank has notice that the completion was improper.*

The italicized portion was changed in 1956 Recommendations to meet a suggestion made



### E. *Miscellaneous*

A few minor changes wrought by part I of article 3 require brief mention. The Code effects a change in present law by permitting alternative drawees.<sup>43</sup> Alternative drawees are occasionally named in dividend and insurance checks as a matter of commercial convenience. The Code also contains a new provision permitting domestic negotiable instruments to be payable in foreign currency.<sup>44</sup> New York varied the official text of this provision by permitting the satisfaction of even instruments payable only in a specified foreign currency by "payment of that number of dollars which the stated foreign currency will purchase at the buying sight rate for that currency."<sup>45</sup> In addition the Code contains a new section providing that an instrument "payable through" a bank designates that institution as collecting bank to make presentment though not itself authorizing that bank to pay.<sup>46</sup> Finally, part 2 contains a novel section concerning the accrual of a cause of action.<sup>47</sup> While according generally with decisional law,<sup>48</sup> this section changes the time for accrual of a cause of action against a drawer of a draft or indorser of any instrument. Under the Code<sup>49</sup> the statute of limitation runs from notice of dishonor or other demand rather than from dishonor as is the present rule.<sup>50</sup> A change in the New York enactment of this Code provision was made to avoid the possibility that interest might run on cashier's checks or demand certificates of deposit from their dates.<sup>51</sup>

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by the New York Law Revision Commission. 1956 Recommendations *supra* note 32, at 159; 1956 N.Y. Law Rev. Comm'n Rep. 430 (app. IV); 1955 N.Y. Law Rev. Comm'n Rep. 1478 (Mulvaney, Study of U.C.C. § 4-401).

<sup>43</sup> UCC § 3-102(1)(b). *Contra*, N.I.L. § 128 (N.Y. Negotiable Instr. Law § 212). See in support of this change made by the Code, Ogden, *Negotiable Instruments* 105 (5th ed. 1947); Cosway, *supra* note 6, at 293.

<sup>44</sup> UCC § 3-107. *Contra*, *Thompson v. Sloan*, 23 Wend. 71 (Sup. Ct. Erie County 1840) (instrument payable in foreign currency and to be paid in the United States not payable in money and hence nonnegotiable). In accord with the Code, see *Incitti v. Ferrante*, 12 N.J. Misc. 840, 175 Atl. 908 (C.P. Bergen County 1933). See generally Britton, *supra* note 11, at 72-79; Britton, *supra* note 15, at 19-21; Cosway, *supra* note 6, at 295-96; Oliphant, "The Theory of Money in the Law of Commercial Instruments," 29 *Yale L.J.* 606, 619-24 (1920); Perkins, "May a Promissory Note Be Payable in Foreign Money?" 5 *Iowa L. Bull.* 209 (1920).

<sup>45</sup> For a further description and criticism of this New York variation see Penney, *supra* note 25, at 997-98.

<sup>46</sup> UCC § 3-120. No New York cases on point were found. For cases in other jurisdictions and criticism of the distinction between "payable through" and "payable at," see Brannan, *supra* note 10, at 1022-23.

<sup>47</sup> UCC § 3-122.

<sup>48</sup> See N.Y. annotations, Hogan & Penney, *supra* note 3, at 104-05.

<sup>49</sup> UCC § 3-122(3).

<sup>50</sup> N.Y. Civ. Prac. Act § 15 provides that the cause of action against drawer or indorser is computed from dishonor ("the time when the right to make the demand is complete"), not from notice of dishonor or other demand. See also N.Y. Civ. Prac. Law & Rules § 206a (effective Sept. 1, 1963).

<sup>51</sup> Section 3-122(4)(a). The phrase "acceptor or other primary obligor of a demand instrument" was substituted for "of a demand note" in the New York enactment. Comparable changes have been made in Connecticut, Illinois, Massachusetts and Rhode Island. 1 *Uniform Commercial Code (U.L.A.)* 409-10 (1962).

*Part 2: Transfer and Negotiation*

Although generally in accord with the present law as to terminology and operative rules,<sup>52</sup> this part contains three notable changes or clarifications.

A. *Reacquisition and "Shelter"*<sup>53</sup> (3-201)

The Code provision spelling out the rights vested in the transferee of an instrument may serve to clear up the conflict of authorities as to the reacquisition by an indorsee who has knowledge of a fraud in a transfer prior to his original acquisition. The law is clearly settled that a reacquiring payee, who had knowledge of the fraud originally, may not acquire the rights of a later holder in due course, even though the payee was not a participant.<sup>54</sup> There is a split of authority in New York as to the effect of reacquisition by an indorsee who with knowledge of the fraud negotiated to a holder in due course and later reacquired. In *Horan v. Mason*,<sup>55</sup> the Second Department held such a reacquirer to be a holder in due course. The Fourth Department reached a contrary result.<sup>56</sup> The Code resolves the conflict in favor of the Fourth Department and against the reacquiring indorsee.<sup>57</sup> The new enactment eliminates the opportunity of persons knowingly to acquire fraud-tainted instruments and improve their position by channeling such paper through holders in due course.

B. *Special Indorsement and Bearer Paper* (3-204)

The Code resolves the much discussed problem of the conflict between N.I.L. sections 9(5) and 40.<sup>58</sup> The question is whether an instrument

<sup>52</sup> See generally Britton, "Transfers and Negotiations Under the Negotiable Instruments Law and Article 3 of the Uniform Commercial Code," 32 Texas L. Rev. 153 (1953).

<sup>53</sup> The "shelter" principle, permitting a transferee with notice to enjoy the rights of a holder in due course without notice, from whom the former took, is described in *Aragon Coffee Co. v. Rogers*, 105 Va. 51, 52 S.E. 843 (1906). The court stated that a purchaser from a holder in due course without notice "is entitled to stand in the latter's shoes and take shelter under his good faith." 105 Va. at 54, 52 S.E. at 844.

<sup>54</sup> See N.I.L. § 58 (N.Y. Negotiable Instr. Law § 97). *Gruntal v. National Sur. Co.*, 254 N.Y. 468, 173 N.E. 682 (1930).

<sup>55</sup> 141 App. Div. 89, 125 N.Y. Supp. 668 (2d Dep't 1910).

<sup>56</sup> *Harter v. People's Bank*, 221 App. Div. 122, 223 N.Y. Supp. 118 (4th Dep't 1927).

<sup>57</sup> UCC § 3-201(1). For a general discussion of this Code provision, see Britton, *supra* note 13, 443-46; Cosway, "Innovations in Articles Three and Four of the Uniform Commercial Code," 16 Law & Contemp. Prob. 284, 299-300 (1951); Palmer, *supra* note 13, at 273-74. For discussion of prior law and collection of cases thereunder, see Britton, *supra* note 11, 320-27, 689-98. See also Chafee, "The Reacquisition of a Negotiable Instrument by a Prior Party," 21 Colum. L. Rev. 538 (1921).

<sup>58</sup> N.I.L. § 9 (N.Y. Negotiable Instr. Law § 28). When payable to bearer.  
The instrument is payable to bearer

5. When the only or last indorsement is an indorsement in blank.

N.I.L. § 40 (N.Y. Negotiable Instr. Law § 70). Indorsement of instrument payable to bearer.

payable to bearer either originally in the designation of the payee or subsequently by indorsement can be controlled by a later indorsement. The majority of courts have held paper originally payable to bearer as capable of further negotiation by delivery alone, regardless of subsequent indorsement.<sup>59</sup> There is some authority for the view that the N.I.L. did not affect the common law rule that an instrument indorsed in blank continues negotiable by delivery notwithstanding any special indorsement.<sup>60</sup> This view has been much criticized, however, and leading commentators have persuasively argued that in such cases the latest or special indorsement controls.<sup>61</sup> The Code abandons the "once bearer, always bearer" rule altogether and gives effect to the last indorsement in all cases.<sup>62</sup> Under the Code, even paper originally payable to bearer will require a further indorsement for negotiation when indorsed specially. The Code rule permitting subsequent holders of the instrument to control its negotiability is preferable.

### C. Restrictive Indorsements (3-205, 3-206)

At the instance of the New York Law Revision Commission, the Code draftsmen included a provision defining restrictive indorsement in the 1956 Recommendations.<sup>63</sup> This definition includes, with slightly different emphasis, the indorsements formerly described in N.I.L. section 36 but with the addition of the indorsement described in N.I.L. section 39 as "conditional."<sup>64</sup> The definitional section treats collection indorsements

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Where an instrument, payable to bearer, is indorsed specially, it may nevertheless be further negotiated by delivery; but the person indorsing specially is liable as indorser to only such holders as make title through his indorsement.

For general discussion and collection of cases see Britton, *supra* note 11, at 146-49.

<sup>59</sup> See cases collected in Britton, *supra* note 11, at 147. There are no New York cases directly in point. In *Irving Nat'l Bank v. Alley*, 79 N.Y. 536 (1880), under a statute preceding the N.I.L., a note payable to the maker was deemed to have the same effect as if payable to bearer, and was valid though negotiated without the indorsement of such maker.

<sup>60</sup> *Parker v. Roberts*, 243 Mass. 174, 137 N.E. 295 (1922) (N.I.L. sections not mentioned), 23 Colum. L. Rev. 488 (1923); 5 Ill. L.Q. 247 (1923).

<sup>61</sup> Brannan, *Negotiable Instruments Law* 628-31 (Beutel 7th ed. 1948); McKeehan, "The Negotiable Instruments Law," 50 *Am. L. Reg.* 437, 461 (1902).

<sup>62</sup> UCC § 3-204(1). For commentary on the Code provision see Palmer, *supra* note 13, at 274-75; Leary, "Some Clarifications in the Law of Commercial Paper Under the Proposed Uniform Commercial Code," 97 *U. Pa. L. Rev.* 354, 380-81 (1949). This problem was one of those involved in an earlier discussion of proposed changes to the N.I.L. See Turner, "Revision of the Negotiable Instruments Law," 38 *Yale L.J.* 25, 34-37 (1928); Turner, "A Factual Analysis of Certain Proposed Amendments to the Negotiable Instruments Law," 38 *Yale L.J.* 1047, 1050-53 (1929).

<sup>63</sup> 1956 Recommendations, *supra* note 32, at 99; 1956 Law Revision Comm'n Rep. 406 (app. IV); 1955 Law Revision Comm'n Rep. 866-68.

<sup>64</sup> UCC § 3-205. Restrictive Indorsements.

An indorsement is restrictive which either

- (a) is conditional; or
- (b) purports to prohibit further transfer of the instrument; or
- (c) includes the words "for collection," "for deposit," "pay any bank," or like terms signifying a purpose of deposit or collection; or
- (d) otherwise states that it is for the benefit or use of the indorser or of another person.

and trust indorsements separately.<sup>65</sup> The major change from the N.I.L. is the reversal of the rule inferred from N.I.L. section 47,<sup>66</sup> that an instrument once restrictively indorsed can no longer be negotiated.<sup>67</sup> In the case of collection indorsements, the Code provision recognizes the unreasonableness of imposing restrictions upon banks in the chain of collection after the first bank taker. Accordingly the present law is reversed as to intermediary banks in the collection process;<sup>68</sup> such intermediary banks are neither given notice nor otherwise affected by the restrictive indorsement.<sup>69</sup> Similarly whereas the first taker under a trust indorsement is bound to apply any value given by him for or on the security of an instrument consistently with the indorsement, a later holder for value is neither given notice nor otherwise affected by the restrictive indorsement unless he has knowledge of a breach of trust.<sup>70</sup>

### *Part 3: Rights of a Holder*

Generally, the treatment of the holder and the holder in due course follows the scheme of the N.I.L. and utilizes the same or similar terminology. The definition of "holder in due course"<sup>71</sup> enlarges upon N.I.L. section 52<sup>72</sup> by incorporating generally accepted decisional law

See Brady, Bank Checks 95-101 (Bailey 3rd ed. 1962), reprinted from 78 Banking L.J. 193-99 (1961).

<sup>65</sup> Compare subsection (a) and (c) with subsection (d) in § 3-205, supra note 64. This permits separate treatment of the two types of indorsement in § 3-206 as to the effect of restrictive indorsements. See Hawkland, Commercial Paper 110-11 (1959).

<sup>66</sup> N.I.L. § 47 (N.Y. Negotiable Instr. Law § 77). Continuation of negotiable character. An instrument negotiable in its origin continues to be negotiable until it has been restrictively indorsed or discharged by payment or otherwise.

See also N.I.L. §§ 36, 37 (N.Y. Negotiable Instr. Law §§ 66, 67).

<sup>67</sup> See Chafee, "Remarks on Restrictive Indorsements," 58 Harv. L. Rev. 1182, 1186, 1193 (1945); Leary, supra note 62, at 381-87 (commenting on the treatment of restrictive indorsements in the 1952 draft of the UCC); Note, 52 Yale L.J. 890 (1943).

<sup>68</sup> Soma v. Handrulis, 277 N.Y. 223, 14 N.E.2d 46 (1938) (intermediary bank held accountable on a check indorsed "for deposit").

<sup>69</sup> UCC § 3-206(2).

<sup>70</sup> UCC § 3-206(4).

<sup>71</sup> UCC § 3-302. Holder in Due Course.

- (1) 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.
- (2) A payee may be a holder in due course.
- (3) A holder does not become a holder in due course of an instrument:
  - (a) by purchase of it at judicial sale or by taking it under legal process; or
  - (b) by acquiring it in taking over an estate; or
  - (c) by purchasing it as part of a bulk transaction not in regular course of business of the transferor.
- (4) A purchaser of a limited interest can be a holder in due course only to the extent of the interest purchased.

<sup>72</sup> N.I.L. § 52 (N.Y. Negotiable Instr. Law § 91). What constitutes a holder in due course. A holder in due course is a holder who has taken the instrument under the following conditions:

1. That it is complete and regular upon its face;

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rules.<sup>73</sup> Paralleling the format of the N.I.L., the section on holders in due course is followed by separate sections elaborating upon value and notice.<sup>74</sup> These latter sections, and the section dealing with burden of proof, warrant some discussion.

#### A. *Value* (3-303)

The Code provision defining value accords generally with present statutory and decisional law.<sup>75</sup> Although the N.I.L. rule, equating value with "any consideration sufficient to support a simple contract,"<sup>76</sup> is carried forward by the Code provision, the new language spells out the distinction between consideration and value.<sup>77</sup> The Code requires that the agreed consideration shall actually have been given.<sup>78</sup> In accord with present law, an antecedent debt may constitute value.<sup>79</sup> Under present decisional law, although an executory promise is sufficient consideration to support an obligation embodied in an instrument,<sup>80</sup> such a promise does not constitute value so as to qualify a transferee as a holder in due course.<sup>81</sup> Also to be noted is the article 4 section on bank credit as value.<sup>82</sup> This section permits a bank giving "credit available for withdrawal . . . whether or not the credit is drawn upon" to qualify as a holder in due course to the extent of the credit given.

The Code definition of value also includes the giving of a negotiable instrument.<sup>83</sup> Although this accords with the rule in some jurisdictions,<sup>84</sup>

2. That he became the holder of it before it was overdue, and without notice that had been previously dishonored, if such was the fact;
3. That he took it in good faith and for value;
4. That at the time it was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it.

<sup>73</sup> See UCC § 3-302(2), (3), (4), and Hogan & Penney, "Annotations of the Uniform Commercial Code to the Statutory and Decisional Law of New York State," New York Annotations to Uniform Commercial Code and Report of Commission on Uniform Commercial Code, 110-11 (N.Y. Comm'n on Uniform State Laws 1961); Palmer, "Negotiable Instruments Under the Uniform Commercial Code," 48 Mich. L. Rev. 255, 276-78 (1950); Hawland, *supra* note 65, at 78 (1959).

<sup>74</sup> See UCC §§ 3-303, 3-304, respectively.

<sup>75</sup> N.I.L. §§ 25, 26, 27, 54 (N.Y. Negotiable Instr. Law §§ 51, 52, 53, 93 respectively); Hogan & Penney, *supra* note 73, at 111-12; Britton, "Holder in Due Course—A Comparison of the Provisions of the Negotiable Instruments Law With Those of Article 3 of the Proposed Uniform Commercial Code," 49 Nw. U.L. Rev. 417, 418-21 (1954). Cosway, *supra* note 57, at 301; Palmer, *supra* note 73, at 278-79.

<sup>76</sup> N.I.L. § 25 (N.Y. Negotiable Instr. Law § 51).

<sup>77</sup> UCC § 3-303(a) and comment 2.

<sup>78</sup> UCC § 3-303(a).

<sup>79</sup> Compare UCC § 3-303(a) and (b) with N.I.L. §§ 25, 54 (N.Y. Negotiable Instr. Law §§ 51, 93).

<sup>80</sup> *Finberg v. DeGoode*, 199 App. Div. 177, 191 N.Y. Supp. 390 (2d Dep't 1921).

<sup>81</sup> *Citizens' State Bank v. Cowles*, 180 N.Y. 346, 73 N.E. 33 (1905). For a full discussion of "value" and "consideration" under the N.I.L. and citations to cases in other jurisdictions, see Britton, *Handbook of the Law of Bills and Notes* at 211-44 (2d ed. 1961).

<sup>82</sup> UCC § 4-209. See also UCC §§ 1-201(44)(a), 4-208. See Britton, *supra* note 81, at 235; Note, 57 Yale L.J. 1419 (1948).

<sup>83</sup> UCC § 3-303(c).

<sup>84</sup> See cases cited in Britton, *supra* note 81, at 241-42; Annot., 69 A.L.R. 408, 409-12 (1930).

others require that the instrument given pass into the hands of a bona fide holder or be paid.<sup>85</sup>

### B. *Notice and Good Faith* (3-304)

The Code continues the present rule that to qualify as a holder in due course the holder must take the paper in good faith.<sup>86</sup> The Code presently contains a perplexing definition of the term "good faith."<sup>87</sup> What does "honesty in fact in the conduct or transaction concerned" mean in the purchase of a note or the cashing of a check by a bank? The removal of the language enlarging upon the "good faith" requirement in the 1952 draft was intended to make clear the retention of the subjective standard of good faith in article 3.<sup>88</sup> The objective standard, exemplified by the case of *Gill v. Cubitt*,<sup>89</sup> was clearly rejected in the 1956 Recommendations.<sup>90</sup> Notwithstanding the rationale of the draftsmen, the term "honesty in fact" promises to tantalize lawyers and judges attempting to define "honesty" in the commercial paper context. This

<sup>85</sup> *Ibid.*

Although no case has been found directly on point, New York has been cited as among those jurisdictions which do not regard the giving of a negotiable instrument in exchange for another as the giving of-value so as to constitute either party to the exchange a holder in due course. It is further stated that where the instrument passes into the hands of a bona fide holder or is paid, the holder of the other instrument will nevertheless be recognized as a holder in due course. See Annot., 69 A.L.R. 408, 412 (1930), citing *Mayer v. Heidelbach*, 123 N.Y. 332, 25 N.E. 416 (1890); *Bacon v. Holloway*, 2 E.D. Smith 159 68 ALR 408, 412 (1853); *Baruch v. Buckley*, 167 App. Div. 113, 151 N.Y. Supp. 853 (1st Dep't 1915). These and other cases, however, all appear to be distinguishable on the point at issue. If, however, a transfer to a bona fide holder or payment is required in New York, this subparagraph will change the rule.

<sup>86</sup> UCC § 3-302(1)(b). See note 70, *supra*. For general discussion see Brady, *supra* note 64, at 119-28, reprinted from 78 *Banking L.J.* 461, 463-72 (1961).

<sup>87</sup> UCC § 1-201. General Definitions.

Subject to additional definitions contained in the subsequent Articles of this Act which are applicable to specific Articles or Parts thereof, and unless the context otherwise requires, in this Act:

(19) "good faith" means honesty in fact in the conduct or transaction concerned.

See Braucher, "The Legislative History of the Uniform Commercial Code," 58 *Colum. L. Rev.* 798, 812-14 (1958); Note, 23 *U. Pitt. L. Rev.* 754 (1962) (remarking upon the variety of uses of the term in different parts of the Code and suggesting that the courts will have to furnish definitions on a case by case basis).

<sup>88</sup> 1956 Recommendations, *supra* note 32, at 102-03. An excellent analysis of the concepts of "good faith" and "bad faith" in the law of negotiable instruments may be found in 1955 *Law Revision Comm'n Rep.* 903-07. See also Britton, *supra* note 81, at 244-49; Britton, *supra* note 75, at 430-32; Palmer, *supra* note 73, at 279-82.

<sup>89</sup> 3 B. & C. 466, 107 *Eng. Rep.* 806 (K.B. 1824), discussed in Britton, *supra* note 81, at 244-46.

<sup>90</sup> 1956 Recommendations, *supra* note 32, at 102-03. The Code leaves the doctrine of "forgotten notice" expressly untouched. See § 1-201(25) ("The time and circumstances under which a notice or notification may cease to be effective are not determined by this Act."). The New York Court of Appeals recently refused to permit a bank to escape liability on the basis of the doctrine in a rather exceptional fact situation. *First Nat'l Bank v. Fazzari*, 10 N.Y.2d 394, 179 N.E.2d 493, 223 N.Y.S.2d 483 (1961), 26 *Albany L. Rev.* 344 (1962); 47 *Cornell L.Q.* 670 (1962); 8 *N.Y.L.F.* 339 (1962); 42 *B.U.L. Rev.* 388 (1962).

Compare UCC § 1-201(25) and (27), with *Restatement (Second), Agency* §§ 268, 272, 278 (1958).

would seem particularly difficult in applying the term to a financial institution.

Lawyers should be particularly aware of the New York amendment to this Code section on notice.<sup>91</sup> Added was a subsection continuing the "bad faith" test of notice, found in N.I.L. section 56,<sup>92</sup> but abandoned by the Code draftsmen. The same New York subsection contains a special rule concerning the qualification of organizations as holders in due course. If such an organization acting as purchaser maintains "reasonable routines for communicating significant information," it is chargeable with knowledge only when the individual conducting the transaction on its behalf has knowledge. This patchwork amendment seems destined to cause difficulty.<sup>93</sup>

Although "good faith" has been, and is in the Code, combined with the requirement that paper be taken without notice of defects, the latter requirement is spelled out in a separate subparagraph of the Code definition of a "holder in due course";<sup>94</sup> a separate hurdle is therefore presented. A new and elaborate section has been drafted to combine and restate the various rules on notice to a purchaser presently reflected in a series of N.I.L. sections and common law rules.<sup>95</sup> These rules are continued with very few changes. The continuance of the N.I.L. rule, in somewhat liberalized form, that only a person taking complete and regular paper may qualify as a holder in due course has been greatly criticized.<sup>96</sup> Particularly questioned has been the continuation of the

<sup>91</sup> N.Y. Sess. Laws, ch. 553, § 3-304 (effective Sept. 27, 1964):

(7) In any event, to constitute notice of a claim or defense, the purchaser must have knowledge of the claim or defense or knowledge of such facts that his action in taking the instrument amounts to bad faith. If the purchaser is an organization and maintains within the organization reasonable routines for communicating significant information to the appropriate part of the organization apparently concerned, the individual conducting the transaction on behalf of the purchaser must have the knowledge.

See discussion of this variation in Penney, "New York Revisits the Code—Some Variations in the New York Enactment of the Uniform Commercial Code," 62 Colum. L. Rev. 992, 998-1000 (1962). A corresponding New York variation for investment securities may be found in N.Y. Sess. Laws, ch. 553, § 8-304(3) (effective Sept. 24, 1964).

<sup>92</sup> N.Y. Negotiable Instr. Law § 95. This section is discussed by Professor Pasley in his Analysis of Section 3-302(1), 1955 Law Revision Comm'n Rep. 903-07.

The remainder of N.Y. Negotiable Instr. Law § 95, peculiar to New York, relating to the drawing, making, endorsing, cashing, or depositing of corporate checks by or to corporate officers or agents, has been transferred to N.Y. Banking Law § 9. N.Y. Sess. Laws 1962, ch. 552.

<sup>93</sup> This amendment, prompted by the criticisms of the New York Clearing House Association, originated as a suggestion that UCC § 1-201(25) and (27) be amended. Penney, *supra* note 91, at 998-99. Amendments to article 1 were apparently avoided because of the possibility of broad ramifications throughout the Code. The writer understands, however, that the New York variations have prompted renewed discussion of amending UCC § 1-201(27) using much of the language as added to §§ 3-304 and 8-304 in New York, but with some changes designed to meet criticisms of the New York legislation.

<sup>94</sup> See subsections (1)(b) and (c) UCC § 3-302, quoted in note 71, *supra*.

<sup>95</sup> UCC § 3-304. See Hogan and Penney, *supra* note 73, at 112-14.

<sup>96</sup> Compare UCC §§ 3-302(1)(c), 3-304(1)(a) with N.I.L. § 52(1) (N.Y. Negotiable Instr. Law § 91(1)). See criticism in Hawland, *supra* note 65, at 81-82; Britton, *supra* note 75,

rule depriving a purchaser of his position as a holder in due course not only with respect to defenses and claims associated with the incompleteness or alteration, but also as to defenses and claims having nothing to do with these "defects."<sup>97</sup> By way of rebuttal, to require a prudent purchaser to question virtually every aspect of visibly altered paper does not seem too unreasonable.

A specific subparagraph of the Code section on notice furnishes rules for determining when a purchaser has notice that an instrument is overdue.<sup>98</sup> Notice that paper is overdue disqualifies the purchaser as a holder in due course.<sup>99</sup> Under present case law, a purchaser after maturity may not qualify as a holder in due course, and although maturity may be subject to acceleration, the absence of knowledge of the fact of acceleration is of no consequence.<sup>100</sup> Under the Code, that paper is overdue in fact does not prevent a person from qualifying as a holder in due course, but rather reason to know that the instrument is overdue either as to any part of the principal or by reason of acceleration is sufficient notice.<sup>101</sup>

Among the N.I.L. sections dealing with the holder in due course, the "stale check" section,<sup>102</sup> disqualifying persons taking demand instruments "an unreasonable time after issue," has long been difficult to interpret. A "reasonable time" has varied with circumstances and the character of the instrument.<sup>103</sup> Even with the check there has been great difficulty in fixing the time period. Presently the period is somewhere between eleven days<sup>104</sup> and twenty-seven months.<sup>105</sup> The Code provides some certainty by creating a presumption that a domestic check thirty days old is stale.<sup>106</sup>

### C. *Burden of Proof* (3-307)

The Code section governing the burden of establishing signatures, defenses and due course holding, is essentially a restatement of N.I.L. section

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at 433-35. See also Brady, *supra* note 64, at 128, reprinted from 78 *Banking L.J.* 461, 472 (1961).

<sup>97</sup> See Britton, *supra* note 75, at 433-35.

<sup>98</sup> UCC § 3-304(3). See Brady, *supra* note 64, at 129, reprinted from 78 *Banking L.J.* 461, 473 (1961).

<sup>99</sup> UCC § 3-302(1)(c).

<sup>100</sup> *Northhampton Nat'l Bank v. Kidder*, 106 N.Y. 221, 12 N.E. 577 (1887). For discussion of this problem, see Britton, *supra* note 75, at 424-26.

<sup>101</sup> UCC § 3-304(3)(a), (b).

<sup>102</sup> N.I.L. § 53 (N.Y. Negotiable Instr. Law § 92).

<sup>103</sup> N.I.L. § 193 (N.Y. Negotiable Instr. Law § 4). For citations to cases, see Britton, *supra* note 81, at 303-05; Annots., 23 A.L.R. 1205 (1923); 60 A.L.R. 649 (1929).

<sup>104</sup> *Springer v. Erdman*, 125 Misc. 112, 210 N.Y. Supp. 224 (Sup. Ct. App. Term 1st Dep't 1925).

<sup>105</sup> *Goldberg v. Manufacturers Trust Co.*, 199 Misc. 167, 102 N.Y.S.2d 144 (N.Y. Munic. Ct. 1951).

<sup>106</sup> UCC § 3-304(3)(c). "A reasonable time for a check drawn and payable within the states and territories of the United States and the District of Columbia is presumed to be thirty days." See also UCC § 4-406 and text following note 347, *infra*.



59.<sup>107</sup> Some clarification and minor changes for the better are accomplished. The Code<sup>108</sup> reverses the common law rule permitting presentation of evidence as to circumstances attending the alleged making of notes sued upon under a general denial.<sup>109</sup> In addition the Code provides that *any* defense shifts the burden of proof.<sup>110</sup> The shifting of the burden where want of consideration is shown reverses the present rule.<sup>111</sup> The expression "it is shown that" in subsection 3-307(3) was reinstated between the 1952 draft and the 1956 Recommendations to continue the law interpreting N.I.L. section 59 and to make clear that no change in the quantum of evidence was intended.<sup>112</sup> The Code provision has been praised for its comprehensiveness, clearer diction, better organization and the anticipation and resolution of many questions.<sup>113</sup>

### ➤ Part 4: Liability of Parties

#### A. General Statement

Part 4 contains substantial material not found in the Negotiable Instruments Law; new provisions are found with respect to impostors,<sup>114</sup> the contract of guarantor,<sup>115</sup> the warranties on presentment and transfer,<sup>116</sup> and the conversion of negotiable instruments.<sup>117</sup> In addition this part clarifies several problems arising under present law and makes several policy changes in N.I.L. rules.

#### B. Signatures (3-403, -404)

The Code includes "other representatives" with agents able to bind others by their signatures.<sup>118</sup> In view of the case law including a wide variety of representatives within the meaning of the term agent,<sup>119</sup> probably no change in the present law is made.

<sup>107</sup> N.Y. Negotiable Instr. Law § 98.

<sup>108</sup> UCC § 3-307(1).

<sup>109</sup> *Hoffstaedter v. Carlton Auto Supplies Co.*, 203 App. Div. 494, 196 N.Y. Supp. 577 (1st Dep't 1922). Cf. N.Y.C. Municipal Court Code § 92. On the burden of proof in negotiable instruments cases generally, see Britton, *supra* note 81, at 249-69; Britton, *supra* note 75, at 446-50.

<sup>110</sup> UCC § 3-307(3). See Cosway, "Innovations in Articles Three and Four of the Uniform Commercial Code," 16 *Law & Contemp. Prob.* 284, 289-90 (1951); Note, 10 *Mercer L. Rev.* 211 (1958).

<sup>111</sup> *Mitchell v. Baldwin*, 88 App. Div. 265, 84 N.Y.S. 1043, (3d Dep't 1903).

<sup>112</sup> 1956 Recommendations, *supra* note 32, at 107.

<sup>113</sup> Carrington, "Banking, Commercial Paper and Investment Securities Under the Uniform Commercial Code," 14 *Wyo. L.J.* 198, 204-05 (1960).

<sup>114</sup> UCC § 3-405.

<sup>115</sup> UCC § 3-416.

<sup>116</sup> UCC § 3-417.

<sup>117</sup> UCC § 3-419.

<sup>118</sup> UCC § 3-403(1).

<sup>119</sup> See, e.g., *Megowan v. Peterson*, 173 N.Y. 1, 65 N.E. 738 (1902) ("trustee" for creditors); *Hellawell v. Garrett Busch & Son, Inc.*, 157 Misc. 805, 285 N.Y. Supp. 717 (Sup. Ct. Nassau County), modified, 248 App. Div. 737, 290 N.Y. Supp. 143 (2d Dep't 1936) (executrix). See also N.I.L. § 20 (N.Y. Negotiable Instr. Law § 39), referring to the consequences of signing "for or on behalf of a principal, or in a representative capacity."

As the Official Comments indicate,<sup>120</sup> the Code adopts the majority view admitting parol evidence against a payee to show that a signature was written in a representative capacity where the name of the person represented is disclosed but the fact of representation is not stated.<sup>121</sup> Also adopted is the New York and minority view admitting parol evidence for this purpose where the fact of representation is disclosed but not the name of the principal.<sup>122</sup> The 1952 draft was different on both of these points; the present language first appeared in the 1956 Recommendations in response to criticism from the New York Law Revision Commission.<sup>123</sup>

The Code adopts the rule of *New Georgia Nat'l Bank v. J. & G. Lippmann*<sup>124</sup> in rendering an unauthorized signature binding on the unauthorized signer in favor of any person who in good faith pays the instrument or takes for value. The Code seems to extend the rule of the *Lippmann* case to forgery as well.<sup>125</sup>

### C. *Impostors and Fictitious Payees* (3-405)

The Code takes an entirely fresh approach in dealing with the problem of impostors and fictitious payees. Under common law<sup>126</sup> and the N.I.L.,<sup>127</sup> paper knowingly made payable to the order of a fictitious person by the drawer is deemed bearer paper and is capable of negotiation by delivery alone. The impostor case is not treated under the N.I.L. Under common law rules, however, where the "intent" of the drawer to make the instrument payable to the impostor is established, an instrument is deemed payable to the order of the impostor and able to be endorsed by him in his assumed name.<sup>128</sup> New York has been more strict than other jurisdictions in requiring a prior course of face-to-face deal-

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<sup>120</sup> UCC § 3-403, comment 3.

<sup>121</sup> *Central Bank v. Gleason*, 206 App. Div. 28, 200 N.Y. Supp. 384 (4th Dep't 1923); *Hoffstaedter v. Carlton Auto Supplies Co.*, 203 App. Div. 494, 196 N.Y. Supp. 577 (1st Dep't 1922). For cases in other jurisdictions see Britton, *supra* note 81, at 487-88, n.4.

<sup>122</sup> *Megowan v. Peterson*, 173 N.Y. 1, 5, 65 N.E. 738, 739 (1902), noted 3 Colum. L. Rev. 211 (1903). See UCC § 3-403(2)(b). For cases in other jurisdictions, predominantly *contra*, see Britton, *supra* note 81, at 487, nn.1, 2. See also Whitney, *Modern Commercial Practices* 395-403 (1958) (apparently commenting upon the 1952 text which differed on these points).

<sup>123</sup> 1956 Recommendations, *supra* note 32, at 107-08; 1956 N.Y. Law Revision Comm'n Rep. 408-09; 1955 N.Y. Law Revision Comm'n in Rep. 985-94.

<sup>124</sup> 249 N.Y. 307, 164 N.E. 108 (1928).

<sup>125</sup> UCC § 3-404(1). See Beutel, "Comparison of the Proposed Commercial Code, Article 3, and the Negotiable Instruments Law," 30 Neb. L. Rev. 531, 552-53 (1951).

<sup>126</sup> Britton, *supra* note 81, at 425-40.

<sup>127</sup> N.I.L. § 9(3) (N.Y. Negotiable Instr. Law § 28(3)).

<sup>128</sup> Abel, "The Impostor Payee: or, Rhode Island Was Right," (pts. 1 and 2). 1940 Wis. L. Rev. 161, 362; Aigler, "When is a Payee an 'Imposter'?" 2 Ariz. L. Rev. 78 (1960). See also Britton, *supra* note 81, at 440-47; Palmer, "Negotiable Instruments Under the Uniform Commercial Code," 48 Mich. L. Rev. 255, 284-88. For collection of cases, Annot., 81 A.L.R.2d 1365 (1962).

ings to identify the impostor as the object of the transferor's dominant intent.<sup>129</sup>

When organizations are involved as drawers the problem is further compounded. Two patterns are common in this context: first, a fraudulent agent, authorized to draw checks in the name of his employer, issues checks to "dummy" payees, intending to obtain the proceeds; second, the fraudulent agent who has no authority to draw checks supplies names to another agent who draws the checks in reliance on the names submitted.<sup>130</sup> In the first case, the loss is placed on the drawer where proper authority for the agent can be shown.<sup>131</sup> In the second, sometimes called the "padded payroll" case, the innocent drawee bank almost always bears the loss.<sup>132</sup> The "fictitious" character of the payee is unknown to the person technically labelled as the drawer and the "impostor rule" often does not apply. In an effort to meet these problems, several states have adopted the Uniform Fictitious Payee Act.<sup>133</sup> These statutes make an instrument payable to bearer

"when it is payable to the order of a fictitious person, or a nonexistent person, or an existing person not intended to have any interest in it, and any such fact was known to the person making it so payable, or known to his employee or other agent who supplied the name of such payee. . . ."

The statute reverses the common law rule which refused to charge the maker with the larcenous knowledge of his employee.<sup>134</sup> The knowledge of the fraudulent employee supplying the name of the fictitious person is imputed to the employer-drawer.

The Code deals with both the impostor and fictitious payee problems in the same section<sup>135</sup> and accomplishes substantially the same result as the

<sup>129</sup> *Cohen v. Lincoln Sav. Bank*, 275 N.Y. 399, 407-12, 10 N.E.2d 457, 461-63 (1937) (prior course of dealings required for purpose of identifying impostor as object of transferor's "dominant intent"). For cases requiring "face to face" dealings, see *International Aircraft Trading Co. v. Manufacturers Trust Co.*, 297 N.Y. 285, 291, 79 N.E.2d 249, 251 (1948) (dicta); *Halsey v. Bank of New York & Trust Co.*, 270 N.Y. 134, 139, 200 N.E. 671, 673 (1936); *American Sur. Co. v. Empire Trust Co.*, 262 N.Y. 181, 186 N.E. 436 (1933); *Mercantile Nat'l Bank v. Silverman*, 148 App. Div. 1, 132 N.Y.S. 1017 (1st Dep't 1911), aff'd mem., 210 N.Y. 567, 104 N.E. 1134 (1914).

<sup>130</sup> These two types of cases are discussed and analyzed in Britton, "Defenses, Claims of Ownership and Equities—A Comparison of the Provisions of the Negotiable Instruments Law with corresponding provisions of Article 3 of the proposed Commercial Code," 7 *Hastings L.J.* 1, 27-31 (1955). See also *Hawkland*, *Commercial Paper* 67-69 (1955); *Farnsworth*, "Insurance Against Check Forgery," 60 *Colum. L. Rev.* 284, 305-09 (1960); *Sutherland*, "Article 3—Logic, Experience and Negotiable Paper," 1952 *Wis. L. Rev.* 230, 241-45.

<sup>131</sup> See Britton, *Bills and Notes* 429-32 (2d ed. 1961).

<sup>132</sup> *Id.* at 432-34.

<sup>133</sup> The amendment is at variance with N.I.L. § 9(3) and was adopted in 1960 as an amendment to N.Y. Negotiable Instr. Law § 28(3). For a list of other states that have adopted the act, see 2 *Paton, Digest* 1867 (Supp. 1942). See also Note, 35 *St. John's L. Rev.* 390 (1961).

<sup>134</sup> See Britton; *supra* note 131 at 432-34; *Swift & Co. v. Bankers Trust Co.*, 280 N.Y. 135, 19 N.E.2d 992 (1939); *City of N.Y. v. Bronx County Trust Co.*, 261 N.Y. 64, 184 N.E. 495 (1933).

<sup>135</sup> Section 3-405. Impostors; Signature in Name of Payee.

Uniform Fictitious Payee Act with some differences. First, rather than require the indorsement of the impostor to characterize the paper as bearer in form, the Code permits an effective indorsement by any person. This comes very close to treating the paper as bearer in form. Indorsement may apparently be supplied by a stranger to the fraud. Although anyone can indorse, the Code requires that the instrument be issued to either the impostor or his confederate in the name of a payee. Some difficulty may arise when a fraudulent scheme involves "issuance" to some innocent person who is employed to deal with the drawer, unless that person can be brought within the meaning of the term "confederate."<sup>136</sup> No distinction is made as to imposture through the mails, thereby departing from the New York rule requiring face-to-face dealings.<sup>137</sup> A prior course of dealing to identify the impostor as the object of the transferor's "dominant intent" is no longer required.

#### D. *The Negligent Drawer and the Rule of Young v. Grote* (3-406)

Adopting the rule of *Young v. Grote*,<sup>138</sup> the common law of the United States holds that the drawer of a check owes a duty to the drawee bank not to act so carelessly as to contribute to alteration.<sup>139</sup> The rule has been typically applied to penalize drawers who negligently leave blank spaces. The Code extends the common law rule protecting drawee banks in such cases to holders in due course.<sup>140</sup> The Law Revision Commission successfully advocated the addition of a requirement that the drawee pay the instrument in good faith and in accordance with reasonable commercial standards to enjoy protection under this provision;<sup>141</sup> the contributory negligence of a drawee will therefore defeat his rights. In this instance the commercial banking group was understandably willing to leave the "reasonable commercial standards test" in the Code. To be considered in the context of the drawer's duties is section 4-406 of article

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- (1) An indorsement by any person in the name of a named payee is effective if
- (a) an impostor by use of the mails or otherwise has induced the maker or drawer to issue the instrument to him or his confederate in the name of the payee; or
  - (b) a person signing as or on behalf of a maker or drawer intends the payee to have no interest in the instrument; or
  - (c) an agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest.

<sup>136</sup> Professor Farnsworth raises this question with the case of *Russell v. Second Nat'l Bank*, 136 N.J.L. 270, 55 A.2d 211 (Ct. Err. & App. 1947). Farnsworth, *Cases on Negotiable Instruments* 212-13 (1959).

<sup>137</sup> See note 129, *supra*.

<sup>138</sup> 4 Bing. 253, 130 Eng. Rep. 764 (C.P. 1827).

<sup>139</sup> See Britton, *supra* note 131, at 662-70.

<sup>140</sup> Under present law holders in due course have no recourse and are not protected as to checks or other instruments negligently prepared by drawers or makers. *National Exch. Bank v. Lester*, 194 N.Y. 461, 87 N.E. 779 (1909). For cases in other jurisdictions, see Britton *supra* note 131, at 665 nn.6, 8, 9, at 666 n.10.

<sup>141</sup> 1956 Recommendations; *supra* note 32, at 109; 1956 N.Y. Law Revision Comm'n Rep. 409; 1955 N.Y. Law Revision Comm'n Rep. 1009-13. See also Britton, *supra* note 130, at 18-20; Sutherland, *supra* note 130, at 245-48.

4 spelling out the drawer's duty to examine his return vouchers or statements.<sup>142</sup>

### E. Alterations (3-407)

Under present law any alteration, even one innocently made, avoids the instrument.<sup>143</sup> No exception is made for alterations made by strangers, sometimes described as spoliatio; nor is any distinction made for the nonfraudulent but material alteration.<sup>144</sup> The Code codifies some of the decisional law<sup>145</sup> ameliorating the harshness of the N.I.L. provision; under the Code no alteration discharges any party unless made by the holder and unless it is both fraudulent and material.<sup>146</sup> Spoliatio does not "avoid" the instrument.<sup>147</sup> The Code continues the N.I.L. rule permitting a subsequent holder in due course in every instance to enforce the instrument according to its original tenor.<sup>148</sup> As to instruments completed after leaving the hands of the drawer, a holder in due course may enforce the instrument as completed.<sup>149</sup>

### F. Acceptance (3-410, -411, -412)

A series of minor changes is made in three sections dealing with acceptance and certification. The Code requires that the acceptance be on the draft,<sup>150</sup> thereby eliminating the collateral, which includes both the virtual or extrinsic, acceptance.<sup>151</sup> The Code abandons any distinction between the various kinds of qualified acceptances found in the N.I.L.<sup>152</sup> The constructive acceptance arising from N.I.L. sections 136 and 137 is abandoned.<sup>153</sup> The rule of *Wachtel v. Rosen*,<sup>154</sup> denying any obligation

<sup>142</sup> See text following note 358, *infra*.

<sup>143</sup> N.I.L. §§ 124, 125 (N.Y. Negotiable Instr. Law §§ 205, 206).

<sup>144</sup> Brady, Bank Checks 444-46 (Bailey ed. 1962).

<sup>145</sup> See Britton, *supra* note 131 at 660-61.

<sup>146</sup> UCC § 3-407(2). Accord as to alteration by a stranger, see *Gleason v. Hamilton*, 138 N.Y. 353, 34 N.E. 283 (1893) (alteration of a mortgage). As to "fraudulent" alterations see *Booth v. Powers*, 56 N.Y. 22, 29-30 (1874); *Oltarsh v. Turf Broadway, Inc.*, 12 Misc. 2d 984, 986, 175 N.Y.S.2d 714, 717 (N.Y. City Ct. 1958).

<sup>147</sup> UCC § 3-407(2).

<sup>148</sup> Compare UCC § 3-407(3), with N.I.L. § 124 (N.Y. Negotiable Instr. Law § 205).

<sup>149</sup> UCC § 3-407(3). The separate rule in N.I.L. § 15 (N.Y. Negotiable Instr. Law § 34), as to incomplete undelivered instruments is reversed. See also *Linick v. A. J. Nutting & Co.*, 140 App. Div. 265, 125 N.Y. Supp. 93 (2d Dep't 1910); *Holzman, Cohen & Co. v. Teague*, 172 App. Div. 75, 158 N.Y. Supp. 211 (1st Dep't 1916). See text following note 38, *supra*.

<sup>150</sup> UCC § 3-410(1).

<sup>151</sup> See N.I.L. §§ 133, 134 (N.Y. Negotiable Instr. Law §§ 221, 222). See discussion in Britton, *supra* note 131, at 505-06; Palmer, *supra* note 128, at 289-90.

<sup>152</sup> Compare UCC § 3-412(1) with N.I.L. § 141 (N.Y. Negotiable Instr. Law § 229). See also N.I.L. §§ 139, 140, 132. N.Y. Negotiable Instr. Law §§ 220, 227, 228. See discussion in Britton, *supra* note 131, at 503-04.

<sup>153</sup> See N.Y. Negotiable Instr. Law §§ 224, 225. The New York law on constructive acceptance is unclear. Compare *State Bank v. Weiss*, 46 Misc. 93, 91 N.Y. Supp. 276 (Sup. Ct. App. Term 1904), with *Matteson v. Moulton*, 79 N.Y. 627 (1880). See generally Britton *supra* note 131, at 515-17.

<sup>154</sup> 249 N.Y. 386, 164 N.E. 326 (1928). See discussion in Britton, *supra* note 131, at 517-20.

of banks to certify checks, has been codified.<sup>155</sup> Finally, the Code requires that prior parties affirmatively assent to an acceptance varying the terms of a draft; otherwise such prior parties are discharged.<sup>156</sup>

#### G. *Accommodation Parties* (3-415)

The official text of the Code imposes no warranty liability upon accommodation parties.<sup>157</sup> The liability of such a party is determined by the "capacity in which he has signed."<sup>158</sup> The New York enactment of the Code reverses this Code policy limiting warranty liability to vendors and retains the substance of the warranty obligation imposed in sections 65 and 66 of the N.I.L.<sup>159</sup> The apparent purpose of the New York amendment was to avoid the possible loss of immediate recourse when a "breach" is discovered prior to the maturity of time paper.<sup>160</sup>

#### H. *Warranties on Presentment and Transfer* (3-417)

The Code imposes warranty liability in article 3 only upon those who "obtain payment or acceptance," "prior transferors" and persons "who transfer an instrument and receive consideration."<sup>161</sup> Irregular indorsers are thereby excluded as are accommodation parties, other than in New York.<sup>162</sup> The most notable change is the extension of warranties to good-faith acceptors and payors<sup>163</sup> as well as to subsequent holders "who take the instrument in good faith."<sup>164</sup> Statutory warranty liability did not run to payor banks under the N.I.L.<sup>165</sup> although various common law theories<sup>166</sup> and other devices<sup>167</sup> were employed to accomplish the same end. Paralleling the N.I.L. the Code provides for: warranties of title,<sup>168</sup>

<sup>155</sup> UCC § 3-411(2).

<sup>156</sup> UCC § 3-412(3). Compare N.I.L. § 142 (N.Y. Negotiable Instr. Law § 230). See Carrington, *supra* note 113, at 207.

<sup>157</sup> UCC § 3-417(2) discussed in Hawkland, *supra* note 130, at 61-62.

<sup>158</sup> UCC § 3-415(2). See also §§ 3-413 (Contract of Maker, Drawer and Acceptor), 3-414 (Contract of Indorser), 3-416 (Contract of Guarantor).

<sup>159</sup> N.Y. Negotiable Instr. Law §§ 115, 116.

<sup>160</sup> See Penney, "New York Revisits the Code: Some Variations in the New York Enactment of the Uniform Commercial Code," 62 Colum. L. Rev. 992, 1000 (1962).

<sup>161</sup> UCC § 3-417(1), (2). See also Aigler & Steinheimer, *Cases on Bills and Notes* 246 (1962).

<sup>162</sup> See text following note 156, *supra*.

<sup>163</sup> UCC § 3-417(1). See Leary, "Commercial Paper: Some Aspects of Article 3 of the Uniform Commercial Code," 48 Ky. L.J. 198, 224-26 (1960).

<sup>164</sup> UCC § 3-417(2). See Hawkland, *supra* note 130, at 62; Aigler & Steinheimer, *supra* note 161, at 246.

<sup>165</sup> See N.I.L. §§ 65, 66 (N.Y. Negotiable Instr. Law §§ 115, 116).

<sup>166</sup> See *Franklin Square Nat'l Bank v. Great Atl. Bldg. Material Supply Corp.*, 186 Misc. 524, 526, 60 N.Y.S.2d 352, 353 (Sup. Ct. N.Y. County), *aff'd mem.*, 270 App. Div. 930, 62 N.Y.S.2d 617 (1st Dep't.), *aff'd*, 296 N.Y. 644, 69 N.E.2d 684 (1946) (discussion of varying theories of recovery).

<sup>167</sup> Legal effect given to endorsement "pay any bank or banker" ABA Bank Collection Code, § 4 (N.Y. Negotiable Instr. Law § 350-c). See also Note, 40 Colum. L. Rev. 320 (1940).

<sup>168</sup> UCC § 3-417(2)(a). Compare N.I.L. § 65(2) (N.Y. Negotiable Instr. Law § 115(2)).

against forged or unauthorized signatures,<sup>169</sup> against material alteration,<sup>170</sup> against defenses,<sup>171</sup> and against insolvency proceedings.<sup>172</sup>

### I. *Price v. Neal* (3-418)

The rule of *Price v. Neal*,<sup>173</sup> codified at least in part by N.I.L. section 62,<sup>174</sup> provides, among other things, that money paid out by an innocent drawee on an instrument bearing a forged signature of the drawer cannot be recovered from an innocent purchaser. The rule is commonly regarded as an exception to the rule that money paid out on a mutual mistake of material fact is recoverable.<sup>175</sup> N.I.L. section 62 does speak of the finality of acceptance but says nothing about payment. Post-N.I.L. decisions have either deemed this N.I.L. language to include payment or have found other grounds for continuing to apply the rule of *Price v. Neal* to payment.<sup>176</sup> The codification of the rule in the Code is found in two sections: one provides that although persons presenting instruments for payment or acceptance make certain warranties, the warranty as to the genuineness of the drawer's signature is not made to a payor or acceptor;<sup>177</sup> the other makes payment or acceptance final in favor of holders in due course or persons who have in good faith changed their position in reliance on the payment.<sup>178</sup>

The common law contains certain exceptions to the doctrine.<sup>179</sup> The drawee may recover from a presenter or cashing bank which acts in bad faith or negligently.<sup>180</sup> The Code abandons the negligence exception.<sup>181</sup> The effect of the bad faith rule is retained in part, however, by virtue of the presentment warranty that the presenter has no knowledge that the

<sup>169</sup> UCC § 3-417(2)(b). Compare N.I.L. § 65(1) (N.Y. Negotiable Instr. Law § 115(1)).

<sup>170</sup> UCC § 3-417(2)(c). Compare N.I.L. § 65(1) (genuineness) (N.Y. Negotiable Instr. Law § 115(1)).

<sup>171</sup> UCC § 3-417(2)(d). This seems to parallel the N.I.L. § 65(3) warranty that all prior parties had capacity to contract and that the instrument is valid and subsisting. See N.Y. Negotiable Instr. Law § 115(3). See generally Brady, Bank Checks 114-115 (Bailey ed. 1962) reprinted from 78 Banking L.J. 212-13 (1961).

<sup>172</sup> UCC § 3-417(2)(e). This seems novel but compare N.I.L. § 65(4) (N.Y. Negotiable Instr. Law § 115(4)). See also Britton, Bills and Notes 632 (2d ed. 1961).

<sup>173</sup> 3 Burr. 1354, 1 W. Bla. 390 (1762).

<sup>174</sup> N.Y. Negotiable Instr. Law § 112 (as to an acceptor).

<sup>175</sup> See Britton, supra note 172, at 375.

<sup>176</sup> Britton, supra note 172, at 380-82. Although there are several post-N.I.L. decisions in New York applying the rule, none of them seems to deal with the applicability of N.I.L. § 62 (N.Y. Negotiable Instr. Law § 112). See Banca Commerciale Italiana Trust Co. v. Clarkson, 274 N.Y. 69, 8 N.E.2d 281 (1937); Bergstrom v. Ritz-Carlton Restaurant & Hotel Co., 171 App. Div. 776, 157 N.Y. Supp. 959 (1st Dep't 1916); Williamsburgh Trust Co. v. Tum Suden, 120 App. Div. 518, 105 N.Y. Supp. 335 (2d Dep't 1907). See also Comment, 13 Syracuse L. Rev. 426 (1962).

<sup>177</sup> UCC §§ 3-417, and 3-417(1)(b). See discussion in text, following note 160, supra.

<sup>178</sup> UCC § 3-418. See Comment, 23 U. Pitt. L. Rev. 193 (1961).

<sup>179</sup> See Britton, supra note 172, at 382; Comment, 13 Syracuse L. Rev. 426, 428 (1962).

<sup>180</sup> See Bergstrom v. Ritz-Carlton Restaurant & Hotel Co., supra note 176.

<sup>181</sup> UCC § 3-418, comment 4.

signature of the maker or drawer is unauthorized.<sup>182</sup> The language at the end of section 3-418, protecting a person who has in good faith changed his position in reliance on the payment, was inserted at the insistence of the New York Law Revision Commission.<sup>183</sup> This appears to codify the restitution rule denying recovery of a mistaken payment where the payee has changed his position.<sup>184</sup>

Section 3-418 is also notable in New York for its reversal of the anomalous rule excepting certification from the doctrine of *Price v. Neal*.<sup>185</sup>

### *Part 5: Presentment, Notice of Dishonor, and Protest*

#### A. General

This part of the Code has involved the greatest paring down and simplification of comparable material found in the N.I.L. Provisions concerning presentment, notice of dishonor and protest, scattered throughout twenty-seven sections of the N.I.L.,<sup>186</sup> are compressed mainly into eleven sections.<sup>187</sup> The archaic and hardly ever used provisions concerning acceptance and payment for honor found in seventeen sections of the N.I.L.<sup>188</sup> are completely eliminated. Few major changes are made and, generally, any notice or demand adequate under existing law is sufficient under the Code.<sup>189</sup>

#### B. Delay in Presentment (3-501, -502)

In applying sanctions for delay, the Code takes a new approach. Although the indorser continues to be completely discharged,<sup>190</sup> any drawer or acceptor suffering a loss on a draft payable at a bank because of a bank failure during the period of the delay may discharge his liability by assigning his rights against the failed bank.<sup>191</sup> The Code con-

<sup>182</sup> UCC § 3-417(1)(b).

<sup>183</sup> 1956 Recommendations, supra note 32, at 116; 1956 N.Y. Law Revision Comm'n Rep. 411; 1955 N.Y. Law Revision Comm'n Rep. 1072-79.

<sup>184</sup> Restatement, Restitution §§ 69, 142-43 (1937). See also Palmer, "Negotiable Instruments Under the Uniform Commercial Code, 48 Mich. L. Rev. 255, 276 (1950).

<sup>185</sup> See Metropolitan Life Ins. Co. v. Bank of United States, 259 N.Y. 365, 182 N.E. 18 (1932), 46 Harv. L. Rev. 151 (1932) (critical). See Comment, 13 Syracuse L. Rev. 426, 430 (1962). New York is not alone in treating certification as an exception to *Price v. Neal*. See Britton, supra note 172, at 390.

<sup>186</sup> N.I.L. §§ 70-118, 143-60. (N.Y. Negotiable Instr. Law §§ 130-48, 160-89, 240-48, 260-68.)

<sup>187</sup> UCC §§ 3-501 to 511.

<sup>188</sup> N.I.L. §§ 161-77 (N.Y. Negotiable Instr. Law §§ 280-89, 300-06).

<sup>189</sup> Carrington, "Banking, Commercial Paper and Investment Securities Under the Uniform Commercial Code," 14 Wyo. L.J. 198, 208 (1960). See general discussion in Hawland, Commercial Paper 38-60 (1959).

<sup>190</sup> Compare UCC §§ 3-501(1)(b), 3-502(1)(a), with N.I.L. §§ 70, 89, 144 (N.Y. Negotiable Instr. Law §§ 130, 160, 241).

<sup>191</sup> UCC § 3-502(1)(b). See discussion in Sutherland, "Article 3—Logic, Experience and



tinues the "reasonable time" measure of timely presentment<sup>192</sup> but adds certain presumptions for domestic uncertified checks. In substitution for the current "one day rule,"<sup>193</sup> the Code requires that a check be presented within thirty days to hold the drawer<sup>194</sup> and within seven days from the date of the indorsement to hold an indorsor.<sup>195</sup> Proving the dates of indorsements, however, may be difficult.

These presumptions have caused a great deal of controversy. The bankers of the City of New York have argued vehemently that these periods are both too short for checks sent abroad and then returned to the United States for presentment and too long for many purely domestic transactions.<sup>196</sup> Since article 1 clearly provides that the presumptions shall fall when evidence is introduced sufficient to support a finding of the nonexistence of such presumptions,<sup>197</sup> the concern of the bankers would seem unfounded. The certainty afforded appears to overshadow potential shortcomings. The Code provision has the virtue of eliminating the discredited and somewhat anomalous N.I.L. interpretation found in the case of *Columbian Banking Co. v. Bowen*.<sup>198</sup> This case, requiring only that a check be presented promptly after the "last negotiation," demonstrates the unfairness to a first indorsor whose liability is unreasonably prolonged by a second indorsor's extended holding of an instrument before further negotiation. Under the Code each party's liability is measured from the date of his handling of the instrument.<sup>199</sup>

As mentioned above, the Code also furnishes a neat solution to the practical problem encountered in a suit against the drawer of a check during the pendency of the drawee's liquidation proceedings. The assignment of the drawer's claim against the drawee<sup>200</sup> avoids the problem of awaiting the termination of the proceeding to determine the extent of the loss. A further gain is reflected in the Code's uniform treatment of the drawer of a check, the drawer of a bill of exchange other than a

Negotiable Paper," 1952 Wis. L. Rev. 230, 248-51. Palmer, *supra* note 184, at 301-03; Brady, *supra* note 171, at 262-64, reprinted from 78 Banking L.J. 461, 679-81.

<sup>192</sup> Compare UCC § 3-503(2) (first sentence) with N.I.L. § 193 (N.Y. Negotiable Instr. Law § 4).

<sup>193</sup> Brady, *supra* note 171, at 250. There seems to be little or no clear New York law on point. See 1955 N.Y. Law Revision Comm'n Rep. 1097.

<sup>194</sup> UCC § 3-503(2)(a).

<sup>195</sup> UCC § 3-503(2)(b).

<sup>196</sup> New York Clearing House Ass'n, Report on the Uniform Commercial Code 20, item 8, (1961). Further discussion of this report may be found in Penney, *supra* note 160.

<sup>197</sup> UCC § 1-201(31).

<sup>198</sup> 134 Wis. 218, 114 N.W. 451 (1908), discussed in Morris, "The Importance of Promptly Presenting Checks for Payment," 61 W. Va. L. Rev. 191, 191-99 (1959) and Palmer, *supra* note 184, at 301-03. See also Delony, "The Presentment Problem in the Collection of Checks Through Banks," 10 U. Fla. L. Rev. 382, 397 (1957).

<sup>199</sup> UCC § 3-503(2)(a), (b).

<sup>200</sup> UCC § 3-502(1)(b). See references in note 191, *supra*.

check and the maker of a note payable at a bank<sup>201</sup> in delayed presentment cases. Under the N.I.L. the drawer of a check is discharged to the extent of his loss;<sup>202</sup> the drawer of a bill of exchange other than a check is discharged fully;<sup>203</sup> and the maker of a note payable at a bank is not discharged at all.<sup>204</sup>

### Part 6: Discharge

#### A. General (3-601)

The Code takes a new approach to the concept of discharge. Discharge is clearly established as a personal defense unavailable against a subsequent holder in due course without notice.<sup>205</sup> The methods of discharge are collected in the first section of this part and generally reflect present N.I.L. or decisional rules.<sup>206</sup> The Code departs from the approach taken by the N.I.L. in providing for the discharge of some or all of the parties to an instrument rather than the discharge of the instrument itself.<sup>207</sup> Abandoned is the N.I.L. scheme that "payment in due course" discharges the payor lacking notice of a defect in the holder's title.<sup>208</sup> The Code substitutes a provision permitting the discharge of a paying party who knows of an outstanding claim unless the claimant follows the "adverse claim" procedure specified.<sup>209</sup> The claimant is required either to secure an injunction against payment or post security to protect the payor. Under present law a payor with knowledge of an adverse claim is on the horns of a dilemma; he risks liability whether he pays or not.

#### B. Suretyship (3-606)

The Code extends the application of suretyship principles to accommodation makers and drawers as well as indorsors. Because of the language in N.I.L. section 120<sup>210</sup> specifying that the extension of the time of payment operates to discharge *secondary* parties, most courts have held that such an extension is no defense to an accommodation party who

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<sup>201</sup> U.C.C. § 3-502(1)(b).

<sup>202</sup> N.I.L. § 186 (N.Y. Negotiable Instr. Law § 322).

<sup>203</sup> N.I.L. § 70 (N.Y. Negotiable Instr. Law § 130)

<sup>204</sup> *Ibid.*

<sup>205</sup> See UCC § 3-602.

<sup>206</sup> See UCC § 3-601 and the annotations to the other sections of the Code to which cross reference is made in that section in Hogan & Penney, *New York Annotations to Uniform Commercial Code* (1961).

<sup>207</sup> Compare UCC § 3-601 with N.I.L. §§ 119, 120, 121 (N.Y. Negotiable Instr. Law §§ 200, 201, 202).

<sup>208</sup> N.I.L. § 119(1), (2) (N.Y. Negotiable Instr. Law § 200(1), (2)). See also N.I.L. §§ 51, 88 (N.Y. Negotiable Instr. Law §§ 90, 148).

<sup>209</sup> UCC § 3-603. Compare N.Y. Banking Law §§ 134 (5), (6), (7); 171 (5), (6), (7); 239 (5), (6) ("adverse claim" statutes as to banks or trust companies, private bankers, and savings banks). See Comment, 65 *Yale L.J.* 807, 810-16 (1956).

<sup>210</sup> N.Y. Negotiable Instr. Law § 201.

appears as maker or drawer on the instrument.<sup>211</sup> This is because such a party is primarily, not secondarily, liable "on the instrument."<sup>212</sup> The Code rejects this anomalous result.<sup>213</sup> The New York Law Revision Commission successfully persuaded the Code draftsmen to modify this section in the 1956 Recommendations so as to extend the defense of release of principal to principals bound otherwise than on the instrument.<sup>214</sup> In addition to extension of the time of payment and release of principal defenses, section 3-606 codifies a suretyship rule by discharging any nonconsenting party to the instrument when the holder "unjustifiably impairs . . . collateral . . . ."<sup>215</sup> All of these suretyship principles are made applicable to primary as well as secondary parties.

Several semantic problems, however, are posed by this suretyship section. First, what changes are wrought by the Code's use of the phrase "agrees not to sue" in describing grounds for discharge is not clear.<sup>216</sup> If the equivalent of a covenant not to sue, this provision appears to reverse the present majority rule.<sup>217</sup> Second, the effect of the Code's omitting the term "binding" to modify "agreement," found in the comparable section of the N.I.L., is uncertain.<sup>218</sup> Under present law the agreement must be binding; forbearance is not sufficient.<sup>219</sup> Third, does release of collateral to the accommodated party discharge the surety under the Code? The Code provision only speaks of "unjustifiably impair[ing] any collateral for the instrument given."<sup>220</sup> Any uncertainty here can be remedied by redrafting.<sup>221</sup>

#### *Part 7: Advice of International Sight Draft (3-701)*

Part 7 of the 1952 draft of article 3 included the provisions on collection of documentary drafts now found in part 5 of article 4. The New York Law Revision Commission vigorously criticized the location

<sup>211</sup> Britton, *supra* note 172, at 698-705.

<sup>212</sup> See criticism in Palmer, *supra* note 184, at 305-06 (written prior to the incorporation of this provision in the Code).

<sup>213</sup> "Any party to the instrument" is discharged. See UCC § 3-606(1).

<sup>214</sup> 1956 Recommendations, *supra* note 32, at 129.

<sup>215</sup> UCC § 3-606(1)(b). *Accord*, Exchange Bank v. Ludlum, 246 App. Div. 892, 285 N.Y. Supp. 862 (4th Dep't 1936) (release of collateral); *Cohen v. Rossmore*, 225 App. Div. 300, 233 N.Y. Supp. 196 (1st Dep't 1929) (release of collateral). But see text following note 219, *infra*.

<sup>216</sup> UCC § 3-606(1)(a).

<sup>217</sup> Britton, *supra* note 172, at 682, n.1. *Contra* and in accord with the Code, see *Brown v. Williams*, 4 Wend. 360 (N.Y. Sup. Ct. 1830). See 1955 N.Y. Law Revision Comm'n Rep. 1177.

<sup>218</sup> Compare N.I.L. § 120(6) (N.Y. Negotiable Instr. Law § 201(6)) with UCC § 3-606(1)(a).

<sup>219</sup> *People's Nat'l Bank v. Hewitt*, 226 App. Div. 412, 235 N.Y. Supp. 392 (3d Dep't 1929), *aff'd*, 253 N.Y. 523, 171 N.E. 765 (1930). See also 1955 N.Y. Law Revision Comm'n Rep. 1179 (analysis of UCC § 3-606).

<sup>220</sup> UCC § 3-606(1)(b).

<sup>221</sup> Memorandum of Professor William F. Starr to New York Commission on Uniform State Laws, January 17, 1962.

of these provisions in article 3 and conditioned approval of them on their being moved to article 4.<sup>222</sup> To avoid the inconvenience of renumbering the rest of article 3, former section 3-806 was transferred to become the new section 3-701.<sup>223</sup> This novel section, purporting to codify current banking practice with respect to letters of advice of international sight drafts,<sup>224</sup> was amended in New York by eliminating its third subparagraph<sup>225</sup> completely. This was done at the behest of the New York City banks which strenuously objected to any codification in this area.<sup>226</sup>

#### *Part 8: Miscellaneous*

The five sections in this part include several provisions novel to the statutory law of commercial paper. Three of these sections bear comment.

##### *A. Conditional and Absolute Payment (3-802)*

Under present decisional law if a check is taken as absolute payment of an underlying obligation and the check is not paid, recourse is limited to the check alone, the underlying debt having been discharged. On the other hand, if a check is taken as conditional payment only, the obligee has the alternative of recourse either upon the check or upon the underlying obligation.<sup>227</sup> A series of rules of presumption have developed to determine whether the check was given as conditional or absolute payment in the absence of expressed intent. Briefly stated, the only combination of circumstances producing a presumption of absolute payment requires the giving of a third person's instrument concurrent with the creation of the debt.<sup>228</sup> When the instrument is given in payment of a precedent debt<sup>229</sup> or when the debtor executes and delivers his own instrument in payment of either a contemporaneous or precedent debt,<sup>230</sup>

<sup>222</sup> 1956 N.Y. Law Revision Comm'n Rep. 417.

<sup>223</sup> 1956 Recommendations, supra note 32, at 130. The sections previously found in part 7 have become UCC §§ 4-501 to 504.

<sup>224</sup> See UCC § 3-701, comments.

<sup>225</sup> Section 3-701. Letter of Advice of International Sight Draft.

(3) Unless otherwise agreed and except where a draft is drawn under a credit issued by the drawee, the drawee of an international sight draft owes the drawer no duty to pay an unadvised draft but if it does so and the draft is genuine, may appropriately debit the drawer's account.

<sup>226</sup> The bankers argued that it "freezes a practice into the laws that may change from time to time" and that "there is a move now among banks with a large volume of foreign business to stop requiring advices in such cases." See Penney, "New York Revisits the Code: Some Variations in the New York Enactments of the Uniform Commercial Code," 62 Colum. L. Rev. 992, 1001.

<sup>227</sup> *Hamilton v. R. S. Dickson & Co.*, 85 F.2d 107, 107-08 (2d Cir. 1936). See generally 3 Daniel, *Negotiable Instruments* §§ 1447-55 (7th ed. 1933).

<sup>228</sup> *Kirkham v. Bank of America*, 26 App. Div. 110, 49 N.Y. Supp. 767 (1st Dep't 1898), aff'd, 165 N.Y. 132, 58 N.E. 753 (1900).

<sup>229</sup> *Cohen v. Rossmore*, 225 App. Div. 300, 233 N.Y. Supp. 196 (1st Dep't 1929).

<sup>230</sup> *Jagger Iron Co. v. Walker*, 76 N.Y. 521 (1879).

the presumption is that the instrument is given as conditional payment only. The Code provision limits the presumption of absolute payment to cases where the instrument given has a bank bound on it as drawer, maker or acceptor and there is no recourse on the instrument against the underlying obligor.<sup>231</sup> The Code makes no distinction between contemporaneous and precedent debts.

### B. "Vouching-In" Third Parties (3-803)

The Code provides new statutory language permitting a "defendant . . . sued for breach of an obligation for which a third person is answerable over under this article" to vouch-in the third person by giving him the appropriate written notice. Vouching-in is a recognized common law device, but is available only against persons who will be directly responsible to the person first sued, if judgment goes against the latter.<sup>232</sup> Earlier, in section 3-306(d), the Code deals with the *jus tertii* problem. In accordance with present law, the Code provides that a defendant, having no defense of his own, may successfully defend if the plaintiff stole the instrument or acquired it, with knowledge, from one who did steal it.<sup>233</sup> The failure to include the *jus tertii* defense of illegality in certain transactions may change New York law.<sup>234</sup> Both the vouching-in procedure and the Code's *jus tertii* provisions will induce third parties to come into the litigation itself.<sup>235</sup>

### C. The Nonnegotiable Instrument (3-805)

An important new provision makes all of article 3 applicable to instruments that fail of negotiability solely for the lack of being payable "to order" or "to bearer."<sup>236</sup> There can, however, be no "holder in due course" of such instruments.<sup>237</sup> Decisional authority dealing with non-negotiable instruments is scarce and will be superseded by article 3.

<sup>231</sup> UCC § 3-802(1)(a). See generally 1955 N.Y. Law Revision Comm'n Rep. 1204-08. On the related problem of bad checks and cash sales see Corman, "Cash Sales, Worthless Checks and Bona Fide Purchaser," 10 Vand. L. Rev. 55 (1956); Vold, Sales 169-84 (1959).

<sup>232</sup> Hartford Acc. & Indem. Co. v. First Nat'l Bank & Trust Co., 281 N.Y. 162, 22 N.E.2d 324 (1939). See also, N.Y. Civ. Prac. Act §§ 193-a (third party practice), 193-b (intervention). Criticisms made by the New York Law Revision Commission are responsible for the wording of the present text. 1956 Recommendations, supra note 32 at 132-33; 1956 N.Y. Law Revision Comm'n Rep. 418-19. For comparable sections under the new Civil Practice Law (effective September 1, 1963), see N.Y. Civ. Prac. Law & Rules §§ 1007-11 (third party practice) and §§ 1012-14 (intervention).

<sup>233</sup> Hays v. Hathorn, 74 N.Y. 486 (1878).

<sup>234</sup> Hurley v. Union Trust Co., 244 App. Div. 590, 280 N.Y. Supp. 474 (3d Dep't 1935); Singer v. Union Table and Spring Co., 151 Misc. 909, 271 N.Y. Supp. 349 (N.Y. Munic. Ct. 1934); N.Y. Pen. Law §§ 991-93. As to the possibility of a *jus tertii* defense in the finder situation, see dictum in Hurley v. Union Trust Co., supra.

<sup>235</sup> UCC § 3-603(1); 1957 Annual Survey of Massachusetts Law 29-30. See also, Britton, "Defenses, Claims of Ownership and Equities," 7 Hastings L.J. 1, 23-27 (1955).

<sup>236</sup> UCC § 3-805.

<sup>237</sup> Ibid.

The few existing rules deal with an indorser's liability,<sup>238</sup> the presumptions of consideration<sup>239</sup> and title.<sup>240</sup>

#### ARTICLE 4

##### *Introductory Comments*

Article 4 reflects the culmination of a long and troublesome effort to achieve a uniform Code in the area of bank deposits and collections.<sup>241</sup> These provisions will supersede the ABA Bank Collection Code and a variety of local collection statutes.<sup>242</sup>

The article is divided into two portions; one governs bank collections and the other the relationship between banks and their customers. The statute embodies much of present law and practice, adding new provisions where codification and certainty seems desirable. Some controversial changes dealing with the bank-customer relationship are made in part 4. The statute recognizes this area of the law as rapidly changing and therefore provides for the application of Federal Reserve and clearing house rules.<sup>243</sup> Also, wide latitude is afforded to vary the terms of the statute by agreement.<sup>244</sup>

Two typical problem patterns are illustrative of areas in which the rules of article 4 will be applicable. Consider the example of a payee in possession of a five hundred dollar check drawn upon an out-of-town bank. The payee indorses the check "For Deposit Only," and then deposits it in his local bank for credit to his account. Suppose that sometime during the course of collection either the payor bank becomes insolvent, the drawer of the check dies, or the drawer of the check stops payment. The Code seeks to define the rights and duties as between the five (possibly even more) different entities or individuals involved. There is the bank of deposit, one or several intermediary banks, the payor bank, and, of course, the payee and the drawer.

A particularly difficult and interesting problem is presented in the case of stopped checks. Perplexing questions are created when a check

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<sup>238</sup> McMullen v. Rafferty, 89 N.Y. 456 (1882) (indorser a primary party); Seymour & Bouck v. Van Slyck, 8 Wend. 403, 422 (N.Y. Sup. Ct. 1832) (indorser not entitled to presentment or notice of dishonor).

<sup>239</sup> St. Lawrence County Nat'l Bank v. Watkins, 153 App. Div. 551, 138 N.Y. Supp. 116 (3rd Dep't 1912); Deyo v. Thompson, 53 App. Div. 9, 65 N.Y. Supp. 459 (3rd Dep't 1900).

<sup>240</sup> Barrick v. Austin, 21 Barb. 241 (Sup. Ct. Monroe County 1855) (dictum). See generally, Willier, "Non-Negotiable Instruments," 11 Syracuse L. Rev. 13-26 (1960).

<sup>241</sup> Malcolm, "Article 4—A Battle with Complexity," 1952 Wis. L. Rev. 265.

<sup>242</sup> For text of ABA Bank Collection Code, local variations and other bank collection statutes see 2 Paton, Digest of Legal Opinions 1372-81 (1942) and supplements to § 27 of Code. Bank Collection Code Statutory Notes 1-14.

<sup>243</sup> UCC § 4-103(2), (3).

<sup>244</sup> UCC § 4-103. See generally Bunn, "Freedom of Contract under the Uniform Commercial Code," 2 B. C. Ind. & Com. L. Rev. 59 (1960).

is stopped but the payor bank inadvertently pays over the stop order. Under present law, in the absence of an exculpation clause, the payor bank must suffer the loss.<sup>245</sup> In most states the innocent but negligent payor bank has no right to be subrogated to the customer's claim against the payee, nor may the payor bank recover or defend against the drawer.<sup>246</sup> The Code goes a long way toward solving these problems.

### *Part 1: General Provisions and Definitions*

As indicated by the heading, part 1 contains the general provisions and definitions applicable throughout the article. There are several noteworthy points among these general provisions.

#### *A. Conflicts of Law Rule (4-102)*

First, in order of appearance, is the section providing that the liability of a bank for its activities in connection with the collection process is to be determined by the law of the place where the bank is situated.<sup>247</sup> This rule, measuring liability by the law of the situs of the bank handling the item in the course of transit, seems highly beneficial and has the advantage of certainty. If this Code section governs the liability of a depository bank to the beneficial owner of an item received from a fiduciary with notice of the fiduciary relation, a change in New York law is effected. In the case of *Weissman v. Banque de Bruxelles*,<sup>248</sup> the law of the place where the agency for collection was to be performed determined the liability of the depository bank rather than the situs of the depository bank which converted the check.<sup>249</sup> On the other hand, in a case involving the failure of an intermediary bank, the New York Court of Appeals refused to measure the liability of the prior intermediary bank, which accepted the failed bank's draft, by the law of the jurisdiction where the prior intermediary bank was situated.<sup>250</sup> The court argued that the contract was to be performed either in Texas, the situs of the payor bank, or in New York where the owner of the instrument was located, rather than in Tennessee, the location of the intermediary bank to whom the New York owner of the check had forwarded the item for collection. The Code conflicts rule seems relatively easy of appli-

<sup>245</sup> *Chase Nat'l Bank v. Battat*, 297 N.Y. 185, 78 N.E.2d 465 (1948). This case presumes the absence of "ratification." See Morrison & Sneed, "Bank Collections: The Stop Payment Transaction—A Comparative Study," 32 *Texas L. Rev.* 259 (1954).

<sup>246</sup> Morrison & Sneed, *supra* note 245 at 312; Comment, 15 *Calif. L. Rev.* 235 (1927). Note, 40 *Harv. L. Rev.* 110 (1926).

<sup>247</sup> UCC § 4-102(2).

<sup>248</sup> 254 N.Y. 488, 173 N.E. 835 (1930) (depository bank converted check by accepting for collection on behalf of fiduciary).

<sup>249</sup> 1955 N.Y. Law Revision Comm'n Rep. 1257; for Notes on the Weissman case, see 31 *Colum. L. Rev.* 704 (1931), 29 *Mich. L. Rev.* 928 (1931).

<sup>250</sup> *Saint Nicholas Bank v. State Nat'l Bank*, 128 N.Y. 26, 27 N.E. 849 (1891).

cation, is preferable to the present muddled state of the law of New York in this area and appears to adopt the majority rule.<sup>251</sup>

B. *Variations by Agreement—Custom and Usage* (4-103)

Article 4 contains a specific provision permitting variation of its term by contract.<sup>252</sup> The only limitations imposed are that such contracts may not exculpate the bank for lack of good faith or failure to exercise ordinary care.<sup>253</sup> The Code further provides that such contracts may not limit the measure of damages for such lack or failure.<sup>254</sup> The section adds, however, that the parties may agree upon standards of care that are not manifestly unreasonable.<sup>255</sup> Appreciation of the importance of banking practices and the "official" and "quasi-official" agreements and rules operative in the banking industry is expressed in the provisions making Federal Reserve regulations, clearing house rules, and general banking usage applicable to article 4 transactions. Of particular interest is that such rules and usage are made binding even without the bank's or customer's assent.<sup>256</sup>

Of primary concern is the application of the article 4 section prohibiting disclaimers of ordinary care to exculpation clauses in stop payment orders. The law of New York and several other states now permit such disclaimers.<sup>257</sup> The validity of such exculpation clauses has been widely discussed and litigated. The weight of authority, including the most recent cases, denies effect to such agreements.<sup>258</sup> Nine states and Puerto Rico have passed upon the validity of exculpatory agreements and stop orders; four jurisdictions uphold such agreements and six treat them as invalid.<sup>259</sup>

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<sup>251</sup> See *Old Company's Lehigh v. Meeker*, 71 F.2d 280 (2d Cir. 1934); 1955 N.Y. Law Revision Comm'n Rep. 1260.

<sup>252</sup> UCC § 4-103(1). Compare N.Y. Negotiable Instr. Law §§ 350-a, 350-b(4). See generally Bunn, *supra* note 244. See also Brome, "Bank Deposits and Collections," 16 Law & Contemp. Prob. 308, 310-14 (1950).

<sup>253</sup> UCC § 4-103(1). *Contra*, *Isler v. National Park Bank*, 239 N.Y. 462, 470, 147 N.E. 66, 69 (1925); *Briggs v. Central Nat'l Bank*, 89 N.Y. 182 (1882); *Allen v. Merchants' Bank*, 22 Wend. 215 (N.Y. 1839).

<sup>254</sup> UCC § 4-103(1).

<sup>255</sup> *Ibid.*

<sup>256</sup> UCC § 4-103(2), (3). See *Hogan & Penney*, *supra* note 206, at 144 for citation of cases where courts have refused to bind nonmember and nonconsenting parties to clearing house rules and local banking customs.

<sup>257</sup> *Gaita v. Windsor Bank*, 251 N.Y. 152, 154-55, 167 N.E. 203, 204 (1929); *Seldowitz v. Manufacturer's Trust Co.*, 12 App. Div. 2d 579, 202 N.Y.S.2d 129 (1st Dep't 1960). For collection of cases in other jurisdictions see *Annot.*, 1 A.L.R.2d 1155 (1948). See also 3 Paton, *supra* note 242, at 3469-74.

<sup>258</sup> 3 Paton, *supra* note 242, at 3469-74.

<sup>259</sup> The two courts currently upholding such agreements, in addition to New York, are Puerto Rico (*Martinez v. National City Bank*, 80 F. Supp. 545 (D.P.R. 1948)) and Indiana (*Hodnick v. Fidelity Trust Co.*, 96 Ind. App. 342, 183 N.E. 488 (1932)). Although Massachusetts was previously in this group (*Tremont Trust Co. v. Buraek*, 235 Mass. 398, 126 N.E. 782 (1920)), the adoption of the Code in 1957 reversed that state's position. States which deny effect to such an agreement are: Alabama (*Commercial Bank v. Hall*,



In New York the rule permitting exculpation clauses has been somewhat modified. The disclaimer clause does not protect the bank from liability for willful disregard of the order.<sup>260</sup> A recent lower court decision denied a summary judgment to the defendant bank where a cause of action in negligence was alleged in the complaint notwithstanding the presence of an exculpation clause.<sup>261</sup>

### C. *Branch Banks* (4-106)

The New York enactment adds language to the section on branch banks to the effect that the receipt of notice by the branch concerned determines the bank's status as a holder in due course.<sup>262</sup> This amendment reflects another instance of the New York City bankers' efforts to achieve a workable legal framework in which their large-scale and multi-branched operations may be economically conducted.<sup>263</sup>

### D. *Extended Day To Obtain Payment* (4-108)

The Code contains a salutary provision continuing the New York statutory rule permitting a collecting bank to extend the time for payment up to one day in a good faith effort to collect.<sup>264</sup> The Code extends the present New York statute, applicable to "items drawn on a drawer other than a bank," to all "specific items."

## *Part 2: Collection of Items: Depository and Collecting Banks*

### A. *Agency and Subagency Relationships* (4-201, -203)

Generally, the bank of deposit takes as agent for collection rather than as owner.<sup>265</sup> The agreement between the depositor and the depository bank often provides for the agency relationship.<sup>266</sup> If the indorsement is general, however, rather than restrictive, courts have held that subsequent banks are entitled to regard the first bank taker as owner.<sup>267</sup>

266 Ala. 57, 94 So. 2d 198 (1957)); California (*Hiroshima v. Bank of Italy*, 78 Cal. App. 362, 367, 248 Pac. 947, 952 (1926)); Connecticut (*Calamita v. Tradesmen's Nat'l Bank*, 135 Conn. 326, 64 A.2d 46 (1949), 25 N.Y.U.L. Rev. 419 (1950)); New Jersey (*Reinhardt v. Passaic-Clifton Nat'l Bank and Trust Co.*, 16 N.J. Super. 430, 84 A.2d 741 (1951), aff'd, 9 N.J. 607, 89 A.2d 242 (1952)); Ohio (*Speroff v. First-Central Trust Co.*, 149 Ohio St. 415, 79 N.E.2d 119 (1948)); Pennsylvania (*Thomas v. First Nat'l Bank*, 376 Pa. 181, 101 A.2d 910 (1954)).

<sup>260</sup> *Pyramid Musical Corp. v. Floral Park Bank*, 268 App. Div. 783, 48 N.Y.S.2d 866 (2d Dep't 1944); *Seldowitz v. Manufacturer's Trust Co.*, supra note 257.

<sup>261</sup> *Capritta v. National Commercial Bank*, 26 Misc. 2d 71, 206 N.Y.S.2d 726 (Albany City Ct. 1960).

<sup>262</sup> N.Y. Sess. Laws, 1962, ch. 553, § 4-106 (effective Sept. 24, 1964).

<sup>263</sup> Penney, "New York Revisits the Code: Some Variations in the New York Enactment of the Uniform Commercial Code," 62 Colum. L. Rev. 992, 1002 (1962).

<sup>264</sup> Compare UCC § 4-108(1) with N.Y. Negotiable Instr. Law § 350-d(2).

<sup>265</sup> See Brome, supra note 252, at 311. See also 2 Paton, supra note 242, at 1251-52.

<sup>266</sup> 2 Paton, supra note 242, at 1256-57.

<sup>267</sup> 2 Paton, supra note 242, at 1254. See also N.Y. Negotiable Instr. Law § 350-c; *Carson v. Federal Reserve Bank*, 266 App. Div. 225, 235 N.Y. Supp. 197 (4th Dep't 1929).

The Code extends the present presumption of agency to apply without regard to the form of the indorsement.<sup>268</sup> It also provides that "unless the contrary appears" the first bank and all subsequent banks in the collection process are agent and subagents not only without regard to the form of the indorsement, but even if credit is given subject to immediate withdrawal or, in fact, withdrawn.<sup>269</sup> This represents an extension of the so-called "Massachusetts Rule," as reflected in the ABA Bank Collection Code.<sup>270</sup> To afford some protection to collecting banks, the Code makes the right of the owner-depositor subject to the rights of collecting banks such as those resulting from its outstanding advances on the item.<sup>271</sup> The collecting bank is given a "security interest" rather than any rights as "owner."<sup>272</sup> Another Code provision establishes a "chain of command" rule as between collecting banks.<sup>273</sup> This Code section permits an intermediary collecting bank to heed only the instructions given by the bank from which the item is taken for collection. This is inconsistent with the approach of the "Massachusetts rule," continued in the Code, insofar as it denies the right of the owner, as principal, to claim an item in the course of collection direct from a so-called "subagent." Apparently the draftsmen felt that any occasional benefit to owner-depositors was not worth impairing the freedom of action of intermediary banks.<sup>274</sup>

#### B. *Direct Routing* (4-204, -212)

The common law deemed the direct sending of items to payor banks for collection improper.<sup>275</sup> The ABA Bank Collection Code and Federal Reserve regulations reversed this rule.<sup>276</sup> The Code also permits direct sending, and in addition allows direct sending to nonbank payors, where

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<sup>268</sup> UCC § 4-201(1).

<sup>269</sup> *Ibid.*

<sup>270</sup> See ABA Bank Collection Code §§ 2, 4. See N.Y. Negotiable Instr. Law §§ 350-a, 350-c. For a discussion of the "Massachusetts rule," see Sneed & Morrison, "Bank Collections—A Comparative Study," 29 Texas L. Rev. 713, 727-28 (1951); Trumbull, "Bank Deposits and Collections in Illinois Under the Proposed Uniform Commercial Code," 55 Nw. L. Rev. 253, 259-61 (1960).

<sup>271</sup> UCC § 4-201(1). See also UCC § 3-206, as to the effect of a restrictive endorsement, and discussion in text following note 67, *supra*.

<sup>272</sup> UCC § 4-208. See Trumbull, *supra* note 270, at 270-72.

<sup>273</sup> UCC § 4-203. Compare N.Y. Negotiable Instr. Law § 350-a (authority to follow instructions of immediate forwarding bank), and *Florida Citrus Exch. v. Union Trust Co.*, 244 App. Div. 68, 278 N.Y. Supp. 313 (4th Dep't 1935).

<sup>274</sup> See Connecticut Temporary Comm'n to Study The Uniform Commercial Code, Study and Report 28-29 (1959). Compare *Soma v. Handrulis*, 277 N.Y. 223, 14 N.E.2d 46 (1938) holding an intermediary collecting bank liable for overlooking a depositor's restrictive endorsement.

<sup>275</sup> Brady, *Bank Checks* 235-38 (Bailey ed. 1962), reprinted from 78 *Banking L.J.* 652-55 (1961).

<sup>276</sup> See ABA Bank Collection Code § 6 (N.Y. Negotiable Instr. Law § 350-e) and Regulations G and J (applicable to Federal Reserve banks). See generally 2 Paton, *supra* note 242, at 1305-24.

the transferor's authorization is obtained.<sup>277</sup> This latter practice is currently sanctioned for Federal Reserve Banks by Regulations G and J and is a growing practice supported by custom and Clearing House rules because of the convenience afforded to the commercial world.<sup>278</sup> New York has adopted the optional Code provision permitting direct return of an unpaid item to the bank of deposit.<sup>279</sup> The delay of handling by intermediary banks is avoided and depository banks may act more quickly to protect themselves. The question has been raised, however, whether such speedy return might not be outweighed by legal complications resulting from such a practice.<sup>280</sup>

### C. *Missing Indorsements* (4-205) and *Bank Transfer Marking* (4-206)

Under N.I.L. § 49,<sup>281</sup> the transferee of an instrument lacking the payee's endorsement takes it subject to any defenses of the drawer against the payee.<sup>282</sup> It has been argued, however, that although a bank is not obliged to pay a check with a missing indorsement, even when guaranteed by a collecting bank, the payor bank should pay the check in the ordinary case "to facilitate business."<sup>283</sup> Apparently depository banks as a common practice supply missing indorsements, notwithstanding the absence of legal sanction. The Code approves this practice in the absence of contrary instructions by the drawer,<sup>284</sup> thereby avoiding the ordinarily meaningless and time-consuming return of the item for indorsement by the customer. A related provision which anticipates electronic check processing, is found in the section providing that any agreed method of marking checks which identifies the transferor bank is sufficient for the item's further transfer to another bank.<sup>285</sup> Banks may therefore simplify their indorsement stamps and adopt a numerical or other code system which by agreement or usage would produce the same result as the layers of undecipherable indorsement stamps now found on the backs of checks. Presumably any type of machine encoding or marking would be sufficient.

<sup>277</sup> UCC § 4-204(2)(b).

<sup>278</sup> Clarke, Bailey, & Young, *Bank Deposits and Collections* 69 (1959).

<sup>279</sup> UCC § 4-212(2). Of the eighteen states including New York that have adopted the Code, all but three, Georgia, New Jersey and Oregon, have also adopted this optional subsection (2).

<sup>280</sup> Clarke, "Bank Deposits and Collections: Article IV; Letters of Credit: Article V," 16 *Ark. L. Rev.* 45, 56 (1961). See also Brady, *Bank Checks* 412-14 (Bailey ed. 1962), reprinted from 79 *Banking L.J.* 393-95 (1962).

<sup>281</sup> N.Y. *Negotiable Instr. Law* § 79.

<sup>282</sup> 2 Paton, *supra* note 242, at 2131-32.

<sup>283</sup> *Id.* at 2134, 2138-39.

<sup>284</sup> UCC § 4-205(1). See Brady, *Bank Checks* 206-07 (Bailey ed. 1962), reprinted from 78 *Banking L.J.* 857-58 (1961).

<sup>285</sup> UCC § 4-206. See *Bankers Manual on the Uniform Commercial Code* 35 (1958). See also Brady, *Bank Checks* 222-23 (Bailey ed. 1962), reprinted from 78 *Banking L.J.*, 873-74 (1961).

#### D. *Warranties of Depositors* (4-207)

The warranties of the depositor may be divided into those given to banks in the chain of collection and those given to the payor. Under present law the indorsing depositor, depending upon the character of his indorsement, gives warranties to subsequent parties.<sup>286</sup> If he indorses generally he warrants "to all subsequent holders in due course . . . that the instrument is at the time of his indorsement valid and subsisting" and engages that on due presentment "it shall be accepted or paid, or both . . . according to its tenor."<sup>287</sup> No warranty is presently made by the depositor to the drawee or payor.<sup>288</sup> The Code imposes the same warranties on "customer and collecting bank" in article 4 as are imposed upon presenting persons and transferors in article 3.<sup>289</sup> The warranties run to both intermediary and payor banks. The warranty sections in both articles 3 and 4 make a distinction, however, between the warranties given to payor banks on the one hand and to transferees and collecting banks on the other. Reflecting the codification of the rule in *Price v. Neal*, earlier discussed,<sup>290</sup> no warranty of the genuineness of the drawer's signature is made to the payor bank by a "customer or collecting bank that is a holder in due course and acts in good faith."<sup>291</sup> The warranties in the article 4 provision are more narrow than those in article 3 in that they are given only by "customers and collecting banks." On the other hand, they cover "items," a broader category than the "instruments" governed by article 3.<sup>292</sup>

#### E. *Media of Remittance* (4-211)

The Code liberalizes the requirements as to the media of remittance acceptable by a collecting bank. Under the present law the collecting bank is permitted to accept bank checks but not checks or drafts drawn on the remitting bank itself.<sup>293</sup> The Code permits the acceptance of the remitter's cashier's check where the collecting and paying bank are members of the same clearing house or group.<sup>294</sup> Unless support for

<sup>286</sup> N.I.L. §§ 65, 66 (N.Y. Negotiable Instr. Law §§ 115, 116); Brannan, *Negotiable Instruments Law* 957-58 (Beutel 7th ed. 1948); Brome, *supra* note 252, at 317-19.

<sup>287</sup> N.I.L. § 66 (N.Y. Negotiable Instr. Law § 116); Brome, *supra* note 252, at 315.

<sup>288</sup> Brannan, *supra* note 286, at 959-60.

<sup>289</sup> Compare UCC §§ 3-417 and 4-207. Note that the article 4 warranties cover "items," a broader category than the instruments governed by article 3.

<sup>290</sup> See text following note 172, *supra*.

<sup>291</sup> UCC § 4-207(1)(b). See generally Brady, *Bank Checks* 223-27 (Bailey ed. 1962), reprinted from 78 *Banking L.J.* 874-78 (1961); Comment, 23 *U. Pitt. L. Rev.* 198, 211 (1961).

<sup>292</sup> Compare UCC § 4-207 with § 3-417.

<sup>293</sup> ABA Bank Collection Code § 9. See also N.Y. Negotiable Instr. Law § 350-i. See Clarke, Bailey, & Young, *supra* note 278, at 92-93.

<sup>294</sup> UCC § 4-211(1)(b).

such a practice may be found in statutes approving "such . . . method of settlement as may be customary,"<sup>295</sup> this is new law.

#### F. *Finality of Payment* (4-213, -303)

A great variety of rules have developed attempting to define the circumstances under which an item may be deemed finally paid. As many as ten different rules have been described.<sup>296</sup> This variety is in part attributable to the two distinct classes of situations where the question of final payment arises.<sup>297</sup> In one class the concern is whether the drawer and indorsers have been discharged. In the other, the issue is whether the amount of the item is still in the drawer's account subject to stop payment, set-off or garnishment. By way of example, the following typical acts have been included as constituting final payment: credit to presenting banks on books of payor bank; drawing of remittance instrument by payor banks; stamping of items "Paid"; entering charge to customer's account. The Code selects and lists a number of acts by the payor bank as constituting final payment.<sup>298</sup> These include payment in cash, the making of final settlement for the item, or of an unrevoked provisional settlement within the time allowed in the deferred posting provision.<sup>299</sup> One of the acts included in the Code is the completion of "the process of posting."<sup>300</sup> Some doubt was expressed in New York and elsewhere as to whether this term means the actual making of entries in the customer's account, or whether it was intended to include other steps in the normal payment procedure. This question is of particular importance to banks utilizing electronic posting techniques. Many such banks complete their electronic "posting" before any manual steps, such as verification of the drawers' signatures, are performed. A new section was included in the New York enactment of the Code to meet this difficulty.<sup>301</sup> The section defines the term "process of posting" to embrace all of the usual steps taken in the processing of checks for payment; the section makes clear, however, that the "key point in time is the completion of all the steps followed in a particular bank's 'payment' procedure."<sup>302</sup>

The Code contains a provision clarifying the question of when a

<sup>295</sup> See ABA Bank Collection Code § 9 (N.Y. Negotiable Instr. Law § 350-i) (variant).

<sup>296</sup> Malcolm, "Article 4—A Battle with Complexity," 1952 Wis. L. Rev. 265, 287-95. Clarke, Bailey, & Young, *supra* note 278, at 74-76.

<sup>297</sup> Trumbull, *supra* note 270, at 273-75.

<sup>298</sup> UCC §§ 4-213(1), 4-303(1).

<sup>299</sup> UCC §§ 4-213(1)(a), (b), (d); 4-303(1)(b), (c), (e). See also UCC § 4-301 (deferred posting section).

<sup>300</sup> UCC §§ 4-213(1)(c), 4-303(1)(d).

<sup>301</sup> N.Y. Sess. Laws 1962, ch. 553, § 4-409 (effective Sept. 27, 1964).

<sup>302</sup> See Penney, *supra* note 263, at 1002-03.

remittance instrument or authorization to charge an account becomes final.<sup>303</sup> Settlement by remittance instrument becomes final at the time the remittance instrument is paid, unless a nonbank check or other instrument not approved by the Code was authorized. In the latter case settlement becomes final upon receipt of the instrument.<sup>304</sup>

### G. *Insolvency and Preference* (4-214)

The Code contains a section governing the effect of the insolvency or other suspension of payments on the part of a collecting or payor bank while an item or its proceeds are in the process of collection or remittance. The Code provision is generally in accord and parallel in organization with A.B.A. Bank Collection Code section 13.<sup>305</sup> Following the approach of the ABA statute, the Code deals with the rights of the parties where:

- (1) final payment of an item has not occurred prior to suspension of a collecting or payor bank;<sup>306</sup>
- (2) the payor bank suspends payments after making final payment but before making settlement;<sup>307</sup> and
- (3) a collecting bank suspends payments after receiving a settlement.<sup>308</sup>

The Code adds a new provision governing the case where a payor or collecting bank gives or receives a provisional settlement and then suspends payments.<sup>309</sup> The Code abandons the trust theory found in the Bank Collection Code. The preference provisions<sup>310</sup> are probably inapplicable to national banks because of the overriding preference provisions of federal law.<sup>311</sup>

<sup>303</sup> UCC § 4-211(3).

<sup>304</sup> UCC § 4-211(3) (b); Trumbull, *supra* note 270, at 276; Clarke, Bailey, & Young, *supra* note 278, at 94. See N.Y. Negotiable Instr. Law §§ 350-b, 350-j; *Jones v. Board of Educ.*, 242 App. Div. 17, 272 N.Y. Supp. 5 (2d Dep't, 1934); *United States Pipe & Foundry Co. v. City of Hornell*, 146 Misc. 812, 263 N.Y. Supp. 89 (Sup. Ct. Steuben County 1933); *Matter of Jayne & Mason*, 140 Misc. 822, 251 N.Y. Supp. 768 (Sup. Ct. Monroe County 1931). The time of final settlement is important in UCC §§ 4-201, 4-212, 4-213, 4-214.

<sup>305</sup> N.Y. Negotiable Instr. Law § 350-1.

<sup>306</sup> Compare UCC § 4-214(1) with ABA Bank Collection Code § 13(1) (N.Y. Negotiable Instr. Law § 350-1(1)).

<sup>307</sup> Compare UCC § 4-214(2) with ABA Bank Collection Code § 13(2) (N.Y. Negotiable Instr. Law § 350-1(2)).

<sup>308</sup> Compare UCC § 4-214(4) with ABA Bank Collection Code § 13(3) (N.Y. Negotiable Instr. Law § 350-1(3)).

<sup>309</sup> See UCC § 4-214(3). There is no comparable ABA Bank Collection Code provision.

<sup>310</sup> UCC § 4-214(4).

<sup>311</sup> *Jennings v. United States Fid. & Guar. Co.*, 294 U.S. 216 (1935). Section 1-108, however, would preserve the applicability of UCC § 4-214 to state banks.

For discussion of UCC § 4-214 generally see Brady, *Bank Checks* 326-34 (Bailey ed. 1962), reprinted from 79 *Banking L.J.* 119-28 (1962); Brome, "Bank Deposits and Collections," 16 *Law & Contemp. Prob.* 324-27 (1950); Clarke, Bailey, & Young, *supra* note 278, at 144-51; Trumbull, *supra* note 270, at 277-80.

*Part 3: Collection of Items—Payor Banks**A. Deferred Posting (4-301)*

Deferred posting has been described as "a practice whereby all checks received by a payor bank on one business day are accumulated and 'posted' to the ledger accounts of the drawers at one time during the next day as contrasted with the practice of 'dribble posting' whereby checks are posted from time to time during the day of receipt."<sup>312</sup> The practice developed as a device to meet personnel shortage problems during World War II. The procedure was first sanctioned by an amendment of Federal Reserve Regulation J and a revision of the deposit contract form. The American Bankers Association then developed and sponsored the so-called "Model Deferred Posting Statute" which, with occasional variations, has been adopted in some 39 states and the District of Columbia.<sup>313</sup> The model statute permits a drawee bank receiving a demand item, other than for payment over the counter, and which remits and gives credit for such item on the day of receipt to return such item for credit or refund at any time before midnight of the next succeeding business day.<sup>314</sup>

The Code continues the substance of the deferred posting statute, but excludes documentary drafts.<sup>315</sup> Anomalously, although the Model Deferred Posting Statute states the bank's duty in the handling of checks for payment, there are no provisions for the results of non-compliance.<sup>316</sup> N.I.L. section 137<sup>317</sup> gives the drawee twenty-four hours to decide whether to accept a bill of exchange and provides that the drawee is deemed to have accepted the bill if he fails to return it within that period. In *State Bank v. Weiss*,<sup>318</sup> a New York court interpreted this N.I.L. section to mean that failure of a drawee bank to return checks presented for payment within twenty-four hours of their delivery, or to give proper notice of dishonor within such period, amounted to an acceptance. The Code includes a specific section making the payor bank "accountable" for items not promptly or properly handled within the limits prescribed by the deferred posting section.<sup>319</sup>

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<sup>312</sup> Brome, *supra* note 311, at 321. See also Leary, "Deferred Posting and Delayed Returns—The Current Check Collection Problem," 62 Harv. L. Rev. 905 (1949).

<sup>313</sup> Brome, *supra* note 311, at 322; N.Y. Negotiable Instr. Law § 350-b. For text of ABA Model Deferred Posting Statute and citations to adopting states, see Paton, Digest of Legal Opinion, "Collection" § 27 (Supp. 1, 1957).

<sup>314</sup> Brome, *supra* note 311, at 322.

<sup>315</sup> UCC § 4-301(1).

<sup>316</sup> Leary, *supra* note 312, at 927.

<sup>317</sup> N.Y. Negotiable Instr. Law § 225.

<sup>318</sup> 46 Misc. 93, 91 N.Y. Supp. 276 (Sup. Ct., N.Y. County 1904). See, however, *Matteson v. Moulton*, 79 N.Y. 627 (1880) (contrary holding under an earlier statute similar to N.I.L.). See generally, Britton, Bills and Notes 515-17 (2d ed. 1961).

<sup>319</sup> UCC § 4-302.

*Part 4: Payor Bank and the Customer*

The most controversial and interesting provisions found in either article 3 or article 4 are found in this part of article 4 dealing with the relationship between the payor bank and its customer. Several of these provisions were at one time located in article 3.<sup>320</sup> It has been vigorously argued that the rules in article 4, part 4, have no proper place in the Uniform Commercial Code in view of the local character of their impact.<sup>321</sup> Undoubtedly, an important reason for their having been subjected to such vigorous criticism is the fact that they may have an important, and sometimes costly, effect on the operations of commercial banks.<sup>322</sup> This is particularly true with respect to the stop payment provisions which, together with the anti-exculpation provision mentioned earlier, would impose an increased burden upon commercial banks.<sup>323</sup> The only offsetting feature is the availability of subrogation rights which presents some problems in New York.<sup>324</sup>

*A. Wrongful Dishonor (4-402)*

The Code provision on wrongful dishonor involves several minor changes in present law. The Code provides a specific rule as to the measure of damages, where the dishonor occurred through a mistake.<sup>325</sup> Actual damages proved is made the limit for innocent mistakes.<sup>326</sup> The changes include: the abandonment of the rule permitting recovery of nominal damages for a technical breach;<sup>327</sup> the abandonment of the "trader" rule;<sup>328</sup> and the abandonment of the special rule for fiduciaries permitting the recovery of substantial damages for innocent mistake without proof of actual injury.<sup>329</sup> The Code contains a novel provision permitting the recovery of damages for arrest or prosecution or other consequential damages when wrongful dishonor is established as the proximate cause of such damages.<sup>330</sup>

<sup>320</sup> Clarke, Bailey, & Young, *supra* note 278, at 12. See also Leary, "Some Clarifications in the Law of Commercial Paper Under the Proposed Uniform Commercial Code," 97 U. Pa. L. Rev. 354, 360-70 (1949).

<sup>321</sup> Malcolm, *supra* note 296, at 295.

<sup>322</sup> On the other hand, Professor Beutel at one time vigorously castigated article 4 as a "piece of vicious class legislation" favoring bankers. Beutel, "The Proposed Uniform (?) Commercial Code Should Not Be Adopted," 61 Yale L.J. 334, 357-63 (1952).

<sup>323</sup> See discussion in text following note 256, *supra*.

<sup>324</sup> See discussion in text following note 341, *infra*.

<sup>325</sup> UCC § 4-402.

<sup>326</sup> *Ibid.* Accord as to innocent mistakes: *Citizens' Nat'l Bank v. Importers & Trader's Bank*, 119 N.Y. 195, 23 N.E. 540 (1890); *Levine v. State Bank*, 80 Misc. 524, 141 N.Y. Supp. 596 (1st Dep't 1913).

<sup>327</sup> Compare *Clark Co. v. Mt. Morris Bank*, 85 App. Div. 362, 83 N.Y. Supp. 447 (1st Dep't 1903), *aff'd*, 181 N.Y. 533, 73 N.E. 1133 (1905).

<sup>328</sup> Compare *Wildenberger v. Ridgewood Nat'l Bank*, 230 N.Y. 425, 130 N.E. 600 (1921).

<sup>329</sup> Compare *Nealis v. Industrial Bank of Commerce*, 200 Misc. 406, 107 N.Y.S.2d 264 (Sup. Ct., New York County 1951).

<sup>330</sup> No New York decisions involving damages for arrest and prosecution caused by



### B. *Stop Payment* (4-403)

The drawer's right to stop payment is not treated by the N.I.L., but several states have enacted controlling statutes.<sup>331</sup> The Code provides for the right of the drawer, by timely action, to stop payment on a check not yet accepted or paid.<sup>332</sup> Oral stop payment orders are validated for 14 days unless confirmed in writing within that period. The written order is effective for six months unless renewed in writing.<sup>333</sup> The provision giving effect to the oral order has been heavily attacked from the time of its drafting.<sup>334</sup> The common and statutory law of most states makes oral orders effective.<sup>335</sup> The six month's limit on written orders is in conformity with the time periods imposed by the majority of statutes enacted on this subject.<sup>336</sup>

The Code also contains a provision requiring that a stop payment order be received at such time and in such manner as to afford a reasonable opportunity for the bank to act.<sup>337</sup>

New York has long adhered to the doctrine of "ratification" in dealing with cases of inadvertent payments by banks over stop payment orders. If a customer ratifies the payment by the payor bank, then the customer is barred in his action seeking a recredit to his account. Although "ratification" has been much discussed, there are relatively few cases demonstrating the application of the doctrine. In *American Defense Soc'y v. Sherman Nat'l Bank*,<sup>338</sup> the court stated that ratification may be evidenced by the fact that the customer "had credited himself upon its books with payment or had in any way recognized his receipt of the money. . . ." <sup>339</sup> To be considered in connection with the doctrine of

wrongful dishonor have been found. See, however, *Robbins v. Bankers Trust Co.*, 4 Misc. 2d 347, 157 N.Y.S.2d 56 (Sup. Ct., Bronx County 1956). See *Morris*, "Bank's Liability To Its Depositor For His Arrest As the Result of the Bank's Failure To Have Properly Honored His Check," 78 Banking L.J. 491 (1961).

On wrongful dishonor generally see *Brady, Bank Checks* 363-74 (Bailey ed. 1962), reprinted from 79 Banking L.J. 278-86 (1962); 1 Paton, *supra* note 313, at 1112-23.

<sup>331</sup> See collection of statutes in 3 Paton, *supra* note 313, at 3462-63.

<sup>332</sup> UCC § 4-403(1). Accord, *American Defense Soc'y v. Sherman Nat'l Bank*, 225 N.Y. 506, 122 N.E. 695 (1919). See generally Note, 28 Ind. L.J. 95 (1952).

<sup>333</sup> UCC § 4-403(2). Oral orders are effective in New York. *K & K Silk Trimming Co. v. Garfield Nat'l Bank*, 127 Misc. 27, 215 N.Y. Supp. 269 (1st Dept., 1926).

<sup>334</sup> See Leary, "Some Clarifications in the Law of Commercial Paper Under the Proposed Uniform Commercial Code," 97 U. Pa. L. Rev. 354, 365-66; (1949); 1954 N.Y. Law Revision Comm'n Rep. 306; N.Y. Clearing House Ass'n Rep. on the Uniform Commercial Code 25 (Dec. 1, 1961).

<sup>335</sup> *Brady, Bank Checks* 425 (Bailey ed. 1962), reprinted from 79 Banking L.J. 194 (1962).

<sup>336</sup> See statutes referred to in note 331, *supra*.

<sup>337</sup> UCC § 4-403(1). Accord, *A. Sidney Davison Coal Co. v. National Park Bank*, 201 App. Div. 309, 194 N.Y. Supp. 220 (1st Dep't 1922). See also *Davis, Inc. v. Chemung Canal Trust Co.*, 9 App. Div. 2d 562, 189 N.Y.S.2d 320 (3rd Dep't 1959).

<sup>338</sup> 225 N.Y. 506, 122 N.E. 695 (1919).

<sup>339</sup> The court also states, however, that the customer may "not make a profit out of the bank's mistake and could only recover that, which it lost." *Id.* at 509. 122 N.E. at 695-96. Compare *Ted Granville Co. v. Chemical Bank and Trust Co.*, 8 Misc. 2d 806, 160 N.Y.S.

ratification, is the nature of the customer's action against the bank for erroneously paying over the stop payment order. Historically, the New York courts have adhered to a theory of "account" with the face amount of the check constituting the measure of recovery.<sup>340</sup> No obligation has been imposed on the customer to prove his actual loss as part of his prima facie case, and the bank has not been permitted to defend by showing a discharge of the customer's obligation to the payee.<sup>341</sup>

### C. Payor Bank's Right to Subrogation (4-407)

The Code draftsmen have provided a right of subrogation to the payor bank in an effort to compensate for the burden imposed by the anti-exculpation clause provision and the rights afforded to customers to stop payment on their checks. An illustrative fact pattern demonstrating a need for such a provision was related in the 1954 Law Revision Commission hearing by Mr. Walter Malcolm.<sup>342</sup> A lady took her fur coat to a furrier for repairs. When she called for the coat she was told that the charges were one hundred fifty dollars. She protested that this was an exorbitant price and argued that the job was only worth fifty dollars. The furrier replied that unless she paid his price, she would not get her coat. The lady grudgingly drew her check for one hundred fifty dollars and obtained her coat. Shortly after leaving the furrier she telephoned her bank and stopped payment. The bank overlooked the stop payment order and paid the check, charging the lady's account. In due course the lady discovered the error and demanded that her account be restored. The bank officials attempted to mollify her by offering to recredit her account for one hundred dollars since she had acknowledged that the repair job was worth at least fifty dollars. She refused and insisted that the full one hundred fifty be credited. Suit was brought against the bank by the lady and the bank, in turn, sued the furrier on the theory that if the bank was indebted to the lady, it had a claim against the furrier. The actions were tried in a lower court in Massachusetts, the bank suffering defeat in both actions. The lady was awarded the full one hundred fifty dollars and the judgment was rendered in favor of the furrier in the bank's action against him.

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2d 959 (1957). See also on ratification, *Woodmere Cedarhurst Corp. v. National City Bank*, 157 Misc. 660, 284 N.Y. Supp. 238 (1st Dep't 1935); *Kasnowitz v. Manufacturers Trust Co.*, 172 Misc. 242, 14 N.Y.S.2d 831 (N.Y. City Court 1939).

<sup>340</sup> Morrison & Sneed, "Bank Collections: The Stop-Payment Transaction—A Comparative Study," 32 *Texas L. Rev.* 259, 313 (1954).

<sup>341</sup> See *American Defense Soc'y v. Sherman*, supra note 338. See also *Woodmere Cedarhurst Corp. v. National City Bank*, supra note 339. 45 *Yale L.J.* 1134 (1936). See also 1955 N.Y. Law Revision Comm'n Rep. Vol. 2 at 67; Comment, 20 *U. Chi. L. Rev.* 667 (1953); Note, 40 *Harv. L. Rev.* 110 (1926).

<sup>342</sup> 1954 N.Y. Law Revision Comm'n Rep. 468.

The lady got her repair job for nothing, the furrier kept the full price, and the bank was out one hundred fifty dollars as a result of some technical rules of law that here seemed to work an unjust result.<sup>343</sup> The new subrogation provision in the Code is designed to give the bank in such a situation the right to be subrogated to both any claim that its customer, the lady, might have against the payee furrier and the rights that the payee may have against the customer. In some states this Code provision would continue similar rules found in local statutes.<sup>344</sup> In other states the provision offers a workable and equitable device for avoiding the harshness of the rules of stop payment.<sup>345</sup> In New York some difficulty may be encountered in view of the Code language that "to prevent unjust enrichment . . . the payor bank shall be subrogated . . ."<sup>346</sup> The problem is presented by the fact that a recent decision of the Court of Appeals has announced that there is no unjust enrichment when a bank inadvertently pays over a stop order notwithstanding that the customer's obligation is discharged in whole or in part by such payment.<sup>347</sup>

#### D. *Stale Checks* (4-404)

Under existing law a bank to which is presented a check dated substantially earlier than the day of presentment, is faced with a serious dilemma. If the check is "stale" then the bank may not charge the drawer's account unless the payment is made with the drawer's consent. On the other hand, if the check is not "stale" and the bank refuses payment, the bank may be liable to the customer for wrongful dishonor. To alleviate this problem stale check statutes have been adopted in some twenty-six jurisdictions, fifteen adopting a one-year limitation, and eleven a six-month limitation.<sup>348</sup>

New York has no such statute. How old a check has to be before it becomes "stale" is not at all certain. The Code provision solves this dilemma by specifically permitting a bank to refuse to pay an item more than six months after its date.<sup>349</sup> The Code contains an additional

<sup>343</sup> In a letter to the Law Revision Commission, Mr. William Wemple suggested that the New York doctrine of ratification might justify the bank in charging the lady's account in this case. 1954 N.Y. Law Revision Comm'n Rep. 364-68. Quære whether retaining the coat would operate as ratification. What else was she supposed to do with it?

<sup>344</sup> 6 La. Rev. Stat. § 42 (1950); N.J. Stat. Ann. 17: 9 A-225(B)(4) (New Jersey statute replaced by UCC § 4-407).

<sup>345</sup> For a discussion of the present law of subrogation in this context, see references in note 341, *supra*.

<sup>346</sup> UCC § 4-407.

<sup>347</sup> *Chase Nat'l Bank v. Battat*, 297 N.Y. 185, 78 N.E.2d 465 (1948). See also 1955 N.Y. Law Revision Comm'n Rep. 1553.

<sup>348</sup> Leary, *supra* note 334, at 364. See also 1 Paton, *supra* note 313, at 1107-12.

<sup>349</sup> UCC § 4-404. See *Goldberg v. Manufacturers Trust Co.*, 199 Misc. 167, 102 N.Y.S.2d 144 (N.Y. Munic. Ct. 1951). See also § 3-304(3)(c) and discussion in text following note 101, *supra*.

provision permitting the bank to pay checks even after six months so long as the bank pays in "good faith."<sup>350</sup> This latter provision has been criticized by the New York City bankers. The criticism stems from a legitimate concern over the meaning of good faith, defined earlier in the Code as "honesty in fact."<sup>351</sup> The bankers have urged abandoning the good faith provision and substituting language permitting the banks to pay at any time in the absence of an effective stop payment order.<sup>352</sup> This would represent a complete departure from the "stale check rule."

Re-insertion of the commercial reasonableness standard might be desirable here. "Honesty in fact" in this context seems virtually meaningless. The provision was apparently designed to protect banks in paying checks which they legitimately, honestly, or in good faith believed their customers would want to have paid. Such checks might include checks payable to the order of tax collectors or insurance companies. The problem, of course, is particularly acute when the drawer cannot be reached.

#### E. *Payment of Checks After Death or Incompetence of Customer* (4-405)

The effect of the customer's death or incompetence on the authority of a payor to pay is set forth in section 4-405. While in general an agency is revoked automatically by death<sup>353</sup> a well recognized exception protects a bank in paying a check or draft without notice of the death of the drawer.<sup>354</sup> Several states have enacted statutes permitting banks to pay for a limited period after death regardless of notice.<sup>355</sup> The Code includes a provision, according with New York decisional law,<sup>356</sup> which authorizes a bank to pay a depositor's checks until it has "knowledge" of the depositor's death. The Code adds a provision, contrary to present law in New York, but similar to the statutes in many states, providing a ten day period even after knowledge of death during which the payor bank may pay or certify checks.<sup>357</sup> The new statute also substitutes a clear rule for a present disparity among the cases in the related drawer-incompetency situation.<sup>358</sup>

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<sup>350</sup> *Ibid.*

<sup>351</sup> UCC § 1-201(19). See discussion of "good faith" in text accompanying note 87, *supra*.

<sup>352</sup> N.Y. Clearing House Ass'n Rep. on the Uniform Commercial Code 25-26 (1961).

<sup>353</sup> Restatement (Second), Agency § 120(1).

<sup>354</sup> *Id.* at § 120(2); *Glennan v. Rochester Trust & Safe Deposit Co.*, 209 N.Y. 12, 102 N.E. 537 (1913); *1 Paton*, *supra* note 313, at 1079-81.

<sup>355</sup> *1 Paton*, *supra* note 313 at 1085-86.

<sup>356</sup> *Glennan v. Rochester Trust & Safe Deposit Co.*, *supra* note 354.

<sup>357</sup> UCC § 4-405(2). See generally *Leary*, *supra* note 334, at 369-70.

<sup>358</sup> The law in New York is unsettled as to whether a bank having knowledge of the actual insanity of its customer, not judicially declared incompetent, must honor his checks. *Riley v. Albany Sav. Bank*, 36 Hun 513 3rd Dep't, *aff'd*, 103 N.Y. 669 (1886); *Mace v. Rockland County Trust Co.*, 249 App. Div. 754, 291 N.Y. Supp. 835 (2d Dep't 1935). Compare *Wallis v. Manhattan Co.*, 2 Hall 495 (N.Y.S. Ct., 1829).

### F. *Duty to Examine Returned Vouchers* (4-406)

Although not governed by statute in New York, decisional law imposes the duty on depositors to use reasonable care in examining returned vouchers and reporting unauthorized signatures and alterations.<sup>359</sup> The Code includes a provision requiring the depositor to exercise reasonable care and promptness in examining his statements and items.<sup>360</sup> On a showing by the bank that the customer failed to exercise reasonable care and promptness, the bank is able to avoid liability on an altered item or an item bearing the unauthorized signature of the customer. The customer is further precluded from asserting unauthorized signatures or alterations by the same wrongdoer on items paid by the payor during a period measured from the fourteenth calendar day after the availability of the first item and statement (or measured from an earlier date if reasonable) until notification by the customer.<sup>361</sup> Backstopping these hard to define duties imposed on customers are the absolute time limits, later provided in the same section.<sup>362</sup> A one-year statute of limitation is provided as to the drawer's signature and alteration.<sup>363</sup> The Code extends New York's two-year statute of limitations as to forged or unauthorized indorsements to three years.<sup>364</sup> The Code section further differs from the present statutes in: (1) its application to any "item," not merely checks; (2) the inclusion of any alterations, not merely "raising"; and (3) the application of this rule where the bank merely holds the customer's statement and items pursuant to his request or otherwise makes them available to him.

### *Part 5: Collection of Documentary Drafts*

These four sections,<sup>365</sup> located in article 3 in the 1952 draft,<sup>366</sup> add novel provisions regulating the handling of documentary drafts processed by banks for collection but normally payable by parties other than banks. There is very scanty New York authority in point.<sup>367</sup> To be read in

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There is authority that the adjudication of insanity itself is regarded as notice for the purpose of terminating the agency of a bank to deal with collateral whether or not the bank, in fact, knows of the adjudication. *McNerney v. Aetna Life Ins. Co.*, 284 App. Div. 21, 130 N.Y.S.2d 152 (4th Dep't 1954), *aff'd*, 308 N.Y. 916, 127 N.E.2d 79 (1955). The Code, in requiring actual knowledge of the adjudication, would change present law.

The Court in the *McNerney* case held that the bank's agency, as pledgee, was coupled with an interest and not revoked.

<sup>359</sup> *Critten v. Chemical Nat'l Bank*, 171 N.Y. 219, 63 N.E. 969 (1902).

<sup>360</sup> UCC § 4-406(1).

<sup>361</sup> UCC § 4-406(2).

<sup>362</sup> UCC § 4-406(4).

<sup>363</sup> *Ibid.* Accord N.Y. Negotiable Instr. Law § 326.

<sup>364</sup> Compare UCC § 4-406(4) with N.Y. Negotiable Instr. Law § 43.

<sup>365</sup> UCC §§ 4-501, 4-502, 4-503, 4-504.

<sup>366</sup> See text following note 221 *supra*.

<sup>367</sup> See Hogan & Penney, "Annotations of the Uniform Commercial Code to the Statutory

conjunction with this part is the earlier section 4-210 permitting a presenting party to notify the primary party that the instrument is held at the bank for acceptance or payment.<sup>368</sup>

#### CONCLUSION

Lest the foregoing discussion stir apprehension in the mind of the reader having labored this far, let it be said again that articles 3 and 4 are basically restatements of present law. Of necessity, attention has been directed to innovations. Largely unsung were the instance after instance of rephrasings or repetitions of present N.I.L. and other statutory provisions. With few exceptions the new statute appears to bring us the best of old and new. What has worked and proven reasonable is continued. Most of the old questions have been answered. This is not to say for a moment that the new statute is perfect or free from perplexities. Indeed, a whole new generation of critics with scalpel and pen "at the ready" have even now undertaken the task of raising new and as yet unnoticed questions of statutory interpretation. Though the practicing bar should take comfort in the notion that many of their problems have been solved, they should also be mindful of potential difficulties on the road ahead. I am sure that they would not begrudge scholars this happy prospect. After all, this and the confusion of generations of law students are the principal objects of the scholar's life.

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and Decisional Law of New York State, New York Annotations to Uniform Commercial Code and Report of Commission on Uniform Commercial Code pp. 162-64 (1961).

<sup>368</sup> Compare N.I.L. § 74 (N.Y. Negotiable Instr. Law § 134) (instrument must be exhibited).