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Some Observations Concerning Article 3 of the Uniform Commercial Code

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SOME OBSERVATIONS CONCERNING ARTICLE 3 OF THE UNIFORM COMMERCIAL CODE

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The now common tendency to characterize article III of the Uniform Commercial Code as a conservative statute which does little more than resolve the conflicts of authority which had developed under the NIL probably can be traced to Dean Frederick K. Beutel. Criticizing article III in 1951, Dean Beutel stated that:

> "The first outstanding change [made by article III] which strikes the eye of one intimately acquainted with the subject is that the draftsmen of the present Code have attempted to codify the holdings of the courts and to settle most of the numerous judicial conflicts which have appeared under seventy sections of the N.I.L. . . . There seems to have been an attempt in these changes to follow the weight of judicial authority rather than any consistent theory."[1]

Proponents of article III found it useful not to attack this statement, but, on the contrary, to use it to rebut the assertion that the article effected a general overhaul of the law of commercial paper. Thus, for example, when the Chase Bank opposed article III in the hearings conducted by the New York Law Revision Commission on the ground that the new statute completely revised the NIL and its enactment, therefore, "would result in a discarding of nearly all case law and experience built up over a period of fifty years," a spokesman for the Code, Professor Arthur E. Sutherland, responded by quoting the remarks of Dean Beutel set out above. Thus posited, Professor Sutherland concluded that:

> "Certainly it was not the intention of the lawyers who participated in drafting the Code, including men from all over the United States whose practice had led them into all fields of commerce, to produce a revolution in the law of negotiable instruments. Rather it was to bring the statutory law up to date, in the light of contemporary practices, and

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1. Beutel, *Comparison of the Proposed Commercial Code, Article 3, and the Negotiable Instruments Law*, 30 NEB. L. REV. 531-32 (1951).

the judicial decisions in the half-century and more since the negotiable instruments law was drafted."[2]

It was probably this kind of process, engaged in by different people at different places and times, which created the impression that article III is basically nothing more than a mere declaration of the best negotiable instruments law which has developed in the United States over the past one hundred years.[3] Whatever its genesis, this description is too modest. Article III makes at least three major contributions to the law of commercial paper: (1) it limits its own scope to short-term money instruments, thus freeing long-term investment paper for the separate coverage of special rules provided by article VIII; (2) it coordinates its rules with the law of bank deposits and collections, set out in article IV, thus facilitating the banking system; and (3) it makes certain basic and sometimes novel changes in the law of commercial paper, thus providing demonstrably better solutions to problems, some of which are age-old.

I. Scope Limited to Commercial Paper

Bonds came into general use in the United States prior to the Civil War as a method of raising the enormous amounts of capital needed to build the nation's railroads and canals.[4] Investors undoubtedly[5] regarded these instruments as negotiable in the sense of feeling that a bona fide purchaser for value and without notice should take the paper free and clear of defenses of the issuer and remote parties and also free of claims or equities of prior ownership. Some courts honored this expectation and held bonds negotiable without showing undue concern for the language employed in the instruments.[6] Other courts, however, regarded bonds as "mere bills or notes" and held that their negotiability depended upon their ability to satisfy the

2. 1 New York Law Revision Commission Report 52 (1954).

3. *Id.* at 241.

4. See, generally, Poor, History of Railroads and Canals (1860), cited in Steffen, Cases on Commercial and Investment Paper 198 (3d ed. 1964).

5. There is an inveterate tendency on the part of investors to regard securities as negotiable, even in the face of judicial hostility. As Carlos L. Israels has stated, "Perhaps no assumption is more generally made in our free securities markets than that all instruments which would be within the catchall phrase 'commonly known as a security' are technically 'negotiable instruments' as that term is used in the Uniform Neogtiable Instruments Law." Israels, *Investment Securities as Negotiable Paper*, 13 Bus. Law. 676 (1958).

6. See, for example, The Junction R.R. v. Cleneay, 13 Ind. 161 (1859); Carr v. Le Fevre, 27 Pa. St. 413 (1856); American Nat'l Bank v. American Wood Paper Co., 19 R.I. 149, 32 Atl. 305 (1895); see, generally, Steffen, Cases on Commercial and Investment Paper 198 (3d ed. 1964).

formal requisites of negotiability laid down by the common law for these short-term money instruments.[7]

Thus, when the NIL was promulgated near the turn of the century, there was a sharp division among common law jurisdictions as to the standard by which the negotiability of bonds was to be tested.

Since security specialists were doubtless aware of this state of affairs and knew how important it was to have the negotiability of bonds and other investment securities tested by standards somewhat more relaxed than those applicable to promissory notes, checks and drafts, it is nothing short of astonishing to find no record of any efforts made by this group to get securities excluded from the coverage of the NIL. Apparently they assumed that the courts would surely treat securities as sui generis instruments falling completely outside the scope of the statute. This assumption may have been predicated on the fact that the NIL did not specifically cover securities and, in section 196, stated that the law merchant should govern cases not provided for by the act. Whatever its basis, the assumption proved to be incorrect in many states and decisions were handed down that securities were negotiable or non-negotiable depending on their ability to satisfy the formal requisites of negotiability set out in the NIL.[8] In the most celebrated of these decisions, *President & Directors of Manhattan Co. v. Morgan,*[9] Justice Cardozo admitted, at least impliedly, that interim certificates were regarded as negotiable by those dealing on the securities market. But, he said, this custom of the trade — the law merchant — could not make these certificates negotiable in the face of specific prohibitions found in the NIL.

> "The law merchant cannot prevail against prohibitions so specific. In holding otherwise, we should do more than supplement the statute. We should disregard and contradict it. The plaintiff's case is not helped by section [196 of the NIL] . . . to the effect that, 'in any case not provided for in

7. See, for example, Ide v. Passumpsic and Connecticut Rivers R.R., 32 Vt. 297 (1859) ("bonds . . . are in fact . . . mere bills or notes, and as strictly negotiable as bank bills.") ; Parsons v. Jackson, 99 U.S. 434 (1878).

8. See, for example, President and Directors of Manhattan Co. v. Morgan, 242 N.Y. 38, 150 N.E. 594 (1926) ; Fidelity & Deposit Co. of Maryland v. Andrews, 244 Mich. 159, 221 N.W. 114 (1928) ; Kohn v. Sacramento Electric, Gas & Ry. Co., 168 Cal. 1, 141 Pac. 626 (1914) ; King Cattle Co. v. Joseph, 158 Minn. 481, 198 N.W. 798, 199 N.W. 437 (1924).

9. See cases cited note 8 *supra.*

this chapter the rules of the law merchant shall govern.' The difficulty is that the case *is* provided for. Unforeseen situations may reveal gaps in the statutory rules. In such circumstances the law merchant is competent to fill them. It is without power to annul what the statute has ordained."[10]

Obviously these decisions holding investment securities to be within the scope of the NIL did great harm to the securities market, because they overlooked the functional differences between investment paper and commercial paper. Thus, though bonds and promissory notes are formally similar, the former usually involve long-term investments, purchased after careful consideration, and not frequently transferred, by investors relying heavily on group action in the case of default. These instruments are frequently several hundred, or even thousand, words in length and are complicated by security, redemption, tax, sinking-fund, registration and other clauses. Notes, on the other hand, are "couriers without luggage"[11] designed to generate short-term financing on a low discount basis. Low discounting depends on keeping the financer's risks and administrative costs at a minimum, and this, in turn, requires that negotiable, commercial-paper, instruments assume a form which will allow the discounter to determine at a glance — surely without elaborate investigation — their present value. Consequently, it is the general rule that the negotiability of a promissory note is defeated by a clause which makes its promise subject to the terms of an extrinsic document, not necessarily because the extrinsic agreement may contain terms and conditions which are offensive to negotiability — though this is usually the case — but because the necessity of having to scrutinize the incorporated agreement increases the cost of adminstering short-term paper to such an extent that it makes low discounting impossible. In short, a long-term investor will routinely study indentures and the like which are incorporated by reference into bonds, and therefore a "subject to" clause does not militate against investment securities performing the functions for which they were created; short-term financers, on the other hand, cannot afford to check out extrinsic matters, and therefore a "subject to" clause in a

10. President and Directors of Manhattan Co. v. Morgan, 242 N.Y. 38, 49-50, 150 N.E. 594, 597-98 (1926).

11. See, Overton v. Tyler, 3 Pa. 346 (1846) in which Chief Justice Gibson announced his famous dictum that a negotiable instrument "is a courier without luggage."

promissory note militates against the low-discounting function for which it was created.

As a result of these considerations, a sharp reaction set in against the decisions holding that the NIL rules also pertained to investment securities. This reaction apparently induced some courts to change their minds. In New York, for example, the case of *Enoch v. Brandon,*[12] decided only two years after *President & Directors of Manhattan Co. v. Morgan,* held a bond negotiable in spite of the fact that its payment was made "subject to" the terms of a trust indenture. This decision, though meeting some critical approval,[13] actually resulted in a great disservice to the commercial world, and particularly the world of commercial paper, because it was based not on the proposition that the NIL does not, or should not, apply to bonds, but that the NIL permitted paper containing "subject to" language to be negotiable. How this decision led the Louisiana court, for example, into a serious error with respect to promissory notes is explained by Dean Beutel in a brilliant article[14] in which he states that:

> "[The 'same sentence' doctrine][15] rose to plague the court in *Newman v. Schwarz.*[16] . . . But it is obvious that the 'same sentence' doctrine, even if it were sound, could apply only

12. 249 N.Y. 263, 164 N.E. 45 (1928).

13. See, for example, Note, 29 COLUM. L. REV. 365 (1929).

14. Beutel, *Common Law of Judicial Technique and the Laws of Negotiable Instruments — Two Unfortunate Decisions,* 9 TUL. L. REV. 64, 73-76 (1934).

15. Most courts agree with the statement made in Powell & Powell v. Greenleaf & Currier, 104 Vt. 480, 482-83, 162 Atl. 377, 378 (1932) : "Where the promise to pay is made 'subject to' some other contract referred to, the authorities seem to be agreed that the obligation is conditional and negotiability is destroyed. . . . On the other hand, the words 'as per terms of contract,' . . . in a promissory note . . . [is] held not to affect its negotiability. For a collection of cases, see HAWKLAND, CASES ON BILLS AND NOTES 18-19 (1956). But Louisiana never adopted the approach of arbitrarily finding that "subject to" promises are conditional and "as per" promises are not. Rather, its courts emphasize the position of the promissory language with respect to the words which refer to the extrinsic matter. If the qualifying language appears in the same sentence as the promissory words, the Louisiana courts usually have held the promise to be conditional. See, for example, Continental Bank & Trust Co. v. Times Publishing Co., 142 La. 209, 76 So. 612 (1917). On the other hand, if the qualifying language appears in a different sentence from the words of promise, they tend to find the promise unconditional. See, for example, Tyler v. Whitney-Central Trust & Sav. Bank, 157 La. 249, 102 So. 325 (1924) : This construction technique is what Dean Beutel calls "the same sentence doctrine."

16. 180 La. 153, 156 So. 206 (1934). In this case the statement, "Rent note. Subject to terms of lease Dated May 2, 1927" was written in red ink across the face of a promissory note. The court held that the promise was unconditional because the "subject to" statement did not relate to the unconditional promise of the maker and amounted to nothing more than a statement of the transaction which gave rise to the note.

where the words alleged to limit the promise were ambiguous. Even the cleverest counsel could not convince the most stupid of courts that words which clearly made the promise in the instrument dependent or conditioned upon some outside document would not destroy negotiability merely because they appeared in a separate sentence.

"When the 'same sentence' doctrine was established in the mind of the Louisiana Supreme Court in considering the facts of *Newman v. Schwarz* there still remained the herculean task of proving that the term 'subject to contract' was ambiguous. . . . Although there is not a word of this in the opinion, the record discloses that this point was hotly argued in the briefs, and herein lies the nub of the story of how a court can go entirely wrong by applying approved common law judicial technique to the interpretation of a statute.

"Up until 1928 all authorities agreed that the words 'subject to contract' no matter where they appeared in an otherwise negotiable instrument rendered it non-negotiable. . . . At this time there appeared in the Court of Appeals of New York the interesting and much discussed case of *Enoch v. Brandon*, which has mothered a whole litter of weasel cases sucking the life out of the N.I.L.

"[Because of this case] the Supreme Court of Louisiana, without a single dissenting vote, fell into the trap, rendering a decision [*Newman v. Schwarz*] which is not only contrary to the weight of authority under the N.I.L. but also contrary to the common sense dictionary meaning of the words of the note and of the statute."

Thus it became apparent, at least to critical observers, that the inclusion of investment securities within the scope of the NIL not only did serious damage to the securities market but was injurious to operations involving commercial paper as well. In some states this mischief was partially mitigated by the enactment of piecemeal legislation, the most popular model of which was the Hofstadter Securities Receipts Act of New York,[17] But it was clear from the start that fragmentary legislation was not the answer to this tough problem, and that only a comprehensive statute completely divorced from the law of commer-

17. N.Y. Sess. Laws 1926, c. 704.

cial paper and setting out detailed rules for investment securities could do the job.[18]

Therefore, article III makes a major contribution to commercial law by excluding from its scope the subject of investment securities. This exclusion is accomplished by section 3-103(1) which provides that:

> "This Article does not apply to money, documents of title or investment securities."

This restriction on its own coverage made by article III paved the way for article VIII which sets out detailed rules governing investment securities. To free the investor from the possibility that a particular security might be drawn in such a way as to satisfy the formal requisites of negotiability of article III as well as article VIII and thus put in doubt the applicable law, section 8-102(1) (b) states that in this case the law of article VIII shall govern.

Through these provisions of subordination and coordination the securities market is free for the first time in American history from the threat of having the negotiability of its instruments judged by a law having no functional relationship to it, and judges now know that they can rigorously apply the formal requisites of negotiability to notes, checks, and drafts without the possibility of injuring investment securities.

II. Coordination Effected with Article IV

Banks in the United States handle about fifty million checks a day. Large numbers of checks also were being collected by the banking system at the turn of the century, but the collection process had not then achieved, nor did it need, the speed and efficiency of today's operation. According to an Oregon case[19] as late as 1919 it was considered normal banking practice for the *president* of a bank to extract from the morning mail all the items sent for collection, to foot these checks up on an adding machine to ascertain that each total corresponded with the cash

18. See, Llewellyn, *Brief Statement for the Proponents: Article III*, in New York Law Rev. Comm. Doc. No. 65(c) — 1954 — 8593, p. 2:"Patchwork amendment could never produce an Article VIII. Only a Code could thus accommodate and give the needed detailed guidance to this burstive flood of transactions and instruments undreamed of when the Negotiable Instruments Law was formed by good and careful men in 1897."

19. Hunt v. Security State Bank, 91 Ore. 362, 179 Pac. 248 (1919).

letter, to examine each check to see that the signatures were genuine and that there were no irregularities, and finally to inspect the state of the drawer's account to determine whether there was a sufficient and free balance to make payment. It was during these halcyon days that the NIL was enacted, and it is not surprising to note that its draftsmen assumed that the banking system could operate smoothly on the basis of its general rules of commercial paper. Consequently, the new statute contained few provisions directly relative to bank collections. Perhaps special bank collection rules were not needed at this time, but as the nation developed into an industrial and commercial giant, the banking system was forced to overhaul its collection process with an aim toward developing greater speed and efficiency. This overhaul necessitated the enactment of a comprehensive bank collection law which would operate uniformly throughout the country. Uniformity was important because many items in the process of bank collection often cross state lines and comprehensiveness was indicated by the complexity which the process had assumed. In response to these needs, the American Bankers Association drafted a Bank Collection Code, but this "Code" was rejected in a number of states and thus never attained uniformity, and it was too incomplete to provide the comprehensive coverage that was needed. As a result, even in states in which the Bank Collection Code had been enacted, the NIL and the common law were frequently called upon to supplement its provisions. Of course, the technique of drafting a statute in such a way that it will be supplemented by another related statute is a wholly acceptable one, if the general and the supplementary laws are carefully coordinated. But no such coordination was effected by the Bank Collection Code, and this is just one of the reasons that its draftsmanship was characterized by one legal scholar as "fifth rate."[20] Though this criticism may be too strong, it is clear that the Bank Collection Code did not prevent the courts from making applicable to the collection process certain NIL rules that were completely at odds with banking practices which had streamlined the machinery employed in the collection of checks. For example, the bank collection process cannot run smoothly and speedily if collecting banks must investigate all indorsements to determine whether or not restrictions or conditions have been imposed. But in 1938 the New York Court of Appeals, because of provisions

20. Townsend, *The Bank Collection Code of the American Bankers Association*, 8 TUL. L. REV. 21, 236, 376 (1933).

of the Bank Collection Code and the NIL, held that a "for deposit" indorsement was restrictive and protected the indorser against all parties, including collecting banks, into whose hands the check might come.[21] The case involved an action against the Federal Reserve Bank for converting a check. The plaintiff, an illiterate woman, received the check late Friday upon the sale of real estate. She was persuaded by Handrulis to let him keep the check for her. She indorsed it "for deposit" and entrusted it to him. Subsequently, it was indorsed by one Alkoff and deposited in her account at Globe Bank. Globe then collected the check through the Federal Reserve Bank of New York. After the item was collected, Handrulis and probably Alkoff absconded with the proceeds. Plaintiff was allowed to prevail against an intermediate collecting bank on the theory that "the indorsement 'for deposit' gave notice of its restrictive and nonnegotiable character generally and of plaintiff's continued title to all parties into whose hands the check might come."

To hold an intermediate collecting bank to the terms of a restrictive indorsement placed on an instrument by some remote party might have been fair in the simpler days of the past, but it was an unfair and unworkable rule for the highly complex state in which banking found itself in the year 1938. As Professor Llewellyn was to say later, the restrictive indorsement proved to be a monkey-wrench thrown into the smooth-running machinery of bank collections.[22]

In correcting the matter of restrictive indorsements and similar impediments to good banking, the draftsmen of the UCC elected to follow the device of having specific banking rules supplemented by the general law of commercial paper, presumably on the ground that this approach avoids a great deal of duplication. Article IV sets out in fairly comprehensive detail a series of rules governing bank deposits and collections. Article III supplements these rules. The two articles are coordinated and their rules reflect a policy of implementing the efficient and speedy handling of checks. For example, the restrictive indorsement problem discussed above is solved by a provision in article III which is incorporated by reference into article IV. Section 3-206(2) provides that:

21. Soma v. Handrulis, 277 N.Y. 223, 14 N.E. 2d 146 (1938).
22. Llewellyn in 1 New York Law Revision Commission Report 194 (1954).

"An intermediary bank, or a payor bank which is not the depositary bank, is neither given notice nor otherwise affected by a restrictive indorsement of any person except the bank's immediate transferor or the person presenting for payment."

This section is incorporated into section 4-203, a provision announcing a general "chain of command" theory to the effect that only the instructions given by the immediate transferor — as contrasted with remote, earlier parties — are binding on collecting banks.

Through this kind of approach, article III does a great service to the banking industry by coordinating its rules with those of article IV and by providing solutions to modern bank collection problems.

III. Some Specific Changes in the Basic Law of Commercial Paper

Article III makes a number of changes in the law of commercial paper as it developed under the NIL. Only a few of these changes can be discussed here, but they should be sufficient to reveal the approach of the article and its thrust toward improving the law of commercial paper.

A. *Formal Requisites of Negotiability*

Section 3-104 provides that an instrument to be negotiable "within this article" must be signed by the maker or drawer, and contain an unconditional promise to pay a sum certain in money on demand or at a definite time, to order or to bearer. These formal requisites are substantially identical to those found in section 1 of the NIL. Subsequent sections of the UCC, however, elaborate the provisions of section 3-104 in such a way as to make some basic alterations in the old law.

One interesting elaboration is found in section 3-105 which outlines the conditional or unconditional character of promises or orders for purposes of negotiability. This section follows the old rule that a promise or order is not unconditional if the instrument states that it is to be paid only out of a particular fund or source,[23] but it makes an exception in two situations which

23. NIL § 3-105(2)(b).

have been bothersome in the past. The first exception relates to paper issued by a government or governmental agency.[24] Governmental units in many states are authorized to execute short-term paper, as well as long-term bonds, to raise capital for public improvements. Frequently, the authorizing statute requires that the paper so issued must be redeemed by funds raised from special assessments of the property benefited by the public improvement and, in this case, the borrowing instrument usually states that its payment is limited to this particular fund. Under traditional notions of commercial paper, such a statement destroys negotiability because the existence of the fund is a condition precedent to the promisor's duty to pay.[25] Nevertheless, lenders and investors have shown a willingness to accept governmental paper so conditioned, and the draftsmen of the UCC saw no merit in denying them the protection of the concept of negotiability. This protection is needed primarily where the instrument has been stolen, because it will enable a holder in due course to take free and clear of the ownership claim.[26] Presumably, the holder in due course will take subject to the possibility that the particular fund will not come into existence or be adequate to make full payment, because this condition is stated in the paper itself. The Code, therefore, seems to draw a distinction, once briefly made by the Washington courts,[27] between negotiability of government paper for purposes of cutting off ownership claims but not for purposes of taking free of conditions and contract defenses.

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24. Section 3-105(1)(g) provides that "A promise or order otherwise unconditional is not made conditional by the fact that the instrument is limited to payment out of a particular fund or the proceeds of a particular source, if the instrument is issued by a government or governmental agency or unit."

25. See, for example, Bank of California v. National City Co., 141 Wash. 243, 251 Pac. 561 (1926).

26. See § 3-305(1).

27. In Manker v. American Sav. Bank & Trust Co., 131 Wash. 430, 230 Pac. 406 (1924) bonds payable only from funds raised through special assessments were held non-negotiable. But Parker, J., dissented: "The local improvement bond here drawn in question is by its express terms, payable to bearer, as are manifestly all of the other bonds of the series to which it belongs. These bonds manifestly were issued for the express purpose of being transferred in the open market by mere delivery. *They may not be negotiable in that large and comprehensive sense which precludes the invoking against them of every possible defense which the city or the owners of the property which the burden might invoke, but, to my mind, they are pure negotiable instruments in the sense that their title passes from holders thereof to purchasers in good faith by mere transfer of possession.*" (Emphasis added.) 230 Pac. at 409. A subsequent case, Bank of California v. National City Co., 138 Wash. 517, 244 Pac. 690 (1926) adopted the view of the dissent in the *Manker* case. On rehearing, however, the court reversed itself and said that there are not two standards of negotiability, that an instrument is negotiable for all purposes or non-negotiable for all purposes..

A second exception to the "particular fund" doctrine is intended by UCC section 3-105(1) (h). This section provides that:

> "A promise or order otherwise unconditional is not made conditional by the fact that the instrument is limited to payment out of the entire assets of a partnership, unincorporated association, trust or estate by or on behalf of which the instrument is issued."

This section is directed toward the practice of some unincorporated associations which desire to limit the payment of promissory notes to the assets of the association, qua association, by expressly excluding the liability of the individual members of the firm. While such instruments are supported as generally as the negotiable instruments issued by corporations, which, of course, carry only the credit of the corporate entity since shareholders normally have no personal liability for corporate debts, technically they are payable only out of a particular fund, because the general credit of the association, which includes the personal responsibility of its members, is not made available for payment. As a result, some courts have held these instruments non-negotiable.[28] Other courts, however, deserting pure logic in the interest of practicality, have held that such paper may be negotiable.[29] There is no doubt that the draftsmen of the UCC intended to adopt this latter approach, for official comment 7 to section 3-105 states that:

> "Paragraph (h) of subsection (1) is new. It adopts the policy of decisions holding that an instrument issued by an unincorporated association is negotiable although its payment is expressly limited to the assets of the association, excluding the liability of individual members. . . ."

Unfortunately, however, the language of section 3-105(1) (h) does not clearly state a rule consistent with this policy, because it provides that the instrument of the unincorporated association may be negotiable when it "is limited to payment out of the *entire assets* of the partnership, unincorporated association . . . by or on behalf of which the instrument is issued." (Emphasis added.) The "entire assets" of a partnership or an

28. See, for example, Lorimer v. McGreevy, 229 Mo. App. 970, 84 S.W.2d 667 (1935), discussed in Notes, 49 HARV. L. REV. 478 (1936), 34 MICH. L. REV. 1030 (1936), 45 YALE L.J. 176 (1935).

29. See the leading case of Hibbs v. Brown, 190 N.Y. 167, 82 N.E. 1108 (1907).

unincorporated association include the personal liability of its members, and paper issued by such business organizations which exempts this liability is not backed by its entire assets. But the words "entire assets" should not be given their plain meaning in view of the fact that the word "limited" in the phrase "limited to payment out of the entire assets" would be rendered meaningless by such a construction and by the fact that the draftsmen have made their purposes clear in the official comment to the section. Fairly construed, section 3-105(1) (h) gives members of unincorporated associations the advantages of shareholders of corporations in this limited situation.

A major improvement in elaborating the formal requisites of negotiability is found in section 3-109(1) (c) which provides, in effect, that the certainty of time payment is not affected by "any acceleration" clause, whether the accelerating event is automatic or at the option of either the holder or the obligor. Under the NIL acceleration clauses were sometimes held to militate against negotiability on the ground that they rendered the time of payment uncertain. For example, instruments payable at a fixed date or sooner "on demand of the holder if he deems himself insecure" were consistently struck down as non-negotiable.[30] Actually, of course, an instrument containing such a clause or, indeed, any acceleration clause is no more uncertain as to its time of payment than a demand instrument which was explicitly permitted to be negotiable under the NIL. But the courts have recognized that deeming-himself-insecure acceleration clauses are not to be treated as the equivalent of promises to pay on demand, because the former, unlike the latter, imply some limitations on the right to call the instrument. Judicial hostility toward acceleration clauses, and particularly those which apparently give the holder an unlimited freedom to declare the instrument due, seems to reflect misgivings regarding the abuse of discretion to accelerate and difficulties in determining the limits on that discretion, rather than concern over the time of payment. In short, the courts, unwilling to treat broad acceleration clauses as making the instrument payable on demand because of implied limitations on the right to declare

30. See, for example, Murrell v. Exchange Bank, 168 Ark. 645, 271 S.W. 21 (1925); Moyer v. Hyde, 35 Idaho 161, 204 Pac. 1068 (1922); Puget Sound State Bank v. Washington Paving Co., 94 Wash. 504, 162 Pac. 870 (1917); *contra*, Dart Nat'l Bank v. Burton, 258 Mich. 283, 241 N.W. 858 (1932).

the paper due, have held the instrument non-negotiable where they have been unable to determine the scope of the limitations.

The UCC changes this approach. Section 3-109(1)(c) broadly validates all acceleration clauses, but section 1-208[31] provides safeguards against abuse and sets forth the limitations on the power to accelerate where wide acceleration language has been used. This approach makes it clear that the draftsmen of the UCC regard the matter of acceleration as one of good faith rather than as one of negotiability.

The broad validation of acceleration clauses by section 3-109(1)(c) probably will nullify one of the purposes of section 3-109(2). Section 3-109(2) attempts to change section 4(3) of the NIL which provided that an instrument is payable at a definite time for purposes of negotiability, if it is payable "on or at a fixed period after the occurrence of a specified event, which is certain to happen, though the time of happening is uncertain." This rule was formulated as a concession to individuals desiring to borrow on their inheritance by use of post-obituary notes (e.g., "I promise to pay six weeks after my Uncle George's death").[32] Post-obituary notes are neither mathematically nor commercially certain as to time of maturity, and there may be good reasons to preserve the defenses of parties who execute them. Because of these reasons, section 3-109(2) attempts to make post-obituary notes non-negotiable by providing that:

> "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."

This provision will effectively police post-obituary notes as now commonly drawn by making them non-negotiable. But a negotiable post-obituary note can be drafted under the Code by using an acceleration clause. A note, "I promise to pay six weeks after my Uncle George's death," would fail of negotia-

31. Section 1-208 provides that: "A term providing that one party or his successor in interest may accelerate payment or performance or require collateral or additional collateral 'at will' or 'when he deems himself insecure' or in words of similar import shall be construed to mean that he shall have power to do so only if he in good faith believes that the prospect of payment or performance is impaired. The burden of establishing lack of good faith is on the party against whom the power has been exercised."

32. For the origin of the rule, see Cooke v. Colehan, 2 Strange 1217, 93 Eng. Rep. 1140 (1743).

bility under section 3-109(2), but an effective post-obituary note, "I promise to pay 100 years from date, but payment shall be accelerated by the death of my Uncle George to a point of time six weeks after said death," would be negotiable under section 3-109(1)(c).

B. *Indorsements*

Reference already has been made in this article to the fact that the UCC solves a bank collection difficulty by exempting intermediate, collecting banks from restrictions placed on an instrument by a restrictive indorser. Other less significant changes also are made by the UCC respecting restrictive indorsements. Under section 3-206 a restrictive indorsee is allowed to be a holder in due course. That is to say, the UCC recognizes that one is not necessarily barred from the status of holder in due course by virtue of the fact that he has taken under a restrictive indorsement. This reverses the rule which has developed under the NIL.[33] Usually, of course, one taking under a restrictive indorsement will do so as an agent of the restrictive indorser and thus give no value for the instrument. In this case, he will not be a holder in due course, not because of his status of restrictive indorsee, but because the concept of holder in due course requires the giving of value. Occasionally the restrictive indorsee will give value, as, for example, where he takes the paper as a representative for some third party. In this situation, there is no merit in denying him the status of holder in due course if he has taken the paper before it was due and without knowledge of defenses. Thus, if *A* restrictively indorses paper, "Pay *B* only on trust for *C*," *B* should be able to cut off prior defenses if he has paid *A* for the instrument and otherwise satisfied the requirements of a holder in due course.

Section 3-204 of the UCC makes another important change respecting indorsements by reversing the common law dogma, "once bearer always bearer." This dogma expressed the rule that bearer paper, whether it became such because bearer on its face, or, if order on its face, by reason of a blank indorsement, could be negotiated by delivery alone. Because a blank indorsement was said to convert an instrument payable to order on its face into bearer paper, the dogma meant that even though the blank indorsement was followed by a special indorsement the

33. See, for example, Gulbranson-Dickinson Co. v. Hopkins, 170 Wis. 326, 175 N.W. 93 (1919).

instrument remained negotiable by delivery alone.[34] This rule limited the ownership rights of the special indorser, because it did not give him the power to determine future methods of negotiation. As a practical matter this prevented him from negotiating the paper in such a manner as to require the indorsement of his indorsee, thus depriving him of a means of obtaining evidence of the satisfaction of his own obligation. Moreover, the "once bearer always bearer" dogma was inconsistent with other commercial statutes which uniformly provided that the last indorsement determined future methods of negotiation.[35] Rectification is made by section 3-204(1) which provides that, "Any instrument specially indorsed becomes payable to the order of the special indorsee and may be further negotiated only by his indorsement," and by section 3-204(2) which states that, "An indorsement in blank specifies no particular indorsee and may consist of a mere signature. An instrument payable to order and indorsed in blank becomes payable to bearer and may be negotiated by delivery until specially indorsed."

C. *Liability of Parties*

The UCC makes several interesting and important changes concerning the liability of parties to commercial paper. One of these changes reverses section 15 of the NIL. Under NIL section 16, lack of delivery of a completed instrument gives rise to a personal defense only. Similarly, under NIL section 14, the unauthorized completion of a partially blank instrument delivered to the payee or holder is only a personal defense. But the two situations taken together — the case of non-delivery of an incomplete instrument — gives rise to a real defense under section 15 of the NIL. This rule seems illogical in view of the fact that its component parts are regarded as creating a personal defense only, and it tends to throw the risk of loss on to the remote payer who is not in a good position to police against it. For this reason, some courts operating under the

34. Smith v. Clarke, Peake 295, 170 Eng. Rep. 162 (1794); Mitchell v. Fuller, 15 Pa. 268, 53 Am. Dec. 594 (1850); Howry v. Eppinger, 34 Mich. 29 (1876).

35. See, for example, § 29 of the Uniform Bills of Lading Act which provides that, "A negotiable bill may be negotiated by the endorsement of the person to whose order the goods are deliverable by the tenor of the bill. Such endorsement may be in blank or to a specified person. If endorsed to a specified person, it may be negotiated again by the endorsement of such person in blank or to another specified person. Subsequent negotiation may be made in like manner." An almost identical provision is found in section 38 of the Uniform Warehouse Receipt Act.

NIL largely ignored section 15 by estopping its assertion.[36] Sections 3-305, 3-306 and 3-115 of the UCC offer a preferable solution, namely a rule which makes lack of delivery and unauthorized completion a personal defense only. Official comment 5 to section 3-115 explains the reason behind the change:

> "A holder in due course sees and takes the same paper, whether it was complete when stolen or completed afterward by the thief, and in each case he relies in good faith on the maker's signature. The loss should fall upon the party whose conduct in signing blank paper has made the fraud possible, rather than upon the innocent purchaser."

An analogous problem — that of the "fictitious payee" — similarly has been solved in a straight-forward manner by the UCC. Under traditional notions of commercial paper, the holder of an order instrument is not divested of his rights if the paper is stolen from him and his indorsement is forged to it. Consistently, the maker or drawee cannot discharge himself from liability by paying the possessor of such an instrument. A different rule, of course, applies to bearer paper. Where paper apparently drawn to the order of a designated payee has been issued as part of a fraudulent scheme under which the person drawing the paper knew that the designated payee was to have no interest in it, the NIL protected payers by characterizing the paper as "bearer" in form. In this connection section 9(3) of the NIL provides that, "The instrument is payable to bearer when it is payable to the order of a fictitious or non-existing person and such fact was known to the person making it so payable." But often in "fictitious payee" cases, one party — often a fraudulent payroll clerk — causes the instrument to be executed by another party — such as the treasurer of a company — who does intend the designated payee to have an interest in it. If the payroll clerk then forges the payee's name to the instrument, should a bank be able to debit the account of the drawer upon making payment, or must it regard the paper as "order" in form and re-credit the account upon notification of the forged indorsement? This question has generated a king-size split of authority under the NIL,[37] and the technicality of the rules in-

36. The leading case is Weiner v. Pennsylvania Co. for the Insurance on Lives, etc., 160 Pa. Super. 320, 51 A.2d 385 (1947). But estoppel is not available in all cases. See, for example, Joseph Heimberg, Inc. v. Lincoln Nat'l Bank, 113 N.J.L. 76, 172 Atl. 528 (1934).

37. For a collection of cases, see BRITTON, BILLS AND NOTES 425-40 (2d ed. 1961).

volved often have prevented the courts from coming to grips with the basic problems of fault and administration of risk which underlie the matter.

Section 3-405 recognizes that various kinds of fraud practiced on business concerns involving commercial paper are business and not banking risks.[38] Thus, commercial paper made payable to fictitious employees (payroll fraud), to nonexistent or fictitious suppliers (invoice fraud) or to impostors create situations in which the bank paying the items can debit the account of the business concern victimized by these schemes. It achieves this result by making effective the indorsement "by any person in the name of a named payee." This solution is regarded as superior to that of finding the paper to be bearer in form, because, as official comment 1 to the section indicates, "on the face of things they are payable to order and a subsequent taker should require what purports to be a regular chain of indorsements."

One important change in the laws governing the liability of secondary parties is the rule of section 3-501(3) eliminating the requirement of protest except upon dishonor of a draft which on its face appears to be either drawn or payable outside the United States. A holder, of course, is still permitted to make protest on any dishonor, but secondary parties are entitled to it only in the case of the international draft. This rule will aid bank collections and obviate unnecessary expense.

IV. *Tabular Summary Comparing the NIL with article III of the UCC*[39]

N.I.L. Section	*U.C.C. Section*	*Remarks*
1	3-103	Investment securities no longer covered by the law of negotiable instruments.

38. Section 3-405 provides that, "(1) An indorsement by any person in the name of a named payee is effective if (a) an imposter 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. (2) Nothing in this section shall affect the criminal or civil liability of the person so indorsing."

39. Reprinted from HAWKLAND, COMMERCIAL PAPER UNDER THE U.C.C. (Joint Committee on Continuing Legal Education 1959) with the permission of the *Joint Committee.*

N.I.L. Section	*U.C.C. Section*	*Remarks*
1	3-104	The Code continues, without much change, the basic formal requisites of negotiability: (a) Writing, signed by maker or drawer; (b) unconditional promise or order to pay a sum certain in money; (c) payable on demand or at a definite time; (d) payable to order or bearer.
1(5)	3-102	Under the Code, unlike N.I.L., drawees may be joint or alternative but not successive. The change is not of commercial importance, because American drafts are seldom drawn on alternative drawees. Section 128 of N.I.L. partially reversed by this Code rule.
2	3-106	Notes providing for a discount for early payment are not necessarily non-negotiable under Code. Like N.I.L., the Code continues to permit some "luggage" without adversely affecting the "sum certain". But, like the N.I.L., no provision is made authorizing tax-concession clauses.
3	3-105	Code makes it clear that, so far as negotiability is concerned, the conditional or unconditional character of the promise is to be determined by what is expressed in the instrument itself. Broad statements of the transaction permitted by Code without destroying negotiability. "Particular fund" doctrine revised.
4	3-109	Code permits "any acceleration" without destroying negotiability; "extensions" also broadly validated by Code. Code attempts to make non-negotiable post-Obit. notes, but negotiability here can be saved by use of acceleration.
5	3-104	The Code omits N.I.L. 5(4) which permits "commodity notes" to be negotiable. Under Code only instruments payable in money can be negotiable. But Code talks only of "negotiability within this article" and this leaves open the possibility that some writings may be made negotiable by other statutes or by judicial decision. Where, therefore, it is important that "commodity notes" be negotiable, local statutes may make them so without any need to amend or manipulate the U.C.C.
5	3-112	The Code permits negotiable instruments to include clauses authorizing the sale of collateral for instrument upon "any default", including a default in the payment of an installment or interest. It is not limited, as is section 5(1) of the N.I.L., to default at maturity. Also clauses are permitted by Code which are designed to protect collateral or to give additional collateral. However, negotiability is affected by "confession of judgment" clauses unless they are limited to situations in which the instrument is not paid when due.
6(1)	3-114(1)	No change.
6(4)	3-113	Seals do not affect negotiability.

N.I.L. Section	*U.C.C. Section*	*Remarks*
6(5)	3-107	"Money" elaborately defined by U.C.C. "Foreign" money all right for purposes of negotiability. Money tested by government sanction under U.C.C.
7	3-108 3-502	U.C.C. rewords N.I.L. and the last sentence of N.I.L. section 7 is omitted. This section defined as "demand" paper any paper issued, accepted, indorsed, etc., after it was due. Code takes care of special problems by appropriate provisions relating to holder in due course, presentment, notice of dishonor and so on.
8	3-110	Under the Code, instruments payable to the order of an estate of a decedent is order paper, not bearer paper as it is under N.I.L. Under the Code a negotiable instrument may be made payable to an estate, partnership, trust, etc. Such paper is order paper.
9	3-111	Like the N.I.L., the Code provides that instruments payable to "cash" or any other indication which does not purport to designate a specific payee, are bearer instruments.
9(3)	3-405	The "fictitious payee" problem is solved in a straightforward way, and order paper is not converted into bearer paper to accomplish the result, as it is under the N.I.L.
9(5)	3-204	The last indorsement controls future method of negotiation under the Code, even though the paper is payable to bearer on its face.
10	—	Section 10 of N.I.L., omitted by Code, but official note 5 to section 3-104 makes it clear that the Code does not require that particular words appear in negotiable instruments.
11 12	3-114	Under Code, negotiability is not affected by fact that instrument is undated, antedated or postdated, even if this is done for an illegal purpose. This changes N.I.L. sec. 12. The date stated on the instrument controls payment where it is payable on demand or at a fixed period after sight. This clarifies sec. 11 of N.I.L.
13 14 15	3-115	The Code omits N.I.L. sec. 13 and part of sec. 14 and reverses the rule of sec. 15. Under the Code an undated instrument is treated as an incomplete instrument. Incomplete instruments, not completed pursuant to authority, give obligors a personal defense, even when such instruments have not been delivered.
16	3-305 3-306	No change.
17	3-118	The Code's rules with respect to ambiguous terms and methods of construction follow the case law which has developed under N.I.L. The rules, set out in section 17 of N.I.L., are completely re-written. One change is made: 3-118(f) provides that the maker must consent to every time extension. Unless otherwise agreed, an agreement to extend time authorizes a single extension for not longer than the original period.

N.I.L. Section	*U.C.C. Section*	*Remarks*
18	3-401	No change.
19	3-403	No change.
20	3-403	Code clarifies N.I.L. rules regarding signatures made in a representative capacity. The liability of the unauthorized representative is handled by a separate section under the Code (3-404).
21	—	Section 21 is omitted by the Code. Signatures "by procuration" are no longer fashionable and do not deserve special statutory treatment. Signature by procuration is still possible under Code and should have the effect stated in N.I.L. 21. See comment 4 to sec. 3-403.
22	3-207	Under the Code, negotiation is effective to transfer the instrument even if it is obtained by fraud, made in breach of duty, or is part of an illegal transaction. This extends N.I.L. 22. The Code permits the defrauded party, the infant, etc., to rescind the transfer, but until he does so he leaves the transferee in a position of power, the exercise of which by negotiation to a holder in due course will result in cutting off the right to rescind.
23	3-404	Under the Code the unauthorized agent is liable to a holder in due course. The forger is also liable on the instrument.
24	3-408	No change.
25 26 27	3-303	Under the Code an executory promise to give value is not value. This changes some cases under the N.I.L. A holder who does not himself give value cannot be a holder in due course. This reverses some holdings under section 26 of N.I.L. A lien acquired by legal process is not value under the Code. This modifies section 27 of N.I.L.
28	3-303 3-305 3-306 3-408	The Code continues the rule of sec. 28 of N.I.L.
29	3-415	Under the Code, an accommodation party is always a surety. He differs from other sureties only in that his liability [is] on the instrument. His suretyship defenses are personal and are cut off by a holder in due course. His suretyship rights remain even after an instrument is "paid".
30	3-202	No change, except 3-202(4) rejects decisions handed down under N.I.L. that words of assignment, condition, waiver, etc., accompanying an "indorsement" show an intention not to indorse. Also payee can be holder in due course under Code.
31	3-202	No change.

N.I.L. Section	*U.C.C. Section*	*Remarks*
32	3-202(3)	The Code makes it clear that the cause of action on an instrument cannot be split. Negotiation takes place only when the entire instrument or unpaid residue is conveyed. But a conveyance of a lesser interest is effective as a partial assignment.
33 34 35	3-204	Code's definition of "special" and "blank" indorsements follows N.I.L. But effect of special indorsement on bearer paper is different. See notes to N.I.L. 40 in this appendix.
36 37	3-205 3-206	Code section 3-205 provides a clear definition of restrictive indorsements. This definition includes what was termed a "conditional indorsement" under N.I.L. sec. 39. Code section 3-206 gives restrictive indorsements a different effect from that accorded them by the N.I.L. Under the Code, a restrictive indorsee can be a holder in due course; intermediary banks may disregard the restrictive indorsement except that of its immediate transferor; and a restrictive indorsement does not prevent further negotiation.
38	3-414	The Code does not use the words "qualified indorsement", but makes it clear that the indorsement contract can be disclaimed by words such as "without recourse".
39	3-205 3-206	Conditional indorsements, under the Code, are treated as restrictive indorsements. This results in no change, since a restrictive indorsee under the Code can be a holder in due course, further negotiation is not prevented, and the payor is not affected by the restrictive indorsement.
40	3-204	The Code reverses the "once bearer always bearer" dogma of section 40 of the N.I.L. A special indorsement of paper which is bearer on its face makes the paper payable to the order of the special indorsee and it may be further negotiated only by his indorsement.
41	3-116	No change, but the law is clarified by a hard-and-fast distinction between paper payable to "A or B" and paper payable to "A and B". Either A or B alone may negotiate the first instrument; both must indorse in order to negotiate the second.
42	3-117	The Code extends the N.I.L. rule so as to cover agents or fiduciaries, identified as such, as payees.
43	3-203	No change.
44	3-414	The Code omits section 44 as unnecessary. The right of the agent to negative personal liability when he indorses in his representative capacity is included in the broad right under the Code to disclaim any liability.

N.I.L. Section	*U.C.C. Section*	*Remarks*
45	3-304	The Code omits section 45 of the N.I.L. Under the Code, the presumption that any negotiation has taken place before the instrument was overdue is of importance only in aid of a holder in due course. Under 3-304 any holder who takes paper without notice that it is overdue can be a holder in due course, whether or not the paper is overdue. This rule makes N.I.L. sec. 45 unnecessary.
46	—	
47	3-206	The rule of section 47 of the N.I.L. that a restrictive indorsement "kills" negotiability is reversed by the Code. See remarks under N.I.L. 36 and 37 in this appendix.
48	3-208	No change.
49	3-201	The Code applies to any transfer, whether by a holder or not. Thus the "umbrella" protection of sections 58 and 49 of the N.I.L. are combined by 3-201. The Code indicates that the transferee for value is entitled to an "unqualified" indorsement. This follows the cases under the N.I.L., but it is contrary to scholarly opinion which holds that, since mere transfer or assignment is closer to the qualified indorsement in effect, the mere transferee should only be able to compel a qualified indorsement.
50	3-208	No change.
51	3-301 3-603	The holder has a basic right to discharge the instrument, and this right is limited only by injunction or by a third-party claim accompanied by an adequate indemnity. The basic right is set out in section 3-301, and the limitations on it are found in 3-603.
52	3-302 3-304	Under Code, a holder in due course is one who takes in good faith, for value, and without notice that the instrument is overdue or of any defense against or claim to it on the part of any person. There is no requirement that the paper be "complete and regular", but this requirement is assimilated by the good faith requirement. Good faith is mainly subjective ("white heart"), but some suspicious circumstances outlined by 3-304 prevent good faith taking. Payees are eligible to become holders in due course.
53	3-304	No change, except that a domestic check is presumed overdue after 30 days.
54	3-303	Code changes rule of N.I.L. that executory promise can be value. Under Code, an executory promise to give value is not itself value except in special cases set out in 3-303(c).
55 56	3-304	The Code is much more explicit with regard to the kind of facts which prevent due course holding.

N.I.L. Section	U.C.C. Section	Remarks
57	3-305	The Code enumerates the real defenses. Failure to deliver an incomplete instrument is only a personal defense under the Code, thus reversing section 15 of the N.I.L. See remarks under sec. 15 in this appendix. 3-305(2)(e) makes it clear that a holder knowing of certain discharges can nevertheless be a holder in due course with respect to undischarged parties.
58	3-201 3-306	Under the Code, a successor to a holder in due course is treated as if he were a holder in due course in his own right. This umbrella protection involves little change from the N.I.L. See section 49 of N.I.L. in this appendix.
59	3-207 3-306 3-307	Code 3-307 continues the N.I.L. rule on burden of proof with regard to due course holding. 3-306 denies the defense of jus tertii except where the decision will be res adjudicata to all parties.
60	3-413(1)	No change.
61	3-413	Section 3-413 sets out the basic contract of the drawer, qua drawer. The section does not change the rule of sec. 61 of the N.I.L.
62	3-413 3-417 3-418	Under the Code, the acceptor of either a check or a draft engages that he will pay the instrument according to its tenor at the time of his engagement, not (in case of alteration before acceptance) to its original tenor. This solves a division of authority under the N.I.L. While a drawee can charge his drawer only to the extent of the instrument's original tenor, he can charge back any loss occasioned by accepting an instrument raised to a larger amount, for 3-417 provides that the one obtaining an acceptance warrants to the acceptor that the instrument has not been materially altered.
63	3-402	No change.
64	3-415	Under the Code, the accommodation party is always a surety, but is liable in the capacity in which he signs. As surety, he is not liable to the principal debtor. These rules make N.I.L. sec. 64 unnecessary.
65 66	3-417	The Code makes a number of changes, mostly for purposes of clarification, in the warranty law of the N.I.L. *Price v. Neal* is retained by the Code, but is stated as a rule of warranty and not as a rule of quasi-contract. Warranties run against persons who obtain payment or acceptance, or who transfer the instrument for value. Warranties run in favor of payors and acceptors and holders who take the instrument in good faith. Code rule makes the mere transferor more liable than the qualified indorser. Warranties may be disclaimed. Damages for breach of warranty not specified by Code.
67	3-414	No change.

N.I.L. Section	*U.C.C. Section*	***Remarks***
68	3-119 3-414	No change. But 3-119 makes it clear that indorsers, among themselves, can regulate order of liability by an instrument external to the negotiable instrument. Holders in due course are not bound by this agreement.
69	3-417(4)	No change.
70	3-501 3-502 3-604(3)	An unexcused delay in presentment discharges "any drawer or the acceptor of a draft payable at a bank or the maker of a note payable at a bank who because the drawee or payor bank becomes insolvent during the delay is deprived of funds maintained with the drawee or payor bank to cover the instrument may discharge his liability by written assignment to the holder of his rights against the drawee or payor bank in respect of such funds, but such drawer, acceptor or maker is not otherwise discharged." This rule greatly extends N.I.L. 186 which applies only to drawers of checks. Indorsers are completely discharged by slow presentment.
71	3-503	Code continues rule that demand instruments be presented in reasonable time. But reasonable time is measured, under Code, from date that party became liable on the instrument, and presumption set out that reasonable time to present or initiate collection of an uncertified check is 30 days to hold drawer and 7 days to hold indorsers. The weird rule of N.I.L. 71 that presentment of demand drafts and checks is reasonable time after last negotiation is reversed.
72 73 74	3-503 3-504 3-505	Under Code, presentment may be made by mail or through a clearing house. Presentment is made by a demand on the party to pay, and it is sufficient no matter where or how made. The N.I.L. requirements of exhibition and the like are not required unless insisted upon by the party to pay. 3-505 gives the party to pay the right to exhibition, identification of presenting party, compliance with place requirements, and a receipt. The presenting party has a reasonable time to comply with these requests.
75	3-503	Presentment to bank, under Code, must be consistent with banking practices. Bank holidays recognized.
76	3-511(3)	Presentment is excused, in most cases under the Code, where the maker, acceptor or drawee is dead or insolvent. This reverses N.I.L. 76.
77	3-504(3)(a)	No change.
78	3-504(3)(a)	Under the Code, presentment may be made to any one of two or more makers, acceptors, drawees or other payors. This reverses N.I.L. 78.
79 80 81 82	3-511	No change. Code 3-511 collects in one place all rules on dispensation of presentment, notice of dishonor and protest.

N.I.L. Section	*U.C.C. Section*	*Remarks*
83	3,503(3) 3-507(4)	Under the Code, return of an instrument for lack of proper indorsement is not a dishonor. And, a term permitting "re-presentment" in case of dishonor, gives the holder, as against any secondary party bound by the term, an option to waive the dishonor without discharging the secondary party. These Code provisions are new, but they express general banking and commercial understanding.
84	3-507(2)	No change.
85	3-503	Under Code, presentment is due on the next full business day for both parties when it originally falls due on a day which is not a full business day for all parties. This recognizes the increasing practice of closing banks and businesses on Saturday and other "holidays".
86	3-503	The Code omits N.I.L. sec. 86 as superfluous. Sec. 86 states a rule applied to all time calculations where commercial instruments are involved. No change in the law is intended. See note 1 to sec. 3-503.
87	3-121	The Code gives enacting states a choice of two alternatives, one of which is identical with N.I.L. sec. 87 as construed in the north and east. The other represents present southern and western thinking.
88	3-603	Payment, under the Code, discharges the liability of the payor, even though he knows that a third party has a claim to the instrument, unless the third party enjoins payment or supplies an adequate indemnity. This reverses the usual meaning given to "payment in due course" under N.I.L. 88.
89	3-501 3-502	Unexcused delay of notice of dishonor, under Code, has same effect as unexcused delay in presentment. See remarks in this appendix to sec. 70 of N.I.L.
90-108	3-508	Section 3-508 collects in one place the rules on notice of dishonor. The Code simplifies the law by omitting many of the detailed requirements of the N.I.L. Some changes are made. Notice of dishonor may be given by merely "sending the instrument bearing a stamp, ticket or writing stating that acceptance or payment has been refused or sending a notice of debit with respect to the instrument." Any person other than a bank has three days in which to give notice of dishonor; banks have until midnight of next banking day. This time leeway takes pressure off need for detailed time rules. Under the Code, any party who can be compelled to pay the instrument may give notice.
109-116	3-511	Code 3-511 combines and simplifies widely scattered rules in N.I.L. Single terms "excused" and "entirely excused" are substituted for "excused", "dispensed with", "not necessary", "not required" and "waived", as used variously in N.I.L. No change in substantive law, however.
117	—	

N.I.L. Section	*U.C.C. Section*	*Remarks*
118	3-501(3)	Protest is required under the Code only in the case of the international draft.
119 120	3-601 to 3-606	The N.I.L. scheme of "payment in due course", "principal debtor", "discharge of the instrument", "discharge of secondary parties", etc., is abandoned by the Code and replaced by a system stating facts which will discharge one or more parties. Discharge amounts to a personal defense only under the Code. Methods of discharge are enumerated and indexed in section 3-601 of Code. These methods involve little change from N.I.L. Suretyship "discharges" available to primary parties.
121	3-208 3-601 3-603	The words of N.I.L. 121 "remitted to his former rights" are omitted by the Code, making it clear that an irregular indorser under the Code can recover on the instrument if he pays it. Under the Code, anyone who pays an instrument succeeds to the rights of the holder, subject to the limitation that one who has himself been a party to any fraud or illegality affecting the instrument or who as a prior holder had notice of a defense or claim against it cannot improve his position by taking from a later holder in due course.
122	3-605 3-602	The N.I.L. does not state how cancellation is to be made other than striking indorsements. Code makes it clear that the cancellation must be done in a manner apparent on the face of the instrument. Effect of cancellation, like that of other forms of discharge, is to give a personal defense only.
123	3-605	Code omits sec. 123 of N.I.L., but no change in the law is intended.
124 125	3-407	Code re-writes sections 124 and 125 without greatly changing law. Under Code, an alteration is "material" if it changes the contract of any party in any respect. But a material alteration does not discharge any party unless it is made for a fraudulent purpose by a holder. If the alteration is not material or if it is not made for a fraudulent purpose, the instrument may be enforced according to its original tenor. In any case, a holder in due course takes free of the discharge and may enforce the instrument according to original tenor.
126	3-104	"Bill of exchange" is called "draft" under Code. No change in substantive law.
127	3-409	No change.
128	3-102(1)(b)	Under Code, drawees in the alternative are allowed. This reverses N.I.L. 128.
129	3-501(3)	N.I.L. terminology of "inland" and "foreign" bills is abandoned by Code. Protest is required by Code only in case of international drafts.
130	3-511	No change.

Section N.I.L.	Section U.C.C.	Remarks
131	4-503	Code 4-503 lists the responsibilities of the presenting bank. One of these is that it "may seek and follow instructions from any referee in case of need designated in the draft". This seems in accord with N.I.L. 131.
132 137	3-410 3-506 3-419 3-409	Code section 3-410 collects in one place the N.I.L. rules of acceptance. Under the Code acceptance must be written on the draft. This eliminates the extrinsic acceptances permitted by N.I.L. sections 134 and 135. Constructive acceptance under section 137 of N.I.L. is also impossible under Code, but action for conversion of breach of contract to accept will give relief to parties aggrieved. The conversion rule is set out in section 3-419 of Code. The contract rule appears in section 3-409(2). Acceptance may be deferred without dishonor until the close of the next business day following presentment. See Code 3-506 (1). Failure to accept within this time limit is a dishonor and not a constructive acceptance.
138	3-410	Under the Code, where the draft is payable at a fixed period after sight and the acceptor fails to date his acceptance the holder may complete it by supplying a date in good faith. This changes to some extent N.I.L. 138.
139- 142	3-412	Code sections 3-412 collects in one place all rules on acceptances which vary drafts. The code abandons the terms "qualified acceptance" in favor of "acceptance varying draft." Consequences of holder assenting to acceptance varying draft are same as N.I.L.: drawer and indorsers are discharged. Holder may reject drawee's proffered varying acceptance and treat draft as dishonored. Same rule under N.I.L.
143	3-501	No change.
144	3-501 3-502 3-503	See discussion under N.I.L. secs. 70 and 71 of this appendix.
145	3-504	Presentment may be made by mail or through clearing house. It may be made to any one of two makers, acceptors, drawees.
146	3-503	See discussion in this appendix under N.I.L. sec. 85.
147 148	3-511	See discussion of this code provision under N.I.L. sections 109-116.
149	3-507	Return of instrument for lack of indorsement is not a dishonor. See discussion this appendix under N.I.L. sec. 83.
150 151	3-501 3-502 3-511	No change in substance.

N.I.L. Section	*U.C.C. Section*	*Remarks*
152- 156	3-509 3-510	Code section 3-509 collects most of the protest rules, and makes some changes in law of N.I.L. Only international drafts must be protested under Code. The protest must indentify the instrument, and recite the fact of presentment or reason why presentment is excused. It may also certify that notice of dishonor has been given. Protest may be certified only by United States consul or vice consul or a notary public or other person authorized to certify dishonor by the law of the place where dishonor occurs. This changes N.I.L. 154(2) which permits protest to be made "by any respectable resident of the place where the bill is dishonored." Under Code, protest need not be made at place of dishonor, but may be made upon information. This reverses N.I.L. 156. Sec. 3-510 states that protest is admissible into evidence and creates a presumption of dishonor and notice of dishonor therein shown. The section also provides two substitutes for protests which have the same evidentiary effect as protest: a stamp on the instrument showing it was dishonored; and the books or records of the dishonoring drawee, collecting bank, etc., even though there is no evidence who made the entry.
157- 159	3-501 3-509 3-511	No basic changes.
160	3-509 3-804	If instrument is lost under Code, protest is still sufficient if it identifies the instrument. But the owner must prove his rights under section 3-804 which deals with lost, stolen or destroyed instruments.
161- 170	None	The practice of acceptance for honor has been obsolete for many years in America, and the Code therefore omits completely all rules relating to this ancient practice.
171- 177	3-603	Payment for honor covered by sections 171-177 of N.I.L. is now handled by 3-603 of the Code. The Code permits "payment or satisfaction (to) be made with the consent of the holder by any person including a stranger to the instrcment." Surrender of the instrument to such a person gives him the rights of a transferee.
178- 183	3-801	No change in substance.
184	3-104	No change except certificate of deposit is separately defined.
185	3-104	No basic change.
186	3-501 3-502 3-503	See discussion in this appendix under N.I.L. sec. 70.
187- 188	3-411	No change.

N.I.L. Section	U.C.C. Section	Remarks
189	3-409	No change.
190	3-101	Code article called "Uniform Commercial Code-Commercial Paper."
191		There are many definitions appearing throughout the Code. They cannot be summarized here.
192	None	The Code has no provision like sec. 192 of N.I.L., but the terms "'primary" and "secondary" are still useful in analyzing the Code.
193	3-503(2)	Code uses "reasonable time" concept, but measures it from a different point and is more specific with respect to drawer and indorsers of uncertified checks.
194 195	None	
196	1-103	Code continues the Law Merchant as a "gap filler."
197	None	
198	10-101	Effective date necessarily up to enacting state.

NEW PROVISIONS IN THE CODE.

U.C.C.	Remarks
3-406	While this section is statutorily new, it simply declares the common law respecting the estoppel effect of negligence which contributes to an alteration or forgery of a negotiable instrument.
3-416	A new statutory definition of the contract of the guarantor. The section declares the common commercial underwriting as to the meaning and effect of words of guaranty added to a signature. One who by indorsement guarantees payment waives the conditions precedent that usually attach to the indorsement contract and becomes for all practical purposes a co-maker. A guarantor of collectibility also waives formal presentment, notice of dishonor and protest, but the holder must first proceed against the primary party or show that such a proceeding would be useless, before turning to the guarantor.
3-510	New law on the matter of protest. See appendix I, sec. 3-510.
3-701	New provision to put America law in line with European with respect to the letter of advice of international drafts. In Europe, a bank paying a check in good faith can charge the drawer's account notwithstanding a forgery of a necessary indorsement. The letter of advice is designed to reduce the chance of successful forgery. It is written by the drawer to the drawee notifying the latter that a certain draft or check has been drawn, etc. The Code adopts the practice and its legal consequences.

U.C.C.	Remarks
3-802	This new section settles some conflicts of authority with respect to the effect of an instrument on the underlying obligation for which it is given. Normally, under the section, where an instrument is taken for an underlying obligation, the obligation is suspended until the instrument is due. Thereafter an action may be maintained on either the instrument or the obligation. If the instrument is discharged, the obligation, too is discharged.
3-803	This section supplements existing rules of civil procedure dealing with interpleader, joinder of parties, and vouching in of interested third parties. It makes just the rule of 3-603(1) that the defense of jus tertii is available only where a decision would be *res adjudicata* to all three interested parties.
3-804	New law on methods of recovery on instruments which are lost, destroyed or stolen. The plaintiff is not a holder of such an instrument, because he is not in possession. He must prove his case by establishing the terms of the instrument, his ownership of it, and account for its absence.
3-805	This section declares the law merchant rules as to instruments not payable to order or bearer but otherwise negotiable. Such instruments are not negotiable under the Code, but are treated as negotiable so far as their form permits. There can be no holder in due course of such an instrument, but, with this exception, most of the other sections of the Code apply to such instruments.