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# How Much Satisfaction Should You Expect from an Accord? The U.C.C. Section 3-311 Approach

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## I. INTRODUCTION

The 1990 revisions to the Uniform Commercial Code ("U.C.C.") codify rules governing an accord and satisfaction by use of a negotiable instrument.[1] This article examines these rules in light of the history and policy of the doctrine of accord and satisfaction.

The doctrine originally developed at common law. In addition, various statutes have addressed issues related to accord and satisfaction over the years, although the reach of some of these statutes has been unclear. Recently, section 3-311 of the U.C.C. was promulgated to establish the boundaries of the doctrine in cases involving a negotiable instrument.

Part II of this article examines the common law roots of the doctrine of accord and satisfaction. Part III examines various statutes that have affected the common law rules, at least one of which appears to have done so unintentionally. Part IV examines and evaluates the rules of new U.C.C. section 3-311, and Part V considers whether the doctrine of accord and satisfaction is a beneficial adjunct to commercial law. Part VI then concludes that despite its faults, the doctrine of accord and satisfaction is here to stay, and that new section 3-311 offers worthwhile improvements to the common law.

## II. ACCORD AND SATISFACTION AT COMMON LAW

Accord and satisfaction is a long-standing doctrine of common law. It can often help provide finality in settling certain disputes. The common law rules of accord and satisfaction have their roots in the rules of contract.[2] If the parties wanted to substitute a new contract in place of the old one, resulting in a novation, they were free to do so.[3] Nevertheless, the parties needed consideration to do this, and payment of a portion of the prior debt could not satisfy this requirement.[4] If the

1. U.C.C. § 3-311, 2 U.L.A. 85-89 (1991). See *infra* notes 50-55 and accompanying text for explanation of the term "negotiable instrument."

2. *See, e.g.*, Wilfredo Caraballo, *The Tender Trap: U.C.C. § 1-207 and Its Applicability to an Attempted Accord and Satisfaction by Tendering a Check in a Dispute Arising from a Sale of Goods*, 11 SETON HALL L. REV. 445, 446-49 (1981).

3. *Id.* at 447.

4. This rule has been attributed by commentators to dictum in Pinnel's Case, 77 Eng. Rep. 237 (C.P. 1602), which was followed by Foakes v. Beer, 9 App. Cas. 605 (H.L. 1884). *See* Albert J. Rosenthal, *Discord and Dissatisfaction: Section 1-207 of the*

prior debt was unliquidated, disputed, or not yet due, however, partial payment *could* be consideration for the entire debt to be discharged.[5] As the common law doctrine of accord and satisfaction continued to evolve, the efficacy of partial payments increased. For example, there is support for finding an accord and satisfaction in cases where the debtor pays the minimum amount conceded to be owed.[6] There is even some support for finding an accord and satisfaction where the debtor pays *less* than the amount concededly owed.[7]

The common law rules of accord and satisfaction have been stated in various ways. One of the most succinct definitions appears in the Restatement (Second) of Contracts: "An accord is a contract under which an obligee promises to accept a stated performance in satisfaction of the obligor's existing duty. Performance of the accord discharges the original duty."[8] An accord and satisfaction typically occurs in cases where an obligation has been disputed. To reach an accord and satisfaction, a creditor[9] agrees to accept something different from or less than his full claim as satisfaction of the debt.[10] Often a debtor will tender a check payable to a creditor with a notation stating that the check is "payment in full" of the debt, or similar wording.[11]

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*Uniform Commercial Code*, 78 COLUM. L. REV. 48, 52 (1978); Caraballo, *supra* note 2, at 446-47.

5. Rosenthal, *supra* note 4, at 53. For a more extensive discussion of the evolution of accord and satisfaction, see Caraballo, *supra* note 2, at 446-51, and Rosenthal, *supra* note 4, at 51-58.

6. *See* Caraballo, *supra* note 2, at 449-50.

7. Rosenthal, *supra* note 4, at 53.

8. RESTATEMENT (SECOND) OF CONTRACTS § 281(1) (1981).

9. In this article, "creditor" is used to signify the person or entity claiming to be owed, and "debtor" is used to signify a person or entity allegedly owing a debt or obligation. Often, the debtor draws a check payable to the creditor. The new accord and satisfaction provision of U.C.C. Article 3 uses the terms "person against whom a claim is asserted" to signify the debtor, and "claimant" for the creditor. U.C.C. § 3-311, 2 U.L.A. 85-86 (1991). This provision applies to situations where a check or other negotiable instrument is involved. *See infra* notes 50-55 and accompanying text.

10. *See, e.g.*, Homewood Dairy Prods. Co. v. Robinson, 48 So. 2d 28, 33 (Ala. 1950); Fuller v. Kemp, 33 N.E. 1034, 1034 (N.Y. 1893).

11. *See* JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 13-24, at 607 (3d ed. 1988). Alternatively, the check may be accompanied by a letter stating that the check represents payment in full. Either way, such a check is referred to as a "full payment check." If the creditor obtains payment of the check and the creditor's claim is sufficiently disputed or unliquidated the common law provides that the claim is fully discharged. *See infra* notes 14-17 and accompanying text.

A study of the case law reveals numerous forms of the "payment in full" language that courts have found sufficient to reach an accord and satisfaction. Some of the language is relatively simple. *E.g.*, Edgar v. Hitch 294 P.2d 3, 4 (Cal. 1956) ("Pd. in full for all Hay Bought From John Edgar @ 32.50 Ton"); Wood Bros. Const. Co. v. Simons-Eastern Co., 389 S.E.2d 382, 383 (Ga. Ct. App. 1989) ("[F]inal payment except for the sum of

At common law, a creditor who obtained payment by means of such a full payment check ran a substantial risk of being bound to an accord and satisfaction; the only way the creditor could reliably preserve the unpaid portion of the claim was to avoid accepting the check.[12] Professors White and Summers, in their well-known U.C.C. treatise, once described this type of transaction as "an exquisite form of commercial torture."[13]

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$2000.00 withheld for completion of grassing."); Sawner v. M.P. Smith Const. Co., 526 S.W.2d 492, 496 (Tenn. Ct. App. 1975) ("Acct. in full 6/3 - 6/16/71"); Charleston Urban Renewal Auth. v. Stanley, 346 S.E.2d 740, 741 (W. Va. 1985) ("January rent in full").

On the other hand, some of the language used is very detailed and specific. For example, in Western Branch Holding Co. v. Trans Mktg. Houston, Inc., 722 F. Supp. 1339 (E.D. Va. 1989), the following language was used:

> By its acceptance and negotiation of this draft, Nitrex accepts this instrument as payment in full from Trans Marketing Houston, Inc., of all sums owing to Nitrex under the terms of one certain Urea Product Purchase Agreement, TMGP—2179/88, between Trans Marketing Houston, Inc. and Nitrex on or about May 4, 1988, and Nitrex does further release Trans Marketing Houston, Inc. from any other and further liability with respect to said Urea Product Purchase Agreement TMGP—2179/88.

*Western Branch Holding Co.*, 772 F. Supp. at 1340; *see also* Ennia Gen. Ins. Co. v. Auld, 506 So. 2d 62, 62 (Fla. Dist. Ct. App. 1987) ("By endorsing the draft the payees accept same in full settlement and release of all claims arising out of occurrence mentioned on the face hereof."). In Phillips v. Phillips Const. Co., 136 S.E.2d 48 (N.C. 1964), the debtor used the following language:

> The payee by endorsement hereon acknowledges receipt of this final payment in the amount of $3,451.89 as full payment and complete settlement for all work performed under subcontract dated October 15, 1957, with Phillips Construction Co., Inc., and/or D. L. Phillips, Builder, and/or Myrtle Beach AFB Housing, Inc., and/or No. 2 and 3 and claims for any and all work performed in addition to subject subcontract at the Myrtle Beach AFB Housing Projects.

*Phillips*, 136 S.E.2d at 51.

12. *See* WHITE & SUMMERS, *supra* note 11, § 13-24, at 607-08 ("*If* the payee indorses the check and receives payment, he has accepted the contract and so discharged his claim for a larger amount") (emphasis added) (footnote omitted); U.C.C. § 3-311 cmt. 2, 2 U.L.A. 85 (1991).

13. JAMES J. WHITE & ROBERT R. SUMMERS, UNIFORM COMMERCIAL CODE §13-21, at 544 (2d ed. 1980). In the current edition of their treatise, Professors White and Summers have substituted the less colorful phrase "exquisite dilemma." WHITE & SUMMERS, *supra* note 11, § 13-24, at 607. While both phrases probably denote the same message, the omission of the former phrasing represents a loss to the field of commercial law. The term "torture" better expresses the drama of certain commercial law issues. Some, perhaps many, students find the U.C.C. tedious. This view has some basis; the "scope" provision of Article 6 on bulk sales provides an example. *See* U.C.C. § 6-103, 2C U.L.A. 67-68 (1991). However, commercial law encompasses many dramatic situations that can have a profound effect on a person's livelihood. Furthermore, financial reversals sometimes have life and death implications. *See, e.g.*, Witold Zygulski, *Farmers End Hunger Strike: Debt Relief Victory*, THE WARSAW VOICE, November 24, 1991 (describing end of hunger strike that farmers had engaged in to force bank into

Consequently, the analysis of whether parties have entered into an accord and satisfaction is heavily fact specific.[14] Some authorities have taken the view that unless there is new consideration, only a disputed or unliquidated claim may be the subject of an accord and satisfaction,[15] but this rule is subject to numerous exceptions.[16] This requirement is also quite elastic. A court wishing to find an accord and satisfaction should usually be able to see some element of dispute in almost any litigated transaction, unless the debtor has been honest or careless enough to concede that he owed the full amount. Conversely, a court wishing to avoid finding an accord and satisfaction can find that there was no "real" dispute.[17]

The doctrine of accord and satisfaction remains alive and well at common law. However, the common law is not the only source of rules on accord and satisfaction. The remainder of this article considers the various statutory incursions into the realm of accord and satisfaction.

## III. ACCORD AND SATISFACTION UNDER PRIOR STATUTES

Prior to the recent promulgation of section 3-311, accord and satisfaction had been considered by many authorities. Several states have enacted statutes prescribing rules for accord and satisfaction similar to common law rules.[18] Some states have also enacted statutes limiting the common law rules of accord and satisfaction.[19] In

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renegotiating debt); *The Home-Grown Homeless*, ST. PETERSBURG TIMES, May 15, 1989, at 10A; Stephen Lilly, *And Now the Drought*, 4 BUS. FIRST-COLUMBUS, July 18, 1988, § 2, at 3; *Farm Debt Help Sought*, CHI. TRIB., February 12, 1986, at 3; Laurent Belsie, *Pulling Together When Financial Troubles Pull Them Apart*, THE CHRISTIAN SCI. MONITOR, December 18, 1985, at 3.

14. *See, e.g.*, Flowers v. Diamond Shamrock Corp., 693 F.2d 1146, 1152-53 (5th Cir. 1982); Security Transactions, Inc. v. Nelson Excavating and Paving Co., 314 So. 2d 297, 302 (Ala. Civ. App.), *cert. denied*, 314 So. 2d 304 (Ala. 1975).

15. *See, e.g.*, Homewood Dairy Prods. Co. v. Robinson, 48 So. 2d 28, 33 (Ala. 1950); Cunningham v. Irwin, 148 N.W. 786, 787 (Mich. 1914); Schnell v. Perlmon, 144 N.E. 641, 642-43 (N.Y.), *remittitur denied*, 147 N.E. 171 (N.Y. 1924); Fuller v. Kemp, 33 N.E. 1034, 1035 (N.Y. 1803).

16. *See, e.g.*, Chicago, Milwaukee & St. Paul Ry. Co. v. Clark, 178 U.S. 353, 364-69 (1900); *Cunningham*, 148 N.W. at 787-88.

17. *Cf.* Wm. Alan Baird, Note, *Role of the Check in Accord and Satisfaction: Weapon of the Overreaching Debtor*, 97 U. PA. L. REV. 99, 101 (1948) (observing that the concept of unliquidated or disputed claims "escapes exact definition").

18. *See, e.g.*, ALA. CODE §§ 8-1-20, 21, 22, 23 (1993); CAL. CIV. CODE §§ 1521-1526 (West 1982 & Supp. 1994); GA. CODE ANN. §§ 13-4-100 to 13-4-104 (1982); MONT. CODE ANN. §§ 28-1-1401 to -1403 (1993); N.C. GEN. STAT. § 1-540 (1993); N.D. CENT. CODE §§ 9-13-04 to -07 (1987); S.D. CODIFIED LAWS ANN. §§ 20-7-1 to -4 (1987).

19. *See, e.g.*, CAL. CIV. CODE § 1525 (West 1982) (permitting partial payment of a disputed amount without resulting in an accord and satisfaction as to the whole); GA.

addition, the U.C.C. itself has approached the issue in several contexts.

Section A describes the controversy over whether section 1-207 of the U.C.C. provided a way for creditors to obtain payment of full payment checks but avoid the effect of the full payment legends. Section B describes a former provision of U.C.C. Article 3 that attempted to codify the rules of accord and satisfaction involving negotiable instruments. Section C notes the deletion of former U.C.C. section 3-112(1)(f), which is no longer necessary now that section 3-311 explicitly contemplates the presence of full payment terms in negotiable instruments.

### *A. U.C.C. Section 1-207*

Prior to the 1990 revisions, section 1-207 read: "A party who with explicit reservation of rights performs or promises performance or assents to performance in a manner demanded or offered by the other party does not thereby prejudice the rights reserved. Such words as 'without prejudice,' 'under protest' or the like are sufficient."[20] The question of whether former U.C.C. section 1-207 applied to an accord and satisfaction has been extremely controversial.[21] The controversy

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CODE ANN. § 13-4-103(b) (1979) (rendering a full payment check ineffective unless there is an independent agreement for accord and satisfaction); UTAH CODE ANN. § 70A-3-607 (1990) (providing that a full payment check is effective to establish an accord and satisfaction only if the payee or its officer agrees in writing to accept the amount in full satisfaction).

20. U.C.C. § 1-207, 1 U.L.A. 145 (1989). This provision appeared in the same form, with the same section number, as early as the May 1950 Proposed Final Draft of the U.C.C. *See* U.C.C. § 1-207 (1950), *reprinted in* 10 UNIFORM COMMERCIAL CODE: DRAFTS 40 (Elizabeth Slusser Kelly ed., 1984).

21. *See* U.C.C. § 1-207 cmt. 3, 1 U.L.A. 39 (1991 & Supp. 1994). Prior to the 1990 revisions, a number of commentators addressed this issue. *See, e.g.*, WHITE & SUMMERS, *supra* note 11, § 13-24, at 608-10; Caraballo, *supra* note 2; Louis F. Del Duca, *Handling "Full Payment" Checks*, 13 UCC L.J. 195 (1981); Patricia B. Fry, *You Can't Have Your Cake and Eat It Too: Accord and Satisfaction Survives the Uniform Commercial Code*, 61 N.D. L. REV. 353 (1985); W. Jack Grosse & Edward P. Goggin, *Accord and Satisfaction and the 1-207 Dilemma*, 89 COMM. L.J. 537 (1984); W. Jack Grosse & Edward P. Goggin, *The 1-207 Dilemma Revisited*, 16 N. KY. L. REV. 425 (1989) [hereinafter *The Dilemma Revisited*]; William D. Hawkland, *The Effect of U.C.C. § 1-207 on the Doctrine of Accord and Satisfaction by Conditional Check*, 74 COMM. L.J. 329 (1969); Rosenthal, *supra* note 4, at 53; Morris G. Shanker, *The Folly of Full Settlement Checks—and a Declaration of their Independence*, 90 COMM. L.J. 7 (1985); Paula G. Walter, *The Rise and Fall of U.C.C. Section 1-207 and the Full Payment Check—Checkmate?* 21 LOY. L.A. L. REV. 81 (1987); Kimm A. Massengill, Comment, *U.C.C. Section 1-207 and the Doctrine of Accord and Satisfaction: Ohio's About-Face in* AFC Interiors v. Dicello, 52 OHIO ST. L.J. 1617 (1991); Pamela K. Strom Amlung, Note, *Ohio's Interpretation of Uniform Commercial Code Section 1-207—You* Can *Have Your Cake and Eat It Too*, 59 U. CIN. L. REV. 1001 (1991).

has centered on whether the payee of a full payment check may accept the check, yet avoid being bound by an accord and satisfaction, by noting on the check or in a separate communication that the check was taken "with reservation of rights" or a similar phrase. Courts in a minority of states have held or suggested that section 1-207 *does* offer this alternative.[22] Professors White and Summers took this position in their U.C.C. treatise, before the 1990 revisions to the U.C.C.[23]

The 1990 revisions redesignated the existing language of section 1-207 as subsection (1) of that section and added a new subsection (2), which provides: "Subsection (1) does not apply to an accord and satisfaction."[24] To the extent that states adopt the 1990 revisions, the controversy will be resolved. The new subsection (2) of section 1-207 explicitly adopts the view that the section is not intended to supersede

22. *See, e.g.*, Bivins v. White Dairy, 378 So. 2d 1122 (Ala. Civ. App. 1979), *cert. denied*, 378 So. 2d 1125 (Ala. 1980); Miller v. Jung, 361 So. 2d 788, 789 (Fla. Dist. Ct. App. 1978); Ditch Witch Trenching Co. v. C & S Carpentry Serv., 812 S.W.2d 171, 172-73 (Ky. Ct. App. 1991); Majestic Bldg. Material Corp. v. Gateway Plumbing, Inc., 694 S.W.2d 762, 765-66 (Mo. Ct. App. 1985); Horn Waterproofing Corp. v. Bushwick Iron & Steel Co., 488 N.E.2d 56, 60 (N.Y. 1985); Baillie Lumber Co. v. Kincaid Carolina Corp., 167 S.E.2d 85, 92-93 (N.C. Ct. App. 1969); AFC Interiors v. DiCello, 544 N.E.2d 869, 873 (Ohio 1989); Kilander v. Blickle Co., 571 P.2d 503, 505 (Or. 1977); Strauss, Factor, Hillman & Lopes, P.C. v. Kohler Gen. Corp., 3 U.C.C. Rep. Serv. 2d (Callaghan) 466 (R.I. Dist. Ct. 1987); Scholl v. Tallman, 247 N.W.2d 490 (S.D. 1976); Robinson v. Garcia, 804 S.W.2d 238, 241 (Tex. Ct. App.), *writ denied*, 817 S.W.2d 59 (Tex. 1991); Frangiosa v. Kapoukranidis, 627 A.2d 351 (Vt. 1993); *cf.* American Food Purveyors v. Lindsay Meats, Inc., 265 S.E.2d 325 (Ga. Ct. App. 1980) (applying, but criticizing, the Georgia Supreme Court's ruling that section 1-207 does not permit a payee of a full-payment check to both accept the check and avoid reaching an accord and satisfaction); U.C.C. § 3-311 cmts. 1-2, 2 U.L.A. 86 (1990); *The Dilemma Revisited*, *supra* note 21, at 430 n.22; Fry, *supra* note 21, at 358, 363-64; Vitauts M. Gulbis, Annotation, *Application of UCC § 1-207 to Avoid Discharge of Disputed Claim Upon Qualified Acceptance of Check Tendered as Payment in Full*, 37 A.L.R. 4TH 358 (1985). *But see* Ennia Gen. Ins. Co. v. Auld, 506 So. 2d 62, 63 (Fla. Dist. Ct. App. 1987); Eder v. Yvette B. Gervey Interiors, Inc., 407 So. 2d 312 (Fla. Dist. Ct. App. 1981); McKee Const. Co. v. Stanley Plumbing & Heating Co., 828 S.W.2d 700, 701-06 (Mo. Ct. App. 1992); Barber v. White, 264 S.E.2d 385, 386 (N.C. Ct. App. 1980); Brown v. Coastal Truckways Inc., 261 S.E.2d 266, 269 (N.C. Ct. App. 1980); Les Schwab Tire Ctrs., Inc. v. Ivory Ranch, Inc., 664 P.2d 419, 420-21 (Or. Ct. App. 1983); Trevino v. Brookhill Capital Resources, Inc., 782 S.W.2d 279, 281 (Tex. Ct. App. 1989); Pileco, Inc. v. HCI, Inc., 735 S.W.2d 561, 562-63 (Tex. Ct. App. 1987).

23. WHITE & SUMMERS, *supra* note 11, § 13-24, at 608-10. In the 1993 pocket part to the treatise, Professors White and Summers acknowledge that the 1990 revisions to the U.C.C. represent a return to the common law rule that a creditor who negotiates a full payment check may not avoid an accord and satisfaction by accepting the check with a reservation of rights. JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 13-6, at 31-32 (3d ed. Supp. 1993).

24. U.C.C. § 1-207(2), 1 U.L.A. 38 (Supp. 1994). The 1990 revisions also added two commas to the text of subsection (1) which do not appear to change its meaning. *See* U.C.C. § 1-207(1), 1 U.L.A. 38 (Supp. 1994).

the common law of accord and satisfaction,[25] and new section 3-311 sets out specific rules for an accord and satisfaction involving a negotiable instrument.[26]

### *B. Former U.C.C. Section 3-802(3)*

The 1990 version of U.C.C. Article 3 is not the first to codify specific rules applicable to accord and satisfaction, although it has been some years since such a provision appeared in Article 3. The 1952 Official Draft of the U.C.C. contained the following provision:

> Where a check or similar payment instrument provides that it is in full satisfaction of an obligation the payee discharges the underlying obligation by obtaining payment of the instrument unless he establishes that the original obligor has taken unconscionable advantage in the circumstances.[27]

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25. *See supra* notes 20-23 and accompanying text (noting the ambiguity of the prior section).

26. *See infra* part IV.B.

27. U.C.C. § 3-802(3) (1952), *reprinted in* 14 UNIFORM COMMERCIAL CODE: DRAFTS, *supra* note 20, at 465; *see also* Rosenthal, *supra* note 4, at 58-63. The Official Comment to this provision states:

> Checks are frequently given with a term providing that they are "in full payment of all claims," or similar language. The holder who obtains payment of such a check takes its benefits subject to the drawer's stipulation that he releases the original obligation. Even where the obligation is for an undisputed and liquidated debt there is no unfairness in the tender and acceptance of an accord and satisfaction; and in this respect subsection (3) changes the law in a number of states.
>
> The exception stated as to unconscionable advantage taken by the obligor has been recognized in a considerable number of decisions. A genuine accord and satisfaction is to be found only where the parties are dealing at arm's length and on fair terms of bargaining equality, without unfair advantage taken by either party.
>
> The following cases illustrate the application of the exception:
>
> a. The debtor sends the creditor a false statement of their account with a check which stipulates that it is in full payment. The creditor cashes the check in good faith reliance on the statement of account. The original obligation is not discharged.
>
> b. The debtor, knowing that it is the practice of the creditor's clerks to put through checks without examining accounts, sends a check for half the amount due which states that it is in full payment. The check is cashed without examining the account. The obligation is not discharged.
>
> c. The debtor sends a check for less than the amount due which states that it is in full payment. The creditor insists that the amount is not correct, and finally cashes the check as the only available means of obtaining any payment. The original obligation is not discharged.
>
> d. An employer hands an employee a check for less than the full amount of wages due which states that it is in full payment, and threatens to fire the employee if he does not accept the amount. When the employee cashes the check the original obligation is not discharged.

Similar provisions appeared in the drafts of 1947, 1948 and 1949.[28] The U.C.C. Editorial Board recommended that section 3-802(3) be deleted because it "evoked criticism on the ground that it would work hardship, and was open to abuse."[29] As a result, the 1957 Official Edition of the U.C.C. did not contain the provision.[30]

### *C. Former U.C.C. Section 3-112(1)(f)*

Prior to the 1990 revisions, Article 3 contained a provision that the negotiability[31] of an instrument was not defeated by "a term in a draft providing that the payee by indorsing or cashing it acknowledges full satisfaction of an obligation of the drawer."[32] This provision has been deleted from the 1990 version of Article 3.

The addition of section 3-311 makes prior section 3-112(1)(f) superfluous. The only function of prior section 3-112(1)(f) was to make clear that including a full payment legend on a check or other type of draft did not prevent the check or draft from being a negotiable instrument. New section 3-311 sets forth explicit rules for accord and satisfaction using a negotiable instrument. These rules clearly contemplate that a negotiable instrument, such as a check or other draft, may contain a full payment legend. Section 3-112(1)(f) is, therefore, no longer necessary. If a check or draft containing the full payment legend contemplated by section 3-311 could not be a negotiable instru-

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> e. An employer hands an employee a check for less than the full amount of wages due which states that it is in full payment. He refuses the employee's demands for the proper amount, and the employee cashes the check in order to obtain money for subsistence. The obligation is not discharged.

U.C.C. § 3-802 cmt. 5 (1952), *reprinted in* 14 UNIFORM COMMERCIAL CODE: DRAFTS, *supra* note 20, at 466-67; *see also* Rosenthal, *supra* note 4, at 59 n.45.

28. *See* Rosenthal, *supra* note 4, at 58-59.

29. AMERICAN LAW INSTITUTE, NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, 1956 RECOMMENDATIONS OF THE EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE 132 (1957), *reprinted in* 18 UNIFORM COMMERCIAL CODE: DRAFTS, *supra* note 20, at 156.

30. *See* U.C.C. § 3-802 (1957), *reprinted in* 18 UNIFORM COMMERCIAL CODE DRAFTS, *supra* note 20, at 156; Rosenthal, *supra* note 4, at 60.

31. Article 3 of the U.C.C. only applies to "negotiable" instruments. *See infra* notes 50-55 and accompanying text.

32. U.C.C. § 3-112(1)(f), 2 U.L.A. 349 (1991). This provision appeared in its current form with its current section number as early as the 1952 Official Draft of the U.C.C. *See* 14 UNIFORM COMMERCIAL CODE: DRAFTS, *supra* note 20, at 322. The same provision, with slightly different wording, appeared in the 1947 Tentative Draft No. 2 of Article 3. According to that provision, the negotiability of an instrument was not affected by "a term in a bill providing that the payee by indorsing or cashing the bill acknowledges full satisfaction of an obligation of the maker or drawer." COMMERCIAL CODE TENTATIVE DRAFT NO. 2—ARTICLE III § 10(1)(h) (1947), *reprinted in* 3 UNIFORM COMMERCIAL CODE: DRAFTS, *supra* note 20, at 59.

ment, section 3-311 would not belong in Article 3, which typically applies only to negotiable instruments.[33]

## IV. THE 1990 REVISIONS TO U.C.C. ARTICLE 3: A NEW APPROACH TO ACCORD AND SATISFACTION

Article 3 of the U.C.C. was revised in 1990 to reflect changes in legislation, regulations, practices, and technology applicable to negotiable instruments.[34] These revisions include a new section 3-311 which explicitly codifies the applicable rules of when an accord and satisfaction takes place.[35] In addition, the drafters added a new subsection (2) to section 1-207, rejecting the minority view that this section provides an escape hatch from accord and satisfaction. Courts in some states have held that the payee of a full payment check could avoid the application of the common law rules of accord and satisfaction by accepting the check "under protest" or "with reservation of

33. *See infra* notes 50-55 and accompanying text.

34. *See* Prefatory Note to Revised U.C.C. Article 3, 2 U.L.A. 7-8 (1991).

35. Section 3-311 provides as follows:

> (a) If a person against whom a claim is asserted proves that (i) that person in good faith tendered an instrument to the claimant as full satisfaction of the claim, (ii) the amount of the claim was unliquidated or subject to a bona fide dispute, and (iii) the claimant obtained payment of the instrument, the following subsections apply.
>
> (b) Unless subsection (c) applies, the claim is discharged if the person against whom the claim is asserted proves that the instrument or an accompanying written communication contained a conspicuous statement to the effect that the instrument was tendered as full satisfaction of the claim.
>
> (c) Subject to subsection (d), a claim is not discharged under subsection (b) if either of the following applies:
>
> (1) The claimant, if an organization, proves that (i) within a reasonable time before the tender, the claimant sent a conspicuous statement to the person against whom the claim is asserted that communications concerning disputed debts, including an instrument tendered as full satisfaction of a debt, are to be sent to a designated person, office, or place, and (ii) the instrument or accompanying communication was not received by that designated person, office, or place.
>
> (2) The claimant, whether or not an organization, proves that within 90 days after payment of the instrument, the claimant tendered repayment of the amount of the instrument to the person against whom the claim is asserted. This paragraph does not apply if the claimant is an organization that sent a statement complying with paragraph (1)(i).
>
> (d) A claim is discharged if the person against whom the claim is asserted proves that within a reasonable time before collection of the instrument was initiated, the claimant, or an agent of the claimant having direct responsibility with respect to the disputed obligation, knew that the instrument was tendered in full satisfaction of the claim.

U.C.C. § 3-311, 2 U.L.A. 85-86 (1991).

rights."[36]

By its terms,[37] and by virtue of its being a part of Article 3 of the U.C.C.,[38] section 3-311 will apply only to an accord and satisfaction involving the use of a negotiable instrument.[39] Therefore, there will continue to be situations where an accord and satisfaction will be reached entirely outside the U.C.C.[40] Nevertheless, as the common law doctrine of accord and satisfaction continues to evolve, courts might elect to incorporate some of the concepts of section 3-311 into the common law. The drafters of revised Article 3 anticipated that their rules may be applied in cases beyond those involving negotiable instruments.[41]

### *A. The Elements of Accord and Satisfaction Under Section 3-311*

Subsections (a) and (b) of section 3-311 set forth a number of elements that the debtor must satisfy in order to have an accord and satisfaction. To start, the debtor must have acted in good faith.[42] Good faith is now defined for purposes of U.C.C. Article 3 as "honesty in fact and the observance of reasonable commercial standards of fair dealing."[43] Previously, the definition was "honesty in fact in the conduct or transaction concerned."[44] The old definition is generally viewed as intending a purely subjective standard of good faith,[45] although courts applying the old definition have not limited their consideration in this way and have incorporated objective

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36. *See supra* notes 20-23 and accompanying text.

37. *See supra* note 35.

38. *See* U.C.C. § 3-102, 2 U.L.A. 19-20 (1991) (stating that Article III applies to negotiable instruments).

39. *See infra* notes 50-55 and accompanying text.

40. *See, e.g.*, Cobb v. General Motors Acceptance Corp., 589 So. 2d 728 (Ala. Civ. App. 1991). *Cobb* involved a loan secured by an automobile. The debtor was behind on her payments and returned the car to the dealership, later testifying that she relied upon a statement by a representative of the creditor that returning the car would satisfy her entire obligation on the loan. *Id.* at 730. Although the trial court had granted summary judgment for the creditor, the appellate court reversed, indicating that if the debtor could prove the facts that she alleged, she could establish a defense of accord and satisfaction. *Id.* at 732-33.

41. U.C.C. § 3-104 cmt. 2, 2 U.L.A. 27 (1991).

42. *See* U.C.C. § 3-311(a), 2 U.L.A. 85 (1991).

43. U.C.C. § 3-103(a)(4), 2 U.L.A. 22 (1991).

44. U.C.C. § 1-201(19), 1 U.L.A. 65 (1989). The general definitions in Article 1 apply throughout the U.C.C. unless supplanted by another definition specific to a particular article. U.C.C. § 1-201, 1 U.L.A. 63 (1989). Thus, the definition from section 1-201(19) applied to accord and satisfaction until 1990, when the drafters added the new definition in section 3-103(a)(4). U.C.C. § 3-103 cmt. 4, 2 U.L.A. 22 (1991).

45. WHITE & SUMMERS, *supra* note 11, § 14-6, at 629.

elements in their analyses.[46] The new definition goes along with the approach of these courts and adds an explicit objective component to the definition of good faith in Article 3.[47]

The duty to act in good faith pervades the U.C.C.[48] Acting in good faith is not usually stated as a specific element for establishing an accord and satisfaction at common law; nevertheless, the good faith requirement found in section 3-311 is consistent with common law cases holding that fraud or concealment renders an attempted accord and satisfaction ineffective.[49]

In addition to acting in good faith, the debtor must use an "instrument" in order to obtain an accord and satisfaction under section 3-311.[50] "Instrument" is shorthand for "negotiable instrument,"[51] and the requisites for negotiable instruments are set forth at section 3-104.[52] In general, negotiable instruments are divided into two

46. *See* WHITE & SUMMERS, supra note 11, § 14-6, at 629-31.

47. A task force of the American Bar Association Section on Business Law, Uniform Commercial Code Committee, recommended a similar revision to the general U.C.C. definition of good faith in section 1-201(19). As revised, section 1-201(19) would have read: "'Good faith' means honesty in fact and the observance of reasonable standards of fair dealing in the conduct or transaction concerned." ABA Section of Business Law UCC COMMITTEE UPDATE 10 (June 1993); *see also* Fred H. Miller, *The Benefits of New UCC Articles 3 and 4*, 24 UCC L.J. 99, 116 n.95 (1991). However, the U.C.C. Permanent Editorial Board subsequently decided to change the definition of good faith in Article 1 only if the drafting committees for the other Articles of the U.C.C. adopt the definition in revised Article 3. Letter from Fred H. Miller, Kenneth McAfee Centennial Professor of Law and George Lynn Cross Research Professor, The University of Oklahoma College of Law, to Gene A. Marsh, Associate Professor of Law, The University of Alabama 1 (Aug. 17, 1993) (copy on file with the author).

48. The U.C.C. itself explicitly states: "Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement." U.C.C. § 1-203, 1 U.L.A. 109 (1991).

49. *See, e.g.*, Metropolitan State Bank v. Cox, 302 P.2d 188, 193 (Colo. 1956); *cf.* U.C.C. § 3-311 cmt. 4, 2 U.L.A. 87 (1991) (analyzing circumstances under which the good faith requirement might not be met in the context of section 3-311); WHITE & SUMMERS, *supra* note 11, § 1-6, at 60.

50. U.C.C. § 3-311(a)(i), 2 U.L.A. 85 (1991); *see also* HENRY J. BAILEY & RICHARD B. HAGEDORN, BRADY ON BANK CHECKS: THE LAW ON BANK CHECKS ¶ 4.17 (7th ed. 1992).

51. U.C.C. § 3-104(b), 2 U.L.A. 25 (1991).

52. Section 3-104 provides in relevant part:

> (a) Except as provided in subsections (c) and (d), "negotiable instrument" means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it:
>
> (1) is payable to bearer or to order at the time it is issued or first comes into possession of a holder;
>
> (2) is payable on demand or at a definite time; and
>
> (3) does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of

categories, notes and drafts.[53] A check is a particular type of draft[54] and is the type of negotiable instrument most commonly associated with an accord and satisfaction.[55]

The next requirement of section 3-311 is that the negotiable instrument must have been "tendered . . . as full satisfaction of the claim."[56] This element largely tracks the common law requirement.[57] Next, the claim must be unliquidated or disputed.[58] This is a stricter rule than that followed by some cases decided under the common law.[59] Next, the section only applies if "the claimant obtained payment of the instrument."[60] This tracks the common law rule that a full payment legend on a check becomes binding when the creditor obtains payment of the check.[61]

The final requirement for establishing an accord and satisfaction under section 3-311 is that the debtor must "prove[] that the instrument or an accompanying written communication contained a conspicuous

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money, but the promise or order may contain (i) an undertaking or power to give, maintain, or protect collateral to secure payment, (ii) an authorization or power to the holder to confess judgment or realize on or dispose of collateral, or (iii) a waiver of the benefit of any law intended for the advantage or protection of an obligor.

* * *

(c) An order that meets all of the requirements of subsection (a), except paragraph (1), and otherwise falls within the definition of "check" in subsection (f) is a negotiable instrument and a check.

(d) A promise or order other than a check is not an instrument if, at the time it is issued or first comes into possession of a holder, it contains a conspicuous statement, however expressed, to the effect that the promise or order is not negotiable or is not an instrument governed by this Article.

U.C.C. § 3-104, 2 U.L.A. 25 (1991).

53. U.C.C. § 3-104 cmt. 4, 2 U.L.A. 28 (1991). "An instrument is a 'note' if it is a promise and is a 'draft' if it is an order. If an instrument falls within the definition of both 'note' and 'draft,' a person entitled to enforce the instrument may treat it as either." U.C.C. § 3-104(e), 2 U.L.A. 26 (1991).

54. The U.C.C. states that: "'Check' means (i) a draft, other than a documentary draft, payable on demand and drawn on a bank or (ii) a cashier's check or teller's check. An instrument may be a check even though it is described on its face by another term, such as 'money order.'" U.C.C. § 3-104(f), 2 U.L.A. 26 (1991).

55. *See* U.C.C. § 3-311 cmts. 1-7, 2 U.L.A. 86-89 (1991) (using frequent examples involving checks).

56. U.C.C. § 3-311(a)(i), 2 U.L.A. 85 (1991); *see also* BAILEY & HAGEDORN, *supra* note 50, at ¶ 4.17.

57. *See supra* note 11 and accompanying text.

58. U.C.C. § 3-311(a)(ii), 2 U.L.A. 85 (1991); *see also* BAILEY & HAGEDORN, *supra* note 50, at ¶ 4.17.

59. *See supra* notes 15-17 and accompanying text.

60. U.C.C. § 3-311(a)(iii), 2 U.L.A. 85 (1991); *see also* BAILEY & HAGEDORN, *supra* note 50, at ¶ 4.17.

61. *See supra* notes 11-12 and accompanying text.

statement to the effect that the instrument was tendered as full satisfaction of the claim."[62] The U.C.C. defines "conspicuous statement" objectively.[63] Almost any statement on a check will be conspicuous if the creditor can be expected to examine the check.[64] Therefore, full payment legends on manually processed checks will almost always be "conspicuous." Such legends may not be conspicuous on checks processed mechanically, however, because a human creditor does not personally indorse these checks. A creditor that receives a full payment check processed mechanically might argue that the full payment legend was not "conspicuous," and therefore should not be the basis of an accord and satisfaction.[65]

Subject to certain exceptions,[66] the general effect under section 3-311 of obtaining payment of a full payment check, as under the common law,[67] is that the creditor is deemed to have accepted the proffered payment as payment in full and thereby loses the ability to sue for the unpaid balance.[68]

### *B. The New Rules for Accord and Satisfaction for Negotiable Instruments*

The general rules for the application of section 3-311 are largely similar to the common law rules for accord and satisfaction. An accord and satisfaction under section 3-311 is, however, subject to new rules as well. These new rules are set forth at sections 3-311(c)

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62. U.C.C. § 3-311(b), 2 U.L.A. 85 (1991); *see also* BAILEY & HAGEDORN, *supra* note 50, at ¶ 4.17.

63. According to the U.C.C., the statement must be "so written that a reasonable person against whom it is to operate ought to have noticed it." U.C.C. § 1-201(10), 1 U.L.A. 64 (1991); U.C.C. § 3-311 cmt. 4, 2 U.L.A. 85 (1991).

64. U.C.C. § 3-311 cmt. 4, 2 U.L.A. 87 (1991). According to the commentary:

> In cases in which the claimant is an individual the claimant will receive the check and will normally indorse it. Since the statement concerning tender in full satisfaction normally will appear above the space provided for the claimant's indorsement of the check, the claimant "ought to have noticed" the statement.

*Id.*

65. U.C.C. § 3-311(c) provides additional ways that a creditor can avoid the imposition of an accord and satisfaction, such as by providing special notice to the debtor or by returning the payment within 90 days. *See infra* part IV.B.1.

66. For a discussion of these exceptions, see *infra* part IV.B.1.

67. *See supra* notes 12-13 and accompanying text.

68. If the requirements are fulfilled, U.C.C. § 3-311(b) specifies the outcome: "Unless subsection (c) applies, the claim is discharged if the person against whom the claim is asserted proves that the instrument or an accompanying written communication contained a conspicuous statement to the effect that the instrument was tendered in full satisfaction of the claim." U.C.C. § 3-311(b), 2 U.L.A. 85 (1991).

and (d). The next two subsections of this Article focus on the mechanics of U.C.C. sections 3-311(c) and (d). The text outlines the mechanisms for preventing an inadvertent accord and satisfaction that are set forth at 3-311(c), and then discusses the limitations on these mechanisms set forth at 3-311(d).

### 1. Subsection (c) of Section 3-311 Provides Ways to Guard Against Inadvertent Accord and Satisfaction

Modern techniques for processing large volumes of checks have replaced human beings with machines in as many stages as possible. Since machines are unable to recognize a full payment legend on a check, this automation increases the risk that a check may be accepted by a creditor who fails to notice the full payment legend.[69] To reduce this risk, subsection (c) provides two new ways that a payee can limit the imposition of an accord and satisfaction.[70] If an organization is concerned that a full payment check may slip by its regular processing procedures, it may send "a conspicuous statement to [its debtors] that communications concerning disputed debts, including an instrument tendered as full satisfaction of a debt, are to be sent to a designated person, office, or place."[71] In most cases, debtors who send full payment checks but fail to comply with the notice requirement will not accomplish an accord and satisfaction unless more than a "reasonable time" elapsed between the creditor's most recent notice and the time the debtor sent the check.[72] Alternatively, any recipient of a full payment

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69. *See* U.C.C. § 3-311 cmt. 5, 2 U.L.A. 87-88 (1991).

70. According to U.C.C. § 3-311(c):

> Subject to subsection (d), a claim is not discharged under subsection (b) if either of the following applies:
>
> (1) The claimant, if an organization, proves that (i) within a reasonable time before the tender, the claimant sent a conspicuous statement to the person against whom the claim is asserted that communications concerning disputed debts, including an instrument tendered as full satisfaction of a debt, are to be sent to a designated person, office, or place, and (ii) the instrument or accompanying communication was not received by that designated person, office, or place.
>
> (2) The claimant, whether or not an organization, proves that within 90 days after payment of the instrument, the claimant tendered repayment of the amount of the instrument to the person against whom the claim is asserted. This paragraph does not apply if the claimant is an organization that sent a statement complying with paragraph (1)(i).

U.C.C. § 3-311(c), 2 U.L.A. 85-86 (1991); *see also* BAILEY & HAGEDORN, *supra* note 50, at ¶ 4.17.

71. U.C.C. § 3-311(c)(1), 2 U.L.A. 85-86 (1991).

72. U.C.C. § 3-311(c)(1) & cmt. 5, 2 U.L.A. 85 (1991). Section 3-311(d) provides an exception to the rule in subsection (c). *See infra* part IV.B.2. Very little guidance is offered on what might constitute a "reasonable time":

check who does not send such a notice may avoid the accord and satisfaction by repaying the amount of the check to the debtor within ninety days.[73]

### 2. Subsection (d) of Section 3-311 Limits the Effect of Subsection (c)

Subsection 3-311(d) limits the relief for inadvertent accord and satisfaction provided to creditors by subsection (c). If the creditor takes a full payment instrument knowing that an accord and satisfaction was intended, the rules in subsection (c) designed to prevent inadvertent accord and satisfaction do not apply.[74] This provision contains some sources of possible confusion.[75] Notwithstanding these areas of confusion, the goal of preventing creditors from abusing the section 3-311(c) safeguards is salutary.

The apparent intent of subsection (d) can be illustrated as follows. Suppose that a buyer purchases widgets from a seller, dealing with the manager of the seller's branch office. The seller delivers a shipment of widgets to the buyer on June 1 and submits a bill for $10,000. The buyer contacts the manager, disputing the value of this shipment and claiming that the bill should have been only for $8,000 due to problems with the widgets. The manager disagrees and declines to adjust the bill, maintaining that the shipment was worth the full $10,000.

Suppose further that the buyer delivers a check in the amount of $9,000 to the manager, payable to the seller and conspicuously marked "Payment in full for June 1 shipment of widgets." When the buyer delivers this check, she explains to the manager that she is offering a compromise to settle the matter. The manager agrees that it is in the

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> The statement must be given to the customer within a reasonable time before the tender is made. This requirement is designed to assure that the customer has reasonable notice that the full satisfaction check must be sent to a particular place. The reasonable time requirement could be satisfied by a notice on the billing statement sent to the customer.

U.C.C. § 3-311 cmt. 5, 2 U.L.A. 88 (1991).

73. U.C.C. § 3-311(c)(2), 2 U.L.A. 86 (1991).

74. Section 3-311(d) provides:

> A claim is discharged if the person against whom the claim is asserted proves that within a reasonable time before collection of the instrument was initiated, the claimant, or an agent of the claimant having direct responsibility with respect to the disputed obligation, knew that the instrument was tendered in full satisfaction of the claim.

U.C.C. § 3-311(d), 2 U.L.A. 86 (1991); *see also* BAILEY & HAGEDORN, *supra* note 50, at ¶ 4.17.

75. *See infra* part IV.C.1.

interest of both parties to settle the dispute, and obtains payment of the check from the buyer's bank.

In this scenario, both the buyer and the manager intended to accomplish an accord and satisfaction. If section 3-311 ended with subsection (c), however, the seller could have an inappropriate means of escape from the settlement, whether or not it had sent the 3-311(c)(1) notice. If the seller *had* sent the notice and specified that full payment instruments and communications be sent somewhere other than to the manager, the accord and satisfaction would not bind the seller, even though the seller's manager agreed to the settlement and the buyer is bound by it.[76] Alternatively, if the seller *had not* sent the notice, it would have a ninety-day option to repudiate the accord and satisfaction.[77] Subsection (d) is designed to prevent this result, although it is not a perfect tool for doing so, as explained in the following section.

### *C. Evaluation of Section 3-311*

If one assumes that the doctrine of accord and satisfaction will remain a part of American law,[78] section 3-311 appears to offer a worthwhile enhancement to the existing common law, although it has some shortcomings. Subsection 1 of this section points out flaws in the language of U.C.C. section 3-311(d). Subsection 2 identifies a risk of refusing a full payment check that is unique to indorsers and accommodation parties. Subsection 3 then explains the benefits of the new U.C.C. rules, which reduce the risk of an inadvertent accord and satisfaction.

#### 1. Drafting Concerns Mar Subsection (d)

In cases involving organizations, the proper relationship between sections 3-311(d) and 1-201(27) is unclear. The tension between these two sections raises two questions.

First, the two sections might both apply to the same situation, but they use different and potentially conflicting phrases to describe the agent through whom an organization is deemed to receive knowledge. Section 3-311(d) states that the inadvertent accord and satisfaction provision (section 3-311(c)) is not available if the creditor or its agent knows the instrument was tendered in full satisfaction of the claim.[79]

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76. U.C.C. § 3-311(c)(1), 2 U.L.A. 85-86 (1991).

77. U.C.C. § 3-311(c)(2), 2 U.L.A. 86 (1991).

78. *See infra* parts V, VI.

79. U.C.C. § 3-311(d), 2 U.L.A. 86 (1991). For a summary of the terminology used in this article, see *supra* note 9.

The use of the phrase "the claimant, or an agent of the claimant having direct responsibility" in section 3-311(d) creates uncertainty as to the proper relationship between this provision and section 1-201(27), which states rules governing how an organization gains knowledge.[80] If the creditor faced with a full payment check is an organization, it cannot know anything except through its agent, which suggests that the rules of section 1-201(27) should apply to determine whether "the claimant" itself knows of the intended accord and satisfaction. Thus, section 1-201(27) charges an organization with the knowledge of "the individual conducting [the particular] transaction."[81]

On the other hand, section 3-311(d) provides a more specific rule for determining when knowledge of agents is to be imputed to a principal: an agent's knowledge is to be attributed to the organization if the agent has "direct responsibility with respect to the disputed obligation."[82] Unless the reference to "the claimant" in section 3-311(d) is surplusage when the claimant is an organization, the question remains whether "the individual conducting that transaction," under section 1-201(27), always defines the same group of agents as the "agent of the claimant having direct responsibility with respect to the disputed obligation," under section 3-311(d).

Second, it is unclear whether an agent of an organization must have actual subjective knowledge of something before the organization will be deemed to know of it, or whether knowledge will be attributed to the organization based upon the objective standard of section 1-201(27). Section 3-311(d) might be read to provide that only an agent's actual knowledge of an accord and satisfaction is to be attributed to an organization: "A claim is discharged if . . . an agent of the claimant . . . *knew* that the instrument was tendered in full

80. Section 1-201(27) states:

> Notice, knowledge or a notice or notification received by an organization is effective for a particular transaction from the time when it is brought to the attention of the individual conducting that transaction, and in any event from the time when it would have been brought to his attention if the organization had exercised due diligence. An organization exercises due diligence if it maintains reasonable routines for communicating significant information to the person conducting the transaction and there is reasonable compliance with the routines. Due diligence does not require an individual acting for the organization to communicate information unless such communication is part of his regular duties or unless he has reasons to know of the transaction and that the transaction would be materially affected by the information.

U.C.C. § 1-201(27), 1 U.L.A. 66 (1991 & Supp. 1994).

81. *Id.*

82. U.C.C. § 3-311(d), 2 U.L.A. 86 (1991).

satisfaction of the claim."[83] Section 3-311(d) is, however, concerned not only with the knowledge of agents, but also with the knowledge of the claimant itself: "A claim is discharged if . . . *the claimant,* or an agent of the claimant . . . knew that the instrument was tendered in full satisfaction of the claim."[84] To determine the knowledge of the claimant, it again seems appropriate to look at Section 1-201(27), which arguably does not distinguish between "knowledge" and "notice" in dealing with organizations, and which imposes an objective standard for imputing knowledge to organizations.[85] Section 1-201(27) provides that an organization has "[n]otice, knowledge or a notice or notification . . . *in any event* from the time when it would have been brought to [the] attention [of the individual conducting the transaction] if the organization had exercised due diligence."[86]

Official Comment 7 to section 3-311 attempts to reconcile the two sections. Although the comment does not address the question of whether knowledge is determined subjectively or objectively, it does take the position that for the purposes of section 3-311(d), "an agent of the claimant having direct responsibility"[87] is the same thing as "the individual conducting that transaction."[88] While this is not an unreasonable interpretation of the statutory language, it is not the only possible reading. For example, one might argue that when a full payment check is sent to a lock box[89] account at a bank, the "transaction" contemplated by section 1-201(27) is merely the deposit of the check in the appropriate account. In this scenario, a court might conclude that "*the claimant* . . . knew that the instrument was tendered in full satisfaction of the claim"[90] based upon the rules of section 1-201(27),

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83. *Id.* (emphasis added).

84. *Id.* (emphasis added).

85. The general U.C.C. definition of "knowledge" requires actual knowledge, a subjective standard. On the other hand, "notice" can result from either actual knowledge or reason to know, an objective standard. *See* U.C.C. § 1-201(25), 1 U.L.A. 65-66 (1991).

86. U.C.C. § 1-201(27), 1 U.L.A. 66 (1991) (emphasis added).

87. U.C.C. § 3-311(d), 2 U.L.A. 86 (1991).

88. U.C.C. § 1-201(27), 1 U.L.A. 66 (1991). The comment states that "the 'individual conducting that transaction' is an employee or other agent of the organization having direct responsibility with respect to the dispute." U.C.C. § 3-311 cmt. 7, 2 U.L.A. 88 (1991).

89. A lock box is an arrangement designed to get a creditor's remittances from its customers into the banking system and available for the creditor's use more quickly. The customers are instructed to send their remittances to the creditor at a designated post office box, which is actually maintained by the creditor's bank. The bank opens the mail, deposits the checks immediately, and then sends the remittance advices to the creditor so the creditor can record the payments in its accounts receivable records.

90. U.C.C. § 3-311(d), 2 U.L.A. 86 (1991) (emphasis added).

even though the lock box clerk lacked knowledge of the dispute between the parties and would not qualify as "an agent of the claimant having direct responsibility with respect to the disputed obligation."[91] The last paragraph of Official Comment 7 attempts to head off this interpretation. However, courts do not always follow the Official Comments.[92]

### 2. Refusing a Full Payment Check May Discharge Indorsers or Accommodation Parties

Often a potential borrower does not alone have sufficient resources to convince a lender to make the requested loan. There are various ways that the lender can obtain sufficient assurance of repayment.[93] When a young-adult buys his or her first car, the lender will often require a parent to share responsibility for repayment. Similarly, lenders often require that corporate officers be obligated in their personal capacity for loans made to a corporation. If the parent or corporate officer in this situation evidences his or her obligation by signing the promissory note, he or she is referred to as an "accommodation party."[94] An "indorsement" is a particular type of signature on a negotiable instrument.[95] A person who places an indorsement on an instrument is referred to as an "indorser."[96] An indorser is obligated to pay the instrument in certain circumstances.[97] An indorser may indorse for accommodation, or for other reasons.[98]

In addition to the pressures placed upon any creditor faced with a partial payment check with a full payment legend,[99] a creditor holding a note on which indorsers or accommodation parties are liable faces a

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91. U.C.C. § 3-311(d), 2 U.L.A. 86 (1991).

92. *See* WHITE & SUMMERS, *supra* note 11, § 4, at 13.

93. *See* WHITE & SUMMERS, *supra* note 11, § 13-13, at 576-79.

94. The U.C.C. defines the relevant terminology as follows:

> If an instrument is issued for value given for the benefit of a party to the instrument ("accommodated party") and another party to the instrument ("accommodation party") signs the instrument for the purpose of incurring liability on the instrument without being a direct beneficiary of the value given for the instrument, the instrument is signed by the accommodation party "for accommodation."

U.C.C. § 3-419(a), 2 U.L.A. 125 (1991 & Supp. 1994).

95. U.C.C. § 3-204(a), 2 U.L.A. 54 (1991).

96. U.C.C. § 3-204(b), 2 U.L.A. 54 (1991).

97. *See* U.C.C. § 3-415, 2 U.L.A. 116 (1991); WHITE & SUMMERS, *supra* note 11, § 13-9, at 561-64; WHITE & SUMMERS, *supra* note 23, § 13-3, at 14-17.

98. In addition to subjecting the indorser to liability on the instrument, an indorsement is essential to transfer ownership of certain types of negotiable instruments. *See* WHITE & SUMMERS, *supra* note 11, § 13-9, at 561.

99. *See supra* notes 12-13 and accompanying text.

special dilemma.[100] Revised U.C.C. section 3-603(b) provides that a refused tender of payment discharges indorsers and accommodation parties to the extent of the tender.[101] For example, suppose a corporation bought a machine from a vendor, and the vendor financed the purchase, requiring the corporate president to sign the note individually, as well as on behalf of the corporation. Subsequently, the corporation demands an adjustment of the purchase price, claiming that the vendor misrepresented the capabilities of the machine. When the vendor declines to adjust the purchase price, the corporation sends its check, conspicuously marked "payment in full," to the vendor for half of the balance on the note. If the vendor obtains payment of the check, it risks being bound by accord and satisfaction.[102] On the other hand, if the vendor refuses the check and if the president is held to have been an accommodation party,[103] the president's personal liability on the note will be reduced by half.[104]

Suppose that the vendor returns the check and the corporation tenders a second check, again marked "payment in full," and again in an amount equal to half of the note's balance. If the vendor refuses this second check, it is arguable that the president's personal liability on the note will be *entirely* discharged by virtue of revised section 3-603(b). Specifically, the president's obligation as to half the balance was discharged by the vendor's refusal of the first check, and the other half may be discharged by the vendor's refusal to accept the second check.

### 3. Section 3-311 Reduces the Risk of Inadvertent Accord and Satisfaction

Section 3-311 provides two ways to reduce the risk of an inadvertent accord and satisfaction.[105] First, an organization concerned about full payment legends slipping unnoticed past its check collection procedures can require that such a legend will only be effective if the check is sent to a special address,[106] where the check

100. This discussion was suggested by a memorandum from John F. Andrews to the Alabama Law Institute, U.C.C. Article 3 & 4 Committee (Feb. 25, 1993) (copy on file with the author).

101. U.C.C. § 3-603(b), 2 U.L.A. 140 (1991).

102. Section 3-311(c) might be of some help to the vendor, but is not pertinent to the larger issues discussed here. *See supra* part IV.B.1.

103. Determining whether a particular party to an instrument is an accommodation party is not always easy. WHITE & SUMMERS, *supra* note 11, § 13-4, at 18-19.

104. *See* U.C.C. § 3-603(b), 2 U.L.A. 140 (1991).

105. For more discussion of the mechanics of this provision, see *supra* part IV.B.1.

106. U.C.C. § 3-311(c)(1), 2 U.L.A. 85 (1991). For more discussion of section 3-

will presumably be scrutinized. Alternatively, a creditor who has not invoked this special address procedure and who inadvertently negotiates a full payment check may avoid the accord and satisfaction by returning the proceeds within ninety days.[107]

Both of these alternatives ameliorate the potentially harsh result which may occur if a creditor inadvertently accepts a full payment check because of failure either to notice the full payment legend or to understand its legal significance. Of course, these protections are neither free nor foolproof. To avail itself of this protection, a creditor must incur costs to set up an additional location for the receipt of checks. Furthermore, if a creditor does not arrange to have checks sent to a special address, there remains the risk that a creditor might obtain payment of a full payment check and not realize the significance of the legend until the ninety-day period for returning the proceeds has expired.

Some commentators have criticized section 3-311(c)(1) for giving organizations a form of protection that is not available to individuals.[108] Notwithstanding this criticism, section 3-311(c)(2) may offer more potential benefits to individuals than to organizations. The average individual is probably less sophisticated about the rules of accord and satisfaction than the average corporate manager of accounts receivable. Therefore, individuals may face more risk than organizations in dealing with a full payment instrument without recognizing the legal consequences. An individual who receives a check with a full payment legend from an insurance company in an amount less than the claim may not be aware that accepting the check can cut off the right to pursue the disputed additional portion of the claim. The ninety-day window presented in section 3-311(c)(2) increases the chance for an unsophisticated creditor to realize his error before it is too late to avoid its application.[109]

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311(c)(1), see *supra* part IV.B.1.

107. U.C.C. § 3-311(c)(2), 2 U.L.A. 86 (1991).

108. *See* Gail K. Hillebrand, *Revised Articles 3 and 4 of the Uniform Commercial Code: A Consumer Perspective*, 42 ALA. L. REV. 679, 691-94 (1991); Jay Winston, *The Evolution of Accord and Satisfaction: Common Law: U.C.C. Section 1-207: U.C.C. Section 3-311*, 28 NEW ENG. L. REV. 189, 219-21 (1993). More generally, these articles assert that section 3-311 does not do enough for consumers, suggesting, *inter alia*, that the word "direct" should be deleted from section 3-311(d). *See* Hillebrand, *supra*, at 694; Winston, *supra*, at 226.

109. *Cf.* U.C.C. § 3-311 cmts. 1, 3, 2 U.L.A. 86-87 (1991) (suggesting situations where the creditor is an individual and the debtor is an insurance company).

Moreover, many corporations need to process large numbers of checks at low cost,[110] but few if any individuals need to do so. Because organizations face challenges in check processing different from those of individuals, it seems reasonable to provide organizations with special consideration. If an individual wishes to bind an organization to an accord and satisfaction and has been notified of the place to send full payment checks, he or she should bear the responsibility for sending the full payment check to the place where it will get appropriate attention.

The rules of new section 3-311(c) place hurdles unknown to the common law before the debtor wishing to impose an accord and satisfaction,[111] but these hurdles do not seem unreasonable. A debtor who wishes to impose an accord and satisfaction on an organization under section 3-311 must determine whether the organization has specified a "person, office, or place" as the focal point for disputed debts, and must be sure to send the full payment check to the right place. If the organization has not specified a place to receive disputed debts, the debtor cannot be assured that the matter is resolved until ninety days after the check is paid.[112] Section 3-311(c) makes it more difficult to establish an accord and satisfaction, but it hardly imposes crippling burdens upon a debtor who is trying in good faith to reach a fair resolution of a dispute.[113]

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110. U.C.C. § 3-311 cmt. 5, 2 U.L.A. 87 (1991).

111. At common law, the creditor bore the burden of identifying checks with a full payment legend, and a creditor who obtained payment of such a check was bound by the resulting accord and satisfaction without any grace period for returning the funds. *See* WHITE & SUMMERS, *supra* note 11, § 13-24, at 607-08.

112. *See* U.C.C. § 3-311(c)(2), 2 U.L.A. 86 (1991).

113. For debtors frustrated by ineffective attempts to communicate with a creditor's unresponsive computer, section 3-311(c)(1) would actually seem likely to *increase* the probability of getting the creditor's attention. An organization will likely give careful consideration before setting up a separate location for the receipt of full payment checks. In addition to the effort and administrative expense required for such a step, invoking the protection of section 3-311(c)(1) requires waiving the 90-day grace period of section 3-311(c)(2). U.C.C. § 3-311(c)(2), 2 U.L.A. 86 (1991) (see last sentence). Moreover, a blanket strategy of merely rejecting any and all full payment checks seems unwise for creditors. The creditor may be better off accepting the compromise in some cases, and rejection of a tendered check may release accommodation parties to the extent of the tendered payment. *See supra* part IV.C.2. It therefore seems likely that a creditor that incurs trouble and expense to specify a separate location for the receipt of full payment checks will staff this office with personnel who are both capable of recognizing the full-payment legends and responsible for taking appropriate action. Thus, section 3-311(c)(1) is something of a substitute for the once-effective technique of folding, spindling, or mutilating a computer punch card. See Rosenthal, *supra* note 4, at 56, where the author states:

> In the early days of automated billing, punch cards were commonly used, and the debtor could often attract human attention to his communication by

Insuring adequate and appropriate protection for debtors is a worthy goal. It would be unwise, however, to give debtors every possible remedy without considering the costs that would be imposed on others' interests. Moreover, some debtor "protections" may actually be adverse to debtor interests, because burdens initially imposed on others may be shifted back to the debtor in a different form.[114]

## V. IS ACCORD AND SATISFACTION BENEFICIAL?

Much of the debate over accord and satisfaction focuses on the appropriate reach of the doctrine—the circumstances in which a court should conclude that a creditor is bound by the full payment legend on a check. However, a more fundamental issue bears examination: Should we allow a full payment check to bind a creditor to an accord and satisfaction *at all*?

The usual justification for the doctrine of accord and satisfaction is that it promotes dispute resolution.[115] This is not a new idea; the New York Court of Appeals, for example, has held this idea for many years.[116] One way to evaluate the doctrine of accord and satisfaction is to compare the benefits received by the beneficiaries to the costs imposed on those harmed. An excess of costs over benefits would suggest that the doctrine makes society as a whole worse off, and should therefore be constrained or eliminated. Conversely, an excess of benefits over costs would suggest that the doctrine is advantageous to society as a whole. Economists call this approach the Kaldor-Hicks

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> folding, spindling, or mutilating the card. Alas, modern technology has developed the computer printout, which affords no such mechanical device to attract the attention of any human being, much less a responsible one, to the customer's communications.

Rosenthal, *supra* note 4, at 56.

114. *See, e.g.*, ARMEN ALCHIAN & WILLIAM R. ALLEN, EXCHANGE & PRODUCTION: COMPETITION, COORDINATION & CONTROL 64-68 (3d ed. 1983) (stating that tax imposed on supplier may be shifted to purchaser). For negative assessments of section 3-311, see Hillebrand, *supra* note 108, at 691-94, and Winston, *supra* note 108, at 218-26.

115. The drafters of the 1990 U.C.C. revisions subscribed to this view, stating: "Section 3-311 is based on a belief that the common law rule [of accord and satisfaction] produces a fair result and that informal dispute resolution by full satisfaction checks should be encouraged." U.C.C. § 3-311 cmt. 3, 2 U.L.A. 86-87 (1991).

116. As early as 1914, the high court of the State of New York stated:

> The law wisely favors settlements, and where there is a real and genuine contest between the parties, and a settlement is had without fraud or misrepresentation, for an amount determined upon as a compromise between the conflicting claims, such settlement should be upheld, although such amount is materially less than the amount claimed by the person to whom it is paid.

Post v. Thomas, 106 N.E. 69, 72 (N.Y.), *remittitur denied*, 106 N.E. 1042 (N.Y. 1914).

definition of efficiency.[117]

The doctrine of accord and satisfaction is obviously beneficial to parties who understand the significance of the full payment legend and use it knowingly. In cases where parties to a dispute understand the relevant considerations and wish to enter into a final, binding settlement, using a full payment legend saves the trouble and expense of executing a formal settlement agreement or release. Where parties enter into an accord and satisfaction knowingly and voluntarily, they likely consider their arrangement advantageous, or else they would not enter into it.[118] As long as both parties understand the consequences of a full payment check, enforcing the rules of accord and satisfaction should be beneficial to all parties. Conversely, non-enforcement would frustrate the parties' expectations.

On the other hand, not every creditor receiving a full payment check will notice the legend and understand its significance. Perhaps the most compelling criticism of the doctrine of accord and satisfaction is that it creates a trap for the unwary creditor.[119] Two types of creditors might unintentionally accept a full payment check, thereby entering into an accord and satisfaction. First, unsophisticated creditors may see a full payment legend on a check but fail to appreciate its ramifications. In addition, because of advances in check processing technology, even sophisticated creditors might reasonably choose not to scrutinize each check, so a full payment legend might slip by unnoticed.[120] The drafters of section 3-311 were concerned about the risk of an inadvertent accord and satisfaction.[121] Although these concerns seem plausible, more empirical data is needed to properly assess the significance of this risk.

It would be difficult, if not impossible, to quantify and compare the relative benefits and costs. It is not clear, however, that the overall benefits of the doctrine exceed the costs. The reductions in transaction costs to be realized from the doctrine are probably not trivial, but

117. RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 13 (4th ed. 1992). This approach has serious limitations. For example, it is often difficult to measure the costs and benefits. *Id.* Moreover, it is not always clear that the benefits to one group are sufficient justification for a policy that imposes costs on another group, particularly if the burdened group receives no compensation. *See id.* at 14-16. Even with these limitations in mind, it will nevertheless be instructive to consider the possible relationships between the benefits and costs of accord and satisfaction.

118. *Cf.* ALCHIAN & ALLEN, *supra* note 114, at 45-48, 52-53 (explaining the reasons people trade with each other, and the benefits derived therefrom).

119. Not all commentators agree that this is a problem. *See, e.g.*, Hillebrand, *supra* note 108, at 691-92.

120. *See* Shanker, *supra* note 21, at 8.

121. *See* U.C.C. § 3-311 cmts. 5-6, 2 U.L.A. 87-88 (1991).

neither are they likely to be very large. If full payment legends on checks were not enforced, parties wishing to settle a disputed debt would have to enter into a more formal agreement, and transaction costs would increase. On the other hand, this increase does not seem particularly significant, at least in cases where the parties have knowingly reached a settlement and intend to document it. If both parties are sophisticated enough to understand the implications of dealing with a full payment check, they should be able to draft an appropriate settlement or release without much additional effort.[122] More importantly, the costs of an unintended accord and satisfaction to an unsuspecting, (i.e., unsophisticated) party can be quite significant.[123]

Furthermore, one cannot say with confidence whether the doctrine generally favors either business or consumer interests.[124] In some situations, consumer interests gain from the availability of accord and satisfaction. For example, an incorrectly billed consumer who repeatedly receives demands for payment from a creditor's computer,

122. Any dispute that can be resolved by tender and acceptance of a full payment check, with the full knowledge and understanding of both parties, is likely to be a relatively simple dispute which could also be resolved by a simple settlement agreement. The resolution of a complex or intractable dispute will usually require a correspondingly complex (and expensive) settlement agreement, if any agreement can be reached at all. A complex or intractable dispute is unlikely to be solved to the ultimate satisfaction of both parties by an accord and satisfaction, although a full payment check may put an end to the dispute if the creditor does not pay appropriate attention to the full payment legend. A debtor attempting to trap an unwary creditor into an inadvertent accord and satisfaction would have a much greater challenge if full payment legends on checks were not enforced. However, this is not an attractive argument in favor of enforcing full payment legends; in fact, this is probably the strongest argument *against* enforcing them.

123. The use of a negotiable instrument in the typical accord and satisfaction should not cloud this analysis. Many of the rules governing negotiable instruments are designed to facilitate the acceptance of negotiable instruments by third parties, making them more useful in commerce. *See, e.g.*, WHITE & SUMMERS, *supra* note 11, § 14-1, at 613-14. An accord and satisfaction, however, affects only the rights and liabilities of the two parties. Even if a check is evidence of an accord and satisfaction, third parties' rights to payment *of that check* are unaffected.

124. U.C.C. § 3-311 cmt. 3, 2 U.L.A. 86 (1991); *see also* Rosenthal, *supra* note 4, at 55. In some ways, the dichotomy between consumer interests and business interests is false. In many ways, consumers are involved in business organizations. Similarly, businesses and other organizations consume many types of products and services. The terms are used here in recognition of the widely held view that consumers are thought to deserve certain protections from businesses because consumers tend to be less sophisticated or tend to have less bargaining power than the businesses with which they deal. *See, e.g.*; DOUGLAS J. WHALEY, PROBLEMS AND MATERIALS ON CONSUMER LAW XXV (1991) ("Our American sense of fair play is badly injured by the outrages practiced daily upon consumers: rapacious plundering too much for any law to ignore."); Stephen Breyer, *Analyzing Regulatory Failure: Mismatches, Less Restrictive Alternatives, and Reform*, 92 HARV. L. REV. 547, 558-59 (1979) (describing unequal bargaining power as one of the "minor justifications" for regulation).

despite attempts to obtain a correction, may find a full payment check quite useful.[125] On the other hand, business interests may use the availability of accord and satisfaction to gain the upper hand in dealing with consumers. For example, an insurance company may use the full payment check to encourage a consumer to settle a disputed claim.[126]

In summary, accord and satisfaction is traditionally viewed as beneficial because it helps resolve disputes. It is certainly true that some disputes can be more easily resolved by accord and satisfaction than by other means. It is not at all clear, however, that the availability of accord and satisfaction offers benefits that exceed the related costs.

## VI. CONCLUSION

If the rules of commercial law were being written on a clean slate, it might be better to deny enforcement of full payment checks. Accord and satisfaction is a useful shorthand for parties who understand it and use it knowingly. It is not clear, however, that this benefit outweighs the potential harm to parties who inadvertently become bound by an accord and satisfaction. In any event, accord and satisfaction is probably so firmly entrenched in American common law that it would be impossible to eradicate, and eliminating it may cause more trouble than it would prevent. This alone may well be a sufficient reason to keep the doctrine.

More empirical information would be useful in order to assess the frequency and significance of inadvertent accord and satisfaction and the relative weight of consumers' and businesses' concerns. The drafters of the new U.C.C. section 3-311 have made plausible assumptions that the inadvertent entry into an accord and satisfaction is a significant concern and that organizations have special concerns about accord and satisfaction that are not faced by individuals. Despite its critics,[127] new section 3-311 offers worthwhile improvements over the common law rules and provides ways for creditors to reduce substantially the risk of an inadvertent accord and satisfaction without placing an unfair additional burden on debtors. However, as long as full payment legends on checks are enforced, it will be difficult, if not impossible, to eliminate completely the potential trap for the unwary.

125. Rosenthal, *supra* note 4, at 56. For further detail, see *supra* note 113.

126. Rosenthal, *supra* note 4, at 55.

127. *See supra* part IV.C.1 and note 108.