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INVESTMENT SECURITIES UNDER THE UNIFORM COMMERCIAL CODE

CORNELIUS W. WICKERSHAM*

The Uniform Commercial Code is the product of years of work by the American Law Institute and the National Conference of Commissioners on Uniform State Laws and represents the greatest effort and achievement of the legal profession that perhaps has ever been undertaken and accomplished on the subjects covered.

These subjects include the great fields of the law of sales, commercial paper, bank deposits and collections, letters of credit, bulk transfers, warehouse receipts, bills of lading and other documents of title. It includes also investment securities, secured transactions, sales of accounts, contract rights and chattel paper.

The present paper will deal with Article 8 of the Code relating to investment securities. Before doing so, however, it is essential to realize that the whole of the Uniform Commercial Code is a coordinated effort to bring together the principles that are common to the whole field, and that these principles are largely based on the law merchant and further that commonly recognized business practices have had as great an influence as was first given to the common law by Lord Mansfield and perhaps even greater.

Many of the subjects dealt with have been covered in the past wholly or partly by the Uniform Acts of the Commissioners on Uniform State Laws and adopted as statute law in many states.

The Uniform Acts, however, or at least some of them, are getting old and are in each case *sui generis* and hence lack the coordination of principles which the Uniform Commercial Code now supplies.

One of the outstanding features of the Code is in the functional approach, and of course the Code itself covers much more ground than the sum total of the older Uniform Acts. Moreover, the authors have succeeded in bringing the subjects up to date so as to reflect changes in commercial law and the needs of business as it has developed in this country in the past half century.

Pennsylvania was the first state to adopt the Code. This was in 1953. Since that time and owing to experience as well as further study a number of amendments were adopted by the sponsoring organizations. In this article I shall refer to the Code, as amended, and known as the "1957 Official Text with Comments."

An extremely useful report on the Code has been made by a

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temporary commission in Connecticut. This report refers to the work as seeking uniformity among the several states by widespread adoption and adds that it achieves uniformity within the state among all branches of commercial law.

The report goes on to show the special interest to a wide variety of individuals such as consumers, depositors, manufacturers, retailers, contractors, as well as insurance companies, security dealers, investment brokers, executors and fiduciaries and to corporations issuing securities.

As to investment securities as provided in Article 8, few subjects come more frequently to the lawyers in commercial and financial centers than those which are covered by this article. For purposes of convenience and good statutory practice, it is divided into four parts. Part 1 includes the short title, definitions and general matters; Part 2 deals with matters of issue and the issuer; Part 3 has to do with the purchase of securities, and Part 4 with registration. Let us take them up in order.

PART 1. APPLICATION AND SUBJECT MATTER.

The five sections, dealing with definitions and general matters, lay the groundwork for the later provisions. The general matters cover the protection of an issuer's lien, the effect of overissues, the conflict of laws question, and negotiability. The latter is the most important, as it establishes negotiability for a great mass of securities commonly treated as negotiable in the world of commerce and finance whose status was doubtful or not recognized under existing law. This is one of the greatest achievements of the Code.

Let us review these vitally important provisions.

After giving the proper citation for Article 8, namely, "Uniform Commercial Code—Investment Securities" (Sec. 8-101),[1] the next section sets forth the definitions (102). It may be said that definitions generally are boresome things. From the point of view of the draftsman, however, they are among the most difficult of all problems. Particularly was this so in attempting to define what was meant by a "security." On the one hand there was an old conception that the word related only to obligations, such as corporate bonds, and not to shares of stock which were merely evidences of a relation between the stockholder and the issuing corporation, or of a share in the assets on liquidation, or both. In the modern world of business, stocks and bonds are both thought of by business men and traders as securities. Many people, however, did not realize the extent to which other

[1] Hereafter in this article only the last digits will be used, since all citations will relate to Article 8, unless otherwise noted.

instruments that were traded in on a market, or an exchange, were regarded by those interested as having all the qualities of securities, often including the characteristics and incidents of negotiability.

It was the intention of the sponsors that Article 8 should cover stocks, bonds and all instruments of a type commonly dealt in upon securities exchanges or markets or commonly recognized in the area in which they were dealt in as a medium for investment, within the definition of "securities."

Accordingly, a security is defined as an instrument which is issued in bearer or registered form, is of a type commonly dealt in as stated above and is either one of a class or series or by its terms is divisible into a class or series of instruments and in addition evidences a share, participation or other interest in property or in an enterprise, or is an obligation of the issuer (102).

Thus, for instance, warrants for right to subscribe to corporate shares would usually be included, and very likely such instruments as are traded in at markets in the southwest representing share interests in the retained percentage of petroleum extracted under contract with the owner of the soil. Incidentally securities dealt in on "over-the-counter" markets would generally be included.

While money is neither a security nor commercial paper, a writing which is a security is governed by this Article and not by the article on commercial paper.

Other definitions include the expression "registered form." A security is in registered form when it specifies a person entitled to the security or its rights, and when transfer may be registered on books maintained for the purpose by or for the issuer, or if the security so states.

A security is in "bearer form" when it runs to bearer according to its terms and not by reason of an endorsement.

There are also general definitions and principles of contract and interpretation in Article 1 which are applicable throughout Article 8.

By the next section the rule of the Uniform Stock Transfer Act (Sec. 15) is applied to all securities covered by Article 8 and thus the issuer's lien upon a security in favor of the issuer is made valid against a purchaser *only* if it is noted conspicuously on the security (103).

The problem of overissues of securities is then dealt with (104). Here the statute provides a new remedy for the innocent holder. The case law has been somewhat unduly influenced by statutory requirements for setting forth in corporate charters the so-called authorized capital and number of shares to be issued, and in some cases the

amount of funded debt. This, despite modern corporation laws authorizing charter amendments or additions.

Overissues. Where the issuer or his transfer agent creates an overissue some case law would result in both the old and the new certificates being good for shares in the hands of innocent purchasers. If an overissue is thereby created the issuer may be liable and subject to penalties for its action even though the result affects the value of its outstanding stock, but the better rule is that the holder of the new certificate which brings about the overissue is entitled only to reimbursement from the company and not to be recognized as a stockholder. While the section adopts this view it also provides that the company issuing the stock is bound to buy shares if it can do so on the market, and otherwise to reimburse the innocent holder at the price paid by the last purchaser for value. This appears to be an excellent solution of a difficult problem, and would overrule decisions that in the past have taken other and less compensatory measures of damages.

Now we come to one of the great advances in the law provided by the Uniform Commercial Code; in fact a rebirth of Lord Mansfield's conceptions of the law merchant and its place in the law of the land. He dealt with the common law, and we are dealing with a proposed act of the legislature. But is there any real difference to those who, as business men, are affected in their daily transactions?

Without the provisions of the Code many instruments of the kind already referred to which passed as negotiable in the minds of the business world were of doubtful negotiability as a matter of law.

Negotiability. The code now make negotiable all securities covered by Article 8 (105). The section also provides that in any action on a security unless specifically denied in the pleadings each signature on the security or in a necessary endorsement is admitted; when its effectiveness is put in issue the burden is on the party claiming under the signature to establish it, but the signature is presumed to be genuine or authorized; when signatures are admitted or established the production of the instrument entitles a holder to recover on it unless the defendant establishes a defense or a defect going to the validity of the security; and when it appears that a defense or defect exists the plaintiff has the burden of establishing that he or his predecessor is a person against whom the defense or defect is ineffective.

Besides the great advance in commercial law provided by the code in making securities regarded and dealt in as negotiable on market and exchanges, negotiable as a matter of law, the broad provisions as to actions will be of great benefit.

Conflict of Laws. The final section of Part 1 deals with the conflict of laws. The section provides that the validity of a security and the rights and duties of the issuer with respect to registration of transfer are governed by the law of the state of organization of the issuer, including the conflict of laws rules (106).

Many corporate transactions, including matters of internal activities, and the relations of the corporation with its stockholders, officers and directors, are governed by the law of the state of incorporation. The conflict of laws rules of the domiciliary state usually recognize that various acts performed in other states are governed by the laws of the states of performance, even where the effect may be felt in the home state. The rights and duties of the issuer to register a transfer are primarily governed by that law, but there may be cases where its conflicts rules would result in constitutional questions. As an illustration, if registration of a transfer was refused, suit brought in a foreign state and judgment obtained requiring the issuer to register the transfer, despite some local defect, would not the home state be compelled to recognize the judgment under the full faith and credit clause of the Constitution, assuming that the foreign court had jurisdiction?

Again the initial validity of the security may well be governed by the law of the state of incorporation, but transactions in other states, to which the issuer or its agent, or other persons concerned were parties, may affect the question, and the issuer or others might be estopped from raising technical points in justice to the parties, resulting in initial validity being affected.

This section, in the writer's opinion, may require amendment.

PART 2. ISSUE AND ISSUER

Part 2, consisting of eight sections (201 to 208), deals with the responsibilities and defenses of the issuing corporation, and matters relating thereto. The definition of a person liable on an instrument as provided in the Negotiable Instruments Law is first adapted to investment securities (201). Thus the "issuer" is to include with respect to obligations on or defenses to a security, a person including a corporation, who places or authorizes placing his name on a security evidencing a share, participation or other interest in his property or in an enterprise or to evidence his duty to perform the obligation of the security, but excepting authenticating trustees, registrars, transfer agents or the like.

The creator of fractional interests in property evidenced by securities, as well as a guarantor of security obligations (to the extent of his guaranty) may also be an "issuer" for these purposes. As to

registered securities or registration "issuer" means also a person for whom transfer books are maintained (Subsec. 3). This latter provision is for purposes of Part 4 of the article (Registration).

Responsibility. Several of the matters affecting a bona fide purchaser for value without notice are dealt with in the next section regarding the issuer's responsibility and defenses (202). Even the Bona Fide Purchaser is to be bound by the terms of the security including certain instruments, statutes, etc. incorporated by reference if they are not contrary to its terms. However, reference alone is not of itself sufficient to charge a purchaser for value with notice of a defect in validity, even if the security states that a person accepting it admits such notice.

Non-governmental securities issued with a defect going to validity are nevertheless valid in the hands of a Bona Fide Purchaser unless the defect involves a violation of constitutional provisions in which case it is valid in the hands of a subsequent purchaser for value without notice of the defect.

This rule applies to governmental issues only if there has been substantial compliance with legal requirements or the issuer has received substantial consideration and a stated purpose of the issue is one for which it has power to borrow money or issue the security.

But lack of genuineness of a security is to be a complete defense even against a Bona Fide Purchaser except in certain cases of unauthorized signatures. (See 205.) All other defenses of the issuer are ineffective against the Bona Fide Purchaser.

The well recognized right of a party to a "when, as and if" contract to cancel in case of a material change is protected by the last sub-section of 202.

It is of course common practice for bonds or debentures issued under or secured by trust instruments to refer to the trust indenture for the terms, usually lengthy and complex, governing the transaction. In the case of preferred or special stocks the corporation statutes usually require a statement of the preferences or other special features, or at least a sufficient summary to give adequate notice to the buyer.

By the provisions of 202 original purchasers in good faith are protected against a claim that substantial value was not received by the issuer in accordance with statutory requirements. But if these requirements are constitutional, then only subsequent Bona Fide Purchasers are protected. These provisions represent the better court decisions.

Throughout the section it is obvious that the principles of estoppel have had a decided influence.

Staleness. In the next section staleness is dealt with as notice of defects or defenses (203). The NIL rule requiring that a holder in due course must take before maturity is largely changed. The fact is recognized by the code that securities in default are traded in on the market in much the same way as other securities. This was particularly so during and after the railroad receiverships or "bankruptcies" that were common in the 1930's and 40's.

On the other hand the corporate issuer (or any issuer) should not be kept waiting indefinitely for determination of its liability on a defective issue.

203 provides in substance that when a security matures either for payment, redemption or exchange the purchaser is charged with notice of defects or defenses, if funds or securities were available at maturity, and he has taken the security after one year, and in any event if he has taken the security after two years. A revoked call, however, is not within the provisions of the section.

Restrictions. An important, although somewhat rare, problem is elucidated in the next section (204). This deals with restrictions on transfer imposed by the issuer. It provides that even if such restrictions are lawful they are ineffective (except against any one with actual knowledge) unless noted conspicuously on the security.

The word "conspicuously" covers some sins. Undoubtedly, if the restriction is printed in very small type or in such a way as not to be conspicuous or perhaps if it is contained in a rider on the back of the security easily to be overlooked, it will not be effective.

The problem arises in closely held corporations where the incorporators or original stockholders have agreed that they will not dispose of their shares without first offering them to the other stockholders or to the corporation or to certain designated persons.

Strictly private agreements between stockholders, however, are not covered by the code. The section applies only where the restriction is imposed by the issuer. Naturally this can be brought about by the incorporators or the stockholders, assuming its legality. Where the issuer by the restriction gives to itself or to other stockholders an option to purchase the security of a holder desiring to sell at a specified or ascertainable price before offering to third persons, the courts have generally upheld the issuer's right to do so.

But the particular restriction must be lawful, and preventive statutes, where applicable, must be observed.

Unauthorized Signatures. A distinct advance over existing law is made in the next section with respect to unauthorized signatures on the issue of securities (205). The problem arises where an employee of the issuer, transfer agent, or registrar has the duty of affix-

ing a corporate seal or adding a signature where required for the issue. Case law has tended to follow the principle of "apparent authority" and to distinguish between cases where the forger is authorized to sign and those where he signs although never having been authorized to do so. The impossible burden put on the purchaser to determine which signature the forger has been "apparently authorized" to sign and those which he has not, is removed by the code. This section provides that the unauthorized signature placed on a security before or in the course of issue, is ineffective except that it is effective in favor of a Bona Fide Purchaser if done by a person entrusted by the issuer with the signing of the security or similar securities or their immediate preparation for signing, or by an employee of the issuer or the others mentioned with responsible handling of the security.

The responsibility is therefore put on the issuer who is in a position to protect himself by careful selection and bonding of the employees or by an action against the transfer agent or registrars who can also bond their personnel.

On the other hand it is not fair to hold the issuer liable for the acts of other employees who have nothing to do with the particular activities. Thus a bank or a trust company acting in any of the capacities mentioned for the issuer is not to be responsible nor is the issuer responsible under the code if an office boy forges a signature on the security.

Completion or Alteration. A somewhat similar problem with respect to completion or alteration of an instrument is the subject of the next section (206). If the security is incomplete in any respect other than the signatures the provision is that any person may complete it by filling in the blanks as authorized; and even though the blanks are incorrectly filled in, the security as completed is to be enforcible by a Bona Fide Purchaser. Moreover, a complete security which has been improperly and even fraudulently altered is to remain enforcible according to its original terms.

Here the issuer is prevented from raising the defense of non-delivery against the Bona Fide Purchaser. Moreover, any holder may enforce an altered security according to its original terms. It should be noted that the section does not deal with signatures, but only with blanks other than those for signing. Nor does it deal with assignments. (See 308.) Overissues have already been discussed.

Issuer and Registered Owners. In the next section we have a rather important change in case law. Mere notice to the issuer is no longer to be sufficient to impose upon the issuer the duty of dealing with a pledgee instead of a registered owner. The issuer or his indenture trustee may treat the registered owner as the person exclusively

entitled to excercise the rights and powers of an owner until there is due presentment for registration of a transfer of a registered security (207). "Due presentment" is determined generally by Part 4 of the article dealing with registration. The section is permissive only and the issuer is free to require proof of ownership before paying out dividends. A subsection provides that nothing in the article affects the liability of the registered owner for calls or assessments.

Effect of Trustees' and Transfer Agents' Signatures. Since the great bulk of securities traded in on the major exchanges bear the signature of an authenticating trustee, as in the case of bonds secured by mortgage or indenture, or of registrars or transfer agents, as in the case of stock and other securities, the extent of the responsibility of the person so signing is important. It is dealt with in the last section of Part 2 (208).

By signing the security such person warrants to a Bona Fide Purchaser that the security is genuine and in proper form, that he has capacity and authority to sign, and that he has reasonable grounds to believe that it does not involve an overissue. Unless otherwise agreed he does not assume responsibility for the validity of the security in other respects.

An intended result of the section is that while authenticating trustees and registrars as well as transfer agents are to warrant the genuineness and proper form of the securities they sign, and certify to their capacity to act and that they are authorized to do so, they are not to be held responsible for validity in other respects than an overissue. Even as to that, their responsibility is discharged if they can show reasonable grounds to believe that the security does not constitute an overissue. Cases holding the transfer agents responsible to testify as to validity (aside from an overissue) are thereby rejected.

Of course issuers may still agree to indemnify the trustees and agents against specific liabilities.

PART 3. PURCHASE

The first section of Part 3 deals with the rights acquired by the purchaser and with the question of adverse claims. Upon delivery the purchaser acquires his transferor's rights except in the case of fraud or illegality or where, as a prior holder, he had notice of an adverse claim. He cannot improve his position by taking from a later Bona Fide Purchaser; but in addition to acquiring the rights of a purchaser a Bona Fide Purchaser also acquires the security free of any adverse claim.

This section is a rephrasing of various sections of the uniform NIL and the Uniform Stock Transfer Act, and extends the policy to

make it uniform for all investment securities. While the rights of a Bona Fide Purchaser are determined by Part 2 and his rights to registration by Part 4, this section is concerned principally with the matter of adverse claims. Bona Fide Purchasers are protected whether the securities were held to be negotiable or non-negotiable under prior laws and the rule so established is in line with modern business conceptions of the characteristics of these instruments. The exceptions as to persons participating in fraud or illegality are similar to the provisions of the NIL. It may be noted that an adverse claim may be either legal or equitable, and that the claimant may be the beneficial, although not the legal, owner of a security; or that the transfer may be in breach of trust or a valid restriction on transfer (301).

Bona Fide Purchaser. The next section sets forth the definition of a bona fide purchaser. The Bona Fide Purchaser is a purchaser for value in good faith and without notice of any adverse claim, who takes delivery of a bearer security or one in registered form issued or indorsed to him or in blank (302).

Here a *caveat* should be noted. The definition is given to establish the Bona Fide Purchaser's rights under 301. But certain claims may not be "adverse", for instance those of a customer against his broker. Apparently the latter may be a Bona Fide Purchaser under this section even with knowledge of his principal's claim.

Notice. Following the definition of a broker (303) the code then deals with the question of notice to the purchaser of adverse claims (304). The purchaser is charged with notice of adverse claims if the security has been indorsed "for collection" or "for surrender" or some other purpose not involving transfer; or if the security is in *bearer* form with an unambiguous statement that it is the property of a person other than the transferor. A further provision eliminates from the destructive notice of adverse claims mere notice that the security is held for a third person, or is registered in the name of a fiduciary, nor does this create a duty of inquiry into the rightfulness of the transfer. However, if the purchaser has knowledge that the transaction is for the fiduciary's individual benefit, he is charged with notice of adverse claims. A broker for the seller or buyer is included as a purchaser, but an intermediary bank is excluded. (See 4-105.)

It should be noted that the listing is not complete as to the purchaser's reasons to know of adverse claims.

Stale Notice. The effect of stale notice of adverse claims is then dealt with (305). The maturity of the principal obligation is not of itself to constitute notice of adverse claims except (1) in case of a purchase after one year from date of maturity for purposes of re-

demption or exchange, or (2) after six months from a date set for payment of money against presentation or surrender if funds are then available for payment. The result is that under certain circumstances there may now be a bona fide purchaser of a matured instrument in states where the code is enacted into law. The words "principal obligation" should be noted, as the section does not apply to unpaid or overdue coupons attached to a bond.

Warranties. Provisions of the NIL and the Uniform Stock Transfer Act are here rephrased and extended to the issuer in appropriate situations (306).

Presentment of a security for registration, payment or exchange is to involve a warranty that the person presenting it is entitled thereto. But a Bona Fide Purchaser, receiving a new, reissued or reregistered security on registration is to warrant only that he has no knowledge of an unauthorized signature in a necessary indorsement.

The warranties involved in transfers to Bona Fide Purchasers and those to intermediaries, pledgees and brokers are individually spelled out. Limitations are due to basic changes made by the code, especially those protecting the Bona Fide Purchaser.

Indorsements. Indorsements are the subject of the next six sections (307 to 312). Where a registered security is delivered to a purchaser without a necessary indorsement he becomes a Bona Fide Purchaser only when the indorsement is supplied, except as against the transferor upon delivery, and he has a right to specific enforcement to have any necessary indorsement supplied (307).

This alters the rule of the Uniform Stock Transfer Act, since as between the parties the transfer would be complete under the Code when the security is delivered.

Section 308 deals at length with the making of indorsements, the subject of special indorsements and allied points. The provisions of the Uniform Acts are rephrased and expanded. The liability of the indorser for the obligations of the issuer are thereby destroyed, since in view of indorsement practices an indorser cannot fairly be held to warrant as to the issuer's actions. The section must be consulted when passing on the matters dealt with therein.

Section 309 is a rephrasing of Sections 1 and 10 of the Uniform Stock Transfer Act as to the effect of indorsements of securities without delivery. Indorsement of a security is not to constitute a transfer until delivery. If the indorsement is on a separate document there will be no transfer until delivery of both document and security, according to the Code.

While indorsement of a security in bearer form may give notice

of adverse claims (304), it is not otherwise to affect any right of registration possessed by the holder (310).

With respect to unauthorized indorsements, the NIL is modified by the Code (311). Unless the owner ratifies, or is estopped, he may assert the ineffectiveness of the indorsement against the issuer, or a purchaser except a Bona Fide Purchaser who in good faith has received a new security, or a reissue or reregistration. Thus the Bona Fide Purchaser would be protected even if the new instrument is still in his hands, and court decisions to the contrary are rejected.[2]

Moreover, the issuer is to be liable if he registers a transfer upon the unauthorized indorsement.

This new rule is based on modern practices, particularly in view of the fact that most security purchases are made today through brokers, and it is unfair to charge the purchaser with notice or reliance on a fake indorsement on the old security.

In order to expedite the transactions in securities, and avoid needless waste of time, the final section on indorsements specifically lays down the exact warranties of (1) the guarantor of the indorser's *signature* only, and (2) a guarantor of the indorsement itself. In the former, the warranty includes *only* that the signature was genuine, the signer was an appropriate person to indorse (see 308), and had legal capacity to sign.

But the guarantor of the indorsement itself warrants more, for in addition to the warranties just mentioned, he warrants the rightfulness of the transfer in all respects, according to the Code (312).

The issuer, however, is not to be allowed to require a guarantee of *indorsement* as a condition to registration.

There is nothing in the existing Uniform Acts on these points.

Delivery. The next six sections of the Article deal with matters relating to delivery. Here again we have the impact of modern financial practices and understanding. The earlier Uniform Acts contemplated only transfer of possession as delivery. As, however, the bulk of securities trading is done through brokers and on established exchanges, the new Code provisions provide for completion of delivery while the security is still in the broker's hands if it is indorsed to or in the name of the purchaser, or if confirmed by the broker and book entry or other identification made. But there must be identification of the specific security since the rule is to be different if the security is part of a fungible bulk held for customers, and despite the customer's acquisition of a proportionate interest in the bulk (313).

[2] Cf. Weniger v. Success Mining Co., 227 Fed. 548 (8th Cir. 1915).

The section is a general modification of the prior rules as to delivery and applies in cases where brokers are involved.[3]

Duty to Deliver. In the next section we again find a new statute with no prior uniform statutory provision. Here the emphasis is put on transactions on organized exchanges or through brokers or dealers as these account for the great bulk of sales of securities (314). Subsection 1 provides in substance that when the seller puts the security in the possession of his broker and the broker places it or a like security in the possession of the buying broker or by effecting clearance according to the rules of the exchange the duty to deliver is completed where the sale is made, unless otherwise agreed. By Subsection 2 governing transactions not covered by Subsection 1 the transferor must place the security in form to be negotiated by the purchaser in his possession, unless otherwise agreed or provided. Thus physical delivery is required if transactions are not consummated on an exchange or through brokers unless the parties have otherwise provided. Provision is made in both sections for designees and for special acknowledgments.

Wrongful Transfer. In the case of wrongful transfer the injured seller is to have an action to reclaim possession or have damages against anyone except a Bona Fide Purchaser, and even against the Bona Fide Purchaser if the wrong is based on an unauthorized indorsement and if its ineffectiveness can be asserted under 311. Equitable remedies are provided (315).

This is a rephrasing of Section 7 of the Uniform Stock Transfer Act with the addition of the rule governing forgeries or unauthorized indorsements.

The next section, which again has no predecessor in the uniform statutes, requires the transferor to supply the purchaser on demand with proof of authority for the transfer or other requisite for registration unless otherwise agreed. However, if the transfer is not for value he need not do so unless necessary expenses are furnished. Failure to comply in a reasonable time carries a right to rescind (316).

Sections 13 and 14 of the Uniform Stock Transfer Act are rephrased in 317 relating to the attachment or levy upon a security which must be reached to constitute a proper levy. There is no change in the substantive effect of the Stock Transfer Act. The liability for conversion of agents or bailees who have in good faith received securities and sold, pledged or delivered them according to the principal's instructions is denied in 318. Hence if a broker acts

[3] To some extent the decision in Isham v. Post, 141 N.Y. 100, 35 N.E. 1084 (1894), is rejected.

in good faith he is not liable for conversion even though the principal had no right to dispose of the securities.

The final section of Part 3 completely rephrases the Uniform Sales Act section relating to the statute of frauds. Here the new code adds requirements for minimum specifications of quantity and price consistent with business practice in the field (319). To be enforceable a contract for sale of securities is to require (a) a writing signed by the party to be charged or his agent or broker sufficient to show the sale of a stated quantity of described securities at a defined or stated price; or (b) delivery accepted or payment made, to the extent of the delivery or payment; or (c) written confirmation received by the adverse party and his failure to object within 10 days; or (d) his formal admission.

Apparently this provision would be satisfied by the usual jargon of brokers, often unintelligible to the customer, but fully understood by the brokers for both parties. This is its justification, and the other provisions are reasonable enough.

PART 4. REGISTRATION

Part 4 deals with the problems of registration. There are six sections, four of which have no predecessors in the Uniform Acts. These sections are based partly on case law and partly on recognized business practices. The duties of an issuer to register transfers are first dealt with (401) and case law is greatly modified in view of the policy to speed up the registration process by narrowing the field in which the issuer, endeavoring to avoid liability for adverse claims, has imposed rigorous requirements of proof against any possible claim of improper action.

The Code therefore requires the issuer to register a transfer upon presentation if (a) the security is properly endorsed, (b) reasonable assurance is given that the indorsements are genuine and effective, (c) the issuer is not under duty to inquire into adverse claims (see 403), (d) applicable tax laws have been complied with, and (e) the transfer is in fact rightful *or* is to a bona fide purchaser. Where the issuer has a duty to register, he is liable for loss resulting from failure or refusal to register or for unreasonable delay in registration.

If in fact the transfer is wrongful the issuer need not register, despite presentation of the security and compliance with the requirements. But this exception is not to apply in the case of a bona fide purchaser.

Whether the Code when adopted will be successful in reducing the requirements of cautious issuers and their agents remains to be seen. The writer has some doubt as to their satisfaction even with a

printed sign produced by the presenter reading "I am a Bona Fide Purchaser."

The section must be read in the light of the next two sections which deal with a number of details that illustrate 401. Thus, on the question of reasonable assurance that the indorsements are genuine and effective, it is provided that the issuer may require in all cases a guaranty of signature of the person indorsing (402). Where indorsement is by agent, the issuer may require assurance of his authority, and where it is by a fiduciary a certificate of appointment or incumbency dated within 60 days. If there is more than one fiduciary, he may require reasonable assurance that all who are required to sign have done so and in other cases appropriate assurance. Subordinate details of these provisions are set forth, and it is provided further that if the issuer has notice that the transfer may be wrongful, further reasonable assurance may be required. However, the issuer is put on notice of all matters affecting the transfer that may then be disclosed.

Thus it is the intention of the Code that the issuer need no longer demand full and convincing evidence that the transfer is proper in all its aspects, thereby delaying registration as frequently happens under existing laws. *Sed quaere.* His right to demand copies of controlling instruments is to be recognized under the Code only when on notice that the transfer may be wrongful and at the risk of being put on notice of all matters contained in the papers. This is designed to implement the policy referred to above to discourage issuers from requiring excessive documentation.

Supplementing the main purpose of the preceding expressions of policy, the issuer's liability to register securities on presentation for that purpose is strictly restricted by the next two sections. The limits of his duty of inquiry are hopefully set forth in detail, the scope of exoneration under previous statutes is enlarged, and the duty of inquiry is limited to specifically defined events (403). The provisions are lengthy and need not be described in detail here.

It may be noted that the customary "stop transfer" notice from the owner of a lost or stolen security, or one designed to prevent improper action, will impose on the issuer the duty of inquiry into adverse claims under this section. Where the security is properly indorsed and there is no remaining duty to inquire into adverse claims, the issuer is not to be liable to the owner or other person suffering as a result of registration of the transfer, except as otherwise provided in tax laws relating to the collection of taxes (404). If, however, he has registered a transfer to a person not entitled to it, the issuer must deliver on demand a like security to the true owner unless registration

was pursuant to the section, or the owner is precluded from asserting a claim for a lost security under 405, or the delivery would result in an overissue. In the latter case, the issuer's liability is to be governed by Section 8-104.

Thus the registered owner's rights under the cases to elect between an action to compel issue of a new security and an action for damages would not be available. He must take a new security except in the case of an overissue, there being no similar security reasonably available for purchase.

Lost Securities. (405) If the owner fails to notify the issuer within a reasonable time after he himself has notice that his security has been lost, destroyed or stolen, and the issuer registers a transfer without notice, there is to be no claim against the issuer under 404 or any right to a new security under this section. However, he is required by the section to issue a new security upon the owner's request before notice of acquisition by a bona fide purchaser, and upon receiving an indemnity bond, and satisfaction of the issuer's other reasonable requirements; and if a new security is issued and a bona fide purchaser of the original security then presents it for registration of transfer the issuer must register unless the result is an overissue. (See Section 8-104.) The issuer may then recover the new security from the person to whom it was issued or any person taking under him except a bona fide purchaser (405).

Section 17 of the Uniform Stock Transfer Act is the parent of this section, but under the new act the issuer must issue a new security without a court order where the provisions of the Code apply. The well-established practice of corporations voluntarily issuing new securities to replace those lost, destroyed or stolen (usually upon being furnished with an indemnity bond, satisfactory affidavits, etc.) now becomes a matter of law, and moreover existing case law is changed by the Code, since the original security may still become effective after the issue of a replacement under the circumstances here dealt with.

Apparently under 405 if both the original and the new security are held by bona fide purchasers *both* must be given recognition if no overissue is involved or an adequate security readily purchasable. It is assumed that in this case the holder of the original security would have only an action for damages.

Duties of Trustees and Agents. The final section of Article 8 provides in substance that authenticating trustees, transfer agents, registrars, and other agents for an issuer in the registration of transfers, or in the issue of new securities or cancellation of surrendered securities, all have a duty of good faith and due diligence to the issuer in performing their functions, and the same obligation to the

holder of securities, and with the same rights and privileges as the issuer in regard to those functions (406). Notice to such persons is to be notice to the issuer with respect to the agent's functions.

The result of the section is that these persons are to be liable both to the issuer and the owner for wrongful refusal to register and for wrongful registration within the scope of their functions if the issuer would itself be liable. The Code is a reversal of case law to the extent of those cases which have denied liability for mere refusal to register.[4] Should the trustee or agent require more documents than may properly be required by the issuer, the agent would incur liability as for a wrongful refusal of registration.

In conclusion, the adoption by any state legislature of the new Uniform Commercial Code and particularly Article 8 dealing with investment securities would bring to the financial world great relief from the fears engendered in the past of liability for common acts of general custom in that sphere. Under modern conditions and in view of the immense growth of security transactions in both number and amount existing law imposes unnecessary restrictions and risks on those who deal in good faith with the daily multitude of transactions in the investment field.

There is no doubt that the proposed legislation, if adopted, will be of great benefit to large numbers of persons in their daily occupations and will eliminate unfair risks of liability at little or no expense of existing legal or equitable rights.

The adoption of the Code by the legislature means, therefore, a forward step much needed for the acceleration of financial business, the elimination of outmoded risks, and the recognition of practices well understood and constantly employed in daily transactions of great magnitude.

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[4] Cf. Hulse v. Consolidated Quicksilver Mining Corp., 65 Idaho 768, 154 P.2d 149 (1944).