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Article 3: Commercial Paper

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ARTICLE 3: COMMERCIAL PAPER

SECTION 3-112. Terms and Omissions Not Affecting Negotiability

SMITH v. LENCHNER
205 A.2d 626 (Pa. Super. 1964)
Annotated under Section 3-113, infra.

SECTION 3-113. Seal

SMITH v. LENCHNER
205 A.2d 626 (Pa. Super. 1964)

Lenchner, the maker of a demand note that authorized confession of judgment at any term of court, petitioned the court to open a judgment entered by confession on the note. The note was under seal. Lenchner contended that the note was given under duress of a threat made by the plaintiff to disrupt a business negotiation, and secondly, that no consideration was received for it. Lenchner relied on Section 3-113 in contending that want of consideration was a good defense despite the fact that the note was under seal. The lower court ordered the judgment to be opened.

On appeal, the order opening judgment was reversed. The court found that there was no merit to Lenchner's contention that he was under duress when he executed and delivered the note because there was no threat of bodily harm or of civil or criminal prosecution.

Section 3-113 provides that "an instrument otherwise negotiable is within this Article even though it is under seal." The court noted that even if this section permitted the defense of want of consideration where the note was under seal, it was first necessary for Lenchner to establish that the note was "otherwise negotiable." This he could not do since, under Pennsylvania case law, a note authorizing confession of judgment *at any time* is non-negotiable. Section 3-112(1)(d) states only that a note's negotiability is not affected by "a term authorizing a confession of judgment on the instrument *if it is not paid when due.*" [Emphasis supplied.] The note being non-negotiable, the seal imported consideration.

COMMENT

The court relied on prior Pennsylvania case law to reach its decision that the note was non-negotiable. The same result could have been reached under the Code. Section 3-104(1)(b) provides that for an instrument to be negotiable, it must contain an unconditional promise or order to pay a sum certain in money but "no other promise, order, obligation or power given by the maker or drawer except as authorized by this Article." A warrant of attorney to confess judgment on a note is an "other . . . power." While Section 3-112(1)(d) provides that a power to confess judgment *on default* will not affect negotiability, neither that section nor any other authorizes the inclusion of a power to confess judgment *regardless of default* at any term of court. Therefore, the promissory note contained an unauthorized power and was non-negotiable. Accord, *Fidelity Trust Co. v. Gardiner*, 191 Pa. Super 17, 155 A.2d 405 (1959).

Both *Thomasik v. Thomasik*, 413 Pa. 559, 198 A.2d 511 (1964), and the present case have avoided the question whether want of consideration is available as a personal defense when the note is under seal. Under Pennsylvania case law prior to the adoption of the Code, *want* of consideration was held to be no defense to a note under seal but *failure* of consideration was considered a good defense. The reason for the distinction was this. When no consideration was given in the first instance, the parties were said to be relying on the seal to import consideration. But when consideration was in fact given in the first instance, the parties were said not to be relying on the seal. Not relying on the seal, the parties were allowed to plead failure of consideration as a personal defense.

H.S.

SECTION 3-302. Holder in Due Course

DLUGE v. ROBINSON
204 Pa. Super. 404, 204 A.2d 279 (1964)
Annotated under Section 3-804, infra.

CITIZENS BANK v. NATIONAL BANK OF COMMERCE
334 F.2d 257 (10th Cir. 1964)
Annotated under Section 4-209, infra.

SECTION 3-303. Taking for Value

CITIZENS BANK v. NATIONAL BANK OF COMMERCE
334 F.2d 257 (10th Cir. 1964)
Annotated under Section 4-209, infra.

SECTION 3-305. Rights of a Holder in Due Course

BURCHETT v. ALLIED CONCORD FIN. CORP.
396 P.2d 186 (N.M. 1964)

Kelly, as representative of an aluminum siding firm, called on the plaintiffs, the Burchetts and the Beevers, in their respective homes, offering to install aluminum siding for a certain price. The houses were to be used as "show houses" and both families were to receive a $100 credit on each aluminum siding contract sold in the area, which would be applied to their contract debt. Kelly gave them a printed contract form to read. Then he handed them another form which they each signed without reading. What the plaintiffs really signed were promissory notes, mortgages on their property, and contracts with no mention of credits for advertising or sales. The notes and mortgages were assigned to the defendant. The siding was installed and the plaintiffs were informed by the defendant that they were delinquent in their first payment. The plaintiffs then brought the present suit to have the notes and mortgages cancelled and declared void, contending that they were fraudulently procured and that a defense of fraud was available against the defendant under Section 3-305(2)(c). That section provides:

> A holder in due course . . . takes free from all defenses of any party to the instrument with whom the holder has not dealt except such

misrepresentation as has induced the party to sign the instrument with neither knowledge nor reasonable opportunity to obtain knowledge of its character or essential terms. . . .

The lower court held for the plaintiffs. On appeal, reversed and remanded with directions to dismiss the complaints. The defendant was a holder in due course, and the weight of the evidence did not sustain the plaintiffs' defense of fraud under the test of Section 3-305(2)(c). The plaintiffs were of sufficient intelligence, able to read and understand what they were signing, and there was no reason why they should have relied on Kelly or had confidence in him. Though victimized, the plaintiffs failed to exercise ordinary care for their own protection.

H.S.

SECTION 3-501. When Presentment, Notice of Dishonor, and Protest Necessary or Permissible

DLUGE v. ROBINSON
204 Pa. Super. 404, 204 A.2d 279 (1964)
Annotated under Section 3-804, infra.

SECTION 3-502. Unexcused Delay; Discharge

DLUGE v. ROBINSON
204 Pa. Super. 404, 204 A.2d 279 (1964)
Annotated under Section 3-804, infra.

SECTION 3-503. Time of Presentment

DLUGE v. ROBINSON
204 Pa. Super. 404, 204 A.2d 279 (1964)
Annotated under Section 3-804, infra.

SECTION 3-504. How Presentment Made

DLUGE v. ROBINSON
204 Pa. Super. 404, 204 A.2d 279 (1964)
Annotated under Section 3-804, infra.

SECTION 3-802. Effect of Instrument on Obligation for Which It Is Given

MALPHRUS v. HOME SAV. BANK
254 N.Y.S.2d 980 (Albany County Ct. 1965)
Annotated under Section 4-403, infra.

SECTION 3-804. Lost, Destroyed or Stolen Instruments

DLUGE v. ROBINSON
204 Pa. Super. 404, 204 A.2d 279 (1964)

Wapner drew two checks payable to the defendant Robinson who indorsed and delivered them to the plaintiff Dluge. Dluge presented them

to the drawee-bank where they were dishonored for insufficient funds. The checks were returned to Dluge who in turn handed them over to the indorser Robinson. Subsequent to bringing this suit against Robinson, Dluge died, and his executors were substituted as plaintiffs. At trial they contended that Dluge demanded payment when he turned the checks over to Robinson, and that Dluge was either a holder of the checks or an owner of lost checks who could maintain the action under Section 3-804. Robinson denied that there was any demand for payment and testified that he himself had returned the checks to Wapner, the drawer. Wapner's testimony that he paid Dluge the amount of the checks and then tore them up was stricken from the record because Wapner was found to be an incompetent witness under the Dead Man's Act. The lower court gave judgment to the plaintiff. On appeal, the superior court reversed and gave judgment n.o.v. to the defendant.

The superior court reasoned that even if the plaintiffs were considered holders in due course, they would have to prove that the checks were presented by Dluge to Robinson within a reasonable time and that for uncertified checks a reasonable time was presumed to be within seven days after indorsement. Sections 3-501(1)(b); 3-503(1)(e); 3-503(2)(b). "Presentment," it went on to quote Section 3-504(1), "is a demand for acceptance or payment . . . by or on behalf of a holder." Since there was no evidence to show that Dluge made a demand for payment within seven days or any reasonable time after indorsement, the plaintiffs could not recover even if they were holders in due course.

They were not, however, holders in due course. Since Dluge had given up the checks to the defendant Robinson, he was not in possession of them and could not be a "holder" under Section 1-201(20). Not being a holder, Dluge could not be a holder in due course under Section 3-302(1).

As to the plaintiffs' alternative argument that they could maintain the action under Section 3-804, the court said that they must prove (1) that Dluge owned the checks and (2) that the checks were destroyed, stolen or otherwise lost. However, the plaintiffs could prove neither element. The surrender of the checks without demand for payment told against Dluge's ownership, and Wapner's evidence being stricken, there was no evidence of destruction, loss or theft.

The court concluded by saying that the plaintiffs were free to sue on the underlying obligations of the checks.

COMMENT

Part of the court's reasoning is based on an erroneous reading of certain sections dealing with presentment, notice of dishonor and protest. The court is confused as to the meaning of these terms. It suggested that presentment was to be made to the indorser and cited Section 3-504(1) as proof that such could be done. However, in quoting Section 9-504(1) it left out several pertinent words. "Presentment is a demand for acceptance or payment *made upon the maker, accepter, drawee or other payor* by or on behalf of the holder." There is no mention of indorser here. A demand for payment upon an indorser is not presentment; it is simply a demand for payment.

For an indorser to be liable on a check, presentment must first be made on the drawee bank within a reasonable time. Then, if the bank refuses to pay, notice of dishonor must be given to the indorser before midnight of the third business day after the indorsee receives notice of dishonor from the drawee bank, under Section 3-508. As the court correctly noted, in the case of uncertified checks drawn and payable in the United States there is a presumption that, if presentment or the initiation of bank collection is made within seven days after indorsement, it is made within a reasonable time. In the present case there is no evidence that timely presentment was not made on the drawee bank. What the plaintiffs failed to prove was that timely notice of dishonor was given to the indorsee, or that tardy notice was excusable. Thus, under Section 3-502(1)(a), the indorser Robinson was discharged. However, as the court goes on to point out, even if timely notice of dishonor were given, the plaintiffs could not prevail since they were neither holders nor owners of lost, destroyed or stolen checks.

H.S.

ARTICLE 4: BANK DEPOSITS AND COLLECTIONS

SECTION 4-104. Definitions and Index of Definitions

MALPHRUS v. HOME SAV. BANK

254 N.Y.S.2d 980 (Albany County Ct. 1965)

Annotated under Section 4-403, infra.

SECTION 4-109. Process of Posting

GIBBS v. GERBERICH

1 Ohio App. 2d 93, 203 N.E.2d 851 (1964)

Annotated under Section 4-303, infra.

SECTION 4-208. Security Interest of Collecting Bank in Items, Accompanying Documents and Proceeds

CITIZENS BANK v. NATIONAL BANK OF COMMERCE

334 F.2d 257 (10th Cir. 1964)

Annotated under Section 4-209, infra.

SECTION 4-209. When Bank Gives Value for Purposes of Holder in Due Course

CITIZENS BANK v. NATIONAL BANK OF COMMERCE

334 F.2d 257 (10th Cir. 1964)

The plaintiff, an Arkansas bank, held a past due note executed by one of its customers. The customer attempted to satisfy the note with a large check payable to him, drawn on an Oklahoma bank. Before cashing the check and discharging the note the plaintiff bank telephoned the Oklahoma bank and asked one of its officers whether the drawer of the check had sufficient funds