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## UNIFORM COMMERCIAL CODE: AN INTRODUCTION 23 (Minnesota)

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ARTICLE III  
(Commercial Paper)

Professor Roy L. Steinheimer

I. Scope of Article 3 (Commercial Paper).

- A. Limited to drafts, checks, certificates of deposit and notes.  
(§§3-103 and 3-104)
- B. Investment securities (stocks and bonds) are covered by  
Article 8. (§3-103)
- C. Documents of title are covered by Article 7. (§3-103)

II. Formal Requisites of Commercial Paper.

A. Unconditional order or promise.

- 1. Order or promise is not rendered conditional because the instrument:
  - a. States that the obligation shall mature in accordance with or "as per" an underlying transaction giving rise to the instrument; [§3-104(1)(b)]
  - b. States that the instrument arose out of a separate agreement; [§3-105(1)(c)]
  - c. States that it is drawn under a letter of credit; [§3-105(1)(d)]
  - d. States that it is secured by a security agreement; [§3-105(1)(e)]
  - e. States that payment is limited to a particular fund or source where the instrument is issued by a governmental agency; [§3-105(1)(g)]
  - f. States that payment is limited to the entire assets of a partnership, unincorporated association, trust or estate. [§3-105(1)(h)]

2. Order or promise is conditional if the instrument states that it is subject to any other agreement. [§3-105(2)(a)]
- B. Sum certain. The sum is certain even though it is to be paid with a stated discount or addition if paid before or after maturity. [§3-106(c)]
- C. Definite time. An instrument is payable at a definite time if it is payable:
  1. At a definite time subject to any acceleration; [§3-109(c)]; see also, §1-208 on options to accelerate at will).
  2. At a definite time subject to extension at the option of the holder. [§3-109(d)]
- D. Payable to order. An instrument is payable to order when it is payable to the order or assigns of any person or when it is conspicuously designated on its face as "exchange." (§3-110)
- E. Negotiability of an instrument is not affected by:
  1. A promise or power to maintain or protect collateral or to give additional collateral; [§3-112(c)]
  2. A term in a draft that the payee by endorsing or cashing it acknowledges full satisfaction of an obligation of the drawer. [§3-112(f)]

### III. Negotiation and Transfer.

- A. Words of assignment, condition, waiver, guaranty, limitation or disclaimer of liability and the like accompanying an endorsement do not affect its character as an endorsement. [§3-202(4)]
- B. Restrictive endorsements.
  1. An endorsement is restrictive if it:
    - a. Is conditional; [§3-205(a)]

- b. Purports to prohibit further transfer of the instrument; [§3-205(b)]
  - c. Includes the words "for collection", "for deposit", "pay any bank" or the like; [§3-205(c)]
  - d. Otherwise states that it is for the use of the endorser or of another person. [§3-205(d)]
2. Effect of restrictive endorsement.
- a. Restrictive endorsement does not prevent further transfer or negotiation of the instrument. [§3-206(1)]
  - b. A holder for value of an instrument which is restrictively endorsed may also achieve status as a holder in due course. [§3-206(3) and (4)]
  - c. Normally only the first taker under a restrictive endorsement is obligated to pay or apply any value given consistently with the terms of the endorsement. [§3-206(3) and (4)]

#### IV. Holders in Due Course.

- A. Payee may be a holder in due course. [§3-302(2)]
- B. Requisites of a holder in due course.
  - 1. Must take the instrument for value. [§§3-302(1)(a) and 3-303]
  - 2. Must take the instrument in good faith. [§§3-302(1)(b) and 1-201(19)]
  - 3. Must take the instrument without notice that it is overdue or has been dishonored. [§3-302(1)(c)] He has notice that an instrument is overdue if he has reason to know:
    - a. That acceleration of the instrument has been made; [§3-304(3)(b)]

b. That he is taking a demand instrument more than a reasonable length of time after its issue which in the case of a check is presumed to be thirty days. [§3-304(3)(c)]

4. Must take the instrument without notice of any defense against or claim to it on the part of any person. [§3-302(c)] He has such notice if:

a. The instrument is so incomplete, bears such visible evidence of forgery or alteration or is otherwise so irregular as to call into question its validity, terms or ownership; [§3-304(1)(a)]

b. He knows that the obligation of any party is voidable or that all parties have been discharged; [§3-304(1)(b)]

c. He knows that a fiduciary has used the instrument in breach of his duty. [§3-304(2)]

C. Rights of a holder in due course.

1. Takes free of all claims to the instrument on the part of any person. [§3-305(1)]

2. Takes free of the following defenses:

a. Failure or lack of consideration. [§3-305(2)]

b. Fraud in inducement. [§3-305(2)]

c. Non-delivery of the instrument. [§3-305(2)]

d. Conditional delivery or delivery for a special purpose. [§3-305(2)]

e. Incomplete instrument which is completed without authority may be enforced as completed. [§3-407(3)]

3. Takes subject to the following defenses:

- a. Fraud in execution, [§3-305(2)(c)]
- b. Infancy, to the extent that it is a defense to a simple contract. [§3-305(2)(a)]
- c. Incapacity, duress or illegality which renders the obligation of the party a nullity. [§3-305(2)(b)]
- d. Discharge in insolvency proceedings. [§3-305(2)(d)]
- e. Any discharge of which he has notice when he takes notice when he takes the instrument. [§3-305(2)(e)]
- f. Forged signatures. [§3-404; see also §3-406]
- g. Material alteration. If the alteration is both fraudulent and material, may enforce the instrument only according to its original tenor. (§3-407)

#### V. Liability of Parties.

##### A. Effectiveness of signatures.

1. Imperfect signature by authorized agent. An authorized agent who signs his own name to an instrument is liable to:
  - a. A remote holder unless he discloses his principal and indicates his representative capacity; (§2-403)
  - b. The payee unless he either discloses his principal or his representative capacity. (§2-403)
2. Signature in name of imposter is effective regardless of who puts the signature on the instrument.
3. Signature in name of fictitious payee is effective regardless of who puts the signature on the instrument if:

- a. The person signing as or for the maker or drawer intends the payee to have no interest in the instrument, or (§3-405)
- b. An agent of the maker or drawer has supplied him with the name of the payee intending the payee to have no interest in the instrument. (§3-405)

B. Makers of promissory notes payable at a bank.

1. Presentment and notice of dishonor are pre-requisites to the liability of the maker [§3-501(1)(c) and (2)(b)]
2. Failure to present and give notice discharges the maker only if such failure deprived the maker of funds maintained at the bank for payment of the note because of intervening insolvency of the bank. [§3-502(1)(b)]

C. Acceptance of drafts and certification of checks.

1. Acceptance or certification must be written on the instrument. [§3-410(1)]
2. Acceptor of a draft payable at a bank.
  - a. Presentment and notice of dishonor are pre-requisites to the liability of the acceptor. [§3-501(1)(c) and (2)(b)]
  - b. Failure to present and give notice discharges the acceptor only if such failure deprived the maker of funds maintained at the bank for payment of the draft because of intervening insolvency of the bank. [§3-502(1)(b)]

D. Drawers and endorsers of drafts and checks.

1. Presentment is necessary.
  - a. On the maturity date as to time drafts; [§3-501(1)(b) and (c) and 3-503(1)(c)]



b. Within a reasonable time after the drawer or endorser becomes liable on the instrument as to demand drafts and checks. [§3-503(1)(e)]

(1) As to drawers of uncertified checks, 30 days after issue is presumed to be reasonable. [§3-503(2)]

(2) As to endorsers of uncertified checks, 7 days after endorsement is presumed to be reasonable. [§3-503(2)]

2. Notice of dishonor is necessary. [§3-501(2)]

a. Notice of dishonor must be given by a bank before its midnight deadline. [§3-508(2)]

b. Notice of dishonor must be given by any other person before midnight of the third business day after dishonor or receipt of notice of dishonor. [§3-508(2)]

3. Failure to make presentment or give notice of dishonor:

a. Discharges the drawer only if the drawee became insolvent during the period of delay in presentment or notice. [§3-502(1)(b)]

b. Discharges the endorser in any case. [§3-502(1)(a)]

E. Accommodation parties.

1. Holder for value who takes the instrument before it is due takes free of the accommodation party's defense of no consideration. [§3-415(2)]

2. Holder in due course who:

a. Takes with knowledge of the accommodation is subject to suretyship defenses. [§3-415(4)]

F. Guarantors.

1. Presentment and notice of dishonor are not necessary to hold endorsers who use words of guaranty. [§3-416(4)]
2. Words of guaranty added to the signature of makers or acceptors does not change their contract. The words simply create a presumption that there is accommodation involved when there are several makers or acceptors. [§3-416(4)]

G. Liability of warrantors.

1. Presentment warranties.

- a. Presenter warrants that he has no knowledge that the signature of the drawer is forged. [§3-417(1)(b)]
- b. Presenter warrants that he has good title to the instrument. [§3-417(1)(a)]
- c. Presenter warrants that the instrument has not been materially altered. [§3-417(1)(c)]

2. Transfer warranties.

- a. Warranty of title. [§3-417(2)(a)]
- b. Warranty against forged signatures. [§3-417(2)(b)]
- c. Warranty against material alteration. [§3-417(2)(c)]
- d. Warranty against defenses. [§3-417(2)(d)]
- e. Warranty against knowledge of insolvency proceedings. [§3-417(2)(e)]

VI. Discharge.

- A. Only parties to the instrument are discharged. No discharge of the instrument. (§3-601)

B. Methods of discharge of parties.

1. By payment. (§3-603)

2. By tender of payment. (§3-604)

3. By cancellation. [§3-605(1)(a)]

4. By renunciation. [§3-605(1)(b)]

5. By impairment of recourse or collateral. [§3-606(1)]

C. Discharge of an obligation on the instrument also discharges the underlying debt. [§3-802(1)(b)]