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## INTERPRETATION, CONSTRUCTION, AND REVISION OF THE COMMERCIAL CODE: THE PRESUMPTION OF HOLDING IN DUE COURSE

FREDERICK K. BEUTEL\*

It is usually assumed that the codification of the law or of a particular statute goes through four stages. These are drafting, enactment, interpretation, and revision.

Due to a number of unusual circumstances, the history of the Uniform Commercial Code has not clearly followed these steps. So as a preliminary matter it might be beneficial briefly to review it.

### I. BRIEF HISTORY OF THE DRAFTING AND ADOPTION OF THE COMMERCIAL CODE

In the beginning the Code was attempted as a revision and single codification of a number of already existing and very successful uniform statutes together with a large number of other legislative acts more or less uniformly adopted in most of the states.<sup>1</sup> After considerable discussion over a period of about ten years,<sup>2</sup> the sponsoring organizations, the Commissioners on

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\*Professor of Law, University of Illinois.

1. For a list of the seven uniform acts repealed by the Uniform Commercial Code [hereinafter cited and referred to as U.C.C.] see U.C.C. § 10-102. They are: Uniform Negotiable Instruments Act, Uniform Warehouse Receipts Act, Uniform Sales Act, Uniform Bills of Lading Act, Uniform Stock Transfer Act, Uniform Conditional Sales Act, and Uniform Trust Receipts Act [hereinafter cited and referred to as N.I.L., W.R.A., S.A., B.L.A., S.T.A., C.S.A., and T.R.A., respectively.] It also lists acts on seven other subjects which should be repealed. The exact wording of this section must, of course, vary in each of the jurisdictions adopting the U.C.C., depending upon the state of the commercial statutes in each state.

2. As far back as 1932 the writer recommended complete codification of the uniform commercial laws. Beutel, *The Negotiable Instruments Act Should Not Be Amended*, 80 U. PA. L. REV. 368, 385 (1932). See also BRANNAN, *NEGOTIABLE INSTRUMENTS LAW* 1124 (5th ed. Beutel 1932); Beutel, *The Proposed Uniform Bank Collections Act and Possibility of Recodification of the Law on Negotiable Instruments*, 9 TUL. L. REV. 378 (1935).

Uniform Laws and the American Law Institute, got down to the serious problems of drafting the Code in 1945.<sup>3</sup> The procedure for drafting was that used by the American Law Institute for creating the Restatements of the Law and by the Commission on Uniform Laws for drafting the other Uniform Laws. The details of this process have been ably set out elsewhere and need not be repeated here.

It is sufficient to say that the Institute and the Commission published the usual preliminary drafts and invited criticism, which was voluminous and not always appreciated or followed by the draftsmen. In fact, some of the exchanges on the merits at times became bitter.<sup>4</sup> However, the Code continued on its way, was offered in final draft in 1952<sup>5</sup> and adopted in Pennsylvania the next year.<sup>6</sup> It was also introduced into the legislatures of a number of states including New York.<sup>7</sup> Here one of the most significant parts of the development of the Code occurred.

The Code in its entirety was referred by the Legislature and the Governor to the Law Revision Commission of the State of New York for study and recommendation. The Commission laid aside all other work, held hearings, and, in cooperation with the Commission on Uniform Laws, the American Law Institute, and other bodies,<sup>8</sup> made exhaustive and scholarly studies of the Code and its effect on the law of New York. After three years and the expenditure of over \$300,000<sup>9</sup> the Commission published its work in three volumes of studies,<sup>10</sup> two volumes of hearings,<sup>11</sup> and a one-volume report.<sup>12</sup>

The result was a vindication of the critics of the Code. While approving the project of codification of the commercial law, the Commission's report concluded:

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3. Braucher, *The Legislative History of the Uniform Commercial Code*, 58 COLUM. L. REV. 798, 800 (1958).

4. Compare Beutel, *The Proposed Uniform [?] Commercial Code Should Not Be Adopted*, 61 YALE L.J. 334, 356-57 (1952), with Gilmore, *The Uniform Commercial Code: A Reply to Professor Beutel*, 61 YALE L.J. 364 (1952).

For an exhaustive bibliography of this discussion see 1 State of New York, Report of the Law Revision Commission and Record of Hearings on the Uniform Commercial Code 37-64 (1954). [hereinafter cited as N.Y.L.R.C. Hearings (1954)].

5. U.C.C. Official Draft (1952).

6. PA. STAT. ANN. tit. 12 (1954).

7. See 1 N.Y.L.R.C. Hearings 7 (1954).

8. State of New York, Report of the Law Revision Commission, Report Relating to the Uniform Commercial Code 7 (1956) [hereinafter cited as N.Y.L.R.C. Report (1956)].

9. See Braucher, *supra* note 3, at 803.

10. 1-3 State of New York, Report of the Law Revision Commission, Study of the Uniform Commercial Code (1955) [hereinafter cited as N.Y.L.R.C. Study (1955).]

11. 1-2 N.Y.L.R.C. Hearings (1954).

12. N.Y.L.R.C. Report (1956).

A uniform codification of commercial law has advantages outweighing disadvantages only if the codification is satisfactory in scope, organization and integration with the general body of law, as well as in its specific provisions. The Commission believes that it is clear, from the criticisms indicated in this Report, that the Uniform Commercial Code is not satisfactory in its present form and cannot be made satisfactory without comprehensive re-examination and revision in the light of all critical comment obtainable. The needed re-examination and revision will require both time and money, and constant consultation with the various groups affected.<sup>13</sup>

One cannot read the whole report and its supporting materials without concluding that it was a thorough rejection of the Commercial Code as it was then written.

It at once became evident that this repudiation of the 1952 draft after its enactment in only one state would be the death of the Uniform Commercial Code unless something drastic was immediately done about it. The backers of the Code were quick to respond. The enlarged Editorial Board of the two sponsoring organizations had already been reactivated to work with the New York Law Revision Commission,<sup>14</sup> and a subcommittee of new experts<sup>15</sup> for each article was formed to rework the Code to meet objections.

Although the backers of the Code publicly played down the objections of the critics,<sup>16</sup> between July<sup>17</sup> and November<sup>18</sup> of 1956 they produced a new

13. *Id.* at 68.

14. Braucher, *The 1956 Revision of the Uniform Commercial Code*, 2 VILL. L. REV. 3, 6 (1956).

15. ALI NAT'L CONFERENCE COMM'RS UNIFORM STATE LAWS, 1956 RECOMMENDATIONS OF EDITORIAL BOARD, U.C.C. vi-x (1957) [hereinafter cited and referred to as 1956 RECOMMENDATIONS], lists the active draftsmen and committees. A list of the original draftsmen and committees can be found in ALI NAT'L CONFERENCE COMM'RS UNIFORM STATE LAWS, CODE OF COMMERCIAL LAW, fly leaves (1948).

16. See, e.g., Braucher, *supra* note 14, at 5:

The Report disapproves one of the eight major articles of the Code—Article 5: Letters of Credit—but does not otherwise recommend any fundamental change. The Report also makes specific adverse reference to the drafting or policy of parts of some 67 of the nearly 400 sections of the Code. However, the problems raised are not at all insoluble. . . .

The 1956 Recommendations cite changes due to the New York Law Revision Commission in 134 sections while omitting all those used in Article 9. Note 21 *infra*. But see Goodrich, 1956 RECOMMENDATIONS vi:

Some of these changes are fairly important. Some are merely alterations in language because some group of critics thought that our meaning was not clear. Since the entire text was under examination anyhow, language changes not highly important in themselves have been made when some serious critic thought we were in danger of being misunderstood.

See generally Schnader, 34 ALI PROCEEDINGS 54-55 (1957).

17. Braucher, *supra* note 14, at 7.

18. Braucher, *supra* note 3, at 804.

version of the Code which appeared within a year of the New York Law Revision Commission's report. The new draft was published in 1957 in a pamphlet entitled *1956 Recommendations of the Editorial Board of The Uniform Commercial Code*. This sets out the changes in each section using brackets for portions deleted and italic type for new material. An examination of this document shows that although it attempts to retain the same general outline and section numbers, by actual count, it contains changes in over two-thirds of the 1952 sections.<sup>19</sup> These range from slight variations of expression in some sections to alterations in basic definitions and replacement of whole sections, articles, and parts of articles. After each section change, there is a note giving the reason for the revision. With the exception of the "reasons" in Article 9, which contains the greatest proportional number of changes in sections reworded or entirely replaced, there is a reference to the organization whose criticism it attempts to meet. Of those named in the other nine articles, the great majority of references to the changes are to the New York Law Revision Commission.<sup>20</sup> Since the Commission was also very critical of Article 9,<sup>21</sup> it is a fair assumption that the changes there were also largely motivated by the Commission.

Shortly after the 1956 Recommendations, there was published in 1957 a *Uniform Commercial Code, Official Edition*, printed without comments<sup>22</sup> but in a form almost identical to that suggested by the 1956 Recommendations. This draft was approved by the Commission on Uniform Laws and the American Law Institute in its meeting of May 1957 without any discussion.<sup>23</sup> Apparently everybody took it on faith. The new com-

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19. The actual percentage of change was 69%, divided as follows: Article 1, General Provisions, 59%; Article 2, Sales, 61%; Article 3, Commercial Paper, 48%; Article 4, Bank Collection, 77%; Article 5, Letters of Credit, 100%; Article 6, Bulk Transfers, 80%; Article 7, Documents of Title, 72%; Article 8, Investment Securities, 80%; Article 9, Secured Transactions, 95%; Article 10, Effective Date and Repealer, 50%. If the percentage of changes is any indication of lack of quality, Article 3, on Commercial Paper, was the best drafted.

20. Out of 228 changes where sources of criticism are mentioned 134 (or 59%) refer to the N.Y.L.R.C. by name.

21. N.Y.L.R.C. Report 464-85 (1956) covers twenty-one pages of closely printed discussion of the 1952 draft and of revisions made by the Editorial Board. The complicated nature of this discussion makes an accurate summary almost impossible but it can be safely stated that out of over 50 sections in Article 9, the New York Commission approved only 6. It approved about 30 changes made by the Editorial Board and made about 70 suggestions for changes.

22. Braucher, *supra* note 3, at 804.

23. 34 ALI PROCEEDINGS 53-54 (1957).

ments which were required by the extensive revisions did not appear until 1958 with the publication of the 1957 edition of the Code.<sup>24</sup>

With the approval of the Commission on Uniform State Laws and the American Law Institute, the initial phases of the drafting came to an end about fifteen years after the definitive work began.<sup>25</sup>

Whether the 1956 Recommendations actually met the criticisms levied against the 1952 draft by the New York Law Revision Commission and others is at present a mystery.

The very size of the project and the six volumes of materials supporting the criticisms by the New York Law Revision Commission make it impossible for a single scholar or the legal staff of even the largest organization in a short time to make the comparison and the integration necessary to answer such a question for the entire Code. This will have to be left to future scholars; but some of the material which follows begins to cast considerable doubt on the sufficiency of the 1956 revision. At any rate, the 1956 Recommendations and the Law Revision Commission's publications have taken their place in the basic source materials needed to solve the questions of the legislative intent of the Code and its Comments, not only for New York but for every state where it has been adopted.<sup>26</sup>

If the Commercial Code is to be uniformly interpreted it is imperative that a definitive commentary based on these materials be produced at once.

After the second final approval, the work of getting the various states to adopt the Code, which had been completely stymied by the New York Law Revision Commission Report, again went into high gear. With the opponents stalled by the enormity of the task of criticism, probably the most effective lobby in the history of state legislation pushed for its enactment. The Code was introduced into the legislatures of Massachusetts, Indiana, and Pennsylvania in 1957,<sup>27</sup> before the revised comments were ready, and was immediately passed in Massachusetts, Pennsylvania, and Kentucky.<sup>28</sup> Thereafter in a whirlwind of activity it swept through the legislatures, in-

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24. U.C.C., 1957 OFFICIAL TEXT (1958).

25. See Braucher, *supra* note 3, at 800; *cf.* 34 ALI PROCEEDINGS 53 (1937). For a discussion of the sufficiency of the time consumed see Beutel, *The Proposed Uniform Commercial Code as a Problem in Codification*, 16 LAW & CONTEMP. PROB. 141, 144 (1951).

26. BENDER'S UNIFORM COMMERCIAL CODE SERVICE contains the full text of the 1956 Recommendations, and the New York Consolidated Laws Service, Uniform Commercial Code, in historical notes in its annotations contains references apparently without citations to the New York Law Revision Commission Reports, and citations to the 1956 Recommendations.

27. See Braucher, *supra* note 3, at 804.

28. Ky. Acts 1958, ch. 77, at 214; Mass. Acts 1957, ch. 765, at 764; Pa. Laws 1959, Acts 426, 687, at 1023, 1883, amending and revising the original Commercial Code, Pa. Laws 1953, Act 1.

cluding New York where it was passed without any further return to or approval by the Law Revision Commission.<sup>29</sup> Today, less than ten years after final approval,<sup>30</sup> it has been adopted in fifty-one jurisdictions.<sup>31</sup> Only Louisiana and Puerto Rico and the federal law are still without it. It is being translated into Spanish for submission in Puerto Rico.<sup>32</sup> But because, if enacted there, it would cut the Civil Codes of Puerto Rico and Louisiana to ribbons, it is doubtful if, short of complete law revision, they will ever adopt it.

Now that, for practical purposes, it is the law of the whole country, discussion of its draftsmanship has become largely academic. It is time to turn to problems of interpretation of the Code, and to its effect on the laws of the jurisdictions which have adopted it.

## II. INTERPRETATION AND CONSTRUCTION GENERALLY

In classical phraseology, the application of a statute to a particular problem has been divided into two stages, interpretation and construction.<sup>33</sup> Although there is no exact scientific division of the two processes, and many courts and writers use the terminology interchangeably,<sup>34</sup> for convenience it may be said that the two steps are about as follows.

Interpretation usually covers the process of determining the meaning of the words as they appear in the statute as applied to the problem at hand. This involves the determination of their plain meaning from dictionary definition of the words, and from their position in context in the statute itself. The context also includes technical statutory meanings to be found

29. N.Y. Sess. Laws 1962, ch. 553, at 2580. To be sure, there was a further study by the New York Commissioners on Uniform Laws which resulted in many more New York amendments to the 1957 draft. See Penney, *New York Revisits the Code: Some Variations in the New York Enactment of the Uniform Commercial Code*, 62 COLUM. L. REV. 992 (1962).

30. The S.A. was adopted in 39 jurisdictions over a period of 56 years, 1 Uniform Laws Annotated (Supp. 1966, at 7) [hereinafter cited as U.L.A.]; the W.R.A., 55 jurisdictions in 54 years, 3 U.L.A. (Supp. 1966, at 9); the B.L.A., 33 jurisdictions in 45 years, 4 U.L.A. (Supp. 1966, at 7); the N.I.L., 55 jurisdictions in 29 years, 5 U.L.A. (Supp. 1966, at 9); the S.T.A., 52 jurisdictions in 35 years, 6 U.L.A. (Supp. 1966, at 7). When it is considered that each of these acts is comparatively short, the speed of adoption of the Commercial Code is truly phenomenal. Or is it possible that because the legislators could not understand it, it was easier to get it adopted?

31. 43 ALI ANNUAL REPORT 16 (1966).

32. 42 ALI PROCEEDINGS 37 (1965).

33. BLACK, *THE CONSTRUCTION AND INTERPRETATION OF LAWS* 1-9 (2d ed. 1911); LIEBER, *LEGAL AND POLITICAL HERMENEUTICS* ch. 3 (3d ed. Hammond 1880); 2 SUTHERLAND, *STATUTES AND STATUTORY CONSTRUCTION* § 365 (2d ed. Lewis 1904).

34. Landis, *Statutes and Sources of Law*, in *HARVARD LEGAL ESSAYS* 213, 218 n.13 (1934).

in definitions made part of the statute. Beyond this, one encounters the meaning in which the legislature intended to use the terms, which may or may not be the traditional technical use of the words by the courts and the legal profession, the purpose for which the statute was enacted, the laws superseded or changed, the legislative history as shown by debates, and so forth. In the case of the Commercial Code, due to the intricate draftsmanship and the complicated history, this now includes the earlier drafts and their comments, the New York Law Revision Commission Reports, the 1956 Recommendations, and the current Comments.<sup>35</sup> Beyond this, the later judicial interpretations of the words of the Code<sup>36</sup> and the law affected by it<sup>37</sup> are already accumulating, and these are by no means uniform. It should also be noted that these various methods of interpretation can, and usually do, reach different results in the same or similar cases.

In this country at least, there appears to be no fixed order of precedence which the courts or the profession are required to give these various types of interpretation. Which one prevails seems to be determined by the equity of the case, the equities of the statute,<sup>38</sup> the reason or logic of its application to

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35. Comments were clearly proper as part of the interpretation of the older uniform laws. See BRANNAN, *NEGOTIABLE INSTRUMENTS LAW* 94 (7th ed. Beutel 1948). With respect to the U.C.C. see 1 N.Y.L.R.C. Study 156-63 (1955); 1956 RECOMMENDATIONS 2-3; Skilton, *Some Comments on the Comments to the Uniform Commercial Code*, 1966 Wis. L. Rev. 597.

36. See, e.g., *Charles Martin Distrib. Co. v. Banks*, 111 Ga. App. 538, 142 S.E. 2d 309 (1965). A word of warning is necessary here that many decisions in Pennsylvania are based on the 1953 statute, which was amended, Pa. Laws 1959, Acts 426, 687, at 1023, 1883, amending and revising Pa. Laws 1953, Act 1, to correspond with the 1956 Recommendations, so that their interpretations are based on words no longer in the U.C.C. Compare, e.g., *Grange Nat'l Bank v. Conville*, 8 Pa. D. & C.2d 616, 5 Lyc. 170 (C.P. 1956) (liability of the principal), with U.C.C. § 3-307 (1)(b). Compare *Perfect's Market, Inc. v. Serro*, 42 Westm. 35 (Pa. C.P. 1959), with U.C.C. §§ 3-302 (1)(b); 1-201 (19); 2-103 (1)(b). There are also cases based on local variations in wording of the U.C.C. which are contrary to the uniform version. See *United Sec. Corp. v. Bruton*, 213 A.2d 892 (D.C. Ct. App. 1965) (discussed in note 73 *infra*). The cases are now being compiled in BENDER'S UNIFORM COMMERCIAL CODE SERVICE; WILLIER & HART, UNIFORM COMMERCIAL CODE REPORTER-DIGEST; and FISCHER & WILLS, UNIFORM COMMERCIAL CODE REPORTING SERVICE.

37. Compare *Delta Oxygen Co. v. Scott*, 238 Ark. 534, 383 S.W.2d 885 (1964); *Epstein v. Giannattasio*, 25 Conn. Supp. 109, 197 A.2d 342 (C.P. 1963); *Lorzrick v. Republic Steel Corp.*, 1 Ohio App. 2d 374, 205 N.E.2d 92 (1965), *aff'd*, 6 Ohio St. 2d 227, 218 N.E.2d 185 (1966); and *Yentzer v. Taylor Wine Co.*, 414 Pa. 272, 199 A.2d 463 (1964), with *Berry v. American Cyanamid Co.*, 341 F.2d 14 (6th Cir. 1965); *Miller v. Preitz*, 221 A.2d 320 (Pa. 1966); and *Hochgertel v. Canada Dry Corp.*, 409 Pa. 610, 187 A.2d 575 (1963).

38. See Landis, *supra* note 34, at 214-22.

the particular facts, the interests of the lawyers, their clients, or the litigants, or simply the caprice of the court.<sup>39</sup>

Construction seems to be the second step in the application of the statute. After its meaning has been determined by the proper interpretation, the question arises as to the effect on the whole body of the law. Should it be construed in such a manner as to control the facts of the case at hand? Over fifty years before the uniform statutes had made any appreciable imprint upon the body of the laws of this country, Dean Pound discussed statutory construction as follows:

Four ways may be conceived of in which courts in such a legal system as ours might deal with a legislative innovation. (1) They might receive it fully into the body of the law as affording not only a rule to be applied but a principle from which to reason, and hold it, as a later and more direct expression of the general will, of superior authority to judge-made rules on the same general subject; and so reason from it by analogy in preference to them. (2) They might receive it fully into the body of the law to be reasoned from by analogy the same as any other rule of law, regarding it, however, as of equal or co-ordinate authority in this respect with judge-made rules upon the same general subject. (3) They might refuse to receive it fully into the body of the law and give effect to it directly only; refusing to reason from it by analogy but giving it, nevertheless, a liberal interpretation to cover the whole field it was intended to cover. (4) They might not only refuse to reason from it by analogy and apply it directly only, but also give to it a strict and narrow interpretation, holding it down rigidly to those cases which it covers expressly. The fourth hypothesis represents the orthodox common law attitude toward legislative innovations. Probably the third hypothesis, however, represents more nearly the attitude toward which we are tending. The second and first hypotheses doubtless appeal to the common law lawyer as absurd. He can hardly conceive that a rule of statutory origin may be treated as a permanent part of the general body of the law. But it is submitted that the course of legal development upon which we have entered already must lead us to adopt the method of the second and eventually the method of the first hypothesis.<sup>40</sup>

The first step recommended by Dean Pound will be recognized at once as the standard method of construing codes in civil law jurisdictions,<sup>41</sup>

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39. It should be noted here that court decisions under a system of uniform laws lose much of their authority. For this development under the N.I.L. see BRANNAN, *op. cit. supra* note 35, at 101-09 & nn.82-104.

40. Pound, *Common Law and Legislation*, 21 HARV. L. REV. 383, 385-86 (1908).

41. See CODE CIVIL arts. 4, 5 (Fr. 63d ed. Dalloz 1964) (prohibits judges from following previous cases); 1 LACONTINERIE, *TRAITÉ DROIT CIVIL DES PERSONNES* 237, 264 bis-XIII (3d ed. 1907); PLANIOL ET RIPPERT, *TRAITÉ ÉLÉMENTAIRE DE DROIT CIVIL* §§ 221-22 (1928); SCHUSTER, *PRINCIPLES OF GERMAN CIVIL LAW* 10-13 (1907).



where the codes are recognized as part of the body of the law itself. In common law countries the progress in this direction has been much slower.<sup>42</sup> But in the case of the uniform laws, there was considerable progress along these lines before the adoption of the Commercial Code.<sup>43</sup>

In addition to the question to which the four propositions stated by Pound are directed, there is now, in this country, a fifth question involving the construction which should be given to one general statute which impinges upon or limits a portion of another in the same field, which by the proper interpretation of both, was clearly not intended to be repealed. Because of its broad scope of subject matter, this fifth problem becomes especially pertinent when dealing with the construction of the Commercial Code.

There are, of course, the familiar rules of statutory interpretation. There is, for example, the familiar rule that statutes which apparently conflict should be so interpreted as to give effect to each.<sup>44</sup> Then there is the further rule of construction that, in case of conflict, the specific controls the general,<sup>45</sup> or the later repeals the earlier.<sup>46</sup>

To this, there might be added a rule that in areas beyond the plain meaning of both, a code statute should be extended by construction (Pound's first and second propositions) whereas a particular statute should not be so extended, or might even be narrowly construed to prevent possible conflict (Pound's fourth category). Here again the choice of action by one applying the statute is so great as to allow him to apply at his caprice the well established and cited rule he desires as an excuse for his conclusion. In the case of the Code, this difficulty is further compounded by the controversy over whether the Commercial Code is really a unified general statute embodying a whole area of the law and repealing others in the field or whether it is a mere collection of specific statutes.

### III. IS THE UNIFORM COMMERCIAL CODE REALLY A CODE?

It is not necessary here to go into the argument on the merits of general codification in which the body of the law is reduced to writing in broad consistent principles, as against the enactment of numerous narrow, spe-

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42. See Landis, *supra* note 34.

43. See BRANNAN, *op. cit. supra* note 35, at 98-101.

44. BLACK, *op. cit. supra* note 33, at 325, 345, 352 (2d ed. 1911); MAXWELL, INTERPRETATION OF STATUTES 32 (11th ed. Wilson & Galpin 1962); SEDGWICK, INTERPRETATION AND CONSTRUCTION OF STATUTORY AND CONSTITUTIONAL LAW 97-116 (2d ed. Pomeroy 1874).

45. CRAIES, STATUTE LAW 321 (4th ed. Scott 1936).

46. BLACK, *op. cit. supra* note 33, at 353; SEDGWICK, *op. cit. supra* note 44, at 96.

cific, and independent statutes directed at particular situations leaving large portions of the resulting regulation to unwritten law.<sup>47</sup> The Code is an accomplished fact but its nature will have a definite effect on the problems of its interpretation and its application to business situations.

If classification is helpful, then it must be said that the Commercial Code in spite of its name and intent, expressed in a number of sections,<sup>48</sup> is not a code in the same sense as the French or German Civil Codes, the French Commercial Code, the Louisiana Civil Code, the Field Codes, or the Georgia or California codes.<sup>49</sup> In spite of much improvement and correlation in the 1956 Recommendations, it still remains as in its earlier drafts<sup>50</sup> a collection of specific statutes with their own often uncorrelated specific<sup>51</sup> and conflicting<sup>52</sup> definitions and theories.<sup>53</sup>

In many instances these statutes are still narrower in scope, subject matter, and language than were the uniform laws which they repeal.<sup>54</sup> It is fair to

47. For a discussion of this problem in relation to the Commercial Code see 1 N.Y.L.R.C. Study 37 (1955).

48. U.C.C. §§ 1-102(1) comment 1; 1-104; 1-106, comment 1; 3-104; 3-805, comment; 8-101; comment; 9-101, comment; 1 N.Y.L.R.C. Study 63 (1955); see U.C.C. § 1-203, comment.

49. Farnsworth, *A General Survey of Article 3 and an Examination of Two Aspects of Codification*, 44 TEXAS L. REV. 645, 656 (1966); Smith, *The First Codification of the Substantive Common Law*, 4 TUL. L. REV. 178 (1930).

50. 1 N.Y.L.R.C. Study 125 (1955); see Beutel, *supra* note 4, at 348; Beutel, *supra* note 25, at 158.

51. See U.C.C. §§ 1-201 (first paragraph), 2-103, 3-102, 4-104, 5-103, 7-102, 8-102, 9-105, 9-109. Numerous additional definitions are embodied in separate articles. *E.g.*, U.C.C. §§ 3-204, 3-416.

52. For example, "value" still has at least three meanings which may apply to the same transaction, as for example the transfer for credit of a draft or note with bills of lading or securities attached, U.C.C. §§ 1-201(44)(a), 3-303, 4-208(1)(b), 4-209, and duly negotiated "in settlement or payment of a money obligation," U.C.C. § 7-501(4). "Notice" has a variation of meanings which would require a treatise to correlate, distinguish and explain. See, *e.g.*, U.C.C. §§ 1-201(25), (26), (27); 2-104(3); 2-201(2); 2-315; 2-616(2); (3), (5); 3-206(4); 3-304; 3-415(4); 3-508; 4-203; 4-205(2); 4-303; 6-107 7-501(6); 8-305; 8-310; 9-307; 9-308; 9-309. "Documentary draft has at least two meanings. Compare U.C.C. §§ 4-104(1)(f), and 5-103(1)(b), with U.C.C. §§ 3-104(3), and 3-105(1)(d).

53. A different type of law for "merchants" seems to belong to Article 2 only. U.C.C. § 2-104, comment 2. The treatment of the concept of "holder in due course," "bona fide purchaser," and the like is almost as various as it was in the earlier drafts. See Beutel, *supra* note 4, at 341-42. There are likewise varying types and theories of negotiability, see U.C.C. §§ 3-305, 5-114, 7-502, 8-201(2), 8-202, 9-206, all of which are chopped up by Article 4. Article 9, except for a trick definition of "debtor," U.C.C. § 9-105(1)(d), contains little reference to the rights and duties *inter se* of assignor and assignee of security agreements. The right to call in third parties who are ultimately liable, and the right to interpleader, which should be general, are found in specific articles like U.C.C. §§ 2-607(5), 3-803, 7-603. Careful study will reveal many more.

54. One of the most startling examples of this change is found in Article 3, which

say that, in some of its parts it partakes of the nature of a general law, in others only a collection of special statutes.

A complete enumeration, classification, and integration of the articles and sections of the Code will have to be left to a later definitive treatise which in volume alone would be required to be at least three times as large as Williston on Sales.<sup>55</sup> Thereafter there still remains the task of using the Code to solve particular cases. In this effort it is not at all surprising to find the courts tangled in the intricacies of particular Code sections, ignoring technical interpretation and resorting to the idea of justice and fairness to decide the problems at hand.<sup>56</sup> This is the type of raw rural justice which hardly

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abandons the attempt to the N.I.L. to codify the entire law of negotiability. See *Crocker Nat'l Bank v. Byrne & McDonnell*, 178 Cal. 329, 173 Pac. 752 (1918); *Kohn v. Sacramento Elec., Gas & Ry.*, 168 Cal. 1, 141 Pac. 626 (1914); *King Cattle Co. v. Joseph*, 158 Minn. 481, 198 N.W. 798 (1924) (and cases cited therein); *President & Directors of Manhattan Co. v. Morgan*, 24 N.Y. 38, 150 N.E. 594 (1926); *Manker v. American Sav. & Trust Co.*, 131 Wash. 430, 230 Pac. 406 (1924). Article 3 retreats to the form of the British Bill of Exchange Act, 45 & 46 Vict. article 3, c. 61 (1882), which covers only checks, drafts, and promissory notes see U.C.C. § 3-103, comment 1, thus leaving vast areas of the law of negotiable instruments, in addition to those areas treated by Articles 4, 5, 7, 8, and 9, entirely uncovered.

U.C.C. § 3-415 omits the provisions of N.I.L. § 64, which it replaces, as to presumed order of liability of anomalous indorsers. See U.C.C. § 3-415, comment 4.

There are also U.C.C. §§ 2-403(2), (3) which replace S.A. § 25 on sale and retention of possession. It covers only goods entrusted to "merchants"; as to non-merchants the section is silent. Section 2-401(2) helps only when there is no specific agreement as to title. COOGAN, HOGAN & VAGTS, SECURED TRANSACTIONS UNDER THE UCC § 1803 (1)(c) (1966); see *Weisel v. McBride*, 191 Pa. Super. 411, 156 A.2d 613 (1959) (overlooking U.C.C. § 9-201). U.C.C. § 3-307 as indicated by the following material is much narrower than N.I.L. § 59 as to presumptions of holding in due course. Many other examples can easily be found.

Much of the balance of this paper will develop some of the problems raised by this type of narrow wording.

55. The latest edition (1948) is in four volumes. An idea of the size and nature of such a treatise can be had from the following: AUBRY & RAU, DROIT CIVIL FRANCAIS, (6th ed. 1938) (12 volumes); BANDRY-LACONTINERIE, DROIT CIVIL (1896) (26 volumes); MARCADE, EXPLICATION DU CODE NAPOLEON (1865) (six volumes); PAUL PONT, EXPLICATION DU CODE NAPOLEON (1868) (11 volumes).

56. *Norton v. National Bank of Commerce*, 240 Ark. 143, 398 S.W.2d 538 (1966), is such a case. In this case the defendant, an auto dealer, sold a car to a customer for a note and conditional sales contract which the defendant immediately discounted with the plaintiff bank, and contracted on a separate printed form furnished by the bank to repurchase the contract on default, for the amount due thereon, waiving any notice of default or foreclosure sale. After two installments, the customer defaulted, the bank repossessed the car, and, without notifying the defendant and contrary to its practice in previous cases, sold it at private sale for seventy-five dollars. The bank sued defendant for \$277.88, the unpaid balance.

In this simple \$300 case we see the interpretation of the Code at work. The lower court gave judgment for the bank and the defendant appealed. The Supreme Court of Arkansas asked for and received the services of the Permanent Editorial Board of the

meets the sophisticated technique which the Code requires. However, it might be useful here to illustrate the types of problems of interpretation and construction which a definitive treatise on the Code would entail.

#### IV. THE PRESUMPTION OF HOLDING IN DUE COURSE IN SUITS UNDER ARTICLE 3

One of the most useful provisions in the old law was the presumption in favor of holders. The Negotiable Instruments Law stated the rule as follows, "Every holder is deemed prima facie to be a holder in due course."<sup>57</sup> This section as so broadly worded applies to all the various situations where a holder is involved both in court and out. While many writers have discussed it only as it applies to law suits on negotiable instruments<sup>58</sup> it is clear that it has application to many other instances. For example, a person purchasing an instrument could assume that the seller was a holder in due course and he did not have to inquire as to the vendor's rights.<sup>59</sup> Even if he was negligent by not so inquiring, the presumption was still in his favor.<sup>60</sup>

Code in the form of two amici briefs which held that the defendant was not a debtor within U.C.C. § 9-504(3) and not entitled to notice of the sales, but reached the result that would follow if he were and awarded him damages under U.C.C. § 9-507(1). The amici briefs differed on the amount of damages. The court found that the defendant was a "debtor," presumably within but not citing U.C.C. § 9-105(d), that the rules for consumers goods in U.C.C. § 9-507(1) did not apply; but reserved judgment on the point. It decided, "In simple fairness he should have had notice," 240 Ark. at —, 398 S.W.2d at 541, and, "Upon the issue of damages simple considerations of fair play cast the burden of proof upon the bank," 240 Ark. at —, 398 S.W.2d at 542. Judgment was reversed and the case was remanded for a new trial. So, after expending far more than the amount involved, the case is ready to start again, to begin the process of applying the Code.

So the interpretation of the Code goes out the window. If one is interested in interpretation he may consult U.C.C. §§ 9-504(3); 9-207(1), comment 1; 9-105(1) (a), (c), (d), (h), (i); 9-501(3) (b); 9-318(1) (a), (b); 9-507(1); 9-109(1), (4); 1-107; 1-201(46). Compare U.C.C. §§ 2-202; 1-205(4); and 1-201(3), with U.C.C. §§ 2-208(1); 3-112(1) (e); and 1-203, and their comments. There may be others, but at any rate all the conclusions worked out by the persons interested in the principal case can find support here, and perhaps a few more. The ultimate result will depend upon how far one reads, and how much weight he places upon, general sections in aid of interpretation of specific sections. Was the court right in deciding it was a matter of "simple fairness"? If it was, "what price" Commercial Code in this case?

57. The entire text of N.I.L. § 59 was as follows:

Who Deemed Holder in Due Course. Every holder is deemed prima facie to be a holder in due course; but when it is shown that the title of any person who has negotiated the instrument was defective, the burden is on the holder to prove that he or some person under whom he claims acquired the title as holder in due course. But the last-mentioned rule does not apply in favor of a party who became bound on the instrument prior to the acquisition of such defective title.

58. See BRITTON, *BILLS & NOTES* § 102 (2d ed. 1961) (and authorities there cited).

59. See cases cited BRANNAN, *op. cit. supra* note 35, at 788.

60. See cases cited *id.* at 772-79.

The provision could also be used to settle the conflict over the question of whether the first indorsee of an instrument indorsed in trust could be a holder in due course,<sup>61</sup> or whether the payee could be a holder in due course.<sup>62</sup> The rule also applied to negotiable corporate bonds,<sup>63</sup> and by broad construction to stocks<sup>64</sup> and documents of title.<sup>65</sup>

The Commercial Code sections which seem to replace N.I.L. section 59 are sections 3-307 and 8-105.<sup>66</sup> Both of these sections are much narrower in their wording than was section 59 of the N.I.L. Section 3-307(2) provides "when signatures are admitted or established, production of the instrument entitles the holder to recover on it unless the defendant establishes a defense."<sup>67</sup> Section 8-105(2)(c) has the same wording but adds the words "or defect going to the validity of the security."<sup>68</sup>

61. See discussion and conflicting cases *id.* at § 37.

62. See discussion and conflicting cases *id.* at § 52. It might also be useful in applying N.I.L. § 66 (first clause) to warranty cases.

63. Paxton v. Miller, 102 Ind. App. 511, 200 N.E. 87 (1936); Parks v. Hughes, 145 La. 221, 82 So. 202 (1919); Gruntal v. United States Fid. & Guar. Co., 254 N.Y. 468, 173 N.E. 682 (1930); Scott v. Platt, 171 Ore. 379, 135 P.2d 769 (1943).

64. Welland Investment Corp. v. First Nat'l Bank, 81 N.J. Super. 180, 195 A.2d 210 (Ch. 1963); 1 COOK, CORPORATIONS § 13 (8th ed. 1923); see Morrison v. Liberty Discount & Sav. Bank, 61 Lack. Jur. 37 (Pa. C.P. 1958).

65. See authorities cited notes 144-47 *infra*.

66. U.C.C. Table of Sections of Prior Uniform Acts, p. xxxvi, cites N.I.L. § 59 as replaced by U.C.C. §§ 3-207, 3-306, and 8-301. Sections 3-307 and 8-105(2)(c), (d) (which is not cited at all—an obvious oversight) seem to have direct bearing on the presumption and the others only marginal effect.

67. The entire section reads:

Section 3-307. Burden of Establishing Signatures, Defenses and Due Course.

(1) Unless specifically denied in the pleadings each signature on an instrument is admitted. When the effectiveness of a signature is put in issue

(a) the burden of establishing it is on the party claiming under the signature; but

(b) the signature is presumed to be genuine or authorized except where the action is to enforce the obligation of a purported signer who has died or become incompetent before proof is required.

(2) When signatures are admitted or established, production of the instrument entitles a holder to recover on it unless the defendant establishes a defense.

(3) After it is shown that a defense exists a person claiming the rights of a holder in due course has the burden of establishing that he or some person under whom he claims is in all respects a holder in due course.

68. The entire section reads:

Section 8-105. Securities Negotiable; Presumptions.

(1) Securities governed by this Article are negotiable instruments.

(2) In any action on a security

(a) unless specifically denied in the pleadings, each signature on the security or in a necessary indorsement is admitted;

(b) when the effectiveness of a signature is put in issue the burden

### A. *In Suits on the Instrument*

In cases involving a suit on the instrument by a holder against the maker, the Code sections are clear. When signatures are established, either under subsection 1 or by evidence, the holder is entitled to recover.<sup>69</sup> This gets the same result as the N.I.L.; but the facts necessary thereafter to shift the burden of proof are different. Under N.I.L. section 59:

“When it is shown that the title of any person who has negotiated the instrument is defective, the burden is on the holder to prove that he or some person under whom he claims acquired the title in due course . . . .”

The Code’s section 3-307(3) uses a different test. It provides:

“After it is shown that a defense exists a person claiming the rights of a holder in due course has the burden of establishing that he or some person under whom he claims is in all respects a holder in due course.”

Note that “defective title” has been changed to “defense exists.” This gets substantially different results than did N.I.L. section 59.

Under the N.I.L., a defective title depended upon the action and state of mind of a person negotiating the instrument. Section 55 of the N.I.L. says that a title is defective:

“When he obtained the instrument, or any signature thereto, by fraud, duress, or force and fear, or other unlawful means, or for an illegal consideration, or when he negotiates it in breach of faith, or under such circumstances as amount to a fraud.”

It should be apparent at once that although the test of defective title included many defenses, it did not cover the defenses of absence of consideration, failure of consideration, accommodation, part payment, or accord and satisfaction. These defenses would be a basis for defects of title only if the holder against whom they were effective negotiated the instrument after they arose “in breach of faith, or under such circumstances as amount[ed] to a fraud.” Generally, under the N.I.L. all defenses of the maker arising

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of establishing it is on the party claiming under the signature but the signature is presumed to be genuine or authorized;

(c) when signatures are admitted or established 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

(d) after it is shown that a defense or defect exists the plaintiff has the burden of establishing that he or some person under whom he claims is a person against whom the defense or defect is ineffective.

69. *Watertown Sav. & Loan v. Spanks*, 346 Mass. 398, 193 N.E.2d 333 (1963).

after negotiation of the instrument to the holder,<sup>70</sup> and some not known to the transferor at the time of negotiation, did not shift the burden of proof. The presumption still acted in the holder's favor.<sup>71</sup>

Although the comments do not indicate any change, the effect of the Code's section 3-307(3) in this respect is quite different. It says, "After it is shown that a defense exists" then the burden shifts to the holder.<sup>72</sup> Obviously, this means any defense existing at the time of the trial and completely eliminates all the exceptions in the N.I.L. applying to defenses arising after negotiation of the paper. The case of *United Sec. Corp. v. Bruton*<sup>73</sup> has already reached this result where the defense arose after negotiation to the plaintiff. This repeals the authority of hundreds of cases decided under the N.I.L.<sup>74</sup> and will have a marked effect upon the pleading and practice in all states.

There are further questions raised by the phraseology of section 3-307(3). First it says, "after it is shown that a defense exists." This would, in its broadest meaning, cover any defense to the instrument whether applying to the defendant or another person not a party to the instant case, such as a co-maker or indorser with the defense of fraud, non-delivery, or the like. Under the last sentence of N.I.L. section 59 it was clear that in such a case the burden did not shift and the holder was entitled to recover if the defendant had become "bound on the instrument prior to the acquisition of such defective title." In such a case, a person liable could pay the holder relying on the presumption that he was a holder in due course and such payment would be payment in due course under N.I.L. section 88.<sup>75</sup> Consequently, there was no necessity for the holder to prove

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70. See N.I.L. § 59 (last sentence), set out in note 57 *supra*.

71. See cases cited BRANNAN, *op. cit. supra* note 35, at 882-84.

72. *Budget Charge Accounts v. Mullaney*, 187 Pa. Super. 190, 144 A.2d 438 (1958) (1952 edition of Code); *First Pa. Banking & Trust Co. v. DeLise*, 186 Pa. Super. 53, 195 A.2d 115 (1958) (1952 edition of Code); see 2 N.Y.L.R.C. Study 976 (1955); 1 N.Y.L.R.C. Hearings 207, 247, 426, 544, 976 (1954). Under the 1952 edition of the Code it was sufficient to raise the defense without proving it, 2 N.Y.L.R.C. Study 975 (1955); 10 MERCER L. REV. 211 (1958), but the 1956 Recommendations returned to the rule of the N.I.L. requiring the defense to be proved before the burden shifted, see 1956 RECOMMENDATIONS 107.

73. 213 A.2d 892 (D.C. Ct. App. 1965). Although, as the court points out, the cause of action arose before the Code became effective in the District of Columbia, the trial occurred after the effective date. The D.C. edition of the Code, D.C. CODE § 28: 10-102 (Supp. 1965), does not contain the provisions of U.C.C. § 10-102(2), so the court properly decided that the procedural matter involved was determined by the law at the time of the trial.

74. See cases cited BRANNAN, *op. cit. supra* note 35, at 882-84.

75. Payment is made in due course when it is made at or after the maturity of the instrument to the holder thereof in good faith and without notice that his title is defective. N.I.L. § 88.

that he was a holder in due course. The defendant, with no defense of his own, having paid without notice of a defect in the holder's title, would be discharged. The Code has abolished payment in due course,<sup>76</sup> giving any party the right to discharge if he pays a holder even with knowledge of adverse claims (except for two exceptions not important here which will be discussed later) unless the third party affirmatively intervenes. It further provides in section 3-306(d):

The claim of any third person to the instrument is not otherwise available as a defense to any party liable thereon unless the third person himself defends the action for such party.

Now, although they are not defined in Article 3,<sup>77</sup> it is clear that technically a claim is not a defense,<sup>78</sup> so it may be said that the Code is silent on the question of whether or not proof of such a defense by a third party shifts the burden. But as a practical matter, claims and defenses often arise from the same facts, so when the sections are read together it seems that "a defense exists" ought to be interpreted as when "the defendant in this suit proves he has a defense." This gives section 3-307 a narrow interpretation limiting it to law suits only. That this was probably the intention of the framers is shown by the fact that they think that section 3-306(d) takes the place of the last sentence of N.I.L. section 59.<sup>79</sup>

It also should be observed here, in passing, that under the Code when an instrument is acquired through a thief or a restrictive indorsement, this becomes a defense to prior parties.<sup>80</sup> So if these facts are "shown" the burden will shift to the holder to show that he is a holder in due course. Perhaps until these matters are better settled, lawyers might do well to act as if the proof of a defense by anybody shifts the burden.

There is a second difficulty of interpretation which requires further examination.

After it is shown that a defense exists a person claiming the rights of a holder in due course has the burden of establishing that he or some person under whom he claims is *in all respects* a holder in due course.<sup>81</sup>

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76. U.C.C. § 3-603, comment.

77. The U.C.C. defines "adverse claim" to include "a claim that a transfer was or would be wrongful or that a particular adverse person is the owner of or has an interest in the security." U.C.C. § 8-301(1).

78. "Claim" and "defense" are widely used throughout the U.C.C. See, *e.g.*, U.C.C. §§ 3-305(1), (2); 3-306(a), (b).

79. See U.C.C. § 3-306, comment 5. See also U.C.C. § 3-304, comment 4.

80. U.C.C. § 3-306(d); 3-306(a), (b), comments.

81. U.C.C. § 3-307(3). (Emphasis added.) See generally *Korzenik v. Supreme Radio*, 347 Mass. 108, 197 N.E.2d 702 (1964).



Literally interpreted, the words italicized would require the holder to show that he was a holder in due course not only as to the defense offered but in every other respect. This literal interpretation is supported by the comment to section 3-307(3),<sup>82</sup> which states that: "in all respects" means that he must sustain this burden by affirmative proof that the instrument was taken for value, that it was taken in good faith and that it was taken without notice."<sup>83</sup> Since these are all the requirements of holding in due course set out in section 3-302, it seems that the draftsmen meant exactly what they said, and any holder who could not prove that he, or some person under whom he claims, was completely a holder in due course, would take as a mere assignee subject to most defenses which could be "shown," whether he knew of them or not at the time he purchased.

This leads to some interesting and important results as to the facts in substantive law which the holder is required to prove. Examples of a few will suffice:

(1) The defendant shows that he has a defense of failure of consideration.<sup>84</sup> The instrument in question "bears . . . visible evidence of forgery or alteration,"<sup>85</sup> in the form of changed words or figures. Can the holder show that in fact the changes were authorized, and that he knew it when he took the instrument? And, therefore, is he a holder in due course as to the failure of consideration? The answer is no. Section 3-304(1) says, "The purchaser has notice of a claim or defense" in these facts, so he did not take it "without notice . . . of any defense against or claim to it on the part of any person;"<sup>86</sup> so he cannot meet the burden of proof that he is other than an assignee.

(2) The defendant shows that he was induced to sign by fraud. The holder took the paper from a known fiduciary to pay the fiduciary's own

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82. U.C.C. § 3-307, comment 3.

83. *Norman v. World Wide Distribs.*, 202 Pa. Super. 53, 195 A.2d 115 (1963) (good faith). This requirement without notice raises the old and interesting question of proof of a negative; but this paper is already too complicated to go into such questions.

84. U.C.C. § 3-408.

85. U.C.C. § 3-304(1)(a).

86. U.C.C. § 3-302(1)(c). U.C.C. § 3-304, comment 4, would seem to indicate that the draftsmen do not adopt this kind of interpretation, but this comment contradicts the plain meaning of the last phrase in U.C.C. § 3-302(1)(c): "on the part of any person." The last phrase of U.C.C. § 3-307(3) is also in support of this statement. See *Abercrombie Estate*, 20 Pa. D. & C.2d 496 (1959).

debt to the holder, but in good faith on evidence that the fiduciary was authorized to do so. The fact that this was not true is now shown. By express provision of the Code, "the purchaser has notice of a claim"<sup>87</sup> against the instrument so he cannot meet the burden of proof. He is therefore a mere assignee.

(3) Accommodation parties have many defenses against negotiable paper.<sup>88</sup> A maker shows that he is an accommodation maker and has a defense of breach of contract, not an accommodation defense. To meet the burden of proof, the holder shows that he bought without knowledge of the accommodation and proves that he is otherwise a holder in due course. In this situation, the holder recovers.<sup>89</sup> But if the defendant was an anomalous indorser, section 3-415 says, "An indorsement which shows that it is not in the chain of title is notice of its accommodation character,"<sup>90</sup> and accommodation can be a defense; ergo, the holder cannot prove that he is in all respects a holder in due course and so it would seem he cannot recover. However, section 3-304 provides that knowledge of the fact "that any party has signed for accommodation . . . does not of itself give the purchaser notice of a defense or claim."<sup>91</sup> How can these two sections be reconciled? Easily, if the chain of title is regular, and the taker knows of the accommodation, he is not charged with notice; but if the accommodation, whether it exists or not, is shown by an anomalous indorsement, he has legal notice and is a mere assignee. If the defense arises from the agreement of the accommodation, the reader can work it out for himself.

(4) One more example; suppose the plaintiff holds under a chain of title containing a restrictive indorsement.<sup>92</sup> Now it must be noted that under the Code "restrictive indorsement" is a different term than it was under the N.I.L.<sup>93</sup> It includes all types of indorsements which were restrictive under the N.I.L. and, in addition, covers what were previously conditional indorsements. While under the N.I.L., parties liable could disregard conditional indorsements and pay the instrument according to its tenor before the conditional indorsement,<sup>94</sup> under the Code prior parties are bound to perform

87. U.C.C. § 3-304(2).

88. U.C.C. §§ 3-601(2), 3-604(2), 3-606(1). See *Rose v. Homsey*, 347 Mass. 259, 263, 197 N.E.2d 603, 606 (1964).

89. U.C.C. § 3-415(3).

90. U.C.C. § 3-415(4).

91. U.C.C. § 3-304(4)(c).

92. U.C.C. §§ 3-205, 3-206. These were not in the 1952 draft but were returned by the 1956 Recommendations of the Editorial Board for the U.C.C., after much criticism. 1956 RECOMMENDATIONS 99-101. See N.Y.L.R.C. Report 404 (1956).

93. Compare N.I.L. §§ 36, 39, with U.C.C. § 3-205.

94. N.I.L. § 39.

according to the terms of the restrictive indorsement,<sup>95</sup> be they conditional or otherwise. Any restrictive indorsement, therefore, raises a defense by prior parties. This being so, the burden of proving he is a holder in due course shifts to the plaintiff. Now what must he prove? If he be a first taker under the restrictive indorsement he will have to show that he acted "consistent[ly] with the terms' of the indorsement."<sup>96</sup> If he is a later holder, he is "neither given notice nor otherwise affected by such restrictive indorsement unless he has knowledge that a fiduciary or other person has negotiated the instrument in any transaction for his own benefit or otherwise in breach of duty."<sup>97</sup> The Code here cites section 3-304(2), which charges the purchaser with such notice of a claim whether or not the instrument is restrictively indorsed.<sup>98</sup> So, unlike the anomalous indorsement which carries notice whether or not it is read, the restrictive indorsement seems to carry no notice to anybody;<sup>99</sup> but the first indorsee and prior parties are still bound to its terms whether or not they know of them.<sup>100</sup> When the prior party's defense rests on facts outside the scope of the restrictive indorsement, it seems that all but possibly a depository or intermediate indorsee bank can prove lack of notice<sup>101</sup> so as to give them in all respects the rights of a holder in due course. The results would seem to be contrary to those in the previous examples, and also contrary to those under the N.I.L.<sup>102</sup> Why? Because the plain words of the Code say so, and no other interpretation seems possible. It should be clear that these results follow in any suit on the instrument whether the defendant be a maker or subsequent party.<sup>103</sup>

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95. U.C.C. § 3-603(1)(b).

96. U.C.C. § 3-206, comment 6. U.C.C. § 3-206(4) does not say so. It says he "must pay or apply any value given by him. . . ." The result of the comment can be reached by applying U.C.C. § 3-303(a), which contemplates later performance as "taking for value."

97. U.C.C. § 3-206(4).

98. Here again the holder has the burden of proving a negative. So normally the plaintiff should allege and prove such facts (facts which are entirely beyond his knowledge), or he may have to be content with alleging them and letting the holder disprove them.

99. *Quaere* about a negative inference from U.C.C. § 3-206(2) (as to depository or intermediate indorsee banks).

100. U.C.C. §§ 3-603(1)(b), 3-206 (by negative inference). This may result in situations where a person bound on an instrument is required to pay twice under a restrictive indorsement under conditions over which he has no control; once to a holder in due course and again to the beneficiary of a restrictive indorsement.

101. See U.C.C. §§ 3-603(1)(b), 3-307(3), 3-206(2) (negative inference).

102. See BRANNAN, *NEGOTIABLE INSTRUMENTS LAW* 614-21 (7th ed. Beutel 1948) (and cases there cited).

103. U.C.C. §§ 3-601 to -606 make no distinction between makers and other parties as

B. *The Operation of the Presumptions and the Shifting Burden of Proof Under the Code*

Whatever may have been the state of the law under previous cases, the Code seems to offer a clear set of rules so far as the presumptions and burdens of proof where suits on an instrument are concerned. As for the instrument itself, it is clear under section 3-307(1) that there is a presumption of the genuineness of its signatures. The Code by definition requires the triers of fact to find the existence of the fact presumed unless and until evidence is introduced which will support a finding of its nonexistence.<sup>104</sup>

As to the rest of the instrument beyond the signatures, the presumptions under the Code are few. Under section 3-114(3), the date is presumed to be correct, and by section 3-115(2), the burden of establishing that a completion is unauthorized is on the party so asserting. By illogical negative inference it might be argued that there was a presumption of proper completion. There is also in section 3-201(3) a statement that mere possession of an instrument by one not a holder carries no presumption of ownership, again another possible negative inference as to holders. These are merely fragmentary presumptions. There seems to be no section corresponding to the first clause of N.I.L. section 59, which says, "Every holder is deemed *prima facie* to be a holder in due course." This not only takes care of the presumption of holding in due course, but as such lends a presumption of recovery on all the terms of the instrument. The draftsmen of the Code substituted for this<sup>105</sup> section 3-307(2): "When signatures are admitted or established, production of the instrument entitles a holder to recover on it unless the defendant establishes a defense." As will be discussed later, this is a much narrower provision than the first clause of N.I.L. section 59, but for the question now under discussion of recovery on the instrument, it gets the same results. Thus the production of the instrument entitles the holder without more to recover unless the defendant establishes its invalidity or another defense.<sup>106</sup> Defenses are of two kinds, those good against the

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far as discharges are concerned. It is fair to assume that the same principle applies to other defenses.

So far as suits on warranties are concerned, unlike the N.I.L. in which there was a presumption in favor of the holder (see note 62 *supra*), the Code is silent, and § 3-307 would have no effect except when the suit involved forgery or other lack of genuineness. Here, of course, by analogy and by ordinary rules of proof, the burden would seem to be on the plaintiff to prove the forgery or other lack of genuineness.

104. U.C.C. § 1-201(31).

105. U.C.C. § 3-307, comment 2.

106. U.C.C. § 3-307(2).

holder in due course<sup>107</sup> and those not.<sup>108</sup> Therefore, when it is shown that a defense of the latter type exists, the burden of establishing that he is a holder in due course falls upon the holder.<sup>109</sup> The comment to section 3-307 and the legislative history make it clear that the defendant must establish by the preponderance of evidence that a defense exists. This preserves the rule under N.I.L. section 59.<sup>110</sup> If the defendant offers evidence of such a defense, the sufficiency of such evidence to establish a defense is for the trier of facts. If the holder offers no evidence, it is still possible for the verdict to be for either party. The holder may rebut the defense and still win,<sup>111</sup> but if, in the opinion of the trier of facts, the evidence is sufficient to support a defense, then the burden shifts to the holder to establish that he is a holder in due course. "Burden of establishing" is defined as "the burden of persuading the triers of fact that the existence of the fact is more probable than its non-existence."<sup>112</sup>

Although the rules are intricate, the Code and its comments in this respect are clearer than was the N.I.L. There is no longer any necessity to continue the conflict in the cases as to the weight of the presumption or the burden on either party. It is also clear that in this area the Code, by its plain interpretation, repeals evidentiary statutes and court rules in the jurisdictions where it is effective. It reduces considerably the rights of holders in due course under the N.I.L. in some cases, and increases them in others. On careful consideration, however, no tears should be shed over this because a holder in due course as such is one in a position to take advantage of the misfortune of another, his rights are statutory, and clarity is more important than the equities.

### C. Suits to Establish Title to Commercial Paper

When one turns from suits on the instrument itself to the numerous cases in which there is a contest between holders and owners or others who claim title to or rights in the paper, a totally different situation exists. Suppose,

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107. See *Imperial Consumer Serv., Inc. v. Walton*, 78 Mont. Co. L.R. 37, 39 (Pa. C.P. 1960); U.C.C. §§ 3-305(2)(a)-(e). The expression "all defenses" in subsection (2) is likely to be misleading. To those listed should be added: alteration, U.C.C. § 3-407, and unauthorized signature, U.C.C. § 3-404.

108. U.C.C. §§ 3-305(1),(2).

109. U.C.C. § 3-307(3).

110. 1956 RECOMMENDATIONS, § 3-307, reason. See BRANNAN, *op. cit. supra* note 102, at 876-82 (and cases there cited). Comments to U.C.C. § 3-307 indicate that the minority cases no longer have any weight.

111. U.C.C. § 3-307, comment 3.

112. U.C.C. § 1-201(8).

for example, (1) a former holder sues a present holder<sup>113</sup> alleging and proving that he is or was the rightful owner or has other legal claims to bearer paper or paper containing his endorsement. At this point it was clear under N.I.L. section 59 that the present holder prevails because "every holder is deemed *prima facie* to be a holder in due course." Suppose further, (2), the plaintiff shows that he was deprived of the paper by fraud, theft, loss, or the like. It is clear under N.I.L. section 59 that the burden of proof now shifts to the holder.<sup>114</sup> How is it under the Code?

In (1) above you would answer that it is clear that the holder prevails. How do you know? If a chattel or non-negotiable paper were involved it is clear the plaintiff would prevail or that the burden would be on the defendant to come forward with proof of estoppel, acquiescence, or the like. Under Code section 3-306 "unless he has the rights of the holder in due course, any person takes the instrument subject to (a) all valid claims to it on the part of any person."<sup>115</sup> Now does he have the "rights of the holder in due course?" The statute is silent. Where is the presumption?

The draftsmen seem to think that section 3-307(2) was a substitute for the presumption in N.I.L. section 59; but as already indicated section 3-307 by its context is definitely limited to suits on the instrument. What is more, section 3-307(2)<sup>116</sup> authorizes the "holder to recover on it unless the defendant establishes a defense." In the instant case, the suit is not on the instrument and the holder is the defendant; so by no proper interpretation can the section be said to apply to the case where the holder is being sued. It should be further noted that the entire section is discussing "defenses," whereas the case involves a "claim." It is therefore clear that section 3-307 does not cover the case. Is there any other pertinent section?

Diligent search has not revealed any pertinent section other than section 1-202.<sup>117</sup> An examination of this section indicates that it covers only third-party documents like bills of lading and the like, and was so intended.<sup>118</sup> It purports only to raise a presumption of genuineness and by no means can it be stretched to one of holding in due course or can it shift the burden of proof; so it seems fair to say that the Code is silent on a suit be-

113. For the definition of holder see U.C.C. § 1-201(20).

114. For the wording of this section see note 57 *supra*. Observe the use of the concept of defective title.

115. See also U.C.C. § 3-207(2).

116. For the wording of this subsection see note 67 *supra*.

117. *Prima Facie Evidence by Third Party Documents.*

A document in due form purporting to be a bill of lading, policy or certificate of insurance, official weigher's or inspector's certificate, consular invoice, or any other document authorized or required by the contract to be issued by a third party shall be *prima facie* evidence of its own authenticity and genuineness and of the facts stated in the document by the third party.

118. See U.C.C. § 1-202, comment 2.

tween claimants of the same negotiable instrument. This includes both cases (1) and (2) above.

Here one is faced with the problem of construing the silence of the Code. Unfortunately, after over fifteen hundred years of applying codes and a much longer experience of trying cases, the legal profession seems to have developed no empirical science of applying statutes or determining facts in court.<sup>119</sup> One is remitted to the nebulous legal maxims, rules of construction, and habits of the bar. As indicated by Dean Pound in the article quoted above,<sup>120</sup> the civil law lawyers, who have a much longer experience with codes, have an entirely different technique than do their common law brethren.

What, then, are the possibilities of solving this important problem? There are at least five different approaches available, all of which have support in the habits of the bar, the intent of the framers, the common law, court decisions, or a combination of one or all of these sources. These are (A) interpretation of the repeal of the N.I.L., (B) carrying forward the court decisions since the N.I.L., (C) return to the common law cases before the N.I.L., (D) construction of the rules based upon analogy to other provisions of the Commercial Code, and (E) resort to statutes and rules of court in various jurisdictions where the cases may be tried.

First, what can be made of repeal of the N.I.L. (A above)? It is clear that the Commercial Code of necessity repealed most of the uniform laws in its field, including specifically, the N.I.L.<sup>121</sup> This repeal covers N.I.L. section 59 and is not saved by the general repealers action repealing "all acts and parts of acts inconsistent with this act."<sup>122</sup>

There are at least three recognized ways of interpreting repeal. (a) The act repealed is wiped out and the opposite result is intended (negative inference); (b) the act was repealed because it was unnecessary, but the same rule is therefore continued; (c) the act was wiped out in favor of a return to the law as if the statute did not exist.<sup>123</sup>

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119. It was to be expected that the Chicago Jury Study might shed some light on this problem.

120. Pound, *Common Law and Legislation*, 21 HARV. L. REV. 383 (1908).

121. U.C.C. § 10-102(1).

122. U.C.C. § 10-103.

123. One desiring to pursue the subject will find the following interesting. CRAIES, *STATUTE LAW* 294 (4th ed. Scott 1936); DWARRIS, *TREATISE ON STATUTES* 160 (Potter ed. 1871); MAXWELL, *INTERPRETATION OF STATUTES* 390 (11th ed. Wilson & Gelpin 1962); SEDGWICK, *INTERPRETATION AND CONSTRUCTION OF STATUTORY AND CONSTITUTIONAL LAW* 116 (2d ed. Pomeroy 1874); SUTHERLAND, *STATUTORY CONSTRUCTION* 544 (Lewis ed. 1904). An examination of these authorities will reveal that this subject is further complicated by acts of Parliament and many state constitutions and statutes.

(a) If one follows the illogical negative inference from repeal, he might reach the result that the presumption is against the holder being a holder in due course, and the burden is upon him to prove he is. This interpretation might receive some support from the substantive provisions of sections 3-207(2) and 3-306. The former provides "Except as against a subsequent holder in due course . . . negotiation is . . . subject to rescission . . . or any other remedy permitted by law," and the latter, "unless he has the rights of a holder in due course any person takes the instruments subject to (a) all valid claims to it on the part of any person." Since the rights of a holder in due course in both sections are exceptional, and since the presumptions and burden of proof were provided only in cases where the holder was the plaintiff, it might be argued, again by negative inference, that the holder has the burden of establishing his affirmative defense, *i.e.*, that he is a holder in due course. Such an argument is illogical and seems to sicken one acquainted with the law of bills and notes before the enactment of the Code. But who is to say that some court may not find it appealing?

(b) The second proposition can be stated about as follows: everybody knows a holder is presumed to be a holder in due course, so the first sentence of N.I.L. section 59 was repealed as unnecessary. There is considerable support for this kind of argument in many of the Commissioners' comments, which seem to indicate that they regard the Code as a sort of restatement of the case law.<sup>124</sup> Although it disregards the nature of statutory law and its place in constitutional structure of the states, this argument has a virtue that it results in continuity of the "law" when nothing more is said on the point.

(c) The third proposition has much support in the writing of the authorities on the subject of statutory interpretation and construction.<sup>125</sup> If one turns to the "law" as if the N.I.L. did not exist he is first remitted to the effect of the cases and the common law (B and C above).

The cases and the common law in the field are both of dubious authority. Whether or not they are to be carried forward depends upon whether or not they were decided before or after enactment of the N.I.L.

As to those cases decided after the enactment of the N.I.L. there is considerable difficulty. There are two arguments as to these cases. First, is

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124. See, *e.g.*, U.C.C. §§ 2-302, comment 1; 3-419, comment 5; 4-103, comment 2; 7-203, comment; 7-301, comment 3; 7-501, comment 1; 8-202(1), comment 1; 8-208, comments. Compare *Fairbanks, Morse & Co. v. Consolidated Fisheries Co.*, 190 F.2d 817, 822 n.9 (3d Cir. 1951), with *United States v. Wegematic Corp.*, 360 F.2d 674 (2d Cir. 1966).

125. See authorities cited note 123 *supra*.



the one set forth by Landis that cases decided under the statutes may become part of the common law.<sup>126</sup> The common law is, of course, consulted when the statute is silent. Second, granting Landis' position that these cases may be absorbed into the common law and therefore may be pertinent when the Code is silent, what is the effect of the repeal of the statute under which they were decided? To continue to give them the effect of "law" after repeal of the supporting statute is to defy the laws of legal gravitation, yet there is much support for this sort of thing in the comments to the Code.<sup>127</sup> As a practical matter, this interpretation preserves all of the conflict in the cases under N.I.L. section 59,<sup>128</sup> which the Code was supposed to remove.

This remits us to the "common law" before the enactment of the uniform laws (C above). Here again the comments to the Code often refer to such "law"<sup>129</sup> as the basis for rules set out in the Code. As often pointed out before,<sup>130</sup> this "common law" of bills and notes is largely a fiction, and to return to it in this case would lead to a gap of almost fifty years in the law of most states.<sup>131</sup> It would also require the return to the authority of ancient cases or statutes in each state, which, if they exist, were in a state of chaos.

Perhaps a better result can be reached by construction of rules based upon articles of the Code (D above). As already indicated, the Code offers satisfactory rules for handling cases in which the holder sues a prior party on the instrument. Why not apply similar rules to contests between holders and other parties with claims on the instrument? This could be accomplished simply by treating section 3-307(2) as if it said, "production of the instrument entitles a holder to recover on it *or retain clear title to it* unless the defendant establishes a defense *or valid claim to it*." Then treat subsection 3-307(3) to read, "After it is shown that a defense *or claim* exists." The rights of the parties would then be determined by a uniform procedure in all cases whether the holder was the plaintiff or the defendant. This is the first type of construction advocated by Pound in the material quoted above<sup>132</sup> and would correspond to the approved manner of applying codes in Europe.

126. Landis, *Statutes and Sources of Law*, in *HARVARD LEGAL ESSAYS* 213 (1934).

127. See, e.g., U.C.C. §§ 3-415, comment 4; 3-503, comment 1; 3-803, comment; 7-501, comment 4; 8-304, comment 1; 8-306, comment 3.

128. See BRANNAN, *op. cit. supra* note 102, at 859-91.

129. See, e.g., U.C.C. §§ 3-303(a), comment 3 (returning to idea of value before N.I.L.); 3-413, comment (*Price v. Neal*); 3-417, comment 4 (*Price v. Neal*); 3-418, comments 1, 2 (*Price v. Neal*).

130. See BRANNAN, *op. cit. supra* note 102, at 72.

131. The N.I.L. was enacted over a period from 1897 to 1933. See *id.* at 1356-60.

132. Pound, *supra* note 120, at 385.

This simple and practical construction has only one difficulty. In jurisdictions which have practice statutes or court rules affecting this problem (E above), one would run into the well-established common law rule of construction that statutes are not to be carried beyond their plain meaning to repeal other statutes.<sup>133</sup> These practice acts are legion.<sup>134</sup> An examination of them is beyond the scope of this paper and should be left to scholars of evidence. Court rules, either as delegated legislation<sup>135</sup> or on their own authority, are also common but too complicated to be examined here. It is clear that these are superseded by the Code in cases in which the holder is the plaintiff. There is also every reason in simplified practice and in the interest of uniformity as commanded by sections 1-102(1) (a) and (c) why they should be overturned by the suggested construction of section 3-307. There is no necessity for courts in construing code statutes in the last half of the twentieth century, when most of our law is statutory, to be bound by medieval rules created when statutes were exceptional and cases were the body of the law. To refuse to so construe the Code would be to admit that it has introduced unbearable intricacies and confusions into the pleading and practice of cases involving negotiable paper.

#### D. *The Presumptions as They Affect Securities—Article 8*

In cases involving securities there are the same classifications of the effect of presumption as in the cases of commercial paper: presumptions of holding in due course generally, in suits on the paper, and in contests over title to the paper.

As is the case in Article 3 there seems to be no general presumption that a holder is a bona fide purchaser.<sup>136</sup> So far as the reissue of securities is

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133. See BLACK, *THE CONSTRUCTION AND INTERPRETATION OF THE LAWS* 351, 367 (2d ed. 1911); DWARRIS, *op. cit. supra* note 123, at 154. Now just give this a little nudge and apply it to common law statutes and court rules. See CRAIES, *op. cit. supra* note 123, at 308.

134. *E.g.*, CAL. EVID. CODE §§ 637, 660; ILL. REV. STAT. ch. 110, § 43(4) (1956); see Cleary, *Presuming and Pleading: An Essay on Juristic Immaturity*, 12 STAN. L. REV. 5, 24 (1959). For an example of the proliferation of these statutes see 10 WIGMORE, *EVIDENCE* 24-125 (1940). By no means all these statutes apply to this problem; but they give some indication of the research necessary to collect all this material.

135. See, *e.g.*, 28 U.S.C. § 2071 (1964); FED. R. CIV. P. 8(c); ILL. REV. STAT. ch. 110, § 2 (Supp. 1966).

136. In spite of the fact that the definition of "holder" in § 1-201(20) applies to investment securities, and in spite of strenuous criticism, *e.g.*, Beutel, *The Proposed Uniform [?] Commercial Code Should Not Be Adopted*, 61 YALE L.J. 334, 341 (1952); Beutel, *The Proposed Uniform Commercial Code As a Problem in Codification*, 16 LAW & CONTEMP. PROB. 141, 152-53 (1951), U.C.G. § 8-302 uses the term "bona fide purchaser."

concerned, there seems to be a duty to inquire into the rights of a holder,<sup>137</sup> and the transferee, with the exception of a bona fide purchaser, gets the rights of his transferor in the same manner as in commercial paper.<sup>138</sup>

In suits on the security, section 8-105(2) sets out almost verbatim section 3-307 as it applies to securities.<sup>139</sup> With minor variations,<sup>140</sup> then, the presumptions and burden of proof in suits on securities should be almost the same as in suits on commercial paper discussed above.

When one turns to contests between claimants to the same security, which are far more numerous than suits on the security itself, Article 8 like Article 3, is eloquent in its silence in regard to presumptions and burden of proof. To be sure, the presumption of genuineness can be reached by easy analogy to section 8-105(2), even though it specifically covers only suits on securities. There is the ever present opposite analogy to sections

137. U.C.C. §§ 8-401 to -403 contrast to the rights to pay commercial paper under U.C.C. § 3-603.

138. Compare U.C.C. § 8-315, with U.C.C. §§ 3-306 and 3-207(2).

139. The subsection reads:

- (2) In any action on a security
- (a) unless specifically denied in the pleadings, each signature on the security or in a necessary indorsement is admitted;
  - (b) when the effectiveness of a signature is put in issue the burden of establishing it is on the party claiming under the signature but the signature is presumed to be genuine or authorized;
  - (c) when signatures are admitted or established 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
  - (d) after it is shown that a defense or defect exists the plaintiff has the burden of establishing that he or some person under whom he claims is a person against whom the defense or defect is ineffective (section 8-202).

Compare U.C.C. § 8-105(2), with U.C.C. § 3-307 (set out in note 67 *supra*). It should be noted that "defect" as used in U.C.C. §§ 8-105(2)(c)-(d) is a sort of "real defense," U.C.C. § 8-202, and not a "defect of title" as used in the N.I.L.

140. It should be noted that the draftsmen removed the earlier direct deference to the remedies of U.C.C. § 3-307, 1956 RECOMMENDATIONS 226-27, and restated the section clearly limiting it to "actions on the security." They also made certain changes in subsection (3) requiring the holder to show that he was "in all respects a holder in due course." These changes may make some difference in the procedure and in the results discussed above. See note 80 *supra*; U.C.C. §§ 8-202; 8-204; 8-304 to -305; 8-308; 8-401 to -403.

In all respects a "holder in due course" also had to be changed to "a person against whom the defense or defect is ineffective" because the requirements of taking with freedom from claims and defenses are different. The former is covered by U.C.C. § 8-302, which requires value, *good faith*, and *no notice*; the latter is in U.C.C. § 8-202(4), which requires only purchase for value and no notice of the "particular" defense. It is doubtful if the draftsmen meant to leave out *good faith*. See U.C.C. § 1-203. U.C.C. § 8-202, comment 4, uses the expression "bona fide purchaser" in this context. This is further evidence that the Code was intended as a collection of special statutes rather than a general enactment of the law.

8-401 to -403, which require issuers to inquire into the signature before they reissue securities. There are also sections 8-304, 8-305, and 8-310 which charge holders with, or withhold from them, certain claims which raise nice questions of proof of facts leading to substantive results.<sup>141</sup> Here again there is a silence as to presumptions and burden. In these circumstances there are the same considerations of the effect of the repeal of N.I.L. section 59, the force of previous cases, and the authoritative rules of practice which are present under Article 3, discussed at length above.

There is one further consideration. Article 8, Investment Securities, is a codification and combination of the laws of three fields: negotiable bonds, formerly controlled by the N.I.L.; stocks, previously governed by the Uniform Stock Transfer Act; and bonds, non-negotiable by the N.I.L., subject to the common law and to numerous state statutes. Here, if one takes the traditional historical approach to the subject, the considerations would be even more complicated than they were under Article 3, Commercial Paper. It seems, however, that it should be recognized that "securities" are a new legal device created and governed by the Code. It would, in the absence of clear provisions to the contrary in the Code itself, be better to apply the analogies of section 8-105 uniformly to all proof in suits on or involving title to securities. If this is done, there will be a uniform method of procedure for commercial paper and securities.

One court of first instance has required of the claimant of an admittedly validly indorsed stock certificate the burden of proving a defect in a negotiation to the holder.<sup>142</sup> This is a good beginning.

#### *E. Documents of Title, Presumptions, and Burden of Proof—Article 7*

Article 7 of the Code, on Warehouse Receipts, Bills of Lading, and Other Documents of Title, like the uniform laws it replaces, seems to have no provisions affecting the problem at hand. To be sure, as indicated above, section 1-202 has a provision for prima facie authority of third party documents,<sup>143</sup> specifically including bills of lading and, by inference, other documents of title; but it contains no presumptions on holding in due course or provisions on shifting the burden of proof. The fact that this section, found in a general article on principles of interpretation, overlooks most of the subject matter of this paper, and the fact that the rest of the

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141. See *Welland Investment Corp. v. First Nat'l Bank*, 81 N.J. Super. 180, 195 A.2d 210 (1963) (not citing U.C.C. § 8-105).

142. *Morrison v. Liberty Discount & Sav. Bank*, 61 Lack. Jur. 37 (Pa. C.P. 1958) (again the court did not cite U.C.C. § 8-105).

143. For the text of this section see note 117 *supra*. See also U.C.C. § 7-501, comment 4. Just what is meant by this comment is not clear.

Code treats it only in a fragmentary fashion, is further proof of the compartmentalized thinking of the draftsmen.

Here again, there arises the problem of construing silence. Unlike the sections already discussed, Article 7 seems to be silent on the matter of burden of proof both in suits on the document and in contests to determine title to the paper or the goods which it represents. Since the previous uniform laws also contain no provisions on this point, it would be a good place to argue for a continuation of the common law cases, if indeed previous cases could be considered "common law."

Here an interesting problem of construction arises. Although the previous uniform laws also appear to be silent on this particular point, their commissioners' notes contain many references indicating that in the area of negotiability they intended to adopt the rules in regard to negotiable bills and notes.<sup>144</sup> Mr. Williston, the draftsman of the Acts, stated this intention in his treatise on sales,<sup>145</sup> and also spoke often of the apparent ownership of holders of documents of title.<sup>146</sup> Some cases decided under these statutes are even more specific in stating the rule almost verbatim as it was under N.I.L. section 59,<sup>147</sup> and citing interchangeably cases under the N.I.L. and under other uniform statutes.

If ever there was a place where an argument could be made in the face of silence in the Code for a continuation of the rules of the cases, this seems to be it. However, N.I.L. section 59, the statutory foundation of the rule, has been repealed; also the cases, as indicated above, were not entirely uniform.<sup>148</sup> The Code, where it covers the subject, uses different language and gets different results. It might be wise in the interest of uniformity as required by section 1-102, to construe the sections cited above broadly and apply them to all cases of the burden of proof arising under Article 7. This would also be in accord with the tradition of those cases which applied the rule of N.I.L. section 59 to documents of title under the previous uniform laws. It would also follow the code construction as developed by experience and understood in the civil law world.

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144. Commissioners' Notes to the following sections: B.L.A. §§ 26, 28, 31, 34, 35, 41, 51, 52, 53; S.A. §§ 27, 28, 29, 35, 36, 37, and substitute §§ 32, 38; W.R.A. §§ 38-40, and substitute §§ 40, 44, 56, 58. See BEUTEL, *UNIFORM LAWS, CASES AND MATERIALS* (Supp. 1950).

145. 2 WILLISTON, *SALES* § 408 (1948).

146. *Id.* at §§ 291-92.

147. See, e.g., *Greenwood Grocery Co. v. Canadian County Mill*, 72 S.C. 450, 52 S.E. 191 (1905); *Young v. Harris-Cortner Co.*, 152 Tenn. 34, 268 S.W. 1120 (1925); *National Bank v. Chatfield*, 118 Tenn. 481, 101 S.W. 765 (1907).

148. See Annot., 18 A.L.R. 18 (1922).

## V. THE NECESSITY AND TECHNIQUE OF AMENDMENT

Although it seems that the construction suggested above is a sensible, if not a simple, way to take care of the hiatuses in the Code as to the effect of presumptions and burden of proof in cases, it still does not solve the problem of presumptions of holding in due course outside of the cases between the parties and claimants which are covered by N.I.L. section 59.

It may well be that the repeal has killed all the advantages which accrued to an apparent holder outside of court. One need not cry crocodile tears if this has happened because the holder of negotiable paper already has too many advantages for the social good. But has it? The complicated rules here suggested are not some nightmare dreamed up by a carping critic, they are a bona fide attempt to simplify and unify the written law of the land. There is now the question of whether or not our court system can digest such technical changes without shattering the methods of pleading and practice. If they cannot, the damage flags are flying. Perhaps lawyers will not change their habits. Perhaps the judicial process of digesting radical new fragmentary rules will be too slow. It may be that judicial procedural reform is already overdue and the Code only indicates a wider necessity. Perhaps businessmen will tire of the whole judicial process and adopt other methods of settling their disputes.

The present Code and the organization surrounding and sponsoring it offer two solutions: (1) creation of new rules by contract between members of the business community, which may entirely shortcircuit the cumbersome and complicated judicial administration of the rules of the Commercial Code; (2) constant study and reorganization of the Code itself.

(1) The first alternative, the creation by contract of new rules and procedures by which the business community can govern itself outside of and in spite of the Commercial Code, was contemplated and approved by the draftsmen. Article 1 states this purpose,<sup>149</sup> and the legislative history shows

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149. Section 1-102. Purposes; Rules of Construction; Variation by Agreement.

(1) This Act shall be liberally construed and applied to promote its underlying purposes and policies.

(2) Underlying purposes and policies of this Act are

(a) to simplify, clarify and modernize the law governing commercial transactions;

(b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;

(c) to make uniform the law among the various jurisdictions.

(3) The effect of provisions of this Act may be varied by agreement, except as otherwise provided in this Act and except that the obligations of good faith, diligence, reasonableness and care prescribed by this Act may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.

(4) The presence in certain provisions of this Act of the words "unless otherwise agreed" or words of similar import does not imply that the effect of other provisions may not be varied by agreement under subsection (3).

the intent to give it full effect.<sup>150</sup> There are also many other sections allowing commercial contracts to supersede the Code.<sup>151</sup> The Code also approves many self-help remedies resting in the hands of businessmen, bankers, and creditors.<sup>152</sup> The practical workings of these extra-legal devices are not always in line with the fairness demanded by a good legal order.<sup>153</sup> These provisions carry the danger that sophisticated, rich, and powerful businesses may, by standard contract provisions or procedures, take advantage of their unsophisticated and poorer customers. This practice is already well established in the consumer credit field, and is likely to spread under the benign influence of the Code.

The Code also contains an even greater threat to the balance of the market. The provisions of section 4-103 allowing change not only by agreement of the parties but also by "Federal Reserve regulations, operating letters, clearing house rules, and the like" give third parties power over transactions where the consumer cannot protect himself. The unfairness and danger of these provisions have already been commented upon by the writer,<sup>154</sup> with the approval of one of the draftsmen,<sup>155</sup> and need not be further elucidated here, except to point out that giving businessmen the right to supersede the law by agreement contains dangers now being graphically illustrated by the riots in Chicago and elsewhere. The economic causes here are by no means limited to color but can be traced to unfair business practices which affect all races.<sup>156</sup>

(2) The second method of improvement by constant revision offers intriguing possibilities which are being developed by the American Law Institute and the Commissioners.

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150. 1956 RECOMMENDATIONS 1-3. See also N.Y.L.R.C. Report 357 (1956); N.Y. L.R.C. Study 141-56 (1955).

151. See, e.g., U.C.C. §§ 2-303; 2-316; 3-511(2)(a), (5); 4-103; 5-102(2); 5-106(1); 5-110(2); 5-111; 7-202(3); 7-204; 7-303; 8-107; 8-202(1). See also Loiseau, *Default Proceedings Under the Texas Uniform Commercial Code*, 44 TEXAS L. REV. 702 (1966). How far this policy applies to Article 9 should be the basis of a separate study.

152. See, e.g., U.C.C. §§ 2-209, 2-316, 2-706, 4-212, 9-503, 9-504. See also Norton v. National Bank, 240 Ark. 143, 398 S.W.2d 538 (1966). These are only a few. Many more can be found.

153. For example, note the workings of service charges for overdrawn checks. BEUTEL & NEGRON, *THE OPERATION OF THE BAD CHECK LAWS OF PUERTO RICO* 20, 53, 55 (1966).

154. See Beutel, *supra* note 136.

155. Gilmore, *The Uniform Commercial Code: A Reply To Professor Beutel*, 61 YALE L.J. 364, 375-77 (1952).

156. See N.Y. Times, Oct. 11, 1966, p. 391, col. 4 (city ed.).

## VI. THE POSSIBILITIES OF THE PERMANENT EDITORIAL BOARD

While the Code was in the hands of the New York Law Revision Commission as indicated above, a new editorial board was created to consider amendments. This board has now been made permanent and is in the continuing process of considering and recommending amendments to the Code. The procedure is to study the suggested amendments, draft them, and circulate them "among all state bar associations, all state banker associations, all state chambers of commerce, all state legislative reference bureaus, or similar agencies, and all services reporting decisions under the Code."<sup>157</sup> After a proper length of time, the board then approves recommendations in the form of amendments which are suggested to state legislatures for enactment.

Whether or not the definitive problems raised in this paper are considered a proper basis for amendments, it is clear that the Permanent Editorial Board represents an important step forward in the development of the science of legislation. It is in the spirit of the recommendations of Mr. Justice Cardozo for a ministry of justice,<sup>158</sup> and in accordance with the latest developments in experimental jurisprudence and systems engineering.<sup>159</sup>

There are at least three difficulties which beset the board as presently constituted. (1) There may be considerable doubt whether it is properly representative of the interests involved in the operation of the Code. (2) It does not seem to have the resources, staff, or motivation to make proper empirical studies of the operation of the Code. (3) The practical problem of getting a flow of continuing amendments, which are certain to come, adopted by over fifty legislatures is at present beyond solution.

(1) There is no doubt that the present method of choosing the board leaves out of consideration such great economic interests as consumers, labor, and the general public. The fact that the American Law Institute and the Commissioners on Uniform Laws, in spite of their diligent desire to operate *pro bono publico*, are private law-making organizations not representative of the needs of the society has been pointed out at length elsewhere and need not be further elucidated here.<sup>160</sup> It is therefore essential

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157. Schnader, Report as Chairman, Commercial Code Committee, Commissioners on Uniform Laws, 1966 Meeting, Montreal, p. 4.

158. Cardozo, *A Ministry of Justice*, 35 HARV. L. REV. 113 (1921).

159. See BEUTEL, *DEMOCRACY OR THE SCIENTIFIC METHOD IN LAW AND POLICY MAKING* 133 (1965). Massachusetts has a special commission empowered to amend the Code. Mass. Acts 1957, ch. 756, § 20, at 938.

160. See Beutel, *Law Making by Professional and Trade Associations*, 34 NEB. L. REV. 431 (1955); BEUTEL, *op. cit. supra* note 159, at 60.



that although this board is an excellent beginning, it must be made more representative of the public in general and should not remain an appendage of the organized bar alone. This might be accomplished by attaching it to the Council of State Governments or by an interstate compact as suggested below.

(2) The board as presently organized is largely a voluntary service organization. It depends for material upon court decisions or spontaneous suggestions brought to it. A commercial code, if it is successful, will regulate the everyday activities of the people in the fantastic depth which is our modern complicated society. Many of the present maladjustments do not get to court nor do they come to the attention of legal scholars. Business organizations and professional reports are certain to be slanted, and the public interest is missed. Only carefully directed, scientific, social research can reveal the real workings of the law. This requires a permanent staff and large continuing expenditures of money, which, over the long run, will make the nearly one million dollars spent up to now on the Code seem like small change. So the present board is without resources as well as economic distribution of interest to handle such a problem.

(3) The third difficulty, getting a legislature to adopt suggested amendments, is the practical stumbling block upon which the project is certain to fall even if it can meet the other two objections. The board has already suggested numerous amendments; but their reception by the states has been pretty dismal.<sup>161</sup> It is not surprising that the legislatures, having adopted on faith a modern Code which was to solve the problems of unifying the commercial law, will look with jaundiced eyes upon a steady flow of amendments to the Code. So it is not surprising that only about a third of those approached have approved the amendments. In addition, there are local eager beaver legislatures which have succeeded in getting 750 non-uniform amendments into 244 of the Code's 399 sections as originally adopted in the forty-nine jurisdictions.<sup>162</sup> These gentlemen and their kind are not likely to approve deletion of their handywork. The history of attempts to amend the old uniform laws, which were failures, gives some indication of what is to be expected in the way of resistance to amendments.<sup>163</sup> But no man, or group of men, is able to create a code which will not have to be changed to keep up with the advances in our dynamic society. So no

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161. See Permanent Editorial Board for the Uniform Commercial Code, Report No. 1 (1962).

162. See Schnader, *supra* note 157, at 2. For an earlier compilation see Permanent Editorial Board for the Uniform Commercial Code, Report No. 2 (1965).

163. See Schnader, *supra* note 157, at 3.

matter how good one thinks the Code is, amendments are necessary and the Permanent Editorial Board is a step in the right direction.

How then, can the board be organized so that it will be at the same time well balanced, well staffed, and effective in keeping the law up to date?

There are two possibilities. Such a board might be created by a compact between the states with delegated power to make the necessary amendments to the law of all jurisdictions, and with appropriations sufficient to meet the need. This idea, though intriguing, and constitutional, is almost too impractical for consideration. Our outmoded system of separate states is not likely to reorganize itself in this fashion.

Mr. Schnader has suggested a second excellent possibility, the enactment of a United States Commercial Code.<sup>164</sup> If we are ever to get complete or substantial uniformity then this will be necessary. If McClung's Barbecue stand in Atlanta is subject to the commerce clause of the federal constitution,<sup>165</sup> then there is power in the federal government to regulate "Commerce with the foreign Nations and among the several States, and with the Indian Tribes"<sup>166</sup> by way of a uniform commercial code. Before this is attempted, the Congress should create an impartial body to study the problems with a view to passing a code and delegating to a federal administrative body the power to promulgate necessary amendments in much the same manner as they created the Federal Aviation Agency.<sup>167</sup>

To adopt the present Code with a few amendments intended to fit it for federal enactment would only lead to more trouble.

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164. See Schnader, *supra* note 157, at 7.

165. Katzenbach v. McClung, 379 U.S. 294 (1964).

166. U.S. CONST. art. I, § 8.

167. For this history see BEUTEL, *op. cit. supra* note 159, at 209.