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John M. Feeney Jr.
University of Pittsburgh

Herbert L. Sherman Jr.
University of Pittsburgh

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AN EXAMINATION OF THE NEGOTIABILITY CONCEPT OF THE UNIFORM COMMERCIAL CODE

HERBERT L. SHERMAN, JR.* AND JOHN M. FEENEY, JR.†

INTRODUCTION

A hasty glance through the index of legal periodicals quickly discloses the generous number of articles that have been written on the general subject of the proposed Uniform Commercial Code. Although some have become dated by the frequent revisions of the Code, the great majority are still valid. Generally speaking, most of the published articles have treated specific divisions and sections of the Code, or have examined the high points throughout the entire Code. Invariably they compare the Code with all the leading uniform acts now in existence.

The aim of this undertaking, however, is to examine the impact, if any, that the new Uniform Commercial Code may have on our concept of negotiability as it has evolved to the present time. Analysis will be confined to this one broad topic, but our considerations are not limited to one section of the Code. Although analytical thought about the negotiability concept has been applied to its many segments, which we call rules, apparently nothing has been written on the Code that has emphasized the expansion of the concept itself which is now possible.

The inspiration for this article stems from the ostensibly innocent words "within this article" found in Section 3-104 of the Uniform Commercial Code.¹ It is contended that these words could completely change the historical policy of the courts and launch us into an entirely new era for the negotiability concept. A full understanding of this position can only be gained by an inquiry into the historical development of negotiability.

* Assistant Professor of Law, University of Pittsburgh.

† Third Year Law Student, University of Pittsburgh.

1. UNIFORM COMMERCIAL CODE § 3-104 (1952). All future references will be to this draft. It might be noted that this is the final draft; in this form it has already been introduced before several state legislatures.

The first part of Section 3-104 is as follows: "(1) Any writing to be a negotiable instrument within this Article must. . ." Thereafter, the well-known formal requisites of negotiable paper are set forth.

HISTORICAL BACKGROUND

Roughly speaking, the law merchant had its most unfettered and spontaneous growth from the time of the Norman Conquest until the decline of the staple system during the sixteenth century.² During these four or five hundred years, the law merchant was a separate body of law that developed solely from the custom and practice of merchants and was administered by merchants. This development reached its peak with the establishment of the staple courts in 1353 by the Statute of Staples.³ By resort to these courts the merchants were able to receive justice based on their own business customs without hazarding the procedural rigidity of the common law courts. The concept of negotiability became highly developed during this period, as did the law of assignments. The staple courts followed the policy of allowing the merchants to develop, through custom, new types of instruments and to make alteration in the existing ones as they became necessary.

The decline of the staple courts was paralleled by an assumption by the common law courts of jurisdiction over mercantile disputes. At first these courts were willing to listen to evidence as to the nature of the law merchant. Their generosity, however, soon faded; they began to speak in terms of the law merchant's being part of the common law, and they started to enunciate their own ideas of what the law merchant had been. This resulted in a repudiation of a sizable portion of the law merchant. Open contempt for commercial practices reached its height when Lord Holt held that promissory notes were non-negotiable in the celebrated English case of *Clerke v. Martin*.⁴ This and similar decisions set the negotiability concept back nearly 300 years. The plight of the merchant remained acute until the fortunate ap-

2. BRANNAN & CHAFEE, *THE NEGOTIABLE INSTRUMENTS LAW*, 2-19 (7th ed., Beutel 1948).

3. This was the most important commercial law enacted in medieval England. The courts set up by the statute had jurisdiction over all things concerning staple commodities. This jurisdiction extended over contracts, torts and crimes. The courts were presided over by the mayors of the staple cities, who were required to be learned in the law merchant. The important thing to remember is that these courts were in no way connected with the common law system. *Id.* at 12.

4. 2 Ld. Raym. 757, 91 Eng. Rep. 6 (K.B. 1702). The unfortunate result in this case led to the enactment of the Statute of Anne, 3 & 4 ANNE, c. 9 (1704). This act established the negotiability of promissory notes and codified that part of the law merchant.

pointment to the bench of Lord Mansfield, the father of our modern commercial law. Commencing with his famous decision in *Miller v. Race*,⁵ he began to formulate the law merchant as we know it today, which was ultimately codified by the English Bills of Exchange Act.⁶ Except, however, for the friendly hand extended by Mansfield, the attitude of the judiciary, when confronted with business needs in this regard, has often reflected a lack of sympathy.

In the United States, the law of negotiable instruments remained largely uncodified until the cure-all philosophy of codification swept this country during the latter part of the last century. This development, that was fostered by David Dudley Field, the great codifier, and the jurists of the analytical school, finally resulted in the enactment of the Uniform Negotiable Instrument Law as we know it today.

This brief outline demonstrates that the concept of negotiability has been growing and changing ever since the Jews began to circulate *starrs*⁷ soon after the Norman Conquest. Has this evolution reached the end of the line? Has the concept of negotiable instruments reached a point where there is nothing left to be desired? It does not seem that an affirmative answer would be any more appropriate now than it was during the eighteenth century when progress in this respect was momentarily halted.⁸

In spite of this obvious truism, however, the overall attitude of the courts has been one of opposition to any change instigated by the commercial world. Similar resistance by the legislatures has likewise been evident.⁹

Whenever this resistance has weakened and the existing law has been changed, it usually became crystallized as of the date of the change, and the process started all over again. No affirmative

5. 1 Burr. 452, 2 Keny. 189, 97 Eng. Rep. 398 (K.B. 1758) (holding that ownership of a negotiable instrument may be acquired through a thief).

6. 45 & 46 Vict., c. 61 (1882), drafted by Judge Chalmers in 1881.

7. This was probably the earliest type of negotiable paper known to Anglo-Saxon jurisprudence. Its purpose was to be a written evidence of a debt, such type of transaction being peculiar to the Jews because their religious beliefs did not prevent the charging of interest as did the Christian religion.

An adequate bibliography of this period may be found in BRANNAN & CHAFEE, *op. cit. supra* note 2, at 8-9.

8. See Clerke v. Martin, 2 Ld. Raym. 757, 92 Eng. Rep. 6 (K.B. 1702).

9. For an excellent discussion of the problem, see Devlin, *The Relation Between Commercial Law and Commercial Practice*, 14 MOD. L. REV. 249 (1951).

policy has ever been followed whereby the necessary flexibility was provided which would permit desirable changes.

Perhaps the outstanding example of crystallization of existing law is the Negotiable Instruments Law itself. Section 1 of this Act states emphatically that, "[a]n instrument to be negotiable *must conform* to the following requirements."¹⁰ [Italics supplied] Thus, the formal requisites of negotiability became frozen as of the time a state adopted the Negotiable Instruments Law; and the development of any new type of negotiable instrument was stymied.

A partial explanation of the broad, sweeping, all-inclusive language of Section 1 of the Negotiable Instruments Law may be found in the historical background of the Act. J. J. Crawford of New York relied heavily on the existing California Civil Code¹¹ in drafting the proposed Negotiable Instruments Law.¹² The California Code also set out stiff requirements for negotiability; in fact, the similarity of the mandatory wording of the two acts is striking. The most important reasons which have been advanced that prompted this complete coverage are twofold: first, the California Code was spreading in popularity so that the uniform law had to be more than a mere narrow rival; and second, the conflicting welter of statutes dealing with negotiable paper in the various states had to be repealed *in toto*. Partial repeal would probably have resulted in even greater confusion than existed previously.

CONSEQUENCES OF THE "MUST CONFORM" POLICY OF THE NEGOTIABLE INSTRUMENTS LAW

Legal history is filled with the conflict between those who favor certainty and those who favor flexibility. The Negotiable Instruments Law is an extreme example of the desire for certainty. While the result of certainty may have been achieved for the aforementioned practical purposes, there is little doubt that the expedience of the moment had unfortunate consequences.

The stereotyping effect of codification was exhibited in the

10. Then follows a listing of the formal requisites for negotiable instruments. The next nine sections elaborate on and attempt to provide guideposts for the proper construction of Section 1.

11. It might be noted that the California Civil Code was drafted by David Dudley Field, who was referred to earlier in this article as the leading exponent of codification during the latter part of the 19th century.

12. BRANNAN & CHAFEE, *op. cit. supra* note 2, at 76-78.

well-known case of *Manhattan Co. v. Morgan*.¹³ That case concerned the negotiability of interim receipts. The receipts did not call for payment of "a sum certain in money"¹⁴ but were payable to bearer in Belgian bonds "when, as, and if" issued. The receipts had been stolen, and, therefore, the crucial question was whether the receipts were negotiable and enforceable by a good faith purchaser. Considerable evidence was introduced to prove that these instruments had, by virtue of custom and usage, long enjoyed the status of negotiable instruments. The court held that the receipts failed to meet the compulsory requirements of the Negotiable Instruments Law. They were not payable in money, nor payable at a time certain. While paying deference to the argument that permitting the business world to create new methods and instruments would result in social gain, Justice Cardozo said in the course of the opinion:

. . . [T]he law merchant is without capacity to make instruments negotiable against the express prohibition of a statute, which says that they are not negotiable.¹⁵

The New York Court of Appeals did recognize the possibility of negotiability by contract or by estoppel. In view, however, of some collateral statements made by the same court, this avenue of escape from the rigid requirements of the Negotiable Instruments Law would not seem to hold much promise for New York litigants. In *Enoch v. Brandon*¹⁶ the bonds involved contained a provision that "the bonds are to be treated as negotiable and all persons are invited by the company to act accordingly." Nevertheless, by way of dictum, the court said, "[b]ut no such statement will make negotiable a bond not in the form provided for by our statute."¹⁷ Also, in *Manhattan Co. v. Morgan*, the court asserted that negotiability by contract or estoppel would not arise merely by virtue of the fact that the document called for payment to bearer.¹⁸ Therefore, the chance of bringing a case within the suggested exception would appear to be small indeed.

Another, and far more common class of instruments that are clearly not negotiable within the purview of the Negotiable In-

13. 242 N.Y. 38, 150 N.E. 594 (1926). A number of other decisions might be cited, such as *Millard v. Green*, 94 Conn. 597, 110 Atl. 177 (1920).

14. NEGOTIABLE INSTRUMENTS LAW § 1 (2).

15. *Manhattan Co. v. Morgan*, 242 N.Y. 38, 48, 150 N.E. 594, 597 (1926).

16. 249 N.Y. 263, 164 N.E. 45 (1928).

17. *Id.* at 266, 164 N.E. at 46.

18. *See* 242 N.Y. 38, 50, 150 N.E. 594, 598 (1926).

struments Law, because they do not call for payment in money, has been stamped with the attributes of negotiability as the result of the enactment of other statutes. Bills of lading and warehouse receipts, entitling the holder to delivery of specific goods, were not considered negotiable instruments under the common law view. Such documents of title, even where the words "order or bearer" were used, were considered to be mere symbols of the goods. As to a bill of lading, the Supreme Court of the United States said:

... True, it is a symbol of ownership of the goods covered by it,—a representative of those goods. But if the goods themselves be lost or stolen, no sale of them by the finder or thief, though to a *bona fide* purchaser for value, will divest the ownership of the person who lost them, or from whom they were stolen. Why then should the sale of the symbol or mere representative of the goods have such an effect?¹⁹

The adoption of the Negotiable Instruments Law by a given jurisdiction then gave rise to the possible argument that a bill of lading could not even become negotiable by development of the common law, because of the exclusive wording of the statute. Such a result would have been very undesirable in view of the customary treatment of order bills by businessmen as negotiable. A number of other statutes, however, came into vogue shortly thereafter which quite generally made the above argument academic. The Sales Act and Warehouse Receipts Act recognized negotiable documents of title, although these two statutes only partially adopted the mercantile view, wherein the purchaser of a negotiable document of title may obtain more rights than could a purchaser of the goods themselves. The Bills of Lading Act espoused the full mercantile view at the outset. Subsequent amendments to the Sales Act and Warehouse Receipts Act were recommended by the Commissioners on Uniform State Laws to make the provisions on negotiability harmonious with the Bills of Lading Act.²⁰

To the list of instruments not accorded negotiable status by the Negotiable Instruments Law must be added the share certificate and the equipment trust certificate. The former has been given treatment similar to that of a negotiable instrument by the Uni-

19. *Shaw v. R.R.*, 101 U.S. 557, 564 (1879).

20. UNIFORM SALES ACT §§ 32, 38 (Commissioner's Notes); UNIFORM WAREHOUSE RECEIPTS ACT §§ 40, 47 (Commissioner's Notes).

form Stock Transfer Act, and the latter has been marked with most of the features of a negotiable instrument by some local statutes.²¹ In the absence of such statutes it may be forcefully argued that the implication of the Negotiable Instruments Law is that the rights and privileges attendant upon the finding of a negotiable instrument should not attach to a share certificate or an equipment trust certificate. The same contention may be made with respect to any document, certificate, or receipt which is not controlled by some other statute and under which the obligor has not unconditionally committed himself to the payment of money. In order to reach what the courts have thought desirable results, resort has been had to the weasel words "quasi-negotiable."²² But if this is a proper approach, why not apply the term to any instrument which fails to qualify under the Negotiable Instruments Law but with respect to which there is evidence of usage that it is treated as negotiable? Obviously this would lead to clear circumvention of the opening sentence of the Negotiable Instruments Law and should not be countenanced under any fair principle of statutory construction. The Uniform Commercial Code, therefore, comes as a welcome relief to this dilemma.

UNIFORM COMMERCIAL CODE

The problem of negotiability has not been dealt with in one separate article in the Uniform Commercial Code. In fact, Article 3 on commercial paper, which deals with ordinary commercial instruments such as checks, drafts, and promissory notes, specifically excludes money, documents of title, and investment securities from the scope of its coverage.²³

Commercial Paper

It is the Code's new and basic approach that sparks the feeling that the legislative policy is about to change. Upon enactment of the Code it will be possible to have negotiable instruments that do not fall within this or any other statute governing negotiable paper.²⁴

21. *E.g.*, PA. STAT. ANN. tit. 56, §§ 511-513 (1930).

22. See *Millard v. Green*, 94 Conn. 597, 110 Atl. 177 (1920).

23. UNIFORM COMMERCIAL CODE § 3-103 (1).

24. UNIFORM COMMERCIAL CODE § 3-104, comment 1:

. . . Even if retention of the old statutes is regarded in any state as important, amendment of this section may not be necessary, since

Article 3 specifically controls only those instruments mentioned previously. The article, at least for present purposes, is tailor-made for these instruments. No longer will it be necessary to push the law of negotiable paper all out of shape in order to hold bonds, securities, etc., negotiable.

The comment to Section 3-104 states that an instrument may not be made negotiable within this article by contract or conduct. The tenor of the comment seems to rule out even the possibility of negotiability by estoppel. Estoppel may, however, present a bar to the use of certain defenses which would otherwise be available where a non-negotiable instrument is involved.

Article 3 makes a good many changes in the prior law,²⁵ settles many conflicts in the existing case law that arose under the Negotiable Instruments Law,²⁶ and in some cases it has reverted back to the law merchant.²⁷ Admittedly these changes have an effect on the broad concept of negotiability, but it is felt that they have been amply discussed in other leading articles.

Documents of Title

The framers of the Uniform Commercial Code have rendered a further service to the practitioner by the consolidation of the law affecting documents of title. So many of the provisions of the Uniform Bill of Lading, Warehouse Receipts and Sales Acts overlap that a merger was almost inevitable. Article 7 of the Code is intended to replace the first two statutes and also Sections 27 to 40 of the Sales Act. It was properly decided that these sec-

'within this article' in subsection (1) leaves open the possibility that some writings may be made negotiable by other statutes or by judicial decision. The same is true as to any new type of paper which commercial practice may develop in the future.

Section 1-102 (f) states: "The Comments . . . may be consulted in the construction and application of this Act but if text and comment conflict, text controls. . . ."

25. *E.g.*, Section 3-206 and Section 3-304 (5) (e) of the Uniform Commercial Code are intended to change the result of *Gulbranson-Dickinson Co. v. Hopkins*, 170 Wis. 326, 175 N.W. 93 (1919), which held that an indorsee under an indorsement in trust could not be a holder in due course and must take the instrument subject to any defenses of equities good against his indorser. *But cf.* *Lipshutz v. Philadelphia Savings Fund Society*, 107 Pa. Super. 481, 164 Atl. 74 (1933).

26. *E.g.*, UNIFORM COMMERCIAL CODE § 3-105 (When Promise or Order Unconditional).

27. *E.g.*, UNIFORM COMMERCIAL CODE § 3-406, which adopts the doctrine of *Young v. Grote*, 4 Bing. 253, 130 Eng. Rep. 764 (1827), concerning the negligence of the drawer in writing out the check, so that it "contributes" to the alteration.

tions, relating to documents of title, should not be replaced by similar or revised provisions in Article 2 on sales, but that the topics which they covered should be consolidated in one article.

The specific provisions defining negotiable documents of title, however, cannot be accorded the same approbation. Section 7-104 of the Uniform Commercial Code reads as follows:

- (1) A warehouse receipt, bill of lading or other document of title is negotiable
 - (a) if it provides for delivery to bearer or to the order of a named person; or
 - (b) where recognized in overseas trade, if it runs to a named person or assigns.
- (2) *Any other document is non-negotiable.* [Emphasis added.]

This smacks menacingly of the "must conform to the following requirements" language of the present Negotiable Instruments Law. Sub-section (2) is sweeping in its exclusion of all other documents from the realm of negotiability. Suppose that a bill of lading runs to a named person (the magic words "order" or "bearer" being omitted), and the issuer plainly marks it negotiable. Such a document is a "straight" bill, and a subsequent transferee who purchases in good faith and for value will not acquire the rights granted to a holder who takes upon due negotiations.²⁸ That such a result is mandatory is made clear by the comment to Section 7-104: "A document of title is negotiable only if it satisfies this section." The comment provides no explanation as to why the approach to documents of title is *contra* to that utilized in Article 3. There seems to be no logical reason for the change of heart unless it is felt that the present documents of title are sufficient and that any gain that might result from allowing innovations would be outweighed by the possibility of confusion. It is submitted, however, that it is very difficult to prophesy what will be the future needs of business.

Investment Securities

Bonds, debentures and similar forms of obligations used for investment purposes have been segregated and are treated in Article 8. Share certificates, equipment trust certificates, and interim receipts also fall within the scope of that article which

28. Those rights are enumerated in Section 7-502 of the Uniform Commercial Code.

will replace the Uniform Stock Transfer Act. At the present time bonds are considered as falling within the provisions of the Negotiable Instruments Law. In their desire to find a number of bond issues negotiable, many courts have strained their interpretation of the Negotiable Instruments Law almost to the breaking point. In *Gerber's Estate*²⁹ the pertinent language on the bond read as follows:

. . . This bond shall mature and become due on September 1, 1956, except as otherwise provided herein and in the deed of trust securing this issue of bonds. . . .

. . . This bond is issued and held subject to the terms and conditions of said deed of trust. . . .³⁰

After stating that "whether the bond is negotiable must be determined by what it says, and without resort to instruments not attached to it,"³¹ the court went on to hold that the bonds were negotiable! Fortunately, under the Uniform Commercial Code, the courts will no longer find it necessary to pull and tug in order to squeeze bonds under laws designed to deal with short-term obligations. The investment securities market, which had its most rapid growth after the drafting of the Negotiable Instruments Law,³² has finally come into its own and has been belatedly recognized as deserving separate and unique treatment in the statutory framework.

Under the Uniform Commercial Code the negotiability of a bond will not be destroyed by reference on the face of it to conditions stated in the deed of trust. And most defenses which a holder in due course of a negotiable instrument would cut off will likewise be cut off, under the proposed provisions, by a bona fide purchaser for value of a bond.³³ Still, the conditions stated in the deed of trust will be binding on the good faith purchaser if they do not materially alter or contradict the language set forth on the bond itself. This compromise between the two diametrically opposed poles of the existing law—negotiability versus non-negotiability—is a happy solution which provides for very desirable flexibility.

29. 337 Pa. 108, 9 A.2d 438 (1939). This case is criticized in 6 U. OF PITT. L. REV. 200 (1940).

30. *Id.* at 122, 9 A.2d at 444.

31. *Ibid.*

32. See Cosway, *Innovations in Articles Three and Four of the Uniform Commercial Code*, 16 LAW & CONTEMP. PROB. 284, 286 (1951).

33. UNIFORM COMMERCIAL CODE § 8-201.

Today draftsmen of bonds are subject to two conflicting pressures; one favors an instrument which clearly qualifies under the Negotiable Instrument Law because of the better market, and the other favors the inclusion of numerous conditions to protect the issuer's interest. The latter tends to make the instrument non-negotiable. In fact, that is the proper result if the reference on the bond to the other document conditions the obligation to pay, as distinguished from a reference of the holder to the document to determine the holder's rights as to the security. With the advent of the Uniform Commercial Code, draftsmen of bonds will no longer have to worry about falling in the pond of non-negotiability while skating close to the edge in an attempt to protect the issuer.

PRACTICAL CONSEQUENCES OF THE NEW POLICY

It may well be asked, even in view of the apparent shift in policy manifested by Article 3 of the Uniform Commercial Code, whether there will be any corresponding practical change. Assuming that a businessman is conscious of the legal requirements for an instrument to be negotiable, will he risk the outcome of future litigation by deliberately failing to conform to such requirements when drafting his instrument or having it drafted? Will he do this even if he is familiar with the use of such non-conforming instruments in his field? Will the newly won freedom of the businessman produce any practical changes, or is it merely academic? Of course, even if it is concluded that a businessman would not consciously take such risks, the problem still remains a real one, *i.e.*, what about the inadvertent failure to conform to the requirements where negotiability is desired and the instrument later gets into litigation? Here the existence of a custom becomes crucial.

These questions may not appear to be of too much importance if we only look at the instruments and documents in present use. Such a limited consideration would ignore the historical evolution of the negotiability concept. On the other hand, the authors do not attempt to fill the role of seers in forecasting the precise types of instruments that may come into common use. Yet a look at the historical development of commercial paper will reveal that the present forms are the products of timeless evolution—not perceptible while it is going on and only fully recognized by

belated hindsight. One could undoubtedly discover a good many business practices carried on every day that are far out of line with the existing law. They are prevalent because of convenience and expedience. Who can say what legal status these practices will attain? It is just as impossible to foresee what new instruments will become necessary, as it would have been for the fifteenth century lawyer to visualize our modern concept of a negotiable bill of lading.

History also reveals the method by which these changes have been effected. Businessmen, heedless of the legal yoke placed on them by the legislatures and the courts, constantly attempt to remedy practical deficiencies in their present methods and devise new ways to expedite the conduct of commerce. These new techniques are not created with an eye toward the refinements of jurisprudence but in spite of them. If the new technique proves to be of any real value, it will not be too long before it spreads and becomes an established component of custom and usage. When and if the instrument gets into litigation, it obviously will be of utmost importance to determine whether its use is sufficiently widespread as to fall within the meaning of the Code.

In the past these needs of businessmen have not been properly recognized by the courts. This sort of judicial approach has not only alienated the commercial world but has created many awkward situations. Indeed, some have been so awkward that they even startled the usually slow-moving legislative branch into quick action.³⁴

It is here that the flexibility permitted by the Code becomes most significant. No longer will the courts be bound by rigid requirements which admit of no exception. In this sense a new era is about to begin upon the acceptance of the Code by the legislatures. It will then be possible for the courts to recognize new devices which have acquired the status of custom and usage, arising out of the faster modes of travel and improved media of communication. New and presently unknown methods of credit financing may reasonably be expected in the years to come. Even our most advanced theory of negotiability may become antiquated, requiring modifications to adapt itself to faster methods of distribution.

34. See note 4 *supra*.

LEGAL RAMIFICATIONS OF THE NEW APPROACH

Although it is clear that Section 3-104 does permit new instruments to be developed despite failure to conform with the formal requisites,³⁵ the Code leaves open the question of the attributes of negotiability which may attach to such instruments. Of course, evidence of custom and usage must be produced to warrant a finding that the instrument is treated as negotiable. But then such specific questions may arise as to what defenses will be cut off, whether negligence in drafting an instrument will preclude the defense of alteration, whether an indorsement is essential or whether given marks constitute valid indorsements, etc. Answers to this type of question may not be provided by the evidence which establishes the general customary treatment of the paper as negotiable.

Where should the court look for such answers? It is submitted that there are at least three main possibilities. First, the Uniform Commercial Code could be consulted for guidance. Second, the court could examine the law merchant of the jurisdiction as it stood prior to statutory modification. Third, it could construct an entirely new body of case law which would be peculiarly adapted to achieve the avowed purpose of the new instrument.

The first suggestion would probably represent the most convenient and effortless choice. The Code is a codification of the most advanced equitable rules of negotiability down to the present time.³⁶ It would provide the court with a ready answer to most of the specific questions that may arise. The choice, however, presents difficulties. The new instrument probably developed beyond the pale of the Uniform Commercial Code because of some obnoxious formal requisite set forth in the Code. Giving controlling weight to the consequences that attach to an instrument that conforms to the Code might very well defeat the very reason for the existence of the new instrument.

To support the second alternative which calls for reference to the law merchant, it may be argued that such was the legislative intent when the legislature provided that a negotiable instrument may exist beyond the ambit of the Uniform Commercial Code. Further support for such a position may be found under one

35. See text supported by note 13 *supra*.

36. See Comment to Section 1-103 of the Uniform Commercial Code for the equitable nature of the Code.

possible interpretation of Section 1-103 of the Code, which states that only those parts of the law merchant inconsistent with the Code are repealed. But this alternative would be vulnerable to the same objection as the prior one, that the then existing law merchant is not geared to the function of the new instrument.

Now let us examine the third possibility in the light of Section 1-103. At first blush it would seem the least likely to succeed. Upon close examination, however, it is submitted that it would present the most realistic approach. Section 1-103 states: "Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant . . . shall supplement its provisions."

It is believed that the true meaning of this section can only be discovered by a close reading of Section 1-102 (1), (2) and the appropriate comment.³⁷ In order to implement the policy of this section, the present law should be examined and those segments that have remained valid should be retained, but those segments that have become antiquated and outmoded by actual commercial practice should be discarded. New rules should then be formulated that would be tailor-made to meet the particular needs that gave birth to the new instrument. Such approach would best fulfill the declared policy of the Code.³⁸

37. Section 1-102 (2) (b) reads as follows:

(2) Underlying purposes and policies of this Act are . . .

(b) to preserve flexibility in commercial transactions and to encourage continued expansion of commercial practices and mechanisms *through customs, usage and agreement of the parties* [emphasis added].

38. UNIFORM COMMERCIAL CODE § 1-102.

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CONTRIBUTORS TO THIS ISSUE

PAUL J. HARTMAN—Associate Professor of Law, Vanderbilt University. A.B. 1936, Maryville College; LL.B. 1939, University of Virginia; LL.M. 1949, Columbia University; JUR. Sc.D. 1952, Columbia University. Assistant Professor, University of Virginia, 1946-47; Associate Professor of Law, Wake Forest College of Law, 1947-48. Member of Tennessee, Virginia, and West Virginia Bars.

IVAN C. RUTLEDGE—Associate Professor of Law, University of Washington. A.B. 1934, Carson-Newman College; A.M. 1940, Duke University; LL.B. 1946, Duke University; LL.M. 1952, Columbia University. Member of Georgia and Washington Bars.

HERBERT L. SHERMAN, JR.—Assistant Professor of Law, University of Pittsburgh School of Law. A.B. 1943, Brown University; LL.B. 1948, Harvard Law School. Assistant Chairman, Board of Arbitration for U.S. Steel Corporation and United Steelworkers of America. Author of several articles.

JOHN M. FEENEY, JR.—Third year student at University of Pittsburgh School of Law. B.A. 1950, University of Pittsburgh.