

SECURED TRANSACTIONS – ARTICLE 9

I. Overview

- A. *Scope of Article 9* – applies to *consensual* security interests in (i) personalty & (ii) fixtures
- B. *Attachment* (i.e. create an enforceable S/I in debtor's collateral) – VCR (value, contract, rights in the collateral)
- C. *Perfection* – by placing the world on (i) *record notice* or (ii) *constructive notice* of the creditor's existence
- D. *Priority* – when more than 1 creditor has a stake in the same collateral, the *1st to perfect takes 1st*
- E. *Default* – if debtor defaults, the Article 9 creditor has *statutory & judicial remedies*

II. Scope of Article 9

- A. **Article 9** applies to *voluntary or consensual security interests in personalty (i.e., goods) or fixtures*
 - 1. If collateral is *personalty or fixtures*, apply Article 9
 - NOTE: if collateral is *real estate*, apply the law of *mortgages*
 - 2. Article 9 applies only to voluntary/consensual collateralizations, & therefore **does NOT apply to statutory or mechanics liens**
- B. **Definitions**
 - 1. *Debtor* – entity that owes the money
 - 2. *Secured party/secured creditor* – entity that lends the money
 - 3. *Security agreement* – the contract/record
 - 4. *Security interest* – the right that creditor has in debtor's personalty or fixtures
 - 5. *Collateral* – personalty or fixtures that creditor can look to for satisfaction on the debt
 - a. *Consumer goods* – items used for personal or familial purposes (e.g. car, oven, refrigerator, car)
 - b. *Equipment* – items used in business (e.g. Macy's cash registers, dentist's chair)
 - c. *Inventory* – goods held for sale or lease (e.g. Ethan Allen's furniture line)
 - d. *Farm products* – crops, livestock, & supplies used in farming operations (e.g. eggs, corn)
 - e. *Fixtures* – items annexed to realty (e.g. lighting fixtures, sprinkler systems, furnaces)
 - f. *Intangible or Semi-intangibles* – e.g. patents, trademarks, copyrights, stocks, bonds, mutual funds, proceeds received upon the sale of collateral, accounts (right to pmt for goods or services), promissory notes & drafts
 - NOTE: the key to classifying collateral is the *primary use in the hands of the debtor* (Subjective Test - e.g., golf clubs in the hands of a golf store are inventory, while in your hands they are consumer goods while in Tiger Woods' hands they are equipment)

III. Attachment – creation of an enforceable Security Interest

- A. **Requirements – VCR**
 - 1. **Value** must be given by creditor (secured party)
 - 2. **Contract** – parties must agree to create the Security Interest, by
 - a. **Security agreement** – must be authenticated (signed or electronically marked) by the debtor & reasonably identify the collateral; OR
 - b. **Possession** of the collateral (no need for a security agreement)
 - 3. **Rights in the collateral** – debtor must have rights in the collateral
- B. **“After-acquired collateral clauses”** – are enforceable (e.g. secured party lends 500K to store, taking a security interest “in all of store's inventory, whether now held or *hereafter acquired*”)

IV. Perfection of Security Interests

- A. **Perfection** – is best understood as a *publicity device*
 - 1. It puts the world on (i) *record* or (ii) *constructive notice* of the secured party's existence
 - 2. **Proper perfection helps to protect the secured party from competing creditors**
- B. **Attaining perfection** – *attachment & one of the following*:
 - 1. **Possession of the collateral by secured party** – taking possession = perfection
 - 2. **Automatic perfection for PMSIs (purchase money security interests) in consumer goods** upon attachment
 - PMSI is a *security interest that enables the debtor to purchase the goods*
 - Article 9 loves PMSIs because they fuel commerce so they get special treatment/exceptions
 - 3. **Filing** – the secured party *files notice* of the security interest in *public records*
 - a. Filing Methods

- (i) *Filing a security agreement (rarely filed – too much information contained in it)*
- (ii) **Financing statement** – a very simple document whose only purpose is to provide interest parties with sufficient information to make *follow-up inquiries*
- (iii) **Electronic filing** – encouraged by Article 9 (it’s “media-neutral”)
- b. Contents of a financing statement (simple & short)
 - Name & address of (i) debtor & (ii) secured creditor AND (iii) description of collateral (even generic descriptions like “all of debtor’s assets” are permissible)
- c. **Where is the financing statement filed?**
 - (i) Centrally with the *Secretary of State*, in the *state where the debtor is located*
 - (a) *Individual* – located in the state of his principle residence
 - (b) *Registered organization* – located in the state under whose laws it’s organized
 - (ii) EXCEPTION: if the collateral is (i) *timber*, (ii) *minerals*, or (iii) *fixtures*, file locally, in the *county where the underlying realty is located*

V. Priority

- A. **Basic concept** – secured party seeks to subordinate, each claimant is entitled to *payment in full* before a subordinated claimant is entitled to take
- B. **Interests** (in descending order of priority):
 1. **BIOC** (Buyer in Ordinary Course) – buyer who purchases a collateral from merchant’s inventory
 2. **PAC** (Perfected Attached Creditor) – Article 9 creditor who succeeds in attaining perfection
 3. **LC** (lien creditor) – general creditor who goes to court to get a judicial lien on the collateral
 4. **NOCie** (Non-Ordinary Course Buyer) – someone who purchases the collateral outside the ordinary stream of commerce (e.g., buying a guitar from an auto mechanic – takes collateral at his peril)
 5. **AUPie** (Attached Unperfected Creditor) – Article 9 creditor who creates an enforceable security interest (attaches), but AUPie either: (i) never bothers to perfect, or (ii) tries to perfect but botches it
 6. **GUC** (General Unsecured Creditor) – lender who never bothered to take collateral (last priority)
- C. **Special Contests**
 1. *AUPie v. the world* – enforceable as against: (i) the *debtor*, (ii) any *subsequent AUPie*, & (iii) GUCs
 2. *PAC v. the world* – basic rule that PAC defeats all, except:
 - a. **PAC v. PAC** – 1st in time, 1st in right
 - **Article 9 gives special effect to filing, & allows for early filing, even at the onset of loan negotiations (if an early filer subsequently attaches, he’s allowed the benefit of his early filing), because priority relates back to the early filing date**
 - b. **Certain PMSI-holders** – relevant contest is between:
 - (i) *After-acquired collateral financier* (AACF) – secured creditor who takes as collateral a security interest in all of D’s equipment/inventory, whether *now held or hereafter acquired*, AND
 - (ii) *Purchase-money security interest* (PMSI) – security interest that enables D to purchase the goods
 - (iii) Outcomes:
 - (a) *Collateral is Equipment* – PMSI holder wins if it files properly within *20 days* after the debtor/buyer takes possession of equipment
 - (b) *Collateral is Inventory* – PMSI holder wins if (i) file properly **before** debtor/buyer takes possession, AND (ii) notify the AACF **before** the debtor/buyer takes possession
 - c. *PAC v. BIOC* – general rule that PAC loses to BIOC, who takes free of a perfected security interest in seller’s inventory (*promotes commerce and consumerism & ordinary buyer’s expectations*)

VI. Default – debtor is in breach (typically for failure to pay); secured creditor can:

- A. **Self-Help Repossession**
 1. Permissible, so long as *creditor does NOT breach the peace* (i.e. creditor actions are likely to cause violence)
 - Relevant question whether the secured party did something provocative or likely to cause violence
 2. *Repossession made over any protest by the debtor* – however mild the protest, constitutes a breach of peace
 - If debtor tells the creditor to stop, repossession must stop
 - If *misuses the color of law* (e.g. impersonating cop) then used *constructive force* & breached the peace
 3. *Civil or criminal penalties* attach to creditor’s misconduct:
 - a. *Repossession when the collateral is debtor’s home* – the home enjoys a “*zone of privacy*” & the secured party may not enter the home without *voluntary & contemporaneous consent*
 - b. *Repossession when the collateral is outside the home* – the secured party may take the collateral so long as there is *no debtor objection*

B. Repossession by Judicial Action

1. Secured party may choose to go to court to obtain a judicial writ ordering the sheriff to obtain possession of the collateral & deliver it to the secured party
2. In NY – appropriate writ is called the *writ of replevin*

C. Strict Foreclosure

1. *Defined* – occurs when the secured party retains the collateral in *full satisfaction of the outstanding debt* (BASICALLY, creditor lawfully retains the collateral & in turn, the debt is cancelled). Strict Foreclosure works best when the value of the collateral approximates the value of the outstanding debt.
2. Accomplishing strict foreclosure – the secured party must send a written proposal to retain the collateral in satisfaction of the debt
 - a. *Collateral is consumer goods* – notice is sent to (i) the debtor & (ii) any *secondary obligors* (i.e. a guarantor of the underlying debt, like a co-signer)
 - b. *Collateral is NOT consumer goods* – notice is sent to (i) the debtor, (ii) other secured parties who have told the foreclosing creditor of their security interest in the collateral, & (iii) perfected secured parties & secondary obligors
 - c. If any of the notified parties objects within *20 days* after the notice is sent – strict foreclosure will NOT be allowed & instead, the collateral must be disposed of *by sale* (party may object for any or no reason)
3. Consumer goods and the 60% Rule
 - a. Strict foreclosure not allowed – if the collateral is consumer goods and the debtor has paid
 - (i) 60% of the loan in the event of a non-PMSI, or
 - (ii) 60% of the cash price in the event of PMSI
 - b. Instead, the secured party must sell the collateral within 90 days or be liable for conversion

D. Sale

1. Secured party may sell the collateral & apply the sale proceeds to the debt – the secured party chooses whether the sale will be public (i.e. auction) or private
2. 2 governing principles:
 - a. Every aspect of the sale must be **commercially reasonable**
 - b. Prior to sale, *reasonable notice must be sent* (presumptively *commercially reasonable*). Article 9 has standard reasonable notice forms – if you do your own, the following principles of notice must apply:
 - (i) To whom
 - (a) Consumer goods – notice must be sent to debtor & any secondary obligors
 - (b) All other types of collateral – notice must be sent to debtor & those secured parties who have advised the foreclosing creditor of their security interest, as well as *perfected secure parties & secondary obligors*
 - (ii) Content of the notice depends on the type of sale
 - (a) Disposition is by *public sale* – notice must state time & place of sale
 - (b) Disposition is by *private sale* – notice must state the time *after which* the sale will be made
 - (iii) Consumer goods – additional consumer-protective provisions are mandatory, including
 - (a) How any deficiency will be calculated, &
 - (b) How debtor can redeem the collateral
 - (iv) *Advance notice requirement* – the standard is one of *commercial reasonableness*, BUT, in a non-consumer action, notice is deemed sent within a reasonable time if it is sent *10 days or more* before the time of sale
 - (v) *Whether secured party can buy at the sale?*
 - (a) YES at a public sale
 - (b) NO at a private sale, unless there are *external market checks* (*too much potential for unregulated self-dealing*)

E. Action for Deficiency Judgment

1. Secured party can proceed against the debtor for a deficiency judgment – if the sale proceeds are insufficient
2. If a secured party sells collateral at a low price to an *inside buyer* – the price that an *independent 3rd party would have paid*, rather than the actual amount paid, is the price that will be used in calculating the deficiency
3. *Debtor's limited right of redemption*:
 - a. Cut off once the secured party has re-sold the collateral or completed a *strict foreclosure*
 - b. To redeem – debtor must pay all obligations secured by the collateral (payments owed), PLUS accrued interest and the *secured party's reasonable expenses* (including reasonable attorney's fees)
 - If security agreement has acceleration clause – must pay off entire unpaid balance, plus accrued interest and the *secured party's reasonable expenses* (including reasonable attorney's fees)

COMMERCIAL PAPER – ARTICLE 3

I. Overview

- **Bright line rule** – when a *negotiable instrument* is *duly negotiated* to an *holder in due course (HDC)*, the HDC takes the instrument free of all claims to it, free of *personal defenses*, & subject only to *real defenses*
- A. **Negotiable Instrument** – when is the given writing a negotiable instrument as opposed to a mere contract
- B. **Theories of liability** – what theories might D get sued. There are only two bases:
 1. K or signature liability
 2. Warranty or transfer liability
- C. **Due Negotiation** – what makes the transfer proper
- D. **HDC** – how does a transferee qualify as an HDC
- E. **Benefits of HDC standing** – *claims & personal defenses v. real defenses*

II. Types of Negotiable Instruments

A. 2 Types of Commercial Paper (writings calling for the payment of money)

1. **Note (Promissory Note)** (a promise to pay)
 - a. Looks like – “**I promise** to pay to the order of X fifty thousand dollars /s/Y”
 - b. Note contains an *affirmative promise to pay* (not just mere IOU)
 - c. 2 Parties:
 - (i) **Maker** – who is called the *promisor* (Y)
 - (ii) **Payee** – who is called the *promisee* (X)
 2. **Draft** (a bill of exchange i.e. a check)
 - a. Looks like: “Pay to the order of X, fifty thousand dollars. First Bank of Denver /s/Y”
 - b. Draft contains a *command or order*
 - c. 3 parties:
 - (i) **Drawer** – who gives the *order* (Y)
 - (ii) **Drawee** – who is ordered to do the *paying* (e.g. bank)
 - (iii) **Payee** – who is the beneficiary of the order (X)
- **Indorser** – appears in the context of promissory notes and checks (indorser *signs* on the back)

B. Negotiable Instruments v. Contracts

1. Requirements for *negotiable instrument* – **WOSSUPP**
 - a. **W** – a **W**riting
 - b. **O** – payable to the **O**rders or to bearer
 - c. **S** – **S**igned by the maker or drawer
 - d. **S** – reciting a **S**um certain (i.e. a specifically ascertainable sum)
 - e. **U** – containing an **U**nconditional promise or order, & no additional promises or orders,
 - f. **P** – **P**ayable on demand or at a definite time, &
 - g. **P** – **P**ayable in currency
2. For each requirement consider:
 - a. Writing must **NOT contain any additional promises or orders** (two is a crowd)
 - E.g. “I promise to pay 5K **AND** give you my vintage album collection” – NON-negotiable
 - b. Writing must be (i) **payable to order**, or (ii) **payable to bearer**
 - (i) **Payable to order** – to be negotiable, the note or draft must use the word (i) “order,” or (ii) “assigns” in connection with the payee’s name
 - (ii) **Payable to bearer** – if the instrument is not payable to order, then to be negotiable it must be payable to bearer, meaning that it is payable to anyone who has it
 - (a) “pay to bearer”
 - (b) “pay to the order of bearer”
 - (c) “pay to Bill Smith or bearer”
 - (d) “pay to cash” (a term of art that satisfies the standard)
 - (e) “pay to the order of cash” (term of art)
 - NOTE: if the writing states “**pay to Bill Smith**” – NOT negotiable, because it doesn’t contain the words: (i) “order,” (ii) “assigns,” or (iii) “bearer” – THIS IS A CONTRACT
 - c. Instrument must be **signed** (i) by the **maker** if it is a promissory note, or (ii) by the **drawer** if it is a draft
 - Any authentication, found anywhere on the instrument, qualifies (need not be formal)
 - d. Instrument must state a **sum certain**, meaning a specifically ascertainable sum – must be able to calculate

- how much is to be paid, either from (i) what the *writing says*, or (ii) *reference to a specific outside source* (also, Interest rate can be based on judgment rate if no specific rate is specified)
- e. Instrument must contain (i) an **unconditional promise** to qualify as a promissory note, or (ii) **unconditional order** to qualify as a draft, , **or it is a contract**
E.g. “I promise to pay if the Mets win” – this is a contract and not a negotiable instrument
 - (i) *By contrast*: conditional = contract
 - (a) *Express condition*
 - (b) *Incorporation clause* (e.g. “incorporates” or “governed by” or “subject to”)
 - (c) *Attempt to limit or condition payment to particular funds*
 - (ii) NOTE: just because an instrument recites the consideration out of which the instrument arose, doesn’t mean that the instrument is conditional
 - f. Instrument must be **payable on demand** or at a definite time
 - (i) *On demand* – means the instrument specifically states that it is “payable on demand” or “at sight” or “on presentation” (if silent as to the time of pmt, it is still negotiable, & deemed payable on demand)
 - (ii) *Definite time* – an instrument is payable at a definite time if, by its terms, it is payable: *on or before a stated date* or *at a fixed period after a stated date*
 - NOTE: *acceleration clauses* are permissible, & do not destroy negotiability (e.g., “pay bearer on 4/15/09, or at my death if I should die sooner”) → BY CONTRAST, “payable when my 1st grandchild is born” is non-negotiable, b/c future event is *not linked to a date certain*
 - g. Sum certain must be **payable in currency** – currency means (i) money, (ii) including foreign currency, but **NOT goods** (ie. An ounce of gold = non-negotiable)

III. Theories of Liability – how does Defendant get sued (2 theories)

A. Contract or Signature Liability

1. *Basic context* – when defendant signs it, D promises to pay it, & that’s how you get sued
2. *Who signed (who’s the D)*
 - a. *Maker* (promisor of the promissory note) – merely by signing his name to the instrument, enters into a K, whereby he agrees to pay the instrument; if he fails to pay, he can get sued
 - b. *Indorser* – signs his name on the back of the instrument;
 - (i) Indorser promises that if the check bounces & is notified, he’ll pay (becomes *secondarily liable*), or
 - (ii) If indorser does NOT honor that promise, he can get sued
 - c. *Drawer* (party who signs the check is also *secondarily liable*) – by signing the check:
 - (i) Drawer promises that if the check bounces & is notified, he’ll pay
 - (ii) If drawer does NOT do so, he’ll get sued
 - d. *Drawee* (party who pays the draft) – typically, this is the bank
 - (i) Drawee does NOT sign, & therefore, is NOT liable (remember, this is *signature liability*)
 - (ii) When the drawee does sign it, he becomes an *acceptor*
 - e. *Restrictive indorsement* – when words “*without recourse*” accompany the signature
 - (i) “without recourse” is a term of art used by indorsers & drawers – represents a *disclaimer of liability*
 - (ii) Thus, indorser or drawer is NOT liable for purposes of contract or signature liability)
 - (iii) Without recourse passes title but not signature liability.

B. Warranty or Transfer Liability

1. *Basic context* – think of this as the seller’s liability for selling a defective instrument
2. *Who’s the D* – any transferor who **sells** the negotiable instrument (unless the transferor is *donor*), can be sued
3. *Who’s entitled to sue D for breach of warranty?*
 - a. *D indorsed* – any P in possession may sue, because *when D indorses (warranties run with instrument)*
 - Example: X indorses his paycheck from his employer & remits the check to Y, for services rendered; Y in turn remits the check to Z for his services – If the check bounces, *Z may sue X*, because X was not a *donor*, & he indorsed the check
 - b. *D NOT indorse* – *then only the D’s immediate transferee may sue* (warranties NOT run with instrument)
 - Example: X, who never indorses his paycheck from his employer, remits the check to Y for services rendered; Y in turn remits to Z – if the check bounces, *Z can NOT sue X*, because X did not indorse the check
4. 5 warranties made by transferor (usually the defendant) – transferor promises that:
 - a. He has *Good title* to the instrument
 - b. *All signatures are genuine & authorized* – thus, *forgery* is a breach of warranty
 - c. *Instrument has not been materially altered* – when the facts tell you the instrument has been tampered with, it is defective

- d. *There is no defense or claim good against transferor* – meaning that the instrument is *enforceable*
- e. *No knowledge of any bankruptcy or insolvency* against the maker or drawer

IV. Due Negotiation – what makes the transfer proper

A. Due negotiation (“*duly negotiated*”) – means that there has been a *proper transfer of the instrument*

1. If the instrument has been properly transferred, the transferee is a *holder in due course* (HDC)
2. If not properly transferred, the transferee is NOT a holder & can not qualify as an HDC

B. Payable to order

1. When instrument is payable to the order of a specific payee, it is negotiated by *delivery of the instrument to that payee* – any further negotiation requires that payee (i) indorse the instrument & (ii) deliver it to the transferee
2. *Payee’s indorsement must be authorized & valid* – if not, chain of title will be broken (e.g. forging the payee’s name *breaks the chain of title*, & no subsequent possessors of the instrument can qualify as holders)

C. Payable to bearer

1. If the instrument is payable to bearer, *indorsement is NOT required*
2. Such instruments are *negotiated by delivery of the instrument to the transferee*

D. Types of indorsement:

1. *Special indorsement* – names a particular person as “indorsee,” who *must sign* in order for the instrument to be further negotiated
2. *Blank indorsement* – does not name a specific indorsee; may be negotiated by delivery alone
3. *Restrictive indorsement* – contains a condition, purporting to prohibit further negotiation (e.g., a check indorsed “for deposit”). If bank stupidly pays, you can recover from bank in conversion
 - a. This is okay because the condition is on the back (& not a condition to the instrument itself)

V. Holder in Due Course – how does a transferee qualify as HDC

- **HDC** – a holder who takes the instrument (i) *for value*, (ii) *in good faith* & (iii) *without notice that it is overdue or has been dishonored or is subject to any defense or claim*:

A. For Value

1. Holder must give value for the instrument – does NOT mean giving consideration, which is a K principle
2. *Consideration v. Value*
 - a. ***Mere promise is NOT value***
 - b. *Old value is good value*
3. Value given in exchange for an instrument need not be equivalent to the face amount of the instrument – an instrument purchased at a discount is sold for *full value* as long as the full price agreed upon has been given

B. In Good Faith – honesty in fact (subjective test – the rule of the pure heart and the empty head)

C. Without Notice – that it is (i) overdue, (ii) has been dishonored or (iii) is subject to any defense or claim (*objective* test, & asks whether the holder knew or had reason to know of the problem)

1. ***Notice that the instrument is overdue*** – should have already been paid
 - a. *Payable at definite time* – if bought too late, holder is NOT an HDC
 - b. *Principal in arrears* – if payment or more of principal is in arrears, holder is NOT an HDC
 - c. NOTE: ***interest in arrears*** – if holder takes with notice that 1 or more payments of *interest* are in arrears, nonetheless *qualify* as an HDC
2. ***Notice of any defense or claim against the negotiable instrument’s enforcement***
 - a. *Appearance of the instrument gives notice* – instrument is irregular (e.g. evidence of forgery or alteration or it says PAID on it). Person should objectively realize that something is wrong.
 - b. ***Notice that the obligation of any party is voidable***
 - Example: X sells a chair to Y – X misrepresents to Y that it is an antique – Y signs & delivers to X a negotiable note for 4K for the chair – X indorses the note & sells the note to Z
 - (a) X & Y – Y’s obligation to pay is voidable, because Y has the defense to enforcement of her promise, given that X defrauded him
 - (b) X & Z – Z would qualify as an HDC, if didn’t have notice or reason to know of Y’s defense
 - c. ***Notice of a competing claim to the negotiable instrument*** – if the instrument is lost by or stolen from the true owner, the transferee could still qualify as an HDC if the instrument has been properly transferred, & the transferee didn’t have notice or reason to know of the theft or loss
 - Example: X steals a negotiable instrument from Y & sells it to Z – Z is still entitled to the negotiable

instrument, if (i) the instrument was properly transferred, & (ii) if Z didn't have notice or reason to know of the theft

- d. *Notice that fiduciary has negotiated the instrument in breach of his fiduciary duty* – if holder did not actually know of breach, then HDC (this is the only time that the standard is one of actual knowledge)

D. The HDC and the Shelter Rule

1. *Basic principle* – a transferee acquires whatever rights her transferor had (i.e. *the transferor takes shelter in the status of her transferor*)
 - a. Rule allows the transferee “*to step into the shoes*” of the HDC, even though he would otherwise clearly fail to meet the requirements of due course holding
 - b. Thus, transferee has all the rights of an HDC, even though the transferee is a *donee* OR *otherwise fails to meet the requirements of due course holding*
2. Example: X, the HDC of a negotiable instrument, makes a gift of the instrument to his son Y – Y is a mere donee – even though he doesn't deserve it, Y qualifies as an HDC because of the shelter rule

VI. Benefits of HDC Status: Personal v. Real Defenses

- **Rule** – HDC (& subsequent transferees who take “shelter” in that status) takes the instrument (i) free from claims, (ii) free from personal defenses, & (iii) subject only to real defenses
- A. HDC takes free from claims**
1. Claim is a right to a negotiable instrument because of *superior ownership*
 2. If a negotiable instrument is duly negotiated to an HDC, the HDC **defeats** the superior owner
- B. HDC takes free from personal defenses**
- Include every defense available in ordinary K actions, such as: *lack of consideration, unconscionability, waiver, estoppel, fraud in the inducement*
- C. HDC is still subject to “real” defenses (MAD FIFI^d)** – can be asserted against HDCs & non-HDCs alike:
1. **Material Alteration** – a change in the terms of the instrument (discharges all parties from liability on the instrument & on the underlying obligation as well, unless a party was negligent)
 - Example: maker writes a check for \$100, & payee changes the amount to 2K, then sells it to an HDC – maker is liable only for \$100, BUT, if the maker was *negligent* (e.g., leaving blanks or leaving wide spaces on a check), he is *estopped* from raising material alteration as a defense
 2. **Duress**
 3. **Fraud In the Factum** (misrepresentation about the instrument) & *forgery*
 4. **Incapacity**
 5. **Illegality** (if illegality in the underlying transaction renders the obligation *void*, not just *voidable*)
 6. **Infancy** (can be asserted only by the infant)
 7. **Insolvency**
- D. Difference between “real” fraud & personal fraud**
1. **“Real” fraud (“fraud in the factum”)** – is assertable against an HDC, & means that ***there has been a misrepresentation about the instrument***
 - Example: X, who cannot read English, signs a promissory note after his lawyer tells him it's a credit application – even in the hands of an HDC, the note is *NOT enforceable*
 2. **Personal fraud (fraud in the inducement)** – is a personal defense, & is ineffective against an HDC
 - a. Example: X sells Y a ring, telling him it's an antique – after paying for the ring by check, Y discovers that it is a fake – if the check is now held by an HDC, Y's defense cannot be asserted, because the fraud defense is *personal only*; unlike in the above example, Y knew he was signing a negotiable instrument, & in the hands of an HDC, the instrument is therefore *enforceable*)

SECURED TRANSACTION / COMMERCIAL PAPER – ESSAY QUESTIONS

I. QUESTION – 1 (COMMERCIAL PAPER)

- A. Whether the checks were duly negotiated to S (S was suppose to receive the checks but Thieves claimed instead)
 - 1. Negotiation of Bearer instrument – accomplished by delivery to the transferee (here failed to deliver)
 - 2. Negotiation of Order instrument – accomplished by delivery to the payee named on the instrument (same)
- B. Whether a person who receives cash has good title – anyone with possession of cash has good title
- C. Drawer’s Rights against the bank
 - 1. Bearer instrument – freely negotiable, like cash; thus bank is protected from liability check made out to “cash”
 - 2. Order instrument – bank is liable when it honors an instrument with a *forged indorsement* when the order is payable to the order of a specific payee
 - a. UCC imposes banks the duty to honor a check as drawn (original draft as written by the drawer – bank not allowed to charge account of its customer where bank pays the wrong person)
 - b. BUT UCC imposes on the drawee the duty to *notify* the bank of such unauthorized use with “reasonable promptness” (within 1 year)

II. QUESTION – 69 (& FEDERAL JURISDICTION)

- A. Extent of Bank’s liability for cashing an altered check (\$1,500 was altered to \$81,500)
 - 1. Bank is liable when drawee notifies the bank o unauthorized use
 - 2. BUT UCC authorizes a drawee bank acting in good faith to charge the account of a customer to the extent of “the original tenor of his altered item” (thus can charge \$1,500)
- B. Whether indorser of an instrument, warranted to bank that the instrument has not been materially altered (*thus if get a materially altered instrument and get paid from bank, bank can recover*)
 - 1. Any person who obtains payment... warrants who pays in good faith... instrument not materially altered
 - 2. Any person who transfers an instrument and receives consideration warrants that ... instrument not materially altered

III. QUESTION – 77 (& CRIMINAL PROCEDURE & EVIDENCE)

- A. Whether a drawer can recover from the drawee bank, when bank paid out on an instrument containing an unauthorized drawer’s signature
 - 1. Generally, bank must recredit for unauthorized signature if notified within reasonable time
 - 2. BUT, if drawer’s negligence contributed to the unauthorized signature, bank may not be required to re-credit (jury determination)

IV. QUESTION – 31 (& CRIMINAL LAW)

- A. What liabilities are of a person who knowingly issues a check for which he has insufficient funds
 - 1. False Pretenses is committed
 - 2. Receiver takes check subject only to real defenses and free of personal defenses
- B. Whether HDC – (i) instrument for value, (ii) in good faith, (iii) without notice any real defenses / claims

V. QUESTION – 84 (& CONFLICT OF LAWS)

- A. Whether a payee’s infancy or the drawer’s death is a defense to the drawer’s duty to pay
 - 1. HDC (took for value with no notice – subject to only to *real defense* (and not personal defenses)
 - 2. To holder drawer liable – HDC must present check at bank for payment & give the drawer notice of bank’s dishonor
- B. Whether a drawee bank owes any duties to a holder to pay a check
 - 1. Even though a bank has a duty to honor its customer’s check, the duty is owed to the customer and not to the holder of the check – bank may stop honoring a customer’s checks upon the customer’s check

VI. QUESTION – 35 (& NY PRACTICE & CONTRACTS)

- A. What remedies are available to a secured creditor when a debtor defaults
 - 1. Right to sue / Right to replevy
 - 2. Perfected Purchase Security Interest (PMSI) – vendor sells it to debtor-purchaser on crest
 - 3. Attachment – written security agreement
 - 4. Perfection – filing financing statement (PMSI need to file when dealing with *equipment*)

VII. QUESTION – 8 (& DOMESTIC RELATIONS / EVIDENCE)

- A. Whether a bank must honor a stop payment order on a cashier’s check
 - 1. Cashier’s check is a draft drawn on the bank, where the drawer is the bank – it’s an unconditional promise to pay form the bank
 - 2. Bank is under no obligation to honor customer’s stop payment order

