

TYPES OF NEGOTIABLE INSTRUMENTS

- **Draft:** An unconditional order to pay by which the party creating the draft (the *drawer*) orders another party (the *drawee*), typically a bank, to pay money to a third party (the *payee*) -- e.g., a **check**.

- **Check:** A draft ordering a drawee bank and payable on demand.

- **Time Draft:** A draft payable at a time certain.

- **Sight Draft:** A draft payable on presentment.

- **Trade Acceptance:** A draft that is drawn by a seller of goods ordering the buyer to pay a specified sum of money to the seller, usually at a specified future time. The buyer *accepts* the draft by signing and returning it to the seller.

- **Promissory Note:** A written promise made by one person (the *maker*) to pay a fixed sum of money to another person (the *payee*) on demand or at a specified future time.

- **Certificate of Deposit:** A note by which a bank or similar financial institution acknowledges the receipt of money from a party and promises to repay the money, plus interest, to the party on a certain date.

NEGOTIABLE INSTRUMENTS: AN OVERVIEW

■ A **Negotiable Instrument** is a:

- (1) **written** instrument,
- (2) **signed** by the maker or drawer of the instrument,
- (3) that contains an **unconditional** promise or order to pay
- (4) an **exact sum** of money (with or without interest in a specified amount or at a specified rate)
- (5) **on demand** or at an **exact future time**
- (6) to a **specific person**, or to **order**, or to its **bearer**.

NEGOTIABILITY: SIGNATURES

- For an instrument to be negotiable, it must be signed by the maker/drawer.
- A signature may be any symbol made by the maker or drawer with the present intention to be a signature.

NEGOTIABILITY: UNCONDITIONALITY

- **Promise or Order:** A negotiable instrument must contain an express order or promise to pay.
 - A mere acknowledgment of a debt is not sufficient without evidence of an affirmative undertaking on the part of the debtor to repay the debt.
 - The exception to this rule is a Certificate of Deposit.

- **Unconditionality of Promise or Order:** A promise or order is conditional (and, therefore, not negotiable) if it states:
 - (1) an **express condition** to payment,
 - (2) that the promise or order is **subject to or governed by** another writing, or
 - (3) that the rights or obligations with respect to the promise or order are **stated in** another writing.

NEGOTIABILITY: A FIXED AMOUNT

- The fourth requirement of negotiability is that negotiable instruments must state a **fixed amount of money**.

- **Fixed amount** means an amount that can be determined from the face of the instrument.
 - This requirement applies only to the principal amount of money.
 - The instrument can reference an outside source to determine the rate of interest.

- **Payable in Money** means the medium of exchange authorized or adopted by the United States or foreign government as part of its currency.

NEGOTIABILITY: TIME FOR PAYMENT

- **Payment On Demand:** An instrument is payable on demand, “at sight,” or “upon *presentment*” if it is subject to payment immediately upon being presented to the payor or drawee.
 - If no time for payment is specified, a negotiable instrument is **presumed** to be payable on demand.

- **Payment at a Definite Time:** An instrument is payable at a definite time if it states that it is payable (i) on a **specified date**, (ii) within a **definite period** of time, or (iii) on a date or at a time **readily ascertainable** at the time the promise or order is made.
 - Such instruments are frequently referred to as **time instruments**.
 - **Acceleration Clause:** A clause that permits a payee or other holder of a time instrument to **demand payment of the entire amount or balance due**, with interest, if a certain event occurs, such as default in the payment of an installment when due.
 - **Extension Clause:** A clause in a time instrument that permits the **date of maturity** to be extended.

NEGOTIABILITY: PAYMENT TO WHOM

- **Order Instrument:** A negotiable instrument that is payable “to the order of” an identified person or “to” an identifiable person “or order.”

- **Bearer Instrument:** A negotiable instrument payable “to bearer” or to “cash,” rather than to an identifiable payee.
 - **Bearer:** The person possessing a bearer instrument.

 - Any instrument payable to the following is a bearer instrument:
 - (i) “Payable to the order of bearer”;
 - (ii) “Payable to Jane Smith or bearer”;
 - (iii) “Payable to bearer”;
 - (iv) “Pay cash”; or
 - (v) “Pay to the order of cash.”

FACTORS NOT AFFECTING NEGOTIABILITY

- Certain ambiguities or omissions, resolvable by applicable U.C.C. provisions and/or rules, will not make an instrument non-negotiable. For example:
 - (1) The fact that an instrument is **undated** does not affect its negotiability, unless the date of the instrument is necessary to understand the payment term;
 - (2) **Postdating** or **antedating** an instrument does not affect its negotiability;
 - (3) **Interlineation** and other written or typewritten **alterations** need not affect negotiability;
 - As with other contract terms, handwritten terms “trump” typewritten terms, and typewritten terms “trump” printed terms.
 - (4) **Words “trump” figures**, unless the words are ambiguous in and of themselves; and
 - (5) If the instrument fails to specify the applicable interest rate, the **judgment rate of interest** (defined by state statute) becomes the interest rate on the instrument.

TRANSFER OF INSTRUMENTS

- **Assignment:** Under general contract principles, a negotiable instrument may be transferred to an assignee, who then holds the instrument with all the rights of the assignor.

- **Negotiation:** Transfer of an instrument in such a form that the transferee becomes a *holder*, who has at least the same rights in the instrument as the transferor, and may have more rights than the transferor.

- **Negotiating Order Instruments:** An order instrument may be negotiated by delivery with any necessary **indorsements**.

- **Negotiating Bearer Instruments:** Unlike an order instrument, a bearer instrument need not be indorsed to transfer the payee's rights to the transferee. All that is required is **delivery** to the new bearer.

INDORSEMENTS

- **Indorsement:** A signature, with or without additional words or statements (e.g., “for deposit only,” “payable to Jane Smith,” “payable from acct. # 000001,” etc.), made by the *indorser* in order to transfer his or her rights to the *indorsee*.

- **Blank Indorsement:** An indorsement that **specifies no particular indorsee** and can consist of a **mere signature**.

- **Special Indorsement:** An indorsement that indicates the specific person to whom the indorser intends to make the instrument payable -- i.e., the indorsee.

- **Qualified Indorsement:** An indorsement which **disclaims any contract liability** on the instrument (e.g., “without recourse”).

- **Restrictive Indorsement:** Any indorsement on a negotiable instrument that requires the indorsee to comply with certain instructions regarding the funds involved.

- **Indorsement for Deposit or Collection:** “*For deposit only.*”