

HOUSE RESEARCH

Bill Summary

FILE NUMBER: S.F. 28

DATE: May 17, 2003

Version: First Engrossment

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Subject: Uniform commercial code

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Overview

This bill makes changes in Articles 3 and 4 of the Uniform Commercial Code (UCC). Those articles of the code deal with the related subjects of checks and other negotiable instruments (Article 3) and bank deposits and check collection (Article 4).

In general, the changes made by this bill use some new terms to make the language accommodate electronic transactions, deal with consumer issues such as holder-in-due-course and payments made to creditors who have transferred the right to collect without notice, and various provisions adjusting or clarifying the rights of parties to a financial instrument.

Article 1: Amendments of Uniform Commercial Code Article 3

This article of the bill deals with Article 3 of the UCC.

- 1** **Definitions.** Adds new definitions of consumer account, consumer transaction, principal obligor, record, remotely-created item, and secondary obligor. Adds the definition of "account" from Article 4 of the UCC as a definition that also applies to Article 3.
- 2** **Unconditional promise or order.** Uses the newly-defined term "record" to replace "writing." The effect is to make the language broad enough to include electronic transactions.
- 3** **Joint and several liability; contribution.** Eliminates a current provision dealing with how the discharge of one party's liability on an instrument affects the ability of another party that

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is jointly and severally liable with the discharged party to recover contribution from the discharged party.

- 4 **Notice of right to defend action.** Same type of change as in section 2 above.
- 5 **Defenses and claims in recoupment.** Broadens a cross-reference in paragraph (a) to encompass the new paragraphs (e) and (f). Paragraph (e) provides that, in a consumer transaction, an instrument that is not subject to the holder-in-due-course doctrine will be treated as such, even if it lacks legally-required language saying so. (The usual source of the legally-required language is the Federal Trade Commission, which by regulation has outlawed the holder-in-due-course doctrine for consumer transactions.) This protects the holder from a claim that the instrument is not enforceable due to the absence of the required language. Paragraph (f) provides that this section of the UCC is subject to law that establishes different rules for consumer transactions, including choice-of-law provisions..
- 6 **Enforcement of lost, destroyed, or stolen instrument.** Permits enforcement of an instrument that has been lost, destroyed, or stolen, by a person who was not necessarily in possession of it or did not necessarily have the right to enforce it, when it was lost, destroyed, or stolen. The effect is to make this section broader, to apply to situations in which legal right to the instrument has been transferred in the meantime or in which a secured party in the instrument has in the meantime become legally able to enforce it.
- 7 **Lost, destroyed, or stolen cashier's check, teller's check, or certified check.** Same type of change as in section 2 above.
- 8 **Transfer warranties.** Adds to transfer warranties a warranty that a "remotely-created item" (one that does not purport to have the signature of the drawer) was authorized by the drawer in the amount indicated. This would typically be an electronic or telephonic transaction. A transfer warranty is a sort of guarantee made by the person who transfers an instrument. The effect is to make the depository bank liable to the drawee bank if the item was not authorized. Paragraph (e) limits that transfer warranty to situations in which that warranty is actually made under applicable law.
- 9 **Presentment warranties.** Same as the preceding section, but applies to presentment warranties. (Presentment warranties are those made to a drawee of an instrument, when presenting it for payment.)
- 10 **Instruments signed for accommodation.** Provides that an accommodation party to an instrument is directly liable on it and has no right to insist that attempts first be made to collect from the accommodated party, unless the accommodation party clearly so indicated on the instrument when signing it. This could be done, for instance, by writing "collection guaranteed" instead of "payment guaranteed." Permits an accommodation party, "in proper circumstances," to have a court force the accommodated party to perform its obligations.
- 11 **Payment.** Provides that a note is considered paid to the extent of a payment made to a party that formerly had authority to enforce the note, if the payment is made before the payer is notified of the transfer of that authority. Adds a broader definition of "signed" to accommodate electronic commerce.
- 12 **Discharge by cancellation or renunciation.** Same types of changes as in section 2 above.
- 13 **Discharge of secondary obligations.** Rewrites the section dealing with the extent to which discharge of a principal obligor on an instrument affects the liability of secondary obligors. This section uses the new definitions of principal obligor and secondary obligors from section 1 of this article. The overall result can be summarized as permitting obligees and principal obligors to enter into agreements that affect their obligations on the instrument,

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with certain protections for secondary obligors.

Article 2: Amendments to Uniform Commercial Code Article 4

This article of the bill makes changes to Article 4 of the UCC, similar to those made to Article 3 of the UCC in the preceding article of this bill.

- 1 1** **Definitions and index of definitions.** Adds cross-references to two of the new definitions added to Article 3 of the UCC in article 1 of this bill. The effect is to make those new definitions apply to Article 4 of the UCC as well.
- 2** **Transfer warranties.** Makes changes similar to those made in Article 1, section 8, of this bill. The difference is that this Article 4 language governs transfer warranties within the banking system, such as the warranty made by the bank that initially received the check to an intermediate collecting bank through which the check will ultimately reach the bank upon which the check was drawn.
- 3** **Presentment warranties.** Makes changes similar to those made in article 1, section 9, of this bill. The difference that this section involves presentment warranties made to a drawee bank.
- 4** **Presentment by notice of item not payable by, through, or at bank; liability of drawer or endorser.** Makes a change similar to section 1, section 2, of this bill, making the language fit electronic transactions.
- 5** **Deferred posting; recovery of payment by return of items; time of dishonor; return of items by payor bank.** Permits a payor to revoke its settlement of an item if, before its midnight deadline, it returns either the item, an image of the item, or a "record" providing notice of dishonor.
- 6** **Customer's right to stop payment; burden of proof of loss.** Makes changes to make language consistent with electronic commerce.