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Quasi-Checks: An Apology for a Mutation of Negotiable Instruments

Jonathan Yovel*

ABSTRACT

This essay deals with one of the persistent problems in the law of negotiable instruments, namely the legal phenomenon of so-called "quasi-instruments" (it focuses on quasi-checks and deals briefly with quasi-notes.) First, it supplies a formal definition for quasi-instruments. It then proceeds to analyze the real-world interests, concerns and risks associated with quasi-checks, dealing respectively with those risks that are germane to banks, payors, payees, and subsequent holders. It proceeds on three levels: analytic introduction of the phenomenon, including the UCC Article 3 "extension rule" that accords fully negotiable status to some quasi-instruments, but no to others; normative and relational analysis pre- and post-revision extension rule; and finally, a certain critique of the prevalent justification to the validation of quasi-instruments (mainly, streamlining banking practices and technology) and forwarding an alternative, relational justification (based on the reliance interests of payees and subsequent holders). The alternative justification calls for a more inclusive approach to quasi-instruments, in one sense favoring the extension rule of pre-revision UCC Article 3 over that of the post-revision (however, the post-revision policy is justified inasmuch as granting holder in due course status quasi-holders is concerned). The essay also makes the claim—made nowhere previously, as far as research could establish—that the post-revision extension rule of UCC Art. 3 contains a serious technical flaw. The fact that practice and application are by and large indifferent to this flaw is not so much a failure of scholarship or the judiciary, but instead indicates that once a satisfactory theoretical solution to the question of quasi-instruments is generally reached, technical failings in the relevant statute (here, UCC §3-104(c)) are relatively inconsequential. Other issues covered are the influence of Check 21 on quasi-instruments.

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the question of depository banks as holders in due course, and other matters. This essay then combines positive and normative analyses of negotiable instruments law with jurisprudential generalizations that follow from these layers of analysis.

I. QUASI-CHECKS IN LAW AND PRACTICE

One of the concerns dealt with in the 1990 revision of the Uniform Commercial Code ("UCC") Article 3 is that of so-called quasi-checks, a subset of quasi-instruments. A quasi-instrument is commercial paper that for some failure of form does not conform to the constitutive requirements of negotiability as set forth in UCC Article 3. It is thus, ostensibly, not a negotiable instrument, although to unsuspecting parties it may appear to be one. Parties may then take such instruments inadvertently, in misguided reliance on its transferability and the relative lack of defenses that are typical of negotiable instruments, especially as entailed by the status of holder in due course. Such parties employ a de facto mistaken allocation of risks regarding the financial aspect of the transaction, one that may be difficult or impractical to remedy short of by falling back on the default contractual level;

1. U.C.C. § 3. "Revision" here and throughout this study indicates the 1990 revision of U.C.C. Article 3; all references are to the revised U.C.C. Article 3 unless otherwise indicated. "Pre-revision" indicates the U.C.C. prior to the 1990 revision, as is still in force, for example, in New York.
2. See U.C.C. §§ 3-102 to 3-104.
3. See id.
4. The right of a holder in due course in an instrument overrides property defenses: the law here must adjudicate a priori between innocent parties in situations where shifting risk to the least cost avoider—ostensibly, the defendant—may seem artificial and unsupported by real life situations (the defendant, whether a drawer or previous holder/indorser, may never be in any actual sense in a position to avoid losing an instrument or having it stolen, than a later and equally innocent holder is from verifying any lack of prior claims or defenses). See U.C.C. §§ 3-302 to 306. A holder in due course is a holder of an instrument who took it for value, in good faith, and without any of a series of notices pertaining to the instrument's integrity or claims against it. See U.C.C. § 3-302. Such a holder's claim preempts any prior property rights in the instrument. See U.C.C. § 3-306. Obviously, the question whether any person in possession of a negotiable instrument is a "holder in due course" requires relatively clear and formal demarcation standards, because the ability to become a holder in due course is a weighty consideration for anyone who considers taking an instrument as a cash substitute or a credit mechanism. For a brief discussion of initial payees as holders in due course, see infra notes 94-95 and accompanying text.
5. Examples of this default contractual level include the doctrine of mistake and substantive breaches of contract that would allow for avoidance of the financial part of the transaction and require the payor to tender payment in substitution. Common law, including contract law, applies to instruments whenever it is not trumped by U.C.C. provisions in accordance with U.C.C. § 1-103 - considered by Professors White and Summers as "probably the most important single provision in the Code." JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE 8 (5th ed. 2000); see also Grant Gilmore, Article 9: What it Does for the Past, 26 La. L. Rev. 285 (1966) (emphasizing the parallel and continuing application of common law in jurisdictions that
misallocation, in any case, frustrates the purpose of paying with an instrument that "propertizes" an obligatory relation between parties by merging artifact with value.\(^6\) Whether such flawed tenders occur innocuously or fraudulently is of little immediate effect, as the formalistic structure of the relevant UCC Article 3 clauses is quite indifferent to the drawer's intent.\(^7\) Even marginal flaws may impair an instrument's validity as such. Whether the instrument would then retain at least a contractual status is debatable and context-specific,\(^8\) and even so, it would be subject to a different—and typically, much wider—array of defenses against enforcement.

The primary function of the law of negotiable instruments is to facilitate exchange by enhancing the attractiveness of cash substitutes such

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\(^6\) This article does not deal with the general question of the desirability of negotiability as a legal category, addressed critically elsewhere. See Albert J. Rosenthal, Negotiability — Who Needs It?, 71 COLUM. L. REV. 375 (1971); see also Ronald J. Mann, Searching for Negotiability in Payment and Credit Systems, 44 U.C.L.A. L. REV. 951 (1997).

\(^7\) See Grant Gilmore, Formalism and the Law of Negotiable Instruments, 13 CREIGHTON L. REV. 441 (1979) (on the formalist structure of Article 3); see also Kurt Eggert, Held Up in Due Course: Codification and the Victory of Form over Intent in Negotiable Instrument Law, 35 CREIGHTON L. REV. 363 (2002). The Article 3 revision committee discussed and rejected switching from a formalist to a functional structure. See ROBERT L. JORDAN ET AL., NEGOTIABLE INSTRUMENTS, PAYMENTS AND CREDITS 26-28 (5th ed. 2000); see also FRED H. MILLER & ALVIN H. HARRELL, THE LAW OF MODERN PAYMENT SYSTEMS AND NOTES 2-7 (2d ed. 1992) (offering a model for such a functional structure). Gilmore condemns contemporary negotiable instrument law for what he sees as being woefully behind the times: "[T]ime seems to have been suspended, nothing has changed, the late twentieth century law of negotiable instruments is still a law for clipper ships and their exotic cargoes from the Indies." Id. at 448. See also Taylor v. Roeder—decided under the pre-revision Article 3—in which the majority and minority clearly express formalist versus relational-functionalist approaches to interpretation, respectively; at bar was the question of whether a variable rate of interest renders a note nonnegotiable—the majority held that it did under pre-revision U.C.C. § 3-104(1)(b) that required a note to contain "a sum certain." Taylor v. Roeder, 234 Va. 99, 360 S.E.2d 191 (Ct. App.1987). See also Grant Gilmore, On the Difficulties of Codifying Commercial Law, 57 YALE L.J. 1341 (1948).

\(^8\) Paper claiming contractual status rather than negotiability must satisfy a different set of conditions, namely those pertaining to formation, consideration, form, etcetera. See Regent Corporation USA v. Azmat Bangladesh Ltd. (N.Y. Sup. Ct., Index No. 120865/94 1994) available at http://www.courts.state.ny.us/comdiv/Law%20Report%20Files/July%201998/regent7.htm. According to the court, a drawee bank does not become contractually beholden to any depository bank or payee without undertaking to pay by "accepting" the instrument. Id. at ¶ 14. In some jurisdictions even the civil procedure governing instrument-based claims is significantly different—shorter, cheaper, with discretionary allowance for defense—than contractual claims.
as drafts, checks, promissory notes, and the like. This requires that questions such as whether an instrument is negotiable, or whether by taking it a person becomes entitled to enforce it relatively free of defenses—e.g., a holder or a holder in due course—be resolvable easily, accurately, with a high degree of certainty, at minimal cost and with as little as possible administrative hassle. Due to the importance of checks in commerce, banking, consumer, and household transactions—as well as payments of personal, social, and other non-commercial nature—this study will focus mainly on checks and on their legal treatment and practical usages (both those practiced by drawers and by banks). Indeed, other payment systems—in particular electronic transfers—have taken a chunk out of the transactional volume dominated by checks. In the year 2000 it was still the case that "the paper check continues to be the most commonly used type of noncash payment instrument in the U.S. economy," as checks were used almost twice as much as debit and credit cards combined—over 42.5 billion check transactions (down, significantly, from almost 49.5 billion in 1995, when checks dominated almost seventy-seven percent of retail transactions). By 2003, however, electronic payments were made for slightly over fifty-three percent of the eighty billion noncash transactions in the U.S. economy. The average annual rate of decline in the number of checks paid is estimated to have been 3.3 percent between 1995 and 2000 and 4.3 percent between 2000 and 2003 (2003 is the last year for which the Federal Reserve published statistics), although checks continued to be the largest noncash payment type by value and exceeded the combined value of all the other noncash payment types.

9. Another function, the creation of credit mechanisms, will not be discussed in this study.
10. A "holder in due course" is a holder of an instrument who took it for value, in good faith, and without any of a series of notices pertaining to the instrument's integrity or claims against it. U.C.C. § 3-302. Such a holder's claim preempts any prior property rights in the instrument. U.C.C. § 3-306.
11. Geoffrey R. Gerdes & Jack K. Walton II, The Use of Checks and Other Noncash Payment Instruments in the United States, 88 FED. RES. BULL. 360, 360 (2002), available at http://www.federalreserve.gov/pubs/bulletin/2002/0802_2nd.pdf. These numbers have later been adjusted slightly downwards. The number of checks quoted is "net": it represents the number of checks used and paid as such, and does not include checks converted to electronic payments at the point of sale or during the process of collection. Although growing, automated clearinghouse systems (ACH) are used almost exclusively for payroll and bill processing, as opposed to more typical commercial and consumer transactions.
12. Id. at fig. 1.
14. Id. at 182.
With all the emphasis on the formalism of the law of negotiable instruments—i.e., a conceptual framework that purports to govern practice—recent developments in the law of checks actually establish a practice-to-law dimension. In other words, practice that becomes entrenched—either spontaneously or institutionally—may create de facto patterns that deviate from the letter of the law but suggest themselves as modifications to the current regulation rather than appear as transgressions of it. The standard case of such a “mutation” in the area of negotiable instruments is that of quasi-checks, a more complex phenomenon than initially apparent. The following sections present quasi-checks as a matter of law and of practice, then move from analysis to the normative considerations underlying them and suggests an alternative justification to the legal validation of quasi-instruments—emphasizing the reliance interests of payees and subsequent holders, rather than the streamlining of banking practices that are generally held to underline quasi-checks. Thus while the opening section will be familiar to any student of negotiable instruments law, it quickly turns to system-analysis and to some of the normative principles of commercial law regulation.

How do quasi-checks come to be? UCC §3-104(a) imposes relatively strict necessary conditions, that when met and only when met—cumulatively—entail negotiability. These requirements are all “internal”: supposedly, they do not require examining any in personam relations and are all manifestable from the instrument itself. As complex as they are from some perspectives, checks are not the appropriate legal text for elaborate interpretative exercises. As the Oklahoma Court of Appeals famously remarked, “[n]egotiable notes are designed to be couriers without excess luggage . . . and so negotiability must be determined from the face of the note without regard to

15. For the processes of entrenchment of practice that subsequently becomes legally-relevant, see Frederick Schauer, Playing by the Rules: A Philosophical Examination of Rule-Based Decision-Making in Law and in Life (1991).

16. Thus, for commercial paper to be a negotiable instrument it must be in writing (U.C.C. § 3-103(6) for “order” and § 3-103(9) for “promise”), signed (§§ 3-104(a) to 3-106), unconditional (§§ 3-104(a) to 3-106), and either a promise (§ 3-104(e)) or an order (§ 3-104(e)) to pay a fixed amount of money (according to § 3-104(a) “with or without interest”). See the official comments to U.C.C. §§ 3-104(a) to 3-112 for provisions regarding interest. Professors White and Summers note that “the adjective ‘fixed’ modifies only ‘amount of money’; ‘interest’ is added in the prepositional phrase . . . and is not modified by ‘fixed.’” White & Summers, supra note 5, at 516. Compare these requirements with the distinctly non-formalistic definition of “contract” in U.C.C. § 1-201(12). While the function of Article 3 requires the limitation of its application to relatively few and distinct things in the world (namely, negotiable instruments), the reach of Article 1 is wider and consequently less definite.
outside sources.”17 Below I argue that the “without regard to outside sources” dictum turns out to be too stern a requirement, as courts in fact cannot help but consider reliance relations when dealing with quasi-instruments.18 “Without excess luggage,” after all, centers around what “excess” would entail in different contexts, and in certain cases may not prove so prohibitive. For the time being, however, it is taken as the basic tenet of instrument construction—a sort of parol evidence rule, by analogy, applicable to instruments rather than to contracts. UCC §3-104(a)(1) adds another requirement, namely that the instrument be “payable to bearer or to order at the time it is issued or first comes into [the] possession of a holder.”19

However, checks—which are a kind of draft, i.e. an “order” rather than a “promise” to pay20— in fact often lack either “order” or “bearer” language because drawers either omit it or cross it out. A familiar case is when drawers who use so-called “legended” checks—those familiar instruments that are issued by banks and commercial printers with imprinted formulas such as “Pay to the order of”—frequently cross out the pre-printed language or parts of it in an effort to limit its negotiability. Such a limitation on negotiability would be seen differently from the point of view of three relevant groups: 1) banks, 2) payors or subsequent indorsers who negotiate the instrument, and 3) payees. For an instant, let us ignore what I offer to term “extension clauses,” namely both the post-revision treatment of quasi-checks in UCC §3-104(c) and the pre-revision treatment in UCC §3-805, that extend negotiability-like privileges to some quasi-instruments or to their holders. We shall examine those shortly, once we have broken down the typical interests involved in transactions involving quasi-checks according to the groups of relevant participants.

A. Banks

Non-negotiable, quasi-checks would pose a problem for the banking system if banks purchased the instruments from their customers and proceeded to enforce them—as holders—against the drawee, i.e. the

18. See infra Part III.
20. See U.C.C. § 3-104(f).
drawer's bank. This would have shifted the enforcement and credit risks associated with cash-substitutes from the payee to her bank, making the latter reluctant to perform such a service without accommodating guarantees—a cumbersome and expensive transaction cost for everyday usage. Such risks are avoided when banks or other persons present instruments for payment as agents "on behalf of a person entitled to enforce the instrument" instead of as holders themselves.

This is simply agency: the presenter bank does not take title and assumes no liability or warranties on the instrument, except as an agent (e.g., for loss). According to professor Rosenthal, depository banks do not, as a rule, become holders in due course in deposited checks, as they do not take them for value. They might, however. The depository bank becomes a holder because banks require customers to indorse checks that they deposit. Most depositors indorse in blank by simply signing on the back of the check, thus making the instrument to bearer, and by physically handing it over to an officer or employee of the bank or to a designated automated system, they complete the negotiation. If the presenter bank irrevocably credits the customer's account before the check is honored by the drawee, the presenter bank in fact becomes a holder in due course (as it took the instrument for value). This may occur following either the federal

21. But see Rosenthal, supra note 6 (according to which depository banks do not, as a rule, become holders in due course of deposited checks, as they do not take them for value).
22. U.C.C. § 3-501.
23. See U.C.C. § 3-501 ("Presentment").
25. A special provision of Article 4, which regulates bank-customer relations, allows banks to become holders in items they receive for collection—as depository banks—"whether or not the customer indorses the item." U.C.C. § 4-205(1).
26. See U.C.C. § 3-204.
27. See U.C.C. § 3-204(a) ("regardless of the intent of the signer, a signature and its accompanying words is an indorsement"). There are exceptions to the rule, notably when the "circumstances unambiguously indicate" that the signature was not an indorsement. Is the act of depositing an instrument such a circumstance? The question is not trivial, as indorsers become liable on the instrument, to any person entitled to enforce it upon dishonor, as well as to subsequent indorsers who paid the instrument upon dishonor. See U.C.C. § 3-415(a). Banking practices may be putting customers at risk of becoming liable indorsers when all the latter wished to do is to empower their bank to present. (Avoiding such a liability is possible through an addition of the words "without recourse." See U.C.C. § 3-415(b)).
28. See U.C.C. § 3-201. For an otherwise restrictive indorsement, see U.C.C. § 3-205.
29. See U.C.C. §§ 3-302, 3-303, 4-205. For the definition of "value" in this context see U.C.C. § 4-211. Efforts to "repatriate" portions of Regulation CC to the U.C.C. Article 4—not, however, those concerned with funds availability but only collection provisions—have been stalled for the time being. See Proposed Amendments to U.C.C. Articles 3 and 4, May 2002 Draft, prepared for the 2002 annual meeting of the American Law Institute, which rescinds intentions expressed in the Reporter's Memorandum to Drafting Committee of U.C.C. Articles 3-4-4A, § 1 (Mar. 30, 2000) available at http://www.law.upenn.edu/bll/ulc/ucc3-4-4A/ucc3m300.htm.
Expedited Funds Availability Act ("EFAA"),\textsuperscript{30} or Regulation CC,\textsuperscript{31} or simply bank practices that, experience proves, are sometimes more forthcoming to depositing customers than the statutes actually require.\textsuperscript{32} Note, however, that such credit may be provisional as EFAA does not affect the bank's right to revoke a provisional settlement on a draft that was later dishonored.\textsuperscript{33}

B. Payors

The power to limit an instrument's negotiability is not trivial for drawers and other payors who wish to restrict its transferability and retain some of its in personam characteristics and the defenses that follow from them—in other words, retaining some of the contractual attributes of the financial transaction as opposed to the more complete in rem "propertization" entailed by negotiability. There may be various reasons for this: some wish to be able to invoke future defenses that are untenable against a holder in due course,\textsuperscript{34} or attach the instrument's enforcement to an obligation pertaining to the underlying transaction (which can be achieved, e.g., in the form of a condition stipulated on the instrument and thus revoke its negotiability),\textsuperscript{35} or rely on an oral promise to defer presentment of the instrument, that even if somehow applicable in personam on the relational level between payor and payee, is certainly not binding in rem. While banks would ostensibly like any instrument they accept to be considered negotiable, payors—especially in small business, social and non-com-

\textsuperscript{31} 12 C.F.R. § 229 (2004).
\textsuperscript{32} According to a Federal Reserve publication from January 27, 2005, “most banks make funds available faster than required [by EFAA].” Federal Reserve Board, Check Clearing for the 21st Century Act: Frequently Asked Questions, at http://www.federalreserve.gov/paymentsystems/truncation/faqs2.htm#ques7 (Feb. 27, 2005). EFAA itself requires the Federal Reserve Board to reduce maximum hold times in step with reductions in actual or “achievable” check-processing times. 12 U.S.C. § 4002(d)(1). While the use of electronic transmissions instead of paper transfers between an intermediary bank and the drawee, encouraged by Check 21 (see infra, section II.A., notes 54-58 and accompanying text) should further this trend, consumer groups have alerted the Federal Reserve that this has yet to occur. A joint letter to the Fed sent on behalf of several such groups (including the NCRC, CFA, US PIRG, Consumers Union and Consumer Action) contends that “industry statistics show that nearly half of all checks are clearing using images, which speeds up check clearing, but consumers are still waiting for an improvement in check hold times.” Letter from Consumers Union et al., to Chairman Bernanke and the Members of the Board of Governors (Oct. 31, 2006) (on file with author) available at http://www.consumersunion.org/pdf/checkholdFRB.pdf. See also Essex Constr. Corp. v. Indus. Bank of Wash., Inc., 913 F. Supp. 416, (Md. 1995).
\textsuperscript{33} 12 U.S.C. § 4006(c)(2); U.C.C. § 4-201.
\textsuperscript{34} Holder in due course is a subset of the set of holders, which in turn is a subset of the more general set of persons entitled to enforce the instrument. See U.C.C. § 3-309.
\textsuperscript{35} See U.C.C. §§ 3-104(a) to 3-106; see also WHITE & SUMMERS, supra note 5, at 513.
mercial contexts—maintain an important interest in the ability to create quasi-instruments.

C. A Dissonance of Law and Practice

In practice, even under the pre-revision Article 3, banks paid little attention to such omissions or deletions of “order” language from the face of the check. What banks care about are indorsements. As a matter of practice, anything that appeared like a standardized check and was properly indorsed counted as a check for purposes of presentment, even if it bore no “order” language and was, strictly speaking, not a negotiable instrument. This reality is largely due to the automated technology that banks employ when they “deal with the billions of checks issued every year.” Checks are processed primarily by optic sensors that read the machine-readable data encoded on the bottom of the check. But even if banks could check the negotiability of checks they process—and as argued below, they can, should, and in fact do—they are by and large uninterested in doing so. A dissonance occurred between the law and the practice of quasi-checks. To deal with it, the revisers of the UCC Article 3 added an “extension clause,” UCC §3-104(c), according to which an order that otherwise is a check—by fulfilling the conditions set in §3-104 subsections (a) (re-

36. At least, such is the premise on which the revision of Article 3 seems to proceed. See Reporter’s Memorandum to Drafting Committee of U.C.C. Articles 3-4-4A, (Mar. 30, 2000) available at http://www.law.upenn.edu/bll/ulc/ucc3-4-4A/ucc3m300.htm.

“Legended Checks (§ 3-104(c))

Section 3-104(c) provides that a check can be an instrument even if it does not include order language. As the comment explains, that ordinarily occurs because the maker crosses out the order language on the preprinted check form. § 3-104 cmt. 2. The rationale for that rule is that banks using current check-processing practices cannot reasonably be expected to notice that type of writing on a check. It happens, however, that customers often write other things on checks (“Void after 90 days” “Not good for over $1,000”). The rationale for § 3-104(c) would apply to those legends as well, but they plainly are not protected by that provision. The questions for the Committee are (a) whether to extend the policy reflected in § 3-104(c) more broadly; and (b) how the extension might be limited to accommodate business practices dependent on such legends.” Id. at § VIII(B).

37. This does not mean that deleting these words from the face of checks has no practical function: it may render the instrument relatively unattractive for future transferees, who might be reluctant to take such instruments in payment. Likewise, their value in the secondary market for negotiable instruments—the market that deals in dishonored and otherwise enforcement-challenged drafts and notes—may be considerably lower than otherwise.


39. According to 3-104(c):

“An order that meets all the requirements of subsection (a), except paragraph (1), and otherwise falls within the definition of “check” in subsection (f) is a negotiable instrument and a check.” U.C.C. § 3-104(c).
Regarding negotiability in general) and (f) (defining checks)—but for failing to be "payable to bearer or to order at the time it is issued or first comes into possession of a holder," is a negotiable instrument and a check. Formal law bowed to practice. One may produce an instrument that does not contain the negotiability language, or delete it from a standard-issue check, and it would still be a check and negotiable at that.

D. Pre-Revision Law: A Different Strategy

It is instructive to observe the differences in the ways that pre- and post-revision Article 3 differ on their treatment of quasi-checks. Pre-revision 3-805 treats any "non-negotiable instruments"—not just checks—as if they were negotiable for most purposes, except that there can be no holder in due course in them. The explanation given for this limitation may seem a bit mysterious. The Official Comment to §3-805 remarks, as if it were evident, that this was an unavoidable outcome of the lack of negotiability language. But the whole way §3-805 proceeds is by analogy—extending the scope of provisions that apply to negotiable instruments to non-negotiable ones, regardless of this lack.

It treats some things (non-negotiable, quasi-instruments) as if they were like other things (negotiable instruments), not as if the former were the latter. And so the denial of holder in due course from quasi-instruments should have been based on an analogical argument as well, or more precisely, a reason to limit the application of analogy

40. U.C.C. § 3-104(a)(1).
41. This, at least, is the prevailing view. In another, forthcoming study of U.C.C. §3-104(c) I point out that the question of quasi-checks' negotiability is not, technically, solved so easily. The reason is that only something that is either a "promise" or an "order" is a candidate to be a negotiable instrument in the first place. See U.C.C. §3-104(a). The quasi-check without the "pay" language is not an instruction according to §3-103(a)(6) and therefore does not qualify as "An order that meets all the requirements of subsection (a), except paragraph (1)" which is the condition under which §3-104(c) kicks in. However, the present study treats the extension clause §3-104(c) as providing an adequate remedy to the formal failures of quasi-checks. This issue is briefly elaborated in Section III, below.
42. Pre-revision U.C.C. § 3-805 provides that: This article applies to any instrument whose terms do not preclude transfer and which is otherwise negotiable. ... but which is not payable to order or to bearer, except that there can be no holder in due course if such an instrument. U.C.C. § 3-805 (1962). The Official Comment declares that this section covers "non-negotiable instruments," but that is a mistake: it covers quasi instruments ("otherwise negotiable"); non-negotiable instruments are in fact excluded from it. Id.
43. Of course, instruments may still be designated as non-negotiable. See Regent Corporation USA v. Azmat Bangladesh Ltd. (N.Y. Sup. Ct., Index No. 120865/94 1994) available at http://www.courts.state.ny.us/comdiv/Law%20Report%20Files/July%201998/regent7.htm, (finding that the drafts in question were "not-negotiable instruments... since they were not payable "on demand or at a definite time" according to pre-revision Article 3).
at the holder in due course point. Moreover, consistency with this approach would require not only that holder in due course status be denied in non-negotiable instruments, but for the most part holder status as well (specified payees remain the only persons who may be "holders" of non-order, non-bearer paper, as it does not have to be negotiable to them).44

Post-revision Article 3 takes a different route both conceptually and on the justificatory level, with significant practical differences. Instead of widening the scope of some provisions pertaining to negotiable instruments to non-negotiable ones, it simply waives some conditions of negotiability for checks, in the sense that checks—but not other instruments—that lack order or bearer language become negotiable instruments for any and every purpose, including holder in due course status.45 Note, however, that the two sections—perhaps slightly modified—could have continued happily together. Courts could then treat quasi-instruments as negotiable ones in general,46 except for the status of holder in due course (but applying such doctrines as warranties etc.),47 which exception would not hold in the case of quasi-checks. Why this should be the case with checks in particular now becomes the focus of discussion.

II. Quasi-Checks in Revised Article 3: An Extension Clause That Does not Extend Enough?

As briefly remarked above,48 the UCC Revised Article 3 still contains a technical glitch—a bug, one might say—according to which, on a strict reading of the extension clause, many quasi-checks would still be excluded from the scope of Article 3, with no pre-revision §3-805 recourse. The argument is that post-revision Article 3 fails to distinguish between the two kinds of quasi-checks: those lacking the order or bearer "language of negotiability," and those lacking the "pay" imperative altogether. While UCC §3-104(c) solves the first case, it is silent on the second, although in most imaginable instances, quasi-checks would in fact fall under both categories. The "Pay" language is

44. See U.C.C. § 1-201(20).
45. U.C.C. § 3-104(c).
46. Except that care must be taken not to overextend "§3-805" to written obligations to pay in general, i.e. contracts.
47. E.g., the liability of indorsers or other signatories to a non-negotiable note can be seen as germane to any quasi-instrument. Of course, even an "extended §3-805" would still apply only to instruments; it should not be applicable to just any written undertaking to pay, thus indirectly becoming a i.e. contracts.
48. See Reporter's Memorandum to Drafting Committee of U.C.C. Articles 3-4-4A, supra note 36.
the imperative that constitutes the order to begin with, and its lack ostensibly revokes not merely the paper's status as bearer or order paper, but its very status as an "instruction to pay" following §3-103(a)(6). If it is not an instruction, such quasi-instrument cannot be an order,\(^49\) let alone a draft\(^50\) or a check.\(^51\) §3-104(c) compensates for a quasi-check's failure to comply with requirements set in §3-104(a)(1)—it takes care of the omission of the order or bearer language—but not with the very essence that defines a check, namely that it is an order to "pay." That requirement is set in the parent clause §3-104(a), not in subsection (1), and thus cannot be covered by §3-104(c) whose scope of application is limited to §3-104(a)(1). Most drawers crossing out the negotiability language from legended checks would tend to cross out both the "pay" imperative and the "words of negotiability"; in real world terms, the distinction between those who do and those who do not is arbitrary and senseless; and yet the distinction is operative under UCC Article 3. Only no one seems to notice or care.

The fact that this does not seem to trouble anyone—that the statutory glitch has gone unnoticed by academia and courts alike—can be interpreted in different ways. One is to consider it a failure of scholarship or of the judiciary since 1990 and the subsequent adoption of UCC Revised Article 3 in most US jurisdictions. Alternately, however, this may indicate that once a theoretical and practical solution within the general question of function v. form is commonly reached—here, the appearance that the extension clause UCC §3-104(c) covers also those quasi-instruments that it technically does not—mere technical failings in the relevant statute are relatively unimportant. A drawer or other party attempting to defend against enforcement of a quasi-check on grounds that it lacks the "pay" imperative and thus is not covered by the extension clauses (either under the revised or pre-revision versions of Article 3) would be technically right, and yet no court would be justified in accepting the defense. The practice of quasi-checks has by now created, \textit{de facto}, such expectations of reliance (again, I am concerned more with those of holders than of banks) that, albeit the Oklahoma Court of Appeals' famous dictum in \textit{Walls},\(^52\) concerns of negotiability cannot be relegated solely to the face of the instrument; nothing in human affairs nor in law is quite "without luggage." In deference to the principle

\(^{49}\) See U.C.C. § 3-103(a)(6).

\(^{50}\) See U.C.C. § 3-104(e).

\(^{51}\) See U.C.C. § 3-104(f)

\(^{52}\) See Gerdes et al., \textit{supra} note 13.
expressed by the court in *Walls*, such principles—at least in the area of negotiable instruments, for the reasons discussed above—are best served when spelled out in the form of a rule such as UCC §3-104(c).

I expect the section to be amended some day—perhaps in the more inclusive direction of pre-revision §3-805, while keeping the allowance for holder in due course status in quasi-checks—but not an awful lot hinges on whether it would or would not be, once courts universally figure the real-world interests involved in instrument-based transactions and make the correct policy judgments concerning the default allocation of risks which the extension clauses entail. For extension clauses are an expression of a jurisprudential principal rather than merely a legal rule covering quasi-instruments. This is the principle according to which real-world reliance and relations between parties are in fact germane to the construction of negotiable instruments, even when this particular legal field is known—whether hailed or abused—by its perceived "formalism."

There is one jurisprudential objection that needs be addressed at this point, itself of a formalistic nature. Namely, the devil's advocate's position would be to claim that there is no lacuna in cases of quasi-checks that lack the "pay" language ("class B" as it were), but instead a positive distinction between two sets of instruments. If no lacuna exists, no analogy may be applied; indeed both continental and common law jurisprudences are generally reluctant to extend the scope of legislation by analogy. However, the above analysis proves that there is no counter argument here at all. The extension of negotiability to "class B" quasi-checks proceeds directly from the clause and does not involve analogy to "class A" quasi-checks (that only lack the language of negotiability). Indeed the distinction between the two classes, as argued before, while formally tenable, is functionally senseless. More precisely: as a principle of construction, it does not make sense to apply formalism itself this way. The extension clause is functional in nature, requiring a garb of formalistic language in order to suit the general environment and structure of Article 3. But when ap-

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plied and constructed, its initial functional rationale calls for a wider application than the mere formal categories suggest. Thus the question of analogy need not be addressed here at all.

III. Why Should Quasi-Checks be Treated as Fully Negotiable Instruments, Anyway?

A. Banks, Again

Interestingly, both pre- and post-revision arrangements give similar rationales for quasi-checks provisions. It appears to be generally reiterated: that in practice, banks process checks automatically, mostly on the basis of machine-readable data printed on the face of checks, and effectively have no opportunity to verify the presence of the negotiability language required by §3-104(a)(1). Since October 28, 2004, the Check Clearing for the 21st Century Act (a.k.a. "Check 21")\textsuperscript{54} encourages banks to transmit checks electronically: banks may capture an image of the check—front and back—along with the associated payment information, then transmit this information electronically for collection in lieu of the paper check.\textsuperscript{55} This does not substantively alter other Article 3 or 4 obligations or liabilities\textsuperscript{56} towards customers,\textsuperscript{57} nor contractual ones.\textsuperscript{58}

Does this mean that banks no longer have ample opportunity to review purported checks for problems of negotiability-signifiers? This does not seem true. Checks that tend to be irregular in this respect are

\textsuperscript{54} 12 U.S.C. §§ 5001-5018.

\textsuperscript{55} The volume of image-based clearings, including images and substitute checks, grew from 20.3 million per month in July 2005 to 283.3 million items per month in August 2006, according to statistics posted by the Electronic Check Clearing House Organization (ECCHO). ECCHO projects an annualized 2006 volume of 3.4 billion items clearing using images. According to ECCHO calculations, this amounts for approximately 9.4% of total checks cleared. Figures are taken from www.ECCHO.org and from a supplement letter sent by ECCHO to Federal Reserve Chairman Ben Bernanke (Dec. 18, 2006).

\textsuperscript{56} One liability is added, namely that the bank using a "substitute check"—in effect, a new kind of negotiable instrument, equivalent to the paper check for which it is standing—warrants that (1) the substitute check contains an accurate image of the front and back of the original check and a legend stating that it is the legal equivalent of the original check, and (2) no depositary bank, drawee, drawer, or indorser will be asked to pay a check that it already has paid.

\textsuperscript{57} U.C.C. §§ 3-501(b)(2), 4-110 authorize banks and other parties to agree to alternative means of presentment, such as electronic presentment. This, however, requires specific contractual agreements with all parties involved. By providing that a properly prepared "substitute check" is the legal equivalent of the original check for all purposes, Check 21 in essence changes the default rule; as federal law it supersedes contradictory state laws, including both the U.C.C. and specific legislation that requires banks to return to customers their original checks.

\textsuperscript{58} If a receiving bank—or its customer, i.e. the drawee—requires a paper check the bank may use the electronic image and associated payment information to create a paper substitute check to present or otherwise use instead of the original check.
mostly personal or small business-issued checks. Such checks always have some hand written, or even typed in, non-machine-readable language on them that banks must confirm manually: for one, the sum to be paid and the correspondence of the words to the figures, indorsement by signature (although not—at this point—its authentication or verification, which may be performed by optic sensors comparing the signature to the sample held by the bank), the issue date, any added language that might impair negotiability, etc. Indorsements are of course pivotal. Other language may compromise an ostensibly-negotiable instrument's status in ways that are not covered by §3-104(c), such as conditions or further undertakings that violate §3-104(a) or §3-104(a)(3), respectively, etcetera.

As banks become holders in instruments that are negotiated to them for the purpose of subsequent presentment they risk taking and passing on a non-negotiable instrument. Check 21 changes none of this, it only allows banks to use digital images of checks rather than the paper artifact. A few scenarios are possible: 1) Banks risk crediting the customer's account prior to actual collection of an unenforceable instrument, either by practice or under an Expedited Funds statute; 2) banks may become liable on the instrument to subsequent holders in case they negotiate it further through indorsement, or under transfer or presentment warranties, subject to the statutory exception that allows an instrument to be denied and returned by the drawee without dishonoring it; 3) with drawee banks the case is not just their own risk, which overall convenience in handling checks may justify, but also their liability to a customer whose account was charged for an instrument that should not have been enforced, such as a non-negotiable order to pay a designated person, that is presented by someone other than the designated payee. The opportunity to inspect those checks in fact exists, when a payee or other person either presents a check or deposits it in her account through negotiation. It then passes at least one manual inspection (machine-readable data is then encoded on it if needed, and the remainder of the clearing pro-
cess may be automated). As noted above, the inspection may include far more than verification of indorsement. Even the Check 21 process that allows banks to send electronic images for purposes of presentment, rather than ship the paper itself, requires a precise image of both sides of the instrument that would include all the data available on the check itself. If so—and this certainly seems to be the case—there actually is an established opportunity for banks to inspect negotiability language on all non-commercial and many commercial checks; on any check, in fact, that is not generated by an automated system that produced wholly machine-readable instruments (such as payroll checks). If banks do not wish to empower a teller or an ATM collector to perform this task they can have irregular checks put aside for future examination by a designated clerk; or they may choose to assume all the risks enumerated above. Even then, their customers' interests are still at risk (in scenario (3), above).

The case is a bit more complicated with checks that are sent to a collection lockbox. The sum and other details are then mechanically or digitally encoded on them in preparation for presentment, a "pre-presentment" as it were. Presentment may then be completed on a purely machine-readable basis, in synergy with Check 21. Even then, an agent of the encoding entity, although not necessarily a bank employee, would manually handle the check (or its precise image) at some point. All this may seem somewhat low-tech in a world where digital and online payment systems multiply geometrically. So it is. With changing technology, this analysis may at some point become obsolete—as may checks or negotiable instruments altogether, or for that matter printed law reviews, books, and other textual artifacts. For the time being, however, they are still here to serve their numerous functions.

The fact that banks have opportunities to inspect checks—be it in paper or electronic form—is, of course, no argument against the obvious benefits of streamlining a costly and in some respects inefficient check collection system (in 2002, prior to the enactment of Check 21,
the Federal Reserve system has spent—on processing 16.6 billion checks—a total of $744.3 million). Nevertheless, some such costs must be incurred by the very nature of the instrument system. Sometimes, institutional and relational considerations pull in different directions. This is not the case with quasi instruments, and the following section offers a relational justification for the validation of quasi-instruments that stands independently of the institutional "argument from efficiency."  

B. Protecting Payees and Subsequent Holders

There is a more compelling reason for disempowering drawers from making non-negotiable checks than that based solely on banks' practice and convenience. It has to do with balancing the limitation on drawers' freedom of action with the enforcement risks born by payees and subsequent holders—the general class of persons who might by paid by the instrument via presentment, whether direct payees or holders down the line of negotiation. As noted above, allowing drawers to limit negotiability, while possibly serving useful functions, is also a haven for crooks. Holders of quasi-checks that are non-negotiable for lack of order or bearer language only, would find themselves in a position where enforcing the instrument is onerous or even impossible. Not entitled to holder in due course status, they would be subject to defenses on the instrument and possibly unable to negotiate it to subsequent holders, including not to a depository bank. They would forfeit the relative ease and confidence that negotiable instruments convey on their holders. More often than not they would not be aware of the enforcement obstacles that the instrument's non-negotiability produces at the time they take it.

If the law should treat non-negotiable quasi-checks as negotiable ones—as §3-104(c) does but the pre-revision §3-805 doesn't—the

69. For which it charged $759 million (the Monetary Control Act of 1980 requires the Federal Reserve to charge fees for providing payments services—including check processing—to cover (i) operational expenses, and (ii) imputed taxes and profits that would be earned by private firms providing similar services.) See Board Of Governors Of The Fed. Res. Sys., Ann. Rep. 128, 139 (2002).


71. The "impossible" scenario is when a quasi-check is transferred through quasi-negotiation, leaving the quasi-holder with no Article 3 recourse to enforce the instrument.
compelling reason is protecting payees and subsequent holders at the expense of the drawers’ power to create quasi-instruments at will. Some commentators treat this limitation in a cavalier manner or ignore it altogether, but it doesn’t seem insignificant. However, a drawer may still limit negotiability through a positive signifier, e.g. by imprinting “non-negotiable” or similar language to that effect on the face of the instrument (this will still require banks to inspect the instrument). I do not see how limiting a drawer’s freedom to create instruments—which is akin to her freedom of contract—may be justified merely by making banks’ life easier, even if unifying banks’ handling of all types of instruments is otherwise advisable and cost-reducing.

The best justification for extension clauses such as §3-104(c) or pre-revision §3-805 lays elsewhere. It follows from assessing the respective interests of drawers on the one hand, and the reliance interests of payees and subsequent holders on the other. Innocent payees, especially those down the line of negotiation, are at a much greater risk from non-negotiable instruments than innocent drawers are from not being able to limit the negotiability of their checks. The official comment hints at this general direction, observing that

Absence of the quoted words [bearer or order language] can easily be overlooked and should not affect the rights of holders who may pay money or give credit for a check without being aware that it is not in the conventional form.

As noted above, drawers have other ways of producing non-negotiable instruments available to them, all of which involve the creation of paper—whether order or promise—that looks sufficiently not like a standard check, for it not to be mistakenly taken for one. The availability of such means is the true reason for allowing the quasi-checks “mutation” as a balance between the typical interests of drawers on the one hand and payees and holders on the other. The fact that this helps banks streamline their processes is an added benefit rather than the main justification.

This analysis also shows why the regulation by the post-revision §3-104(c) is—in the case of checks—preferable to the pre-revision §3-

72. In this section I use “holder” in a broad sense, that includes non-holders who are entitled to enforce the instrument. See U.C.C. § 3-301.
73. This interest is recognized in the Federal Reserve’s Regulation CC, whose definition of a check includes nonnegotiable items, drafts not drawn on a bank (as long as they are payable at or through a bank), postal money orders, traveler’s checks, and such instruments that identify the payor bank only by routing number (see Reg. CC, 12 C.F.R. § 229.2(k)). See Fed. Res. Bank of Boston Memorandum Re Comments on U.C.C. Article 3, 4 and 4A Revision Draft of 7/12/00, (Aug. 9, 2000) (on file with author).
74. U.C.C. § 3-104 cmt. 2.
805. Only according to the revised provision does the payee—and not less to the point, subsequent holders—receive the adequate protection of holder in due course status. On the other hand, it still allows the drawer to produce a non-negotiable order or other instrument if the context of any transaction requires it. On the other hand, the post-revision extension clause applies to checks only, and this will be criticized in the conclusion, below, following a look at the diverse ways in which quasi-instruments fared in courts in the absence of a unified applicable jurisprudence.

C. Payees and Holders, Again

As unusual as UCC §3-104(c) seems—within the otherwise formalistic framework of Article 3—it in fact expresses insights that governed some court decisions even prior to the 1990 Revision. In those instances, courts—correctly, I claim—set aside the strict “grammar” of negotiability in favor of a functional and practice-based analysis, considering the reliance of payees and holders in accepting the quasi-instrument in payment. Significantly, this would not violate the prevalent “face of the instrument” interpretative rule-of-thumb, because even when strict grammatical rules in the formation of instruments are not followed, the face of the instrument may still provide enough signifiers and indications of negotiability. Comparing two cases, an earlier one (1975) from Illinois, a later one (1998) from Tennessee, is instructive in more than one way. In both cases, quasi-notes failed to designate either a payee or, by use of such words as “bearer” or “cash,” constitute bearer paper. As a negotiable instrument must be one or the other, this would generally seem a good defense against enforcement. At best, such quasi-notes would then be reduced to contractual status—pending comity or proper assignment—and consequently subject to the contractual defenses that the merger doctrine overcomes. In both cases the language immediately following the

75. On the status of initial payees as holders in due course see discussion below.
76. See Skiles v. Sec. State Bank, 494 N.W.2d 355 (Neb. App. 1992) (Certificates of Deposit—that ostensibly are a kind of promissory notes—were ruled non-negotiable instruments for a number of reasons, such as not being payable to order or to bearer).
77. Both cases fell under pre-revision U.C.C. § 3-111, according to which an instrument is bearer paper if it is payable to:
   (a) bearer or the order of bearer; or
   (b) a specified person or bearer; or
   (c) “cash” or the order of “cash,” or any other indication which does not purport to designate a specific payee.
78. i.e., merging instrument with value, rather than having the instrument merely represent external value. For merger doctrine see Gilmore, supra note 7; SNS Fin., LLC v. ABCO Homes, Inc., 167 F.3d 235 (5th Cir. 1999); Lambert v. Barker, 348 S.E.2d 214(Va. 1986). In fact, as long as
promise/order language indicated, instead of a payee or some designation of bearer, the sum of money held by the instrument (for instance, "Pay to the order of three hundred dollars.")\(^{79}\) In such cases defendants' claim is that the promise or order paper failed to satisfy the constitutive conditions of bearer paper by failing to feature—after the promise or order language—any proper indication of a payee, according to the requirements of pre-revision UCC §3-111 that governed the cases.\(^{80}\)

In the Illinois case of *Broadway Mgmt. Corp. v. Briggs*,\(^{81}\) the purported instrument at issue—which the court interpreted as a note (it had both "promise" and "order" language, the former preceding the latter)\(^{82}\)—read in pertinent part as follows:

> "Ninety Days after date, we, or either of us, promise to pay to the order of Three Thousand Four Hundred Ninety Eight and 45/100 - - - - - Dollars."\(^{83}\)

The underlined words and symbols were typed in; the remainder was pre-printed. On pre-revision UCC §3-111, was this bearer paper? It certainly does not fall under the provisional alternatives of §3-111(a) ("bearer or the order of bearer") nor §3-111(b) ("a specified person or bearer"). Does §3-111(c) apply? Or does the purported instrument contain "any other indication which does not purport to designate a specific payee"?\(^{84}\) The court held that this alternate condition of §3-111(c) was not satisfied:\(^{85}\)

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there are any defenses against enforcement of the instrument, on the one hand, and some protections against loss or destruction of the instrument on the other, the merger doctrine is always qualified. The easiest way to measure this qualification is the absolute merger of value and artifact that cash represents (where the only defense is forgery, a kind of fraud really).

79. I use the term "sum of money held" by an instrument in preference to "represent" and the like, as better fitting the so-called merger doctrine. A valid instrument does not merely represent a sum of money: the value is invested in the instrument, which is that sum.

80. See supra, note 77. There is no real significance to the fact that these are pre-revision cases: the concept of quasi-instrument remains the same, and the revision § 3-104(c) refers only to checks (which are drafts), while these cases concerned notes. Pre-revision § 3-104(e) stated that "Any writing to be a negotiable instrument within this Article must. . . (d) be payable to order or to bearer." Thus the double condition—that the instrument be payable, and that it must be either to bearer or to order, is similar in pre-and post-revision versions.


82. Not an unusual case. When an instrument can be equally interpreted as a draft as well as a note, it is the prerogative of the person entitled to enforce it to chose either (U.C.C. § 3-104(e)). In *Broadway Mgmt.* the promise language precedes the order language, thus extending the promise function over the order function; everything that follows the promise language is subject and parenthesized by it.


84. U.C.C. § 3-111(c) (pre-revision).

85. Influenced, perhaps, by the Official Comment's emphasis on a different situation, namely that of leaving a blank after the order language: "Paragraph (c) is reworded to remove any
The instrument here is not bearer paper. We cannot say that it "does not purport to designate a specific payee." Rather, we believe the wording of the instrument is clear in its implication that the payee's name is to be inserted between the promise and the amount. . .

Such is also the position of Anderson's treatise on the UCC: "When a note is improperly written so that the blank for the name of the payee shows the amount to be paid, the paper is not bearer paper." The court goes out on a limb to uphold the "face of the instrument" doctrine with no consideration for the context of its creation and negotiation. It does not concern itself with the common-law method of analogical reasoning, asking whether the paper in question is more like a blank one, which—to follow the official comment (always a tricky business)—is patently not bearer paper and not a negotiable instrument; or is it more like a paper stating "Pay to cash," which is both?

In a similar but later case, a Tennessee court analyzed a purported instrument in its functional contexts. In the case of Waldron v. Delfs, the paper read as follows:

[Promise to pay to the order of one hundred and fifty three thousand and four hundred and forty dollars Dollars (sic).

The underlined text was inserted, handwritten, between the pre-printed legends. Among other defenses on the instrument, the main question was the same as in Broadway Mgmt.: on §3-111, was this bearer paper? The court ruled that it was:

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86. Broadway Mgmt. Corp., 332 N.E.2d at 133.
89. See supra note 85.
90. See U.C.C. § 3-111(c) (pre-revision).
92. As the facts in Waldron occurred prior to Tennessee's enactment of U.C.C. revised Article 3 in 1995, the case was decided under pre-revision Tennessee Code Annotated §§ 47-3-104, 47-3-111.
It would appear to be a "perversion of logic" if an instrument payable to "cash" qualifies as bearer paper, whereas an instrument payable to a specific amount of cash fails to qualify as bearer paper. In both Broadway Mgmt. and Waldron, enforcement was clearly based on legitimate reliance. In Waldron, the court deemed it absurd to rule on a strict, "face-value" rule. Instead, it first determined whether in the context of relations among the parties there were good grounds for reliance—namely, for the payee taking the instrument as such. Once the court determined that there were, technical flaws on the face of the document could not, in themselves, negate negotiability on a doctrine whose purpose is to protect legitimate reliance. Although not regarding a check and thus not subject to the post-revision extension clause directly, the kind of policy considerations pertaining to quasi-checks may have influenced the court’s liberal construction in Waldron.

There is a related question that while not crucial to this analysis must be mentioned, namely whether the status of holder in due course may be accordable to the initial payee or only to subsequent holders. It is not crucial to the analysis because the reliance of subsequent holders on the negotiability of the instrument is not altogether different from that of initial payees (although not identical, of course, as designated payees may present non-negotiable instruments); and because the argument would hold even if the interests and risks born by the initial payees would not support it. Nevertheless, settling this issue would help integrating quasi-checks in the general template of negotiable instruments. The question itself is in some dispute. There is some merit to the claim that a holder in due course could only be a person to whom the instrument was negotiated, which would preclude, in the case of checks at least, the initial payee to whom the instrument was tendered in payment rather than negotiated. In other words, the argument is that the unusual status of holder in due course is required by the very transferability of the cash substitute rather than in the context of its initial tender as a payment device (thus official comment 2 to UCC §3-305 holds that "In most cases the holder in due course will be an immediate or remote transferee of the payee. . ."). According to

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93. This is a supplemental reason; it joins the argument that under U.C.C. § 3-111(c) there was no "any other indication which does not purport to designate a specific payee." The court adds that

There is no logical justification for creating a distinction between the designation of an inanimate object. . . as the payee and the designation of a certain sum of money as the payee. Judicially creating such a distinction would risk uncertainty for contracting parties, thus thwarting the very intent of the adoption of the U.C.C.

Supra note 91, at 5 of the unpublished decision.
the Colorado Court of Appeals, "[A] payee on an instrument... who deals directly with the drawer or issuer is not typically entitled to assert the rights of a holder in due course."94 Contrariwise, pre-revision UCC §3-302(2) specified that "a payee may be a holder in due course." Although this clause was omitted from the revised UCC §3-302, official comment 4 admits that "the payee... can be a holder in due course, but... [this] is not the normal situation."95 Granted; yet the initial payee may be a holder in due course; and that should apply to quasi-checks, as well. Of course, even if they might not count as holders in due course themselves, initial payees have a clear interest in negotiability precisely because the subsequent holders who take the instrument for value will normally become holders in due course, which directly effects the value of the negotiated instrument.96 The unavoidable conclusion is that even for initial payees, a negotiable instrument and a non-negotiable one are different entities of different value. In this respect—although not in the sense of direct enforcement of the instrument, where payees have an advantage—the reliance on the negotiability of a quasi-instrument is shared by payees and subsequent holders alike.

IV. Conclusion

Quasi-instruments pose real problems of reliance in any system characterized by a formalistic jurisprudence of construction. Dealing with these problems requires breaking down the typical risks born by the several parties involved in payment systems. While I argue that the claims brought by the banking system in favor of treating some quasi-instruments (i.e., quasi-checks) as fully negotiable ones are weighty—irrespective of Check 21 which, if at all, made the inspection of purported-checks easier rather than harder—I justify the doctrine on the basis of the payee and subsequent holders' reliance on apparent-instruments, while retaining payors' ability to create non-negotiable instruments explicitly, limiting their in-rem application. I show that

94. Flatiron Linen, Inc. v. First Am. State Bank 1 P.3d 244 (Co. Ct. App. 1999). See also H. BAILEY & R. HAGEDORN, BRADY ON BANK CHECKS §§ 9.4, 9.6. (rev. ed. 1998) (asserting that in most cases, the holder in due course doctrine is irrelevant if defenses are being asserted against the payee of instrument).

95. See also U.C.C. § 3-305 cmt. 2 (admitting that "[I]n a small number of cases the payee of the instrument may be a holder in due course.").

96. Payees may prefer to negotiate an instrument rather than present it for payment for an array of real-world reasons: e.g., the presented instrument may be consumed by a payee's overdraft, lien or other defenses that her bank may have against crediting her with the sum collected by presentment; the payee may wish to keep the instrument out of the regular circulation of bank-held funds, etc.; or the payee may fear dishonor of the instrument—a risk that a subsequent holder may be more willing to assume.
some courts were sensitive to this concern while others were not, and supply an alternative justification for an extension clause that extends full negotiability to quasi-checks (namely, UCC §3-104(c)). The clause expresses a functional, reliance-based, legal-realistic approach to negotiability at the expense of the strict formalism for which Article 3 jurisprudence has time and again been faulted.97

This justification, however, seems to apply to quasi-instruments in general, rather than privileging only quasi-checks. The 1990 revision, by abolishing §3-805 has deepened the divide between checks and other instruments. It justifiably struck down the awkward restriction that there may be no holder in due course in quasi-instruments, but also limited the scope of application of the provision to quasi-checks only. This would be justified on a so-called "bank-based" interest due to the banking system's special interest in checks and the costs of processing them, discussed above. If, however (as I claim) a truer justification for the extension clause is the relational "payee/holder-based" or "reliance-based" interest, than the distinction between quasi-checks and the other several types of quasi-instruments is misplaced. The court in Waldron followed this logic implicitly.

I have also shown that there is a "bug" in the formulation of the current UCC §3-104(c), and that the extension rule is in fact extended as a matter of practice beyond its black-letter scope of application. It would make good sense to codify this "extended extension" in the next round of Article 3 revision and obliterate the formal and artificial distinction between the two classes of quasi-instruments discussed above—that lacking the language of negotiability and that lacking the "pay" imperative.

The Oklahoma court in Walls required approaching negotiable instruments as "couriers without excess luggage,"98 employing a literate rather than unequivocal policy. The dictum invokes the play Le voyageur sans bagage [Traveler without Luggage] by the French playwright Jean Anouilh, whose protagonist is an amnesiac veteran of the Great War who has completely lost his memory.99 When approaching such texts as negotiable instruments, the formalistic principle of construction requires us to "forget," to an extent, the contextual and relational history of its creation in favor of clear demarcation criteria of validity. Nevertheless, equivocation persists because the court did not instruct that the courier be considered as carrying no luggage at all. Determining what kinds of luggage and how much of it is "excessive" is not a

97. See supra note 7.
98. Supra note 17.
matter for legislative innovation but lays squarely in the domain of application and adjudication. As shown above, a certain amount of "luggage of relations" between the parties is carried even by the stingiest of couriers. Otherwise—while perhaps simpler to apply—this provision would just be too arbitrary.

This essay is titled "an apology for a mutation." By this point in the argument it should be clear that the term "apology" is used here in the classic sense of an argumentative justification rather than the more modern term of an act of contrition or an excuse.\textsuperscript{100} And if we think of quasi-checks as a "mutation" from the standard form of negotiable instruments it is because quasi-checks originated not by fiat, as formal law tends to proceed, but in and through practice, to contest a prevailing formal structure and, in a small way, win it over. For mutation, although prevalent mostly in the life sciences, is really a logical structure of change. Its essence consists of variation from established phenomena that occur not by design but spontaneously, in real terms rather than by construction. In the life sciences—mainly, biology—mutations are studied, analyzed, classified, described and sometimes technologically manipulated. In normative discourses such as law, mutations that emerge through practice suggest themselves for our perusal and critique. Determining whether—and for what justifying reasons—we should support such mutations, has made up the bulk of this apology.

\textsuperscript{100} The model, of course, is PLATO, THE APOLOGY OF SOCRATES (1899) in which Socrates both argues for his notion of the examined life as model for the good life (as well as involving others in it through discourse) and justifies himself in front of the Athens court that eventually condemned him.