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THE STOP PAYMENT OF CHECKS AND THE HOLDER IN DUE COURSE: A CONFLICTS AND COMPARATIVE LAW VIEW

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This article will examine the problems which arise when the drawer of a check stops payment because of fraud in the inducement, failure of consideration, or some other personal defense. Three hypothetical situations will serve as the basis for the discussion:

I. A New York drawer issues a check drawn on a New York bank and payable to a New York payee. The drawer then stops payment on the check, and the payee indorses it to a holder.[1]

II. A New York resident, staying in either New York or Latin America, draws a check on a New York bank and delivers it to a Latin American payee. The drawer then stops payment, and the payee indorses the check to a Latin American holder.

III. A New York resident, while visiting or living in Latin America, issues a check, drawn on a Latin American bank, to a payee in the same country. The drawer then stops payment, and the payee indorses the check to a holder in the same country.

Although these fact patterns vary only with regard to the situs of one or more of the parties, it is this minor variation which creates the difficulties.

I

A New York drawer issues a check drawn on a New York bank and payable to a New York payee. The drawer then stops payment on the check, and the payee indorses it to a holder.

At the outset, it should be noted that stopping payment of a check is not a panacea. The drawer who stops payment may be gaining only a temporary, tactical victory in that the check will not be honored. This forces the payee, or a subsequent holder, to institute an action against the drawer. If litigation is begun, the drawer "has the burden of establishing any and all defenses, not only in the first

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[1] Use of New York as the state involved in these transactions is purely arbitrary, and its law will not be emphasized.

instance but by a preponderance of the total evidence."[2] Because of this burden, the drawer may have done nothing but delay the date of payment. At best, if there is in fact a valid defense to the payment of the check, the payee may decide to let the matter drop if he is unable to secure payment from the payor bank.

There is, however, a third alternative between these extremes: if the payee should negotiate the check to a holder in due course after payment has been refused, the holder in due course will take free of any personal defenses existing between the drawer and the payee.[3] When the drawer is sued by the holder in due course, he will have the same burden of proof regarding defenses as he would have had if the payee were suing on the check. Once the drawer has sustained his burden by showing that a "defense exists," the holder then has the burden of "establishing that he or some person under whom he claims is in all respects a holder in due course."[4] He must "sustain this burden by affirmative proof that the instrument was taken for value, . . . in good faith, and . . . without notice . . . ."[5] In some instances, a holder may believe that he is unable to prove all of these elements and may elect to proceed against the payee rather than the drawer. Consequently, the drawer may escape with no loss in the transaction.

The necessity for speed in the effectuation of the stop-order is recognized in the Uniform Commercial Code, which provides that an oral stop-order is binding upon the bank for not more than fourteen days unless confirmed in writing within that period.[6] Unfortunately, Florida[7] and California[8] have eliminated oral stop-orders from their versions of the Code. In these jurisdictions, a fraudulent payee may be able to win the race to the bank. Banks in these areas may in practice accept an oral stop-order, and this may be held to constitute a waiver of the Code requirement for a written notice.[9] The wording of the Code provisions in these jurisdictions, however, seems to imply nonacceptance of a waiver concept.

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2 U.C.C. § 3-307, Comment 2. The unfortunate phrase "burden of establishing" a fact "means the burden of persuading the triers of fact that the existence of the fact is more probable than its non-existence." U.C.C. § 1-201(8). The "burden of establishing," then, seems to be roughly equivalent to the "burden of persuasion" rule recognized by the laws of evidence and procedure. James, Civil Procedure 248-80 (1965). For a trenchant criticism of the Code's language, see Britton, Holder in Due Course—A Comparison of the Provisions of the Negotiable Instruments Law with Those of Article 3 of the Proposed Commercial Code, 49 Nw. U.L. Rev. 417, 447-50 (1954).

3 U.C.C. § 3-305. See Britton, Bills and Notes 521 (2d ed. 1961).

4 U.C.C. § 3-307(3).

5 U.C.C. § 3-307, Comment 3.

6 U.C.C. § 4-403(2).

7 Fla. Stat. Ann. § 674.4-403 (1966).

8 Cal. Comm. Code § 4403 (West 1964).

9 U.C.C. § 4-403, Comment 6. See also Brady, Bank Checks 425 (3d ed. 1962).

The Code also provides that the stop-order must be received "at such time and in such manner as to afford the bank a reasonable opportunity to act on it prior to any action by the bank with respect to the item[s] described in Section 4-303."[10] Section 4-303 provides generally that the stop-order shall not be effective if it is received after the bank has (1) certified or paid the check, (2) settled for it without having a right to revoke the settlement, (3) completed the process of posting to the account of the drawer or, (4) become accountable for the check under a provisional posting arrangement or because of its late return of the check. Florida's Code adopts the above concepts, and then adds that the bank is not liable for failure to comply with the stop-order on the same day it is received "unless such . . . failure . . . results from the willful and intentional disregard of such order."[11]

Assuming that the bank pays a check after the receipt of a valid stop-order, the Code provides that the "burden of establishing the fact and amount of loss resulting from the payment . . . is on the customer."[12] For example, if a bank, in violation of a valid stop-order, paid the item to a holder in due course, the bank would obviously have a complete defense to a suit brought against it by its drawer-customer: the drawer would have had to pay the check to a holder in due course, and the drawee bank steps into the shoes of such holder when he is paid.[13] Conversely, if the bank improperly pays the check to a payee or a holder who is *not* a holder in due course, the bank becomes subrogated to the rights of the drawer against the payee or holder.[14]

A number of cases decided prior to the Code held that a customer could contractually relinquish any claim which he might have against the bank if it should negligently pay a check in contravention of a stop-order.[15] These cases are apparently overruled by the Code, which provides that the effect of Article Four may be varied by agreement, "except that no agreement can disclaim a bank's responsibility for its own lack of good faith or failure to exercise ordinary care or can limit the measure of damages for such lack or failure . . . ."[16]

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[10] U.C.C. § 4-403(1).

[11] Fla. Stat. Ann. § 674.4-403(1) (1966).

[12] U.C.C. § 4-403(3).

[13] U.C.C. § 4-407(a). See Brown, Bank Deposits and Collections, 48 Ky. L.J. 232, 235-36 (1960); Comment, Stop Payment: An Ailing Service to the Business Community, 20 U. Chi. L. Rev. 667, 674 (1953).

[14] U.C.C. § 4-407(c).

[15] Some courts held that these contractual waivers were invalid because they lacked consideration or were contrary to public policy. Cases in the area are discussed in Britton, op. cit. supra note 3, at 520-21; Note, Stop Payment and the Uniform Commercial Code, 28 Ind. L.J. 95, 98-99 (1952); Comment, supra note 13, at 675-76.

[16] U.C.C. § 4-103(1). Although the term "ordinary care" is partially defined in

Certified Checks. Under both the Negotiable Instruments Law and the Code, the certification of a check upon the request of a *holder* results in the discharge of the drawer and all prior indorsers.[17] Certification of the check upon the request of the *drawer,* however, does not discharge him. These differing results, predicated upon the fact of who sought the certification, led courts working with the N.I.L. to hold that when a check had been certified by the bank at the request of a holder, the drawer could not stop payment because he was discharged from the instrument.[18] On the other hand, if the drawer had the check certified, he would not be discharged from liability, and some courts have held that he would be able to stop payment on it.[19] Consistent with these propositions, it has been held that when the payee or subsequent holder brought suit against a bank which refused to pay a certified check over the drawer's stop-order, the certifying bank could not assert any defenses of the drawer if the bank had certified at the request of the payee or subsequent holder.[20] Conversely, if the drawer had the check certified, the bank could avail itself of his defenses when it was sued by the payee or a subsequent holder.[21] Of course, if the payee or the subsequent holder were found to be a holder in due course, the bank would be liable on its certification no matter who had requested it.[22] Furthermore, if the check were certified at the request of the drawer, he too would be liable to the holder in due course.[23]

It is submitted that these rules were traps for the unwary, because a subsequent holder would have no certain way of knowing whether the drawer or the payee or some prior holder had had the check certified. The Code provides that a stop-order received by a payor bank arrives too late if it is received after the bank has certified the item.[24] This section of the Code is stated in categorical terms, and makes no reference to the qualifications that prevailed under the N.I.L. As comment 5 to section 4-403 specifically states, there is no right to stop payment after certification of a check or other acceptance of a draft, "and this is true no matter who procures the certification." This comment clearly enlarges the meaning of the literal text of sec-

§§ 4-103(3) and 4-202, the Code states that "the term 'ordinary care' is not defined and is here used with its normal tort meaning and not in any special sense relating to bank collections." U.C.C. § 4-103, Comment 4.

17 N.I.L. § 188; U.C.C. § 3-411.

18 See generally Brady, op. cit. supra note 9, at 161-62; Britton, op. cit. supra note 3, at 517-20; Ogden, Negotiable Instruments 498-502 (5th ed. 1947).

19 Ibid.

20 E.g., Bulliet v. Allegheny Trust Co., 284 Pa. 561, 131 Atl. 471 (1925).

21 E.g., Sutter v. Security Trust Co., 95 N.J. Eq. 44, 122 Atl. 381 (1923).

22 Ibid.

23 Supra note 18.

24 U.C.C. § 4-303.

tions 3-411 and 4-303.[25] The same comment continues with the statement that "the acceptance is the drawee's own engagement to pay, and he is not required to impair his credit by refusing payment for the convenience of the drawer." If the certifying bank accedes to a request to stop payment, and is then sued by the holder, the bank should be able to assert the defenses of the drawer, if it certified the check at his request, by "vouching in" the drawer as a party defendant.[26]

II

> A New York resident, staying in either New York or Latin America, draws a check on a New York bank and delivers it to a Latin American payee. The drawer then stops payment, and the payee indorses the check to a Latin American holder.

In the first hypothetical fact situation, the legal relationships between the drawer, drawee-bank, payee, and holder were all governed by the law of New York. In this second situation, the rights and liabilities of the drawer with respect to the drawee-bank may be governed by the law of New York or by the law of some Latin American country, depending upon where the check was drawn. Furthermore, the rights and liabilities of the payee and subsequent holders vis-à-vis the drawer may be governed by the local law of the place of payment (New York) or the local law of the place where the payee indorsed to the holder. Whenever any of the various parties to a check are in different jurisdictions, this may result in a choice-of-law problem. This section of the article will examine the alternative fact situations presented in the above hypothetical problem from the standpoint of the choice-of-law rules in the United States and Latin America.

A. *The United States*

The Uniform Commercial Code. The Code attempts to articulate one specific and one general choice-of-law rule in the field of negotiable instruments. The specific provision firmly fixes the conflicts-of-law rule for banks, whether they be payor, collecting, or depositary banks:

> The liability of a bank for action or non-action with respect to any item handled by it for purposes of presentment, pay-

[25] This is so because the text of § 3-411 speaks only in terms of those parties which are discharged when the holder procures certification, and § 4-303 simply announces the procedures by which a customer may stop payment on an item payable to his account.

[26] U.C.C. § 3-803 seems broad enough to allow this result. See also The Law of Certification of Checks, 78 Banking L.J. 369, 384 (1961). But see Leo Syntax Auto Sales, Inc. v. Peoples Bank & Sav. Co., 6 Ohio Misc. 226, 215 N.E.2d 68 (C.P. 1965).

> ment or collection is governed by the law of the place where the bank is located. In the case of action or non-action by or at a branch or separate office of a bank, its liability is governed by the law of the place where the branch or separate office is located.[27]

The comments to the above section explain that the phrase "action or non-action" is intended to make the rule applicable to all phases of deposit, forwarding, payment, remittance or credit of proceeds, as well as to the stop payment process and the customer's right to stop payment.[28] It would appear, therefore, that the rights of a drawer to stop payment of a check would be determined by the location of the bank, and any local law where the drawer happened to draw the check would affect neither his rights nor the obligation of the bank to comply with the order. For example, if the drawer should happen to be in Argentina (which forbids a stop-order on a check until after the period for presentment has expired),[29] and should draw on his bank in New York and then seek to stop payment, his right to stop payment, and the obligation of the bank to comply, would be controlled by New York law rather than the law of Argentina.

The comments to this section further state that the rule of *Weissman v. Banque de Bruxelles*[30] is rejected. In *Weissman*, a United States Government check was issued in Washington, D.C. and mailed to the payee-corporation in New York. The president of the corporation wrongfully indorsed the check to the Banque de Bruxelles in Brussels, Belgium, for deposit to his own account. The Belgian bank collected the check through collecting banks in New York and Washington. The president then withdrew the amount of the deposit for his own use. The assignees of the receiver of the subsequently defunct corporation brought suit in New York against the Belgian bank. Judge Pound held that if the Belgian bank had acquired full title to the check, the law of Belgium might properly be applied. However, there was no full transfer of the check to the Belgian bank; the check was received for collection, and the bank became an agent of the dishonest indorser. The court was not entirely clear in its reasons why New York law should be used to determine the effect of the indorsement to the Belgian bank. Under the Code, the law of Belgium would be applied to determine the rights of the indorsee-bank.

The specific reference to a rule governing the action or non-action of a branch or separate office of a bank should be of great value to

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[27] U.C.C. § 4-102(2).
[28] U.C.C. § 4-102, Comment 2(c).
[29] Decreto Ley No. 4776, 12 junio, 1963, art. 29.
[30] 254 N.Y. 488, 173 N.E. 835 (1930).

banks in the United States which have branches located in Central and South America. Any suit brought against the parent bank in the United States for the "action or non-action" of a branch located in another country will be controlled by the commercial law of that other country, rather than the local law of the state in which the parent bank happens to be located.

In contradistinction to the clarity of the specific choice-of-law rule governing the liability of banks, the Code's general choice-of-law rule displays ambiguities which are only exceeded by its brevity:

> Except as provided hereafter in this section, when a transaction bears a reasonable relation to this state and also to another state or nation the parties may agree that the law either of this state or of such other state or nation shall govern their rights and duties. *Failing such agreement this Act applies to transactions bearing an appropriate relation to this state.*[31] (Emphasis added.)

In the ordinary case, the parties (drawer, payee, and indorsees) will not, as a practical matter, have any express agreement that the law of any one state or nation will govern the transaction. Therefore, the italicized words present the Code's only practical choice-of-law provision applicable to the rights and duties of the drawer vis-à-vis subsequent parties, including the payee and indorsees.

It is submitted that this provision is, at best, useless, and, at worst, a complete reversal of the traditional notions governing the rights and duties of the parties to a check. The comments to this section explain that the words "appropriate relation" would exclude a case "where the parties have clearly contracted on the basis of some other law, as where the law of the place of contracting and the law of the place of contemplated performance are the same and are contrary to the law under the Code."[32] After excluding this relatively easy case, the comments procede to the more difficult situations, but offer no guidance. "Where a transaction has significant contacts with a state which has enacted the Act and also with other jurisdictions, the question what relation is 'appropriate' is left to judicial decision."[33] No attempt is made to define the term "significant contacts." The comments continue: "In deciding that question [appropriate relation], the court is not strictly bound by precedents established in other contexts."[34] The comments then attempt to illustrate this statement:

> Thus a conflict-of-laws decision refusing to apply a purely

[31] U.C.C. § 1-105(1).
[32] U.C.C. § 1-105, Comment 2.
[33] U.C.C. § 1-105, Comment 3.
[34] Ibid.

> local statute or rule of law to a particular multi-state transaction may not be valid precedent for refusal to apply the Code in an analogous situation. Application of the Code in such circumstances may be justified by its comprehensiveness, by the policy of uniformity, and by the fact that it is in large part a reformulation and restatement of the law merchant and of the understanding of a business community which transcends state and even national boundaries . . . . *In particular, where a transaction is governed in large part by the Code, application of another law to some detail of performance because of an accident of geography may violate the commercial understanding of the parties.*[35] (Emphasis added.)

Let us assume that a court has to determine the title and status of a holder who acquired a check in Argentina. The check was drawn by a New York drawer, upon a New York bank, payable to the order of a New York payee, and the drawer has a personal defense to payment. A court could seize upon the italicized words and hold that the indorsement to the holder was "an accident of geography" and that the application of the local law of Argentina to determine the title and legal status of the holder would "violate the commercial understanding of the parties." This result would be contrary to the rule of *lex rei sitae* adopted by most of the western world. On the other hand, a court could also decide that the choice-of-law rules of the Code are of no help and then decide the case by the usual choice-of-law principles.

It is submitted that the expressions "significant contacts" and "appropriate relation" are traps for the businessman who must make a prompt decision to receive or reject a check drawn and payable in a foreign country. How can he predict what a court will decide as to what contacts are significant or insignificant? How can he decide what is or is not appropriate? Judicial hindsight is hardly a substitute for business foresight. On the other hand, this foreign businessman, using the traditional rule, will understand that his title and legal status in relation to the drawer are governed by the local law where he acquired the instrument. In fact, the general choice-of-law rule of the Code is so vague that a court can use traditional choice-of-law concepts while still paying lip service to the Code.

The Restatement of the Conflict of Laws. The 1960 Tentative Draft of the Restatement of the Conflict of Laws (Second) states that the obligations of the drawer of a bill are determined by the local

[35] Ibid.

law of the state where he delivered the instrument.[36] If a bill indicates where it was dated, that state is presumptively the state where the drawer delivered the instrument, "and this presumption is conclusive in the case of a subsequent holder in due course."[37] Since a city and state are indicated on most checks, it seems that if the drawer draws a check on his New York bank and mails it to a payee in Latin America, New York would presumptively be the state of delivery. If the payee then indorses the check to a holder in the same Latin American country, this presumption would be conclusive. The same rule apparently would prevail even if the drawer actually drew the check while visiting or temporarily residing in the same Latin American country in which the payee and the subsequent holders resided. This somewhat arbitrary rule has much to commend it because it helps eliminate the awkward problem of determining the legal situs of the contract when a check is drawn in one state and then mailed to another. It should be noted, however, that if suit were brought against the drawer in Latin America, the Latin American court could apply the law of the place where the check was to be paid rather than the law of the presumed state of delivery.[38]

The comments to these provisions of the Restatement explain that the term "obligations of a drawer" includes questions of whether he had capacity to bind himself, and "whether he can successfully raise against a subsequent holder in due course personal defenses, as fraud in the inducement and lack of consideration, that would have been available to him in a suit by his immediate transferee."[39] Although the Restatement does provide that "minute details of presentment, payment, protest and notice of dishonor are determined by the local law of the state where these activities take place,"[40] it is questionable whether the drawer's right to stop payment would be classified as a "minute detail." It would seem, however, that the drawer's right to stop payment should be controlled by the law of the state of "delivery" of the check. Inasmuch as this presumed state of delivery will, in most cases, be the state in which the drawee-bank is located, the bank's duties in complying with the stop-order could then be said to follow the law of the place of its location. This is the rule articulated in the Code.

Although the local law of the presumed state of delivery of the

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36 Restatement (Second), Conflict of Laws § 354e (Tent. Draft No. 6, 1960) [hereinafter cited as Restatement].

37 Ibid.

38 See, e.g., Convention for the Settlement of Certain Conflicts of Laws in Connection with Checks, 1931, arts. 5, 7(7), 143 L.N.T.S. 407.

39 Restatement § 354e, comment C.

40 Id. at § 354g.

instrument establishes whether the drawer may assert personal defenses against a holder in due course, the Restatement provides that the validity and effect of an attempted transfer of a negotiable instrument are determined by the law of the state where the instrument was at the time of the transfer.[41] It should be noted that the Restatement has utilized the property concepts of "delivery" and "where the instrument was at the time of transfer" rather than the contractual term of *lex loci contractus*—the law of the situs of the contract. Reasonable men may differ as to the place of the contract when a check is drawn in one state and mailed to a payee in another state, but most people could agree that the state of the payee is "where the instrument was at the time of its transfer."

B. *International Conflicts-of-Law Treaties*

The majority of the Latin American countries, as well as the continental European countries, have entered into a number of multilateral conventions which affect the choice-of-law rules controlling negotiable instruments. Unfortunately, the United States has not been a party to any of these conventions, and, of course, they do not bind its courts. Some attention, however, ought to be given to them by the courts because they reflect, in a readily accessible form, the choice-of-law rules prevailing in Latin America. North American courts ought to exhibit judicial respect for the choice-of-law rules of a country whose law may be involved in the construction and enforcement of a negotiable instrument. Further, a U.S. court could reason by analogy from these conventions when the choice-of-law rules of the forum are ambiguous or nonexistent. Finally, adoption by the United States of the principles articulated in these conventions might induce courts in Latin America to follow similar principles when dealing with U.S. citizens who are parties to a negotiable instrument.

The Bustamante Code. The Bustamante Code of 1928[42] has been ratified by Bolivia, Brazil, Chile, Costa Rica, Cuba, Dominican Republic, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Nicaragua, Panama, Peru, and Venezuela, and signed but not ratified by Argentina, Colombia, Mexico, Paraguay, and Uruguay.[43] This Code deals with most of the choice-of-law questions which could arise in the field of negotiable instruments. Under the Code, the forms of order, indorsement, acceptance, and protest of a bill of exchange are subject to the law of the locality in which each one of these acts takes place.[44] These rules are applicable to checks as well as to bills of ex-

[41] Id. at § 354f.
[42] 4 Hudson, International Legislation 2283-354 (1931).
[43] Pan American Treaty Series, 9 rev. 1961.
[44] Bustamante Code art. 263.

change.[45] In the absence of an express or implied agreement, the legal relations between the drawer and the payee are governed by the law of the place where the bill is drawn.[46] Similarly, the legal relations between the indorser and the indorsee depend upon the law of the place where the bill has been indorsed.[47]

In summary, it would appear that under the Bustamante Code, if a check were drawn in New York and mailed to a payee in Latin America, the law of New York—the place where the check was drawn —would control the legal relations between the drawer and the payee. If, however, the payee should then indorse the check to a holder in his country, the law of that country would determine the status of the holder vis-à-vis the New York drawer. The Code fails to make any specific statement as to which law controls if the drawer should attempt to stop payment of a check. However, since the form of the order is controlled by the law of the country where the act occurs, it seems that a stop-order should be governed by the same law.[48]

C. *Certified Checks and the Choice of Law*

The questions relating to whether a check can be certified, and the effects of certification, present peculiar problems in the conflicts-of-law area. Many Latin American countries do not permit certification of checks, and those Latin countries which do permit it do not agree on the legal effects of certification.[49] In the United States, the certifying bank becomes the primary party on the instrument, the drawer is discharged, and the holder may seek payment only from the drawee-acceptor or the indorsers when a party other than the drawer has had the check certified.[50]

As indicated above, the U.C.C. provides that the law "of the place where the bank is located" controls the effects of certification of a check.[51] Suppose, for example, that the holder of a check provides certification of the check by a branch of a New York bank, which branch is located in a non-Code state. If the certifying branch refuses payment because the drawer had obtained a stop-order, and the holder brings suit in New York against the New York bank, the forum state (New York) should apply the law of the non-Code state

[45] Bustamante Code art. 271.

[46] Bustamante Code art. 264.

[47] Bustamante Code art. 266.

[48] Among other less important compacts are the Convention for the Settlement of Certain Conflicts of Laws in Connection with Checks, 1931, 143 L.N.T.S. 407, ratified only by Nicaragua, and the Treaty on International Commercial Terrestial Law of 1940, 8 Hudson, International Legislation 498 (1949), ratified only by Argentina, Paraguay, and Uruguay.

[49] See, e.g., Código de Comercio de Nicaragua art. 689.

[50] See discussion pp. 228-29 supra.

[51] U.C.C. § 4-102(2).

to determine whether a drawer may stop payment of a certified check, and, if so, the effects of the certification.

On the other hand, the 1960 Tentative Draft of the Restatement provides that the obligations of the acceptor of a bill are determined "by the local law of the state designated in the instrument as the place of payment."[52] If a bill does not indicate a place of payment, the obligations are determined by the local law of the state where the acceptor delivered the instrument, and "that state is presumptively that state where the instrument is dated, if such a state is indicated, and this presumption is conclusive in the case of a subsequent holder in due course."[53] It appears, however, that despite the difference in wording between the U.C.C. and the Restatement, the result would ordinarily be the same, because the place where the certifying bank is located would generally be the place of payment. This latter result would be true even in the unlikely case of a drawer who draws a check in Latin America and then mails it to New York for certification before he negotiates it, and it certainly would be true when the drawer draws a check and has it certified in New York or delivers it to a payee in New York who then has the bank certify it. It would also be true if the Latin American payee had the check certified by a New York bank. Under both the U.C.C. and the Restatement, the location of the person who presents a check for certification, whether he be the drawer, payee, or indorsee, should have no bearing on the bank's obligations.

The Bustamante Code provides that the form of the acceptance is subject to the law of the locality in which the act of acceptance takes place.[54] Likewise, "the obligations and rights existing between the acceptor and the holder are regulated by the law of the place in which the acceptance was made."[55] It would seem that the Bustamante Code is consistent in result with both the U.C.C. and the Restatement, although the wording of the rules is quite different.[56]

Thus, there are three different approaches to the question of what

[52] Restatement § 354d.

[53] Ibid.

[54] Bustamante Code art. 263.

[55] Bustamante Code art. 265. These rules are applied to checks through article 271.

[56] The Convention for the Settlement of Certain Conflicts of Laws in Connection with Checks, 1931, 143 L.N.T.S. 407, provides that the law of the country in which the check is payable shall determine "whether a check can be accepted, certified, confirmed or visaed and what effects are respectively of such acceptance, certification, confirmation or visa." The article also provides that the law of the place of payment determines whether the drawer may countermand payment of a check. Arts. 7(3), (7). The Treaty on International Commercial Terrestial Law of 1940, 8 Hudson, International Legislation 498 (1949), provides that the law of the place where the check is to be paid determines "whether or not the check can be accepted, crossed, certified or confirmed, and the effects of these operations" and "the right of the drawer to revoke the check or to oppose payment." Arts. 33(2), 34(4).

law should control the obligations of an acceptor. The Restatement suggests the place of payment, the U.C.C. suggests the location of the bank, and the Bustamante Code suggests the place of acceptance. Regardless of which rule is applied, however, the result should be the same, since the place of payment, location of the bank, and place of acceptance are generally the same.

III

> A New York resident, while visiting or living in Latin America, issues a check, drawn on a Latin American bank, to a payee in the same country. The drawer then stops payment, and the payee indorses the check to a holder in the same country.

The laws of the various Latin American countries governing stop-orders are far from consistent. Although there are certain countries which have stop-order provisions similar to those of the U.C.C.,[57] most Latin American countries approach the problem differently.[58] The type of provision that is perhaps most unusual is that which allows a stop-order but provides criminal penalties for an unjustified attempt to stop payment. The Dominican Republic uses this tactic.[59] That country permits the countermand of a check if a written stop-order is received by the bank before it makes payment. However, a drawer who stops payment risks being convicted of embezzlement on the ground that "he had ordered the drawee, without justified cause, not to effectuate payment."[60] Honduras provides that if a drawer stops payment before expiration of the time for presentment, the drawer has committed embezzlement unless "he proves that he did not have a deceitful intention."[61] Chilean law requires a drawer to make funds available to pay the amount of the check and judicial costs within three days after protest is made or be sentenced to hard labor.[62]

Another unusual way of attacking the problem is that adopted by Brazil, whose law provides that "those who issue checks without dates or with false dates, or who by counterorder without legal reason procure to frustrate their payment, subject themselves to a penalty

[57] E.g., Bolivia, Ley de 5 de diciembre, art. 9; Ecuador, Ley de Cheques de 18 de noviembre, 1927, art. 27; Código de Comercio del El Salvador, art. 460.

[58] E.g., Argentina, Decreto Ley No. 4776, 12 junio, 1963, art. 29; Mexico, Ley General de Títulos y Operaciones de Credito, 1932, art. 185.

[59] Ley de Cheques No. 2850, 12 de mayo de 1951, art. 33b.

[60] Ley de Cheques No. 2850, 12 de mayo de 1951, art. 66.

[61] Código de Comercio art. 606.

[62] Decreto No. 3777 de 3 de noviembre de 1943, art. 22, Modificado por la ley 7498 de 17 del agosto de 1943. Venezuela also provides for criminal penalties. Código de Comercio art. 494.

of ten per cent above the respective amount [of the check]. . . ."[63] This appears to be a clever approach to the problem since payment may be stopped for a legal reason, but a monetary penalty is assessed if the stop payment is made for some illegal reason.[64]

Certified Checks. The Anglo-American concept that a drawee-bank may certify a check and thereby become liable as an acceptor is strange to most civil-law countries.[65] In those Latin American countries which permit certification, however, there does not seem to be any uniformity as to its legal effect or the effect of a stop-order issued against a certified check. In Argentina, "certification only has effect to establish the existence of the funds and to impede their withdrawal by the drawer during the period agreed [not to exceed five days] . . . ."[66] In Honduras and El Salvador, certification is permitted, but the drawer may revoke the check if he returns it to the bank for cancellation.[67]

The Concept of Holder in Due Course vis-à-vis the Drawer. Although there is no Latin American equivalent to the U.S. distinction between defenses as either real or personal, most civil-law countries have divided the concept of defenses into two classes: the *cambiarias* exceptions—absolute defenses, which pertain exclusively to suits involving negotiable instruments pursuant to the commercial codes; and *extra-cambiarias* defenses—relative defenses, which arise out of the provisions of the civil codes or codes of civil procedure. The *cambiarias* defenses, similar to the real defenses of Anglo-American law, may be asserted against any holder, but the *extra-cambiarias* defenses will not have the same effect as the personal defenses in U.S. law.

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[63] Decreto N. 2.591 de 7 del agosto de 1912, art. 6. See 3 Waldemar Ferreira, Instituições de Direito Commercial § 821 (1953).

[64] Nicaragua states that the drawee shall refuse payment "when the drawer or holder has provided in writing to the drawee that it should not make payment and this notice has been received before the presentation of the check." Código de Comercio art. 691. Costa Rica's new Código de Comercio permits a counterorder for theft, robbery, loss, or because violence was exercised in the obtaining of the check. Arts. 822-25. The Uruguayan Ley 6895, 1919, states that banks shall refuse to pay checks "if the drawer and the holder have advised the bank in time and in writing that it is not to make payment." Art. 13b.

[65] Guatemala expressly prohibits acceptance of a check. Código de Comercio art. 787. Nicaragua also prohibits acceptance. Código de Comercio art. 689. Ecuador's law is less clear, but it seems that in Ecuador, acceptance does not bind the drawee bank. Ley de Cheques de 18 de noviembre, 1927, art. 21.

[66] Decreto Ley No. 4776, 12 junio, 1963, arts. 48-49.

[67] Código de Comercio de Honduras art. 621; Código de Comercio del El Salvador art. 461. Mexican law is very similar, and "the certified check is not negotiable." Ley General de Títulos y Operaciones de Credito, 1932, art. 199. See Tena, Títulos de Credito § 253 (1956). Costa Rican law articulates a conceptual approach which is similar to that in U.C.C. §§ 3-411, 4-303. Código de Comercio art. 828. Colombia and Panama, through their respective adoptions of the N.I.L., permit certification and forbid the stop payment of a certified check. Código de Comercio de Colombia arts. 188-90; Código de Comercio de Panama arts. 187-89; see Velarde y la Guardia, Tradado Sobre la Ley de Documentos Negociables 534-38 (1951).

At the risk of over-generalizing, it might be said that most of the civil-law countries include the following as *cambiarias* defenses:[68]

(1) The drawer or maker was incompetent.
(2) Signatures of the drawer or other obligated persons were obtained by force.
(3) Material limitations were added with the signature of an obligated person, *e.g.*, the drawee accepted the bill of exchange for a lesser amount than called for by the drawer, or an indorser indorsed "without responsibility."
(4) The transferral of the instrument was defective or the legal character of the plaintiff was defective, *e.g.*, an irregular chain of indorsements.
(5) There was a violation of the legal provisions which require certain specific formalities, *e.g.*, failure to present the bill for acceptance, failure to make protest after refusal, or defects in the protest.
(6) There was a formality prohibiting the *cambiarias* action, *e.g.*, statute of limitations.
(7) There was payment, provided that the fact of payment has been noted on the instrument.

The above *cambiarias* defenses, with the exception of number (5), closely resemble some of the real defenses in Anglo-American law. The following *extra-cambiarias* or "relative" defenses are applicable in most civil-law countries:[69]

(1) Those defenses based on the transaction underlying issuance of the instrument. For example, a check is issued in payment of merchandise and the merchandise was never delivered by the payee. This breach of contract may be asserted by the drawer of the check when issued by the payee. This defense may not, in the usual case, be asserted against an indorsee from the payee.
(2) Those defenses derived from personal relations existing between the defendant and the plaintiff. For example, if the drawer of a check is sued by the indorsee, the drawer may assert that the indorsee owes money

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[68] See generally Ascarelli, Derecho Mercantil 512-16 (Mex. 1940); Antelo y Bellucci, Técnica Jurídica del Cheque 130-32, 168, 255-60 (Argen. 2d ed. 1961); Cucurella y Aviles, Derecho Mercantil 448-53 (Spain 2d ed. 1953); Davis, La Letra de Cambio 221-25 (Chile 1957); I Vincente y Gella, Curso de Derecho Mercantil Comparado 406-10 (Spain 2d ed. 1951).

[69] See authorities cited note 68 supra.

to the drawer as the result of a separate loan transaction.

(3) The defenses of novation, compromise, remission, compensation, confusion, and payment may be asserted, provided that they arise out of the personal relations of the defendant and the plaintiff, but the defense of payment may be asserted against any one if the fact of payment is noted on the instrument.

It should be noted that these *extra-cambiarias* defenses are not synonymous with the personal defenses of Anglo-American law. The former are limited to use against an indorsee who has had one of the specified legal relationships with the drawer, while personal defenses in Anglo-American law can be asserted against any indorsee who takes with knowledge of the existence of the defense, without giving value, or in bad faith.[70]

This last point, the good or bad faith of the holder, is treated quite differently in Latin American countries. Most Latin American text writers do not even mention good or bad faith when discussing these concepts in relation to the question of what "contractual" defenses the drawer may assert against the holder. These concepts, when discussed at all, are usually mentioned in conjunction with questions of title; the holder who has acquired the instrument in bad faith may not be the legitimate *owner* of the instrument, and for that reason the drawer may assert defenses against him which do not pertain exclusively to the question of title, but may also include contractual defenses.[71]

For a holder to have taken in bad faith under the U.C.C., it is sufficient if he has been unilaterally dishonest.[72] In Latin America, on the other hand, it is generally required that the dishonesty involve collusion between the indorser and indorsee.[73]

In addition to the requirement that the holder take in good faith and without notice of any defense or claim to the instrument on the part of any person, the U.C.C. requires that the holder take the instrument "for value."[74] In all Latin America, however, only two countries, Colombia and Panama, clearly require that a holder take for

[70] The complex procedural devices of the civilian systems further complicate the concepts of *cambiarias* and *extra-cambiarias*. See Murray, A Survey of Civil Procedure in Spain and Some Comparisons with Civil Procedure in the United States, 37 Tul. L. Rev. 399 (1963).

[71] Supra note 68.

[72] U.C.C. § 1-201(18).

[73] Davis, La Letra de Cambio 224 (1957).

[74] U.C.C. §§ 1-201(44), 3-302, -303.

value in order to be a holder in due course, and this is because both countries have copied the American N.I.L.[75]

It might be argued that any discussion of the question of value is more theoretical than real, because the vast majority of holders will in fact take for value. There is, however, one transaction which could present a very real problem. In the hypothetical situation presented in this section, the payee, rather than indorsing to a holder, might deposit the check to his account in a bank in his country. If that bank does not allow its customer to draw on the check, but indorses it to its U.S. branch for collection, the branch would step into the shoes of its indorser—the Latin American bank. The plaintiff-collecting bank in the United States, though never having given value, would merely have to prove that its principal (the indorser) had not knowingly acted to the detriment of the drawer. It should then be able to recover against the drawer who might have some personal defense against the payee.

IV. Conclusion

There seems to be little hope that the United States and the majority of Latin American countries will ever agree on the terms of a meaningful convention unifying the negotiable instruments laws of the two hemispheres.[76] The mutations of the original *lex mercatoria* by Anglo-Saxon and continental developments would appear too diverse to be reconciled. The unfortunate reluctance of the United States to become a party to conventions dealing with private international law would seem to mitigate against unification of the choice-of-law rules. If there is a solution to this problem, it seems to be only in the mutual, widespread dissemination of knowledge of the laws of the respective countries.

[75] Uruguay might arguably be included in this small group. Ley 6895, 1919, art. 19; Código de Comercio arts. 822-23.

[76] See Nadelmann, The Uniform Law on the International Sale of Goods: A Conflict of Laws Imbroglio, 74 Yale L.J. 449 (1965).