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SOME SUGGESTIONS FOR NONURGENT REFORMS IN THE UCC’S TREATMENT OF ACCOMMODATION PARTIES

James A. Martin*

Lasciate ogni speranza, voi ch’entrare.†

—Dante Alighieri

Anyone who has studied those provisions of the Uniform Commercial Code (UCC or Code) that deal with accommodation parties—chiefly Sections 3-415, 3-416, and 3-606—knows a certain amount of despair at trying to decipher the meaning of these provisions. Fortunately, most of the problems raised are fairly narrow, and few of them have yet posed significant problems for the courts, either because they have not yet arisen or (more often) because the courts have cut through ambiguous language to reach desirable and justifiable results. Thus, most of the problems discussed below do not cry out for immediate legislative attention.

The position of the Permanent Editorial Board for the Uniform Commercial Code with respect to amendments to the Code is a salutary one: “Amendments should be the result of experience rather than of theory.”1 To the extent that this rule is a reflection of the fact that the uniformity of the Code will not be preserved if amendments are suggested in a piecemeal fashion, the suggestions made below may be worthy of consideration—even if the underlying problems have not yet generated litigation—when and if a general revision of Article Three occurs (like the 1972 revision of Article Nine). Whether or not any of the suggestions discussed below ever deserve consideration, it is safe to assume that some will never get it. Some suggestions contained in studies far more

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† Abandon all hope, you who enter.
1 PERMANENT EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE, REPORT NO. 2, at 12 (1964).
illustrious than this one\(^2\) as well as suggestions in some less illustrious works\(^3\) have been ignored in the past.

I. THE DEFENSES OF THE ACCOMMODATION PARTY

A. An Example

Accommodation parties are persons (natural or artificial) who sign negotiable instruments for the purpose of lending their credit to another party to the instrument. Assume, for example, that Edsel was a bright young businessman in need of capital to start or expand his business. He applied to Local Bank for a loan, but the bank was not as convinced as Edsel that the business would succeed and that he would be able to repay the loan. The bank was willing to lend the money only if Henry, Edsel’s rich father, was willing to guarantee the loan. Thus the following arrangements were made: Edsel signed the note as maker, naming Local Bank as payee, and Henry indorsed it, thus becoming an accommodation party. Henry could have signed as a comaker, or even as an acceptor, and still have been an accommodation party although with somewhat different procedural rights.\(^4\) Unfortunately Edsel’s venture failed, and he was unable to repay the note. As a result the bank turned to Henry for payment. Henry is an honest man and will pay if the law says he must, but he is not eager to do more than is required. In some sense he may also feel less obligated than Edsel toward Local Bank, for he himself received nothing of value for guaranteeing his son’s debt.

Henry probably understood his obligation to pay if his son did

\(^2\) For example, the excellent and painstaking Report of the New York Law Revision Commission for 1955: Study of the Uniform Commercial Code [hereinafter cited as NYLRC STUDY], which significantly influenced the shape of the entire Uniform Commercial Code (UCC or Code), was ignored on some matters with no apparent reason. Thus, although the report notes that Subsection 3-415(3) and its use of “oral proof” was inconsistent with the corresponding comment’s use of “parol evidence,” and although the report notes further that the latter term was undoubtedly the one intended, the mysterious “oral proof” was never changed. Id. at 1060.

\(^3\) At least modest powers of discrimination are necessary to understand the complexities of the law of accommodation parties. The reader who glanced to the bottom of the page in full expectation of seeing the author identify in public print those examples of works he considers to be less illustrious than his own should probably not continue into the substance of this article.

\(^4\) As an indorser, Henry has the rights of an indorser under Subsection 3-415(2), which include the right to have the note presented to and dishonored by Edsel before Henry becomes liable. UCC § 3-414. He also has the right to notice of these events. Id. Accommodation comakers and acceptors, on the other hand, have the same rights and responsibilities as ordinary comakers and acceptors with respect to such matters as presentment, dishonor and notice—which is to say no rights at all under Subsection 3-413(1).
not, but not all accommodation parties seem to be this knowledgeable—at least if their statements in court are to be believed. One often sees the defense that the accommodation party did not understand the nature of his obligation, or sees the defense that regardless of what the instrument said, there was an understanding among the parties that the accommodation party would never really have to pay, his name having been added to the instrument only to fulfill half-understood formalities required by the lender. Such defenses rarely if ever succeed. The court may employ some theory of estoppel (i.e., having signed as an accommodation party, the defendant is estopped from denying his obligations as such), or may simply be skeptical of the claim that a lender would require the presence of an accommodation party without intending to take advantage of the rights he gains thereby.

It is not clear that accommodation parties who claim that they were told they would never have to pay are lying. They may have misinterpreted, for example, statements that it was very unlikely that they would ever have to pay. In our example, if Henry had been doubtful about his desire to get involved in Edsel’s financial dealings, Edsel might have minimized as much as possible the likelihood that Henry might some day be liable. In fact, it is even possible that Edsel lied to his father about the latter’s obligations. Such a lie, if unknown to the bank, would presumably not affect the bank’s rights against Henry.

For whatever reasons, either the ones mentioned above or others, accommodation parties seem far more willing than others to raise as many defenses as they can.

B. The Defense of Lack of Consideration

One defense that never works under the Code, but is still raised time after time by forlorn accommodation parties, is that no

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6 Even if the bank does not have the rights of a holder in due course with respect to Henry, Henry is limited to the Code’s special defenses for accommodation parties, not here applicable, and to those defenses available to any other party against a holder under Section 3-306. The defense of Subsection 3-306(b)—“all defenses of any party which would be available in an action on a simple contract”—seems applicable here, with the assumption that the “simple contract” in this situation is the contract of a surety, i.e., the contract defenses are those that would be available in the same situation if no negotiable instruments were involved. The rule in suretyship law is that misrepresentation by the principal debtor is no defense in an action by the creditor against the surety as long as the surety was ignorant of the misrepresentation. L. SIMPSON, HANDBOOK ON THE LAW OF SURETYSHIP 93 (1950).

7 Well, almost never. The accommodation party who signs an instrument that is taken for value, but signs only after it is due (an unusual case) may be deemed not to be liable on his engagement. At least he falls outside the scope of Subsection 3-415(2), which refers to cases in which the instrument is taken for value before it is due.
consideration was received by the accommodation party, even though consideration was received by the accommodated party. In the usual situation, such as our hypothetical, the accommodation party himself does not receive any actual cash or its equivalent in return for his or her signature. In fact, the old Negotiable Instruments Law, in its treatment of the subject, defined an accommodation party in part as one who signed an instrument "without receiving value therefor.\textsuperscript{8} Value and consideration are not the same thing of course, and it is beyond dispute that if the accommodation party signed in order to enable the principal debtor to receive consideration and the latter in fact does receive it, then the accommodation party has received sufficient consideration to support his obligation.

The distinction between value and consideration is usually clear enough in simple fact situations, but when the facts become more complicated, as in \textit{Franklin National Bank v. Eurez Construction Corp.},\textsuperscript{9} even intelligent judges can lose sight of the point. In \textit{Eurez} plaintiff bank was in possession of a note payable to the order of one Eurez. Apparently through oversight the note was not indorsed by Eurez, although he had received the proceeds of the note. Thus plaintiff was deprived of the status of "holder." The note had not been paid when due, and the bank sought to compel Eurez's indorsement and to receive payment from various parties to the instrument, including three guarantors of Eurez's obligation. The guarantors defended on the basis that they had received no consideration, pointing out that the bank was not a holder in due course because it was not a holder, and pointing to Section 3-408 of the Code, which states in part:

\begin{quote}
Want or failure of consideration is a defense as against any person not having the rights of a holder in due course (Section 3-305), except that no consideration is necessary for an instrument or obligation thereon given in payment of or as security for an antecedent obligation of any kind.
\end{quote}

The court noted that no exception from this rule was made for the case of the accommodation party, and took this omission as suggesting that plaintiff, who was not a holder in due course, was subject to the defense of lack of consideration. The more specific provisions of Subsection 3-415(2), however, were seen as controlling:

\begin{quote}
(2) When the instrument has been taken for value before it is due the accommodation party is liable in the capacity in
\end{quote}

\textsuperscript{8} \textit{Uniform Negotiable Instruments Law} § 29.

\textsuperscript{9} 60 Misc. 2d 499, 301 N.Y.S.2d 845. 6 U.C.C. Rep. Serv. 634 (Sup. Ct. 1969).
which he has signed even though the taker knows of the accommodation.

The court noted that the language of the latter section applies to "takers" like the plaintiff and not just to holders. It noted further that the section applies when the taker has taken for value but does not specify that the value must have passed to the accommodation party. It further concluded that this section was meant to support the contract of the accommodation party even when he received no direct consideration and even when the taker was not a holder.

The court's conclusion was correct, although as noted in its own decision, there is a danger that the Subsection 3-415(2) argument may prove too much. The substance of the 3-415(2) argument is that if a taker satisfies the two conditions of the subsection (that the instrument be taken for value and before it is due), the conclusion of the subsection—liability—follows. Since the accommodation party's defense of lack of consideration is inconsistent with the imposition of liability, that defense must be cut off. The problem with this argument is that there are other kinds of defenses that clearly should not be cut off simply because the instrument has been taken before it was due and for value. For example, the accommodation party's defense of discharge under Section 3-606 was clearly meant to apply even when the conditions of Subsection 3-415(2) are fulfilled. Yet the argument that the court used to cut off the defense of lack of consideration seems by its terms to be equally available for the defense of discharge. Only the extra information supplied by Comment 3 to Section 3-415 provides a necessary limitation: Subsection 3-415(2) was designed specifically to deal with problems of consideration, and not with other kinds of defenses.\(^\text{1}\) Thus it should not be interpreted to cut off defenses unrelated to consideration.

There is a more fundamental problem, however, with the reasoning used by the Eurez court. The court created unnecessary difficulty for itself by reading into Section 3-408 an implication that the defense of want of consideration might be available under the facts of that case. It is true that if there had been no consideration, Section 3-408 would by implication have provided a valid

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\(^{1}\)Comment 3 to Section 3-415 states:

Subsection (2) is intended to change occasional decisions holding that there is no sufficient consideration where an accommodation party signs a note after it is in the hand of a holder who has given value.

Although this is not quite the same problem as that in the Eurez case, it seems clear that the stated intention behind Subsection 3-415(2) was not limited to the precise situation mentioned in the comment, while it is equally clear that the subsection was directed at consideration problems, to which the comment makes other references as well.
defense to the accommodation parties in *Eurez*, but there was consideration: the loan made to the accommodated party. The fact that the loan was not received by the accommodation parties (for whom it was never intended) is irrelevant; in fact it would be a very rare case in which the accommodation party personally received value for the use of his name. In most cases the consideration supporting the obligation of the accommodation party is the receipt of value by the accommodated party. The *Eurez* court was undoubtedly aware of this principle in the abstract, but was apparently thrown off the track by the fact that the claimant was not a holder in due course and the fact that Section 3-408 links the notion of holder in due course with that of consideration. A moment’s reflection, however, will make it clear that whether or not there is legal consideration sufficient to support the obligation of the accommodation party is unrelated to subsequent events, like the making of necessary indorsements, that determine whether or not the taker of an instrument will be a holder in due course. Section 3-408 is inapplicable here, not because, as the *Eurez* court thought, it is superseded in the case of accommodation parties by the more specific language of Subsection 3-415(2), but because by its own terms it deals with a factual premise (lack of consideration) not present in the *Eurez* case.  

Section 3-408 is not, however, irrelevant to accommodation parties.  

It is applicable, for example, to cases in which the accommodated party has received no value. In such a case the

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11 So far no reference has been made to the following language of Section 3-408: "[N]o consideration is necessary for an instrument or obligation thereon given in payment of or as security for an antecedent debt." That language may provide alternative support for argument in the text that Section 3-408 is consistent with the result in *Eurez*. One could argue that the obligation of the guarantor on the instrument was given as security for an antecedent debt, i.e., the debt of the accommodated party created when the note was signed. A more likely interpretation, however, is that the quoted language refers to cases in which there is a pre-existing debt for which a note is given, either in payment or for security. In such a case the note is taken for value (Section 3-303(b)), and Section 3-408 says that such value is enough—consideration is not necessary either for the accommodated or accommodation party. (It might have been tidier to say that such facts mean that there is value, rather than that none is necessary.) The proposed interpretation of this language is supported by two further observations: (1) the quoted language is introduced by the word “except.” If the argument in the text is correct that the rule of Section 3-408 is generally inapplicable to the *Eurez*-type situation, there is no need to make an explicit exception. (2) The possibility that the quoted language is applicable to the *Eurez*-type situation, as discussed above, relies on the assumption that the debt of the accommodated party is “antecedent.” That proposition is dubious but at least arguable when the accommodated party is the maker and the accommodation party the indorser, but when their formal roles on the instrument are reversed, or when the two are co-makers and the accommodation party signs first, the debt of the accommodated party is not even technically antecedent.  

accommodated party himself can raise the defense against one who is not a holder in due course, but so too can the accommodation party since his consideration ordinarily consists in the fact that the accommodated party has received value. Interpreted in this light, Section 3-408 can rarely conflict with Subsection 3-415(2), since the latter by its own terms is applicable only when the instrument has been taken for value. If the value for which it is taken is value given to the accommodated party,\(^\text{13}\) the case is outside the scope of Section 3-408.

C. The Defense of Discharge

The discharge rules of Section 3-606\(^\text{14}\)—provide the ordinary accommodation party with the best chance for a successful defense. Section 3-606 never specifically refers to accommodation parties because it covers a more general class of parties: those who have recourse against other persons who have obligations on the instrument or obligations associated with it. Thus indorsers, who have recourse against drawers, makers, and previous indorsers, fall within the scope of Section 3-606. Accommodation parties are covered because they have a right of recourse against the accommodated party under Subsection 3-415(5). Sureties who are parties to the instrument but who are not accommodation parties (because the principal debtor is not a party to the instrument)\(^\text{15}\) are also covered.

The discharge rules fall into two categories: first, Subsection

\(^{13}\) There are ambiguities in the language of Subsection 3-415(2), "taken for value before it is due." In particular one might ask, taken for value by whom? In other words, is the requirement that the instrument be taken from the accommodated party for value (i.e., that the accommodated party receive value), or is the requirement that the taker have given value to his transferor? The two are not equivalent to each other in the case in which the first taker promises, but does not give, value to the accommodated party and subsequently negotiates the instrument to another taker who gives value for it. This problem is explored in Peters, Suretyship Under Article 3 of the Uniform Commercial Code, 77 YALE L.J. 833, 845–48 (1968).

\(^{14}\) Section 3-606(1) provides:

(1) The holder discharges any party to the instrument to the extent that without such party's consent the holder

(a) without express reservation of rights releases or agrees not to sue any person against whom the party has to the knowledge of the holder a right of recourse or agrees to suspend the right to enforce against such person the instrument or collateral or otherwise discharges such person, except that failure or delay in effecting any required presentment, protest or notice of dishonor with respect to any such person does not discharge any party as to whom presentment, protest or notice of dishonor is effective or unnecessary; or

(b) unjustifiably impairs any collateral for the instrument given by or on behalf of the party or any person against whom he has a right of recourse.

\(^{15}\) See text accompanying notes 49–52 infra.
Accommodation Parties

Section 3-606(1)(a) defenses that arise because the holder of the instrument has discharged, or more commonly granted an extension of time to, the principal debtor on the instrument; second, Subsection 3-606(1)(b) defenses that arise when the underlying obligation is backed not only by the credit of the accommodation party but the collateral as well, and the holder "unjustifiably impairs" that collateral. Both cases theoretically represent examples of discharge justified by the fact that the holder has injured the accommodation party by harming the latter's ability to avoid ultimate liability, either by collecting from the principal debtor or by proceeding against his collateral.

One is immediately put on guard by the introductory language of Section 3-606 that it is "the holder" who discharges the accommodation party or others by certain acts. Subsection 3-415(2), as we have already seen, indicates that an accommodation party is liable to "the taker" when the instrument has been taken for value before it is due. "Taker" is not defined by the Code, but the notion of "taking" rather clearly involves something less than being a holder. Thus, Subsections 3-413(2) and 3-413(1) (the contract of the drawer, and contract of the maker and acceptor) state the obligations there imposed to be those of paying the instrument to the holder or to any indorser "who takes it up." This would include, for example, an indorser who has paid the present holder (or a later indorser), and has "taken up" the instrument from the person he paid. This taker may not be a holder since the instrument may have been indorsed to the order of the person paid, and not thereafter indorsed back to the taker. Subsection 3-603(2) allows payment or satisfaction on the instrument to be made by a stranger to it (with the consent of the holder), and states that surrender of the instrument gives him the rights of a "transferee." Section 3-201 gives the transferee the rights of his transferor, and it gives the transferee for value a further right against his transferor to require the transferor's indorsement. The only limitation here is that "negotiation" does not take place until that indorsement has been given, and without negotiation the transferee is not yet a holder. The practical significance of this fact is that a transferee cannot be a holder in due course—although he seems to have all the other rights that a holder might wish.

From the usage noted in the previous paragraph, it seems clear that the drafters of the Code were fully aware of the difference between the meaning of holder on the one hand and transferee or taker on the other. It is not clear, however, that there is a dis-
tinction between the meanings of "taker" and "transferee." In any event, the fact that Subsection 3-415(2) gives rights against an accommodation party to a mere taker, while Section 3-606 discharges an accommodation party for certain acts of the holder, raises the possibility that the variance was intended to have significance. Yet at the same time it is reasonably clear that the rationale of Section 3-606 calls for discharge of the accommodation party whether the acts enumerated in that section are performed by a holder or by a taker, on the basis of a fortiori argument: holders are, at a minimum, takers with a proper indorsement, and if they are to be subject to discharge of the accommodation party for certain acts, so too should the taker. The fact that if a stranger to the instrument unjustifiably impairs collateral, the accommodation party is not discharged does not call for the use of "holder" as opposed to "taker," since both terms would exclude strangers. The Negotiable Instruments Law's section equivalent to Subsection 3-415(2) referred to "holders for value." That provision was, of course, changed with the adoption of the Code. The retention of the word "holder" in Section 3-606 thus may have been an oversight. There is at least one other example of a change in Section 3-606 that was not made in Section 3-415, apparently through oversight.

Three acts of the holder will discharge the accommodation party: (1) releasing or agreeing not to sue any person against whom the accommodation party has, to the knowledge of the holder, a right of recourse; (2) agreeing to suspend the right to enforce the instrument or security interest in collateral against such person; and (3) otherwise discharging such person. None of these acts effects a discharge, however, if there is an "express reservation of rights" against the accommodation party. Why should the enumerated acts discharge the accommodation party? The traditional justification, from the law of suretyship, was that these acts impaired the surety's right to collect from the principal debtor (the person against whom the accommodation party has recourse, in the terminology of the statute). In our example it would be clearly unjust for the bank to be able to change Henry's contingent liability (that he will pay if Edsel does not and that he will have the right to proceed thereafter against Edsel) into an absolute liability, thus depriving Henry of his right of recourse against Edsel. Yet the statute really does not prevent such an outcome, since this deprivation cannot occur in any event.

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16 Uniform Negotiable Instruments Law § 29.
17 See text accompanying notes 50-52 infra.
accommodation party’s right to proceed against the principal debtor is rooted not only in subrogation, but also in a right to reimbursement. Thus, the discharge of Edsel’s debt to the bank might render worthless Henry’s right to be subrogated to the debt, but it has no effect on Henry’s independent right to proceed against Edsel for reimbursement.  

This right does not depend on the continued existence of an obligation between the principal debtor and the holder. The logic of this discharge rule is further obscured by the fact that the holder does not discharge the accommodation party when the release of the debtor is accompanied by “an express reservation of rights.” Such a reservation would preserve all the bank’s rights against Henry as of the time the instrument was originally due. The reservation of rights, to be effective, need not even be communicated to Henry, nor is there any requirement that the reservation be in writing. It need only be “express.”

What sense can be made of such a rule? Since discharge of the principal debtor, coupled with an express reservation of rights against the accommodation party, does not impair the accommodation party’s right to proceed by way of reimbursement against the principal debtor (nor, by statutory fiat, his right to proceed by way of subrogation) the “discharge” of the principal debtor looks rather ephemeral. It has the procedural effect of barring a direct suit by the bank against Edsel, requiring instead the circuity of two suits, one against and one by Henry, but that is hardly a recommendation. As the New York Law Revision Commission Study indicated many years ago, the arrangement almost seems to amount to fraud against Edsel, who may think that he is actually getting something of value from the discharge by the bank. Instead he gets a law suit by Henry. Moreover, to the extent that the effectiveness of the reservation of rights turns on an “express” but perhaps unwritten reservation of rights, the temptation for the bank to claim a reservation when none was made is obviously great.

Perhaps the general arrangement can be best justified on the grounds that the releasing holder is presumed not always to understand the law. The bank may have had any of several in-


\footnote{19} UCC § 3-606(2)(c) provides:

(2) By express reservation of rights against a party with a right of recourse the holder preserves

\ldots

(c) all rights of such party to recourse against others.

(Emphasis added).

\footnote{20} NYLRC STUDY, supra note 2, at 1189. (The analysis of Section 3-606 was prepared for the Commission by Professor Bertram F. Wilcox. Id. at 1154.)
intentions in releasing Edsel. Two seem most likely: an intent to release the entire debt, with no intention to seek payment either from Edsel or Henry; or an intent to release Edsel with no intent to release Henry, making the latter solely responsible for the debt. (The fact that the second intent is unfair and not permitted by the law, as noted above, does not mean that the bank did not entertain it.) It should not be assumed automatically that the bank intended to discharge the entire debt. In cases in which it is clear that that was not the bank’s intention, there should be no such total discharge. If the bank had specifically reserved its rights against Henry, it would be clear that it did not intend to discharge the entire debt. Thus, the “specific reservation” rule can be taken as a way of protecting holders like the bank from a complete discharge when they (perhaps innocently) attempt to accomplish a result not permitted by law.

If that is the explanation for the specific-reservation rule, it is clear that the rule works haphazardly at best: it is true that all holders who specifically reserve rights against the accommodation party can be assumed not to have intended a complete discharge of the debt, but it cannot necessarily be said that even a substantial portion of those who do not intend to discharge the entire debt will think to make a specific reservation of rights. If holders deserve protection from their own ignorance of the law, the protection ought to run on something more substantial than the recitation of a few words. The point is particularly strong, since the same ignorance from which the holder is being saved by the specific-reservation rule will keep him from knowing that he can be saved by the appropriate formula. His use of it will be an accident at best. Even assuming some sense to the rule, why should the holder’s release of the principal debtor force circuity of action—why not say simply that a release which attempts to reserve rights against the accommodation party is ineffective as a release of either accommodation party or principal debtor? Section 3-606 provided an opportunity for a rationalization of this part of the law of suretyship, at least in the area of negotiable instruments. It is unfortunate that the opportunity was not taken. A reform of this area of law of suretyship would admittedly mean different results depending on whether or not the debt in question was evidenced by a negotiable instrument, but uniformity is not to be preserved at all costs. It seems that half a loaf of reform is better than none.

The discharge rule discussed above also applies when the holder grants the principal debtor an extension of time, and not an
Accommodation Parties

outright release. Here the question whether the accommodation party ought to be discharged should turn not on the intent of the holder, as in the case of discharge of the principal debtor, but on the extent of the prejudice to the rights of the accommodation party. Unfortunately, that is neither the message of Section 3-606 nor the actual content of the suretyship law on which it is based. The assumption calcified into Section 3-606 seems to be that any extension granted to a principal debtor, be it a day, a week, or a year, so prejudices the accommodation party that his obligation ought to be discharged altogether.

It is certainly true that an extension may prejudice the accommodation party. As an example, assume that Edsel comes to the bank and convinces one of its officers that although his assets are sufficient to satisfy a judgment on the note, conversion of those assets into cash would ruin his business. On the other hand, Edsel tells the bank officer, business prospects are good, and Edsel has no doubt that a year hence he will be liquid enough to pay the debt without harm to his business. The bank officer believes Edsel and is willing to grant an extension on the note because interests rates are high, or because he would rather not get bad publicity for the bank among other local borrowers. Thus, a year's extension is granted without the signing of a new note. A bit less than a year later, Edsel goes into bankruptcy, and his general creditors are paid only eight cents on the dollar. The bank turns to Henry for payment on the note. Henry might well complain that the bank should not have granted the extension, and that if it had not it could have collected directly from Edsel or it could have collected from Henry, who could in turn have enforced his right of reimbursement at a time when Edsel was still solvent. This scenario makes a good case for the proposition that extensions of time may harm the accommodation party and should in some cases serve to discharge his liability.

This situation raises several questions. How often will the extension actually have produced any harm to the accommodation party? Why, for example, should the bank which extends the payment period when the principal debtor is already insolvent (in the hope that business may improve) lose its rights against the accommodation party? In the latter case, the bank's

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21 The actual statutory language of Section 3-606 refers to one who "agrees to suspend" the obligation. Comment 4 to Section 3-606, however, makes it clear that an extension of time is one of the "suspensions" contemplated.

22 The accommodation party may be ignorant of the extension, either because he is not following the entire transaction or because he assumes, absent a demand for payment, that the principal debtor has paid the obligation.
acts may have improved, rather than impaired the accommodation party's chances to avoid an ultimate out-of-pocket expense. What of those cases, probably more numerous than either mentioned above, in which the extension of time has had no effect on the accommodation party's ultimate fate?

If the rule laid down by Section 3-606 is unsatisfactory in the contexts outlined above in which it fails to take into account the harm actually suffered by the accommodation party, it is doubly so when it is recalled that the holder can avoid discharge of the accommodation party by an "express" reservation of rights. This reservation need not be communicated to the accommodation party. That this was specifically intended is indicated by the fact that a provision of Section 3-606 making any reservation of rights ineffective unless communicated to the party affected was deleted from an earlier draft of the Code. Thus, to the extent that the rule might express a concern for actual avoidable harm to the accommodation party (albeit with a meat cleaver approach), it fails even in that purpose because it makes notice unnecessary.

A problem which complicates the entire matter of time extensions yet further is the fact that the Code does not make an extension per se the cause of discharge of the debtor. Instead, Section 3-606 refers to the situation in which the holder "agrees to suspend the right to enforce." Need such an agreement be binding? That is to say, does the statute refer to an agreement supported by consideration? Professor Willcox pointed out that the use of "agreement," which is defined by Subsection 1-201(3) of the Code as "the bargain of the parties in fact" as opposed to the use of "contract," which under Subsection 1-201(11) means "the total legal obligation," suggests that the suspension or extension was not meant to be limited to binding arrangements. Subsection 3-802(2) provides, "The taking in good faith of a check which is not postdated does not of itself so extend the time on the original obligation as to discharge a surety." Such a rule is unnecessary if Section 3-606 is limited to binding extensions, for the mere taking of an instrument does not seem to constitute a binding agreement. The old Negotiable Instruments Law contained a

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23 See UCC § 3-606(3) (Official Draft 1952).
24 NYLRC STUDY, supra note 2, at 1179.
25 Taking an instrument does constitute a suspension of the right to sue on the underlying obligation until dishonor under Section 3-802(1)(b), but that is a legal effect, not an agreement. Perhaps, however, the point is made weaker by the introductory language of Section 3-802(1), "Unless otherwise agreed .... It could be that Section 3-802(2) was simply designed to avoid the implication that failure to agree that the taking of the instrument would not suspend the obligation constituted an agreement that it would.
requirement that the agreement be "binding," but the drafters of the UCC eliminated the term without comment.

As a matter of sense, the "agreement" referred to in Section 3-606 should not be read too narrowly, since it will make little difference to the accommodation party whether the delay that causes him prejudice (or fails to but is covered anyway) is the result of a binding or nonbinding arrangement between others. As far as the accommodation party is concerned, the problem is not the binding nature of the agreement but the delay itself. Because the rule is supposedly designed for his protection, it would make more sense to read Section 3-606 as if the words "agrees to" were not in it. This approach does not do undue violence to the language, for agreement in the colloquial sense could be found in the act of the holder together with the presumably eager acquiescence of the principal debtor whose debt is being extended. This approach would also focus on the effect of the underlying acts, rather than the words in which they are cloaked.

From the foregoing it is clear that the rule of Subsection 3-606(1)(a) makes little sense in its treatment of time extensions. That it matches the law of suretyship on this subject is of no significance. As was noted in another context, half a loaf of reform here would be better than none at all. Proper deference to the rights of the accommodation party could be preserved by a rule that provides that any extension of the underlying obligation would discharge the accommodation party to the extent that it caused him loss, and that the burden would be on the holder to demonstrate the absence of such loss. Express reservations not agreed to by the accommodation party would be ineffective. The common use of clauses in the original instrument allowing time extensions without notice to or the permission of the accommodation party would still pose problems. These clauses should continue to be given effect, subject to the same rules that govern waivers generally. Under this rule the accommodation party would at least have had the opportunity to protect himself.

Admittedly, one may feel uncomfortable in allowing such a clause to govern, recognizing the fact that the clause often will not be read by the accommodation party. Although it is tempting to point out that one is generally bound by contractual terms whether or not he has read them, so that the result here is no worse than that generated by the general contract rule, the point has already been made in the text of rejecting such arguments in favor of the half-a-loaf principle. However, one retreat from this is the notion, which cannot be proven, that hard problems of substantial breadth, like that of what to do when a person has not read contractual language in a form contract, are best approached uniformly, while uniformity is not a particularly important goal on such relatively narrow questions as discharge.

26 **Uniform Negotiable Instruments Act** § 120(6).

27 Admittedly, one may feel uncomfortable in allowing such a clause to govern, recognizing the fact that the clause often will not be read by the accommodation party. Although it is tempting to point out that one is generally bound by contractual terms whether or not he has read them, so that the result here is no worse than that generated by the general contract rule, the point has already been made in the text of rejecting such arguments in favor of the half-a-loaf principle. However, one retreat from this is the notion, which cannot be proven, that hard problems of substantial breadth, like that of what to do when a person has not read contractual language in a form contract, are best approached uniformly, while uniformity is not a particularly important goal on such relatively narrow questions as discharge.
general approach avoids quibbles about agreements and allows a notice requirement to be reintroduced, without danger of unjust results, by providing that no further discharge of an accommodation party would take place as a result of any harm he suffered after being notified of the extension.

A corresponding clarification should be made in those sections dealing with the accommodation party's right to make early payment. At present, Subsection 3-604(2) discharges an accommodation party when the principal debtor tenders full payment after the instrument is due and the tender is refused. It would seem to follow a fortiori that the accommodation party's own refusal of full payment after the instrument is due should discharge his liability. At the moment such a result is not clear, especially since Subsection 3-603(2) allows "any person" to pay the instrument, even if he is a stranger to it, but only "with the consent of the holder." Consent might reasonably be withheld in the case of the stranger who attempts payment, but the holder should not be permitted to refuse payment by the accommodation party.

It should also be noted that Section 3-606 does not totally ignore causality. Even though the accommodation party may be discharged by acts of the holder that do not really prejudice him, he is discharged only "to the extent that" the holder takes any of the steps enumerated in Subsection 3-606(1). Thus, a partial discharge of the principal debtor, without an express reservation of rights against the accommodation party, would result in a partial discharge of the accommodation party. This limitation is more significant when applied to the holder's impairment of collateral, since it is probably more common for collateral to be partially impaired than it is for debts to be partially discharged or extended. Subsection 3-606(1)(b) provides that to the extent the holder unjustifiably impairs collateral, the accommodation party is discharged. The reason for giving this effect to impairment of collateral is that the accommodation party, after paying the instrument, is subrogated not only to the holder's rights on the instrument against the principal debtor, but also to the holder's security interest in the collateral. Thus impairment of that collateral may have a very practical effect on the accommodation party's ability to recover his losses.

Consistent with the actual-impairment approach implied by the "extent" language of Section 3-606, one case decided under the UCC has indicated that the release of a worthless second mort-

gage leaves the accommodation party's obligations unaffected.\textsuperscript{29} Another court has dealt with this problem in a less understandable way. In 	extit{Key Credit Corp. v. Young}\textsuperscript{30} the holder of a note released to the principal debtor a portion of the collateral which secured the note. The report of the case makes it unclear how much of the collateral was released, but it was less than all. Despite that fact and the court's acknowledgment of the proposition that a release of only some of the collateral may result in only a partial release of the accommodation party, it was held that the accommodation party was totally released. The details of the reasoning were not supplied (and a cynic might note that the defendant accommodation party was a missionary), but the case does raise the question of how to implement the "to the extent" language of Section 3-606. If the collateral is worth ten times the value of the debt, what effect should the release of thirty percent of the collateral have?\textsuperscript{31} None at all, because enough remains to cover the debt? Or a thirty-percent reduction in the amount of the debt? The former approach seems more consistent with the notion of suiting the remedy to the amount of harm suffered. Of course, this principle must be limited to cases in which an adequate "cushion" is maintained: collateral may not bring its "true" value at a foreclosure sale, and various costs must first be deducted from the proceeds of the sale.\textsuperscript{32} If the sale has not yet taken place, the burden should be placed on the holder who releases collateral to show that the proceeds of what remains will actually pay the accommodation party's reimbursement rights plus his costs in selling and storing the collateral as well. It is not clear under Subsection 3-606(1)(b) whether the holder has the alternative of showing that payment is available from the principal debtor himself and that impairment of the collateral thus caused the accommodation party no real harm.\textsuperscript{33}

The kinds of impairment of collateral discussed above (physical release of the collateral or legal release of the security interest), along with physical harm to the collateral, are obvious examples

\textsuperscript{31} See NYLRC STUDY, supra note 2, at 1189–90.
\textsuperscript{32} UCC § 9-504(1).
\textsuperscript{33} Theoretically, the accommodation party could argue that he had suffered real harm from the impairment or release of the collateral even if the principal debtor, against whom he still had a right of recourse, is Howard Hughes, for the accommodation party, subrogated to the rights held by the holder-secured party under Section 9-504(1), would have the right to charge the expenses of "retaking, holding, preparing for sale, selling and the like," and if agreed, reasonable attorneys' fees, against the collateral. If the accommodation party has to sue the principal debtor, however, he has no similar right to collect his expenses or attorneys' fees.
of the kind of impairment which will result in release of the accommodation party, but there is one common type of impairment as to which the courts have split: does the holder's failure to perfect the security interest in the collateral constitute the kind of impairment contemplated by Subsection 3-606(1)(b)? There are obvious differences between release of the collateral, release of the security interest, or physical harm to the collateral, on the one hand, and failure to perfect on the other. The former acts are essentially incurable by the accommodation party: once they have taken place there is nothing he can do about them. Moreover, there is little he can do before he agrees to become an accommodation party to prevent their occurrence. He could have obtained an agreement that would make their occurrence wrongful, but he could not prevent them.

Perfection, on the other hand, is different. If the debtor is cooperative, the accommodation party could probably accomplish the perfection himself in most cases by filing the appropriate financing statement. Whether or not he could be deemed a "secured party" for purposes of the signature requirements of Subsection 9-402(1), he would probably have no difficulty in obtaining the actual secured party's signature, since the latter's failure to perfect is far more likely to be negligent than willful. Under the 1972 version of Subsection 9-402(1), of course, the signature of the secured party would be unnecessary. Even if there were ex post facto difficulties in the accommodation party's perfecting a security interest (through refusal of the debtor to sign the financing statement, for example), the accommodation party always has the opportunity to arrange for filing before he signs the instrument. The holder might also argue that the refraining from releasing collateral or the security interest in it imposes no burden on him and refraining from doing physical harm to the collateral imposes no burden not already imposed by Section 9-207, while the requirement of filing does require of him something he is not otherwise bound to do, even though he would be wise to do it. Because the nature of the ordinary accommodation party's undertaking is to allow suit against him without affirmative "procedural" preconditions such as suit against the principal debtor, it would be consistent to allow suit against the accommodation party without such affirmative "procedural" preconditions as filing a financing statement.

34 This inheres in the statement of Section 3-415(2) that when the proper conditions are met the accommodation party "is liable in the capacity in which he has signed." A maker is liable without presentment to a comaker under and an acceptor is liable without presentment to another party. UCC § 3-415(1). An indorser's liability is contingent upon presentment, but not upon suit against the maker or drawer. UCC § 3-414(1).
All the factors above tend to distinguish failure to perfect from other kinds of impairment of collateral. Nonetheless, it is not clear as one court apparently thought it was, that the accommodation party's ability to perfect, if it exists, should relieve the holder of the instrument of his obligation to do so. The majority of lenders who make use of negotiable instruments are likely to be legally knowledgeable. Often, for example, they will be banks whose business generally requires them to know the law in this area. On the other hand, one of the more frequent examples of the accommodation party is one spouse's accommodating the other on an instrument. It seems more rational to give the burden of perfecting to one who understands it better. The burden, moreover, is not as significant as some others, for the rational secured party will usually perfect his security interest in all cases. Thus, allocation of the burden to the lender will not increase the amount of work he should have done in any event, while allocation of the burden to the accommodation party will give him a task that he would not have had to perform under ordinary circumstances.

Two reported cases decided under the Code have ruled in favor of the proposition that failure to perfect by the holder constitutes an unjustifiable impairment of collateral. The case that held to the contrary, Rushton v. U.M. & M. Credit Corp., involved a situation in which the holder was not the original secured creditor but a transferee from the secured party. Moreover, the parties in the latter case stipulated that the holder believed that its transferee had properly perfected the security interest. Although Subsection 3-606(1)(b) (involving impairment of collateral) contains no knowledge requirement like that of Subsection 3-606(1)(a) (involving discharges and time extensions), the use of "unjustifiably" in the phrase "unjustifiably impairs" in Subsection (b) could be used to import the knowledge requirement into it. That suggestion has been made by others in a different context, and it would harmonize the result in Rushton with the holdings of the two cases finding that failure to perfect results in discharge.

36 At least one Ann Arbor bank has determined that it is cheaper in certain cases involving automobiles (given filings and other statutory fees) to obtain insurance than it is to perfect the security interest.
38 245 Ark. 703, 434 S.W.2d 81, 5 U.C.C. Rep. Serv. 1078 (1968).
39 J. WHITE & R. SUMMERS, supra note 18, at 434 n.123.
40 It should be noted, however, that the court in Rushton did not rely on the argument noted in the text. Rather, it added a one-line justification for its result that may be inconsistent with the reasoning discussed in the text here: in order to protect himself the accommodation party could have perfected in this case, and therefore he should not complain that the holder had not done so. 245 Ark. at 708, 434 S.W.2d at 84, 5 U.C.C.
D. Other Problems

Section 3-606 leaves unresolved other problems as well. The release of the accommodation party caused by release or extension for the principal debtor occurs only if the holder has "knowledge" that the accommodation party is an accommodation party. Yet Subsection 3-415(4) supplies the rule that an indorsement outside the chain of title supplies "notice" of its accommodation character. This "notice" provision relates back most obviously to Subsection 3-415(3), which states in effect that "oral" proof of accommodation is admissible against even a holder in due course, if he has "notice" of the accommodation, "to give the accommodation party the benefit of discharges dependent on his character as such." Since the Code spells out no defenses good against a holder in due course with "notice" but without "knowledge," it appears that the slippage between the "notice" of Section 3-415 and the "knowledge" of Section 3-606 was unintended. Intended or not, the slippage causes problems. Assuming that an anomalous indorsement (i.e., one outside the chain of title) is intended to fulfill the "knowledge" requirement of Section 3-606, and not merely to give "notice," which is of no obvious value, are we to infer that "notice" is the proper general standard for Section 3-606? Or are we to assume that "knowledge" is still the proper standard, with one exception, the anomalous indorsement? The difference could be significant because the Code defines "knowledge" (somewhat circularly, but nonetheless significantly) as "actual knowledge," while a person has "notice" of something when "from all the facts and circumstances known to him at the time in question he has reason to know it exists." Both the notice and knowledge standards seem reasonable for Section 3-606, and it does not seem strained to say as a matter of statutory construction either that references to "notice" in Subsections 3-415 (3) and (4) imply a notice standard of Section 3-606 as well, or that the anomalous indorsement, being a particularly clear form of notice, should be taken as being as good as knowledge, which otherwise remains the standard for Section 3-606.

This distinction could be important in a fairly common situation

Rep. Serv. at 1083. However, even this observation can be limited to its circumstances. In other words, the court may have decided that as between an accommodation party and a holder who had no knowledge of nonperfection, the fact that the former could have perfected was enough to excuse the holder. It is not clear that the same reasoning would have been applied if the holder had known of the lack of perfection.

41 UCC § 1-201(25).
42 Id.
outside the area of accommodation parties. A comaker's right to contribution from fellow comakers is determined by the contract among the comakers, but unless otherwise agreed it is assumed that each will bear a proportionate share.\textsuperscript{43} Thus, in the case of two comakers it is assumed that one who pays the entire instrument may collect one half the amount from the other. This rule would seem to supply "notice" to the holder that one co-maker has a one-half recourse against the other. But does it supply "knowledge" of such recourse? The comakers could have an agreement that splits their liability \textit{inter se} in a different manner and a holder could claim that he had no knowledge that they had not done so. The correct approach, whatever the words of Section 3-606, would seem to be to adopt the "notice" reading and conclude that ordinarily the discharge of one comaker discharges the other for half the obligation. There is, however, reason to believe from Comment 3 to Section 3-606 that discharge of one comaker does not discharge the other at all:

3. The words "to the knowledge of the holder" exclude the latent surety, as for example the accommodation maker where there is nothing on the instrument to show that he has signed for accommodation and the holder is ignorant of that fact. In such a case the holder is entitled to proceed according to what is shown by the face of the paper or what he otherwise knows, \textit{and does not discharge the surety} when he acts in ignorance of the relation.\textsuperscript{44}

If the surmise above about a one-half discharge of the comaker is correct, it would seem that the secret surety should be discharged by at least one-half, since that would be the result even if he were a mere comaker. It is not clear whether the implication of the comment in terms of comakers is to be believed, whether one should simply note the fact that the comments are not part of the statute, or whether one should note that the primary concern of the quoted comment was accommodation makers, and that the commentator, in his concern for such parties, may have forgotten to be careful in his statements about ordinary comakers. Pre-Code practice (under the Negotiable Instruments Law) would not have partially discharged an ordinary comaker by reason of the discharge of a fellow comaker, but little can be deduced from this in interpreting Section 3-606, for there was no discharge of an accommodation comaker by reason of the discharge of his fellow


\textsuperscript{44} UCC § 3-606, Comment 3 (emphasis added).
comaker either—only parties secondarily liable could be discharged by the discharge of parties against whom they had recourse.45

Subsection 3-606(1)(b), dealing with discharge due to impairment of collateral, does not raise similar problems because it has no requirements of knowledge or notice. The absence of these requirements seems simply to be a practical one: it is difficult to think of a case in which a holder can know of the existence of collateral without knowing that impairing it will have an unjustifiable, adverse effect on some party to the instrument. One can think of odd hypotheticals in which this would be the case,46 but they are probably not worth an exception to the rule laid down in this section.

Somewhat more likely, perhaps, is the possibility that a holder could be ignorant of the very existence of the collateral, and thereby impair it. Take, for example, the case in which the original payee of a note demands both collateral and an accommodation party. He then negotiates the note to another holder, but for some reason does not mention or attempt to transfer the security interest. The common law is such that the security interest is transferred nonetheless,47 and the failure of the new holder to perfect the security interest, because of his ignorance of its existence, might result in loss of the collateral to another secured party of the principal debtor. Presumably such a failure should not result in discharge of the holder. The statutory language of Subsection 3-606(1)(b) on which this result could be pegged is the word “unjustifiably” that modifies “impairs any collateral.” The accommodation party can avoid the loss of his rights under such circumstances, as a practical matter, by requiring that the note recite that it is backed by collateral, or better, by personally attending to the filing of a financing statement. A notation would not, of course, destroy the negotiability of the instrument.

45 Uniform Negotiable Instruments Law § 120.

46 One is hereby supplied cheerfully. If the maker of a note were the principal debtor and the first indorser were his accommodation party, and if the note were negotiated by the payee to a holder who had no knowledge of the underlying relationships, the maker might represent that he was the accommodation party and purport to give the holder permission not to file a financing statement covering the collateral. If the holder believed this story, he might never inquire to find out that the true debtor was the maker, who wished to be able to use the collateral as security with other lenders. The holder’s failure to perfect the security interest in the collateral might be considered an unjustifiable impairment of the collateral, even though he had no knowledge that his failure to perfect potentially impaired the real accommodation party’s right of recourse against the maker.

47 See L. Simpson, supra note 6, at 215-17.
II. PROBLEMS WITH SECTION 3-415, “CONTRACT OF ACCOMMODATION PARTY”

Subsection 3-415(1) defines an accommodation party as “one who signs the instrument in any capacity for the purpose of lending his name to another party to it.” Others have already pointed out that the last restriction—that the accommodated party be a party to the instrument—is an unnecessary one. Very little can be advanced in favor of the restriction. A similar restriction was included in an earlier draft of Subsection 3-606(1)(a) discussed above, but was removed after adverse comment by Professor Palmer and the New York Law Revision Commission. Thus, under Subsection 3-606(1)(b), the holder discharges a party who has recourse against any other person by impairing collateral given by or on behalf of that person. It is unnecessary that such a person (the equivalent of an accommodated party) be a party to the instrument. Similarly, Subsection 3-606(1)(b) contains no restriction that the recourse be on the instrument. The only utility to the requirement that the accommodated party be a party to the instrument would seem to be in preserving the regularity of the instrument and protecting the holder from discharge in his dealings with one whom he did not know to be the accommodated party. Yet because Subsection 3-606(1)(a) already contains a knowledge (or notice) requirement, and because the reasons for which Subsection 3-606(1)(b) contains none apply whether or not the accommodated party is a party to the instrument, this intended protection for the holder is unnecessary. This conclusion is especially strong in view of the fact that the Code allows unexpected parties to be accommodation parties; for example, it is possible for a maker to be an accommodation party for a payee. The failure to allow a party to an instrument to be an accommodation party for a nonparty does have one obvious procedural disadvantage for the would-be accommodation party: he cannot use Subsection 3-415(5), which gives the accommodation party a right of recourse against the accommodated party “on the instrument,” with all the procedural advantages that implies. Presumably ultimate liability would not be affected. Professor Peters, noting that the Negotiable Instruments Law contained no restrict-

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48 E.g., Peters, supra note 13, at 838–39.
49 UCC § 3-606(1)(a) (Official Draft 1952).
51 NYLRC STUDY, supra note 2, at 1178–79.
52 Peters, supra note 13, at 838.
tion of the type under discussion here, suggested that courts ignore it as a drafting error. 53

A more serious problem provided by Subsection 3-415(3) is the restriction as to the kinds of proof that may be introduced to show accommodation status for purposes of discharge rights. That subsection states:

(3) As against a holder in due course and without notice of the accommodation oral proof of the accommodation is not admissible to give the accommodation party the benefit of discharges dependent on his character as such. In other cases the accommodation character may be shown by oral proof.

Despite reference to the problem in the New York Law Revision Commission Study, 54 the drafters of the Code never removed the glaring misuse of terminology represented by the word “oral” in this subsection. It is clear that the reference should be to “parol evidence,” whether written or oral, and not merely to oral proof. Comment 1 to this section refers to “parol evidence” as if those were the words of the statute. 55

Even ignoring this drafting oversight, the fundamental meaning of Subsection 3-415(3) is unclear. On the surface the message is simple: the fact of accommodation may be proven by parol evidence against both holders in due course with notice of the accommodation and persons who are not holders in due course. So stated, the section seems to say too little or too much, especially with regard to the holder in due course. How is one to show that a holder in due course had notice of the accommodation? Subsection 3-415(4) indicates that an anomalous indorsement provides notice. Is that the only admissible evidence of notice? If so, there is little reason to split the rule up between Subsections (3) and (4). It would have been much easier to say that parol evidence is admissible against those other than holders in due course and against holders in due course when the alleged accommodation party is an anomalous indorser, yet none of the comments suggests this result. Moreover, it would seem bizarre to allow the holder in due course to overlook the words “accommodation party” after the regular indorsement of a party, and even when the accommodation party’s status is not noted on the instrument, there is at least one ordinary fact setting in which the restriction would seem intolerable: assume once more that Edsel seeks a loan from the bank, which insists on Henry’s signature as an

53 Id. at 838–39.
54 NYLRC STUDY, supra note 2, at 1060.
55 UCC § 3-415, Comment 1.
accommodation party. Edsel makes the note, Henry signs as comaker, and the bank becomes the payee of the note. A payee may be a holder in due course if it takes for value, in good faith, and without notice of a claim or defense. Knowledge that any party has signed for accommodation does not of itself constitute notice of a claim or defense. Thus, the bank would in most cases be a holder in due course. There is no anomalous indorsement. Giving the bank the right to avoid a Section 3-606 discharge seems not only unfair, but inconsistent as well with the general treatment accorded the holder in due course under Subsection 3-305(2): his status as holder in due course provides him no protection against any of the ordinary defenses of a party with whom he has dealt. It seems unlikely that Subsections 3-415(3) and (4) were meant to break that general rule and disallow means other than anomalous indorsements to show that the holder in due course had notice of the fact of accommodation.

Unfortunately, there seems to be no middle ground between the restrictive interpretation suggested above and the free admission of any parol evidence to show notice. (Under this latter interpretation Subsection (4) would be interpreted as merely stating one case in which there is an irrebuttable presumption of notice.) If this position is taken, what has actually been accomplished by this miniature parol evidence rule? It can now be stated thus: parol evidence may not be introduced to show the fact of an accommodation against a holder in due course who does not have notice of the accommodation, but parol evidence may be introduced to show the fact of notice of accommodation. Presumably the overlap between the evidence tending to establish notice of accommodation and the evidence tending to establish the accommodation itself will be significant. Nonetheless, this bifurcated approach might make some sense if it were clear that the initial function of determining the existence of notice was committed to the judge, and that of weighing the parol evidence thereafter admitted committed to the factfinder, whether judge or jury. Such an allocation of functions might have much to be said for it, but if this was in fact the point of Subsection 3-415(3), this section is one of the better examples of skillful obfuscation of legislative intent.

The whole problem could be easily solved by allowing parol

56 Id. §§ 3-302(1), (2).
57 Id. § 3-304(4)(c). The result would be different if the payee were the accommodated party, perhaps, since then he would have notice of the accommodation party's Subsection 3-415(5) defense.
58 My colleague, Professor James J. White, raised this possibility.
evidence against any party to show that he had knowledge that another was an accommodation party and not an ordinary party to the instrument. This is simply not an area in which the virtues of the parol evidence rule are necessary. The knowledge requirements of Section 3-606 already provide the holder with adequate protection.

Subsection 3-415(5), stating that "An accommodation party is not liable to the party accommodated, and if he pays the instrument has a right of recourse on the instrument against such party," has provided an odd twist in two Code cases. It is usual in the case of an accommodation indorser that he accommodates the maker, although it is possible that he is accommodating the payee. The form of the instrument would not necessarily show which was the intended beneficiary of his credit, and the language defining accommodation party in Subsection 3-415(1) as one "lending his name to another" does not clarify the matter. In view of the fact that the accommodation party is not liable to the party accommodated, it would be very handy for an anomalous indorser to be able to convince a court that the payee-plaintiff was the accommodated party. Here there would be no problems with ordinary discharge arguments, for the defense is absolute.

In the Massachusetts case of Gibbs Oil Co. v. Collentro & Collentro, Inc. a note was made by a laundering business payable to a fuel oil company in payment for deliveries of oil. The note was executed by one Irving Atkin for the corporation. After executing the note, Atkin indorsed it on the back with words of indorsement waiving presentment and notice. When the note was not paid by the corporation, Atkin was sued on the instrument. He successfully convinced the trial court that his signature as maker did not bind him personally and that his signature as indorser had been for the accommodation of payee, so that the latter could negotiate the note. A two-to-one majority in the Appellate Division accepted these arguments, despite a vigorous dissent from Judge Shamon, and was affirmed by the Supreme Judicial Court. It is hard to picture the joy and amazement in the law offices of the attorney for defendant Atkin when it was learned that the case had been won by convincing not just one, or two, but three courts, that Atkin, who signed as maker for the corporate obligor in the first instance, had indorsed in his private capacity for the accommodation of the payee and not for the accommodation of his corporation, and was thereby allowed to

invoke Subsection 3-415(5) against the payee. The beneficence of Massachusetts businessmen toward lenders is sometimes breathtaking; fortunately the Massachusetts courts are quick to reward it.

Perhaps the traditionally greater skepticism prevalent in Missouri led its supreme court to formulate a more conservative rule in McIntosh v. White. Although the court’s statement that “[a] negotiable instrument becomes accommodation paper for the payee only in those cases where it clearly appears that it was executed solely for the purpose of negotiation by the payee to obtain credit,” arose in connection with a maker (and not an indorser as in Gibbs) who claimed to be accommodating the payee, the court’s requirement of clear evidence would seem to be a proper standard for all situations in which common sense suggests that the accommodation party originally signed for one other than he now claims.

III. PROBLEMS WITH SECTION 3-416, "CONTRACT OF GUARANTOR"

The last mystery of accommodation parties here to be explored is the meaning of Subsection 3-416(4):

(4) No words of guaranty added to the signature of a sole maker or acceptor affect his liability on the instrument. Such words added to the signature of one of two or more makers or acceptors create a presumption that the signature is for the accommodation of the others.

Is the first sentence intended to mean that a sole maker or acceptor cannot be an accommodation party? When the first sentence is compared with the second, which creates the presumption that the signature is for the accommodation of others in the case of multiple makers or acceptors, the temptation is strong to read the first sentence in contrast: taking it as imposing the irrebuttable presumption that the signature of the sole maker or acceptor is not

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61 Id. at 78, 7 U.C.C. Rep. Serv. at 211 (emphasis added).
62 T.W. Sommer Co. v. Modern Door & Lumber Co., - Minn. -, 198 N.W.2d 278, 10 U.C.C. Rep. Serv. 1197 (1972), is the only other reported Code case in which the result turns on the believability of the defendant-accommodation party’s claim that he signed to accommodate the payee, and not the maker. Although there, as in Gibbs, the accommodation party signed as maker for his corporation and again as guarantor-indorser, and although no special standard of proof is stated, the court’s analysis is far sounder than that in Gibbs. The court inspected the evidence and noted two important factors: first that the guarantor-indorser was a friend of the payee for many years, and second, that the guarantor’s company was in the process of liquidation (under the control of another creditor) and the guarantor had little reason to lend his credit to the corporation.
for the accommodation of another. Yet, of course, that is not exactly what the first sentence says. Instead it says that added words of guaranty do not affect the "liability" of the party. Because Subsection 3-415(2) makes the accommodation party, in most cases, "liable in the capacity in which he has signed," a much more limited reading of the first sentence, and a more reasonable one, would seem to be that a solo guarantor-maker cannot be a collection guarantor, for the liability of a collection guarantor is not the same as the liability of a maker. Words of guaranty will not be allowed to change his liability. Thus, if we change our running example so that Henry becomes the (sole) accommodation maker, but still intends to be an accommodation party, with Edsel as the accommodated payee and the bank as transferee, Henry will not be allowed to limit his liability by adding "collection guaranteed" after his name. Ordinarily the words "collection guaranteed" would mean that the bank would be required to obtain a judgment against Edsel and show that it could not be satisfied before it could proceed against Henry. Here, however, Subsection 3-416(4) would bar that result. This interpretation would not prevent Henry, after writing "collection guaranteed" behind his name, from enjoying the rights of an accommodation party, in particular his rights of discharge under Section 3-606 and contribution or subrogation under Subsection 3-415(5). Because there is nothing to keep Henry, as a solo maker, from being accommodation maker when he avoids words of guaranty, there is no reason to deprive him of that status when he uses words of guaranty, especially since the use of those words, however misguided, does provide some notice to the bank that Henry does not intend to be an ordinary maker. If the interpretation suggested is the right one, it could have been achieved in a far more straightforward fashion by stating that the sole accommodation maker or acceptor cannot limit his liability to that of a collection guarantor. So stated, the restriction makes sense: the collection guarantor's liability is secondary, that is, he is not liable at least until demand for payment has been made against the principal debtor. Yet when the guarantor is the sole maker and the principal debtor is a mere payee-indorser, the principal debtor can point out that as indorser he has no obligation to pay unless demand has been made of the drawer or maker. Even the narrow interpretation of the first sentence of Subsection 3-416(4) breaks this circle, and that is all we need.

The second sentence of Subsection 3-416(4) poses other prob-

\[63\] It might show instead that it was useless to get a judgment in the first place. UCC § 3-416(2) & Comment.
lems. By creating the presumption that the one comaker who writes "payment guaranteed" behind his name is signing "for the accommodation of the others," is there any intent to indicate that the comaker is an accommodation party for "the others" but not a guarantor? This result seemed possible to the authors of the Minnesota Study of the UCC, but it seems that their conclusion derives in part from their belief that a guarantor need not be an accommodation party. If that belief is correct, saying that "there is a presumption that the signature is for the accommodation of the others" might suggest that all guarantor-makers are assumed to be accommodation parties until it is shown otherwise. It might even imply that such persons are accommodation parties and not guarantors, despite the words of guaranty. This effect would come as an unpleasant surprise to a comaker who wrote "collection guaranteed" after his name, since it would mean that he was an accommodation party "liable in the capacity in which he has signed," i.e., liable as a maker, without the right to demand that the holder first proceed against the principal debtors. A better interpretation of the second sentence is that the drafters, in writing the words "create a presumption that the signature is for the accommodation of the others" were concentrating not on the "accommodation" language, which they intended merely as a general shorthand for accommodation parties including guarantors, but were concentrating on the words "of the others" and the presumption that the beneficiaries of the guaranty were the other comakers, and not some other party to the instrument, such as the payee. This conclusion is buttressed by the fact that Subsection 3-415(1), in an earlier draft, defined accommodation parties as those who sign an instrument "as surety for another party to it," and Subsection 1-201(40) still provides that "[s]urety' includes guarantor." Thus, when Subsection 3-416(4) was drafted, creating a presumption that a party was accommodating others in no way suggested that he was not doing so as a guarantor. Again, it would be fairly easy to rewrite the language and remove this ambiguity by referring directly to the concept of guaranty, and not to that of accommodation.

IV. CONCLUSION

The discussion above does not exhaust the list of problems encountered in the interpretation of the sections dealing with

65 Id. at 370.
66 UCC § 3-415(1) (Official Draft 1952).
accommodation parties. An attempt has been made to raise issues not raised in other works and to add a different perspective to problems already discussed. The main substantive criticisms that can be directed at these sections are (1) the failure of Section 3-415 to include parties who are sureties for persons not parties to the instrument, and (2) the failure of Section 3-606 to rationalize the law of discharge of sureties insofar as it deals with negotiable instruments. The other criticisms concern draftsmanship, and although some of them may call for eventual statutory revision, intelligent interpretation will fill the gap until then.