**Indorsement Liability and Transfer and Presentment Warranties**

Welcome to this podcast on Indorsement Liability and Transfer and Presentment Warranties brought to you by CALI. I am Professor Jennifer S. Martin. The topic of this podcast is when a party that has suffered a loss can shift the loss to another party who indorsed the instrument or who either transferred or presented an instrument for payment. Why is this important? Oftentimes an examination question will simply ask who is liable, which often involves analysis of whether a liable party can shift liability to others. This podcast primarily covers the rules of §§ 3-415 - 3-417. You should read those sections carefully.

The capacity in which a person handles an instrument will tell us whether they have liability on an instrument, and whether they might have a claim against another party.

Let’s look at indorsers, meaning those who do not issue an instrument, but rather sign the instrument for the purposes of negotiation. Negotiation being the transfer of a negotiable instrument. Most often the signature is on the reverse side of the instrument. There are rules of the road as to when an indorser can be liable on an instrument. First, an indorser only has liability if the instrument has been dishonored. Second, the liability is for the terms of the instrument at the time indorser supplied the indorsement or if the indorser signs an incomplete instrument, the terms when completed. Third, liability is owed to any person entitled to enforce the instrument (a PETE) or subsequent indorser obligated to pay on its own indorsement. If there are multiple indorsers, the rule of § 3-415 holds each indorser liable to all prior indorsers. Fourth, if the indorsement was made on a check which is not presented to a depositary bank within 30 days after the indorsement, then the indorser does not have liability.

Let’s look at some hypotheticals.

Hypo #1. Presume I write a check for $100 to my friend Scott. Scott, needing lunch money, indorses the back of the check and gives it to Sharlene in exchange for $95. Sharlene, needing money herself, cashes the check at Check Casher, Inc. Next, Check Casher indorses the check and deposits the check at Depositary Bank, which pays Check Casher and presents the check for payment. When my bank dishonors the check, because I am short of funds, Depositary Bank may bring a claim against Check Casher, Sharlene, or Scott under their obligation as an indorser. If Depositary Bank brings a claim for indorsement liability against Check Casher, then Check Casher can bring a claim for indorsement liability against Sharlene or Scott. If Sharlene must pay on the item, then she can bring a claim for indorsement liability against Scott.

Hypo #2. Same facts, but Sharlene forgets about the check and does not present the check for payment until 45 days after she received it from Scott. When Sharlene indorses the check and deposits it at Depositary Bank, my bank dishonors the check, because I am short of funds. Depositary Bank may bring a claim against Sharlene for indorsement liability, but Sharlene will not have a claim against Scott under any obligation as an indorser, because his indorsement liability only lasted 30 days.

Those who transfer an instrument, whether or not they indorse it, are called transferors and make a transfer warranty under § 3-416 and possibly § 4-207. If the warranty is breached, then the transferor has liability. This liability is owed to later transferees in the chain, not including the payor bank. The transferor makes a warranty that includes, among other things, that the warrantor is a PETE, all signatures on the instrument are authentic and authorized, that the instrument has not been altered, and that the instrument is not subject to defense or claim in recoupment of any party which can be asserted against the warrantor.

Let’s look at some hypotheticals.

Hypo #3. Presume Thief steals a check from my mailbox made out to me, indorses it with a blank indorsement and sells it to Scott. Scott then sells the check to Sharlene. Putting aside the Thief, Scott would be a transferor who made a warranty to Sharlene that he was a PETE and that all signatures were authentic. Because the warranty is not true, Scott would have liability to Sharlene. In this case, Scott might take the loss if he cannot find the Thief.

Hypo #4. I purchase a new car from Euro Dealer, signing a $40,000 promissory note as payment. Euro Dealer indorses the note and negotiates it to First Bank. If I fail to pay the note, because the car is a lemon, we might look at indorsement liability. Because more than 30 days have passed since the indorsement of Euro Dealer, indorsement liability is not available to First Bank. First Bank can assert a breach of transfer warranty against Euro Dealer on the basis that the instrument is subject to defense in the form of a breach of contract claim that I could assert against Euro Dealer.

The payee and all other parties in the chain through the depositary bank are called presenters and make a presentment warranty under § 3-417 and § 4-208. If the warranty is breached, then the presenter has liability. This liability is only owed to the payor bank that makes payment or accepts the instrument in good faith. Presentment warranties are slightly more narrow than transfer warranties and include, among other things: (i) that the presenter is a PETE; (ii) that the draft has not been altered; and (iii) the warrantor has no knowledge that the signature of the drawer is unauthorized.

Let’s look at our last set of hypotheticals.

Hypo #5. Recall the check stolen by Thief and transferred to Scott and Sharlene in Hypo #3. If Sharlene deposits the check at Depositary Bank and Payor Bank honors the check, then Depositary Bank, Sharlene, Scott, and Thief will have made presentment warranties to Payor Bank. The presentment warranties would be breached, because none of the parties would be a PETE, due to the theft of the check from my mailbox.

Hypo #6. I write a check made out to the electrician for $200, but the electrician adds a zero to the number making it $2000. Pursuant to the rules of alterations, I as drawer am only liable for the original amount of $200. Moreover, my liability is only to a person taking the check for value, in good faith, and without notice of the alteration. But presume further that the electrician deposits the check at Depositary Bank, which presents it for payment to the drawee, Second Bank. If Second Bank makes payment on the check, it will have a claim against Depositary Bank and electrician for breach of presentment warranties. Here, the presentment warranty that was breached, was that the draft had not been altered. That warranty was not true due to the alteration by electrician.

At this point, you should be able to describe who has indorser liability on an instrument, to whom such liability is owed, and when it can be asserted. You should also be able to describe which parties may claim breach of transfer and presentment warranties, to whom the warranties are made, and when a breach of the warranty can be asserted.

I hope you’ve enjoyed this podcast on Indorsement Liability and Transfer and Presentment Warranties.

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