**Who Can Enforce a Negotiable Instrument?**

Welcome to this podcast on Who Can Enforce a Negotiable Instrument brought to you by CALI. I am Professor Jennifer S. Martin. The topic of this podcast is who has the right to enforce a negotiable instrument. Enforcing a negotiable instrument means a legal right to demand payment from an obligated party. We will also look at enforcement of lost, destroyed, or stolen instruments. It is important to try and use the correct terminology so be on the lookout for the following: holder, negotiation, person entitled to enforce (PETE), presentment, and dishonor.

We sometimes consider the benefit of using a negotiable instrument in that it is highly liquid, meaning the payee can easily sell the obligation and convert it to cash. At some point, though, a party will want to obtain payment on the instrument. Payment can be obtained when the proper party makes what we call a presentment of the instrument to the obligor. In the case of a check, § 3-501 explains that the presentment is made to the drawee bank. In the case of a note, the presentment is made to a party obligated to pay the instrument, typical006Cy the maker unless the note is payable at a bank.

There are some rules in Article 4 covering bank relationships related to enforcement of instruments, Article 3 also provides several rules. First, a demand for payment is effective when received, but while the presentment can be made by any commercially reasonable means, it has to be made at the place of payment if payable at a bank. Second, upon demand of the person to whom a presentment is made, the person making the presentment must do several things, including giving reasonable identification, exhibiting the instrument and signing a receipt. Third, a party to whom presentment is made can return the instrument if it does not have the proper indorsement, if the presentment does not comply with the terms of the instrument or applicable law. Fourth, if a presentment is made after an established cut off hour no earlier than 2:00 PM, the party to whom presentment is made can treat it as occurring on the next business day.

The presentment rules of § 3-501 turn on a demand being made by or on behalf of a person entitled to enforce the instrument (a PETE). As such, it’s the PETE that can enforce the instrument and obtain payment. Pursuant to § 3-301, a PETE is most commonly simply a person who is a holder, even if the person is not the owner of the instrument or has wrongful possession of it. However, it is not necessary to be a holder or to be a PETE. There are some non-holders in possession of an instrument who have the rights of a holder. Additionally, there are persons not in possession of an instrument who are PETEs, pursuant to §3-309 on lost, destroyed, or stolen instruments, or § 3-418(d) on mistake.

Let’s look at some hypotheticals.

Hypo #1. I write a $100 check payable to the order of my daughter, Emma, and give it to her. Emma would be a holder. In this case, Emma would be a holder because she is a person in possession of the instrument, and she is the person identified as payee. Because she’s a holder, she also qualifies as a PETE, under
§ 3-301, and may enforce the instrument to obtain payment.

Hypo #2. I write a $100 check payable to the order of my daughter, Emma, and give it to her. Emma would be a holder. Emma adds her indorsement to the reverse side of the check and sells the check to her friend Ashley. In this case, Ashley would be a holder because she is a person in possession of the instrument and Emma added a blank indorsement, making the check bearer paper. Because Ashley is the person in possession of the instrument, she is a holder and a PETE under § 3-301. Ashley may enforce the instrument to obtain payment.

Hypo #3. I write a $100 check payable to the order of my daughter, Emma, and give it to her. Emma adds her indorsement to the reverse side of the check, intending to give it to her friend Ashley. Thief picks up the check before Emma delivers it to Ashley. In this case, Thief would be a holder, because she is a person in possession of the instrument and Emma added a blank indorsement, making the check bearer paper. Even though the Thief is not the owner of the instrument and is in wrongful possession of it, Thief is the person in possession of the instrument, so she is a holder and a PETE under § 3-301. Thief may enforce the instrument to obtain payment.

Sometimes non-holders can also be PETEs. The rule of § 3-203 explains that an instrument is transferred when it is delivered by a person, other than its issuer, for the purpose of giving the person a right to enforce the instrument. When an instrument is transferred for value, a transferee does not become a holder because of the lack of indorsement, there is no negotiation, but the transferee has a right to obtain the indorsement.

Hypo #4. I write a check for $100 payable to the order of my daughter Emma and give it to her. Emma sells the check to her friend Ashley for $100, but forgets to provide her indorsement. Ashley would not be a holder, because she does not have the proper indorsement. Despite the lack of indorsement, Ashley, a non-holder, would obtain Emma’s right to enforce the instrument and would be a PETE. Because Ashley has a right to obtain the indorsement, once she obtains it, she would also be a holder. Ashley may enforce the instrument and obtain payment.

The last classification of PETEs, is that of certain persons who are not in possession of the instrument, but are entitled by statute to enforce it nevertheless. The two statutory provisions are § 3-418(d) and § 3-309.

The rule of § 3-418(d) operates in a limited situation where the bank pays an item by mistake, but is able to recover the payment or revoke acceptance of it. The person who suffers from the recovery of the payment is a PETE, even though they don’t have possession of the instrument any longer, often because it’s been destroyed.

The rule of § 3-309 provides a person not in possession of an instrument that has been lost, destroyed, or stolen PETE status. In order for this rule to operate, the person has to have been entitled to enforce the instrument, when the loss occurred or acquired ownership of the instrument from a person who was a PETE when the loss of possession occurred. Of course, for this rule the person must not be able to obtain possession of the instrument and must prove the terms of the instrument and their right to enforce it. Additionally, because of the risk of loss when a PETE cannot present the instrument, the person required to pay must be adequately protected from other claims.

Hypo #5. I write a $100 check payable to the order of my daughter Emma and give it to her. Emma has not indorsed the check and it is destroyed in a fire. Emma would be a PETE, even though she’s not in possession of the instrument, because she was entitled to enforce the instrument before the fire and she cannot obtain possession of the instrument, because it was destroyed. Emma should be able to use the rule of § 3-309 to claim PETE status and enforce the instrument.

At this point, you should be able to describe the process of presenting an instrument for payment, as well as which parties will be able to enforce the instrument as a PETE, including holders, non-holders with rights, and even certain persons not in possession of the instrument.

I hope you’ve enjoyed this podcast on Who Can Enforce a Negotiable Instrument.

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