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Effect Upon Negotiability of Provisions for Acceleration or Extension of Time in Bills and Notes

C. Severin Buschmann
Indianapolis Bar Association

COMMENTS

EFFECT UPON NEGOTIABILITY OF PROVISIONS FOR ACCELERATION OR EXTENSION OF TIME IN BILLS AND NOTES

The decisions are in considerable disagreement as to the effect upon negotiability of a provision for acceleration of an instrument otherwise negotiable. The courts seem to make a distinction between a provision for acceleration which places upon the maker the conditional duty to pay at an earlier date, and one which gives a power to the payee or holder to declare the instrument due.

The majority of the decisions, both prior to and since the adoption of the Negotiable Instruments Law, hold that a provision placing upon a maker the conditional duty of paying at an earlier day than the day fixed does not render the instrument non-negotiable. For example, the decisions are fairly consistent in holding that a provision rendering the note due by reason of some default upon the part of the maker does not impair negotiability. Nor is this affected by the fact that the provision might provide that the holder shall have the power to declare the instrument due in case of such default. The theory of these cases is that the maker has fixed a day certain upon which he is under a legal duty to make payment, but that he is also under a conditional duty to pay at an earlier date in case of a failure upon his part to comply with certain conditions.[1]

In the case of *Nickell v. Bradshaw*, there was a provision in the instrument for the acceleration of the due date upon the happening of special events solely within the control of the maker at the option of the holder. In holding the instrument negotiable, the court said, in quoting from another decision:[2]

" 'To constitute a negotiable promissory note, the time, or the event, for its ultimate payment, must be fixed and certain; yet it may be made subject to contingencies, upon the happenings of which, prior to the time of its absolute payment, it shall become due. The contingency depends upon some act done or omitted to be done by the maker, or upon the occurrence of some event indicated in the note; and not upon any act of the payee or holder, whereby the note may become due at an earlier date.'

"We think the general rule should be, and the same is, hereby adopted in this state; and, applying it to the paper here in question, we hold that the same is negotiable. None of the conditions in the acceleration clause depend upon the act of the holder, nor are they within his control; but all of such contingencies depend either upon some act or omission of the maker, or upon an event indicated in the paper, not within the control of either party."[3]

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[1] *McCormick & Co. v. Gem State Oil and Products Co.* (Idaho) 222 Pac. 286, 34 A. L. R. 876, 872; *Nickell v. Bradshaw* (Ore.) 183 Pac. 12, 11 A. L. R. 623; 3 R. C. L. 910, 8 C. J. L39.

[2] *Nickell v. Bradshaw* 183 Pac. 12 a p. 18.

[3] *Ernst v. Steckman*, 74 Pa. 13, 15 Amer. Rep. 542.

The court thus reiterates the rule frequently stated to the effect that an acceleration provision in favor of the holder in case he deems himself insecure renders the instrument non-negotiable. The only explanation seems to be an idea that acceleration clauses entirely under the control of the holder and completely dependent upon his whim or caprice, independent of any act of the maker, are to be condemned.[4]

It is difficult to see why a note containing a conditional promise by the maker to pay at an earlier date upon the commission or omission of some act by him, at the option of the holder, should be negotiable, and a note giving the holder the power to declare the note due whenever he deems himself insecure should be held non-negotiable. In both situations there is a fixed or determinable time of payment. In the first situation the maker is under a conditional duty to pay at an earlier date, and the holder has a conditional right to demand payment at such earlier date upon exercise of the power (option) given him. In the second situation, the holder has a power to demand payment at such earlier date, and the maker is under a correlative liability that the holder will exercise the power.

Moreover, instruments have been held negotiable which give the maker the power or privilege of payment at an earlier date; for instance, "on or before a certain date."[5]

There seems to be no sufficient difference in the existing legal relations in the two situations to reach opposite results upon the question of negotiability. To decide that a note is or is not negotiable, depending upon whether it is accelerated by the act of the maker or holder, can find no support in the negotiable instruments law. It seems to be more nearly an effort upon the part of the courts to curtail the powers of a holder of commercial paper upon some vague ground of public policy rather than the result of reasoning and interpretation. Of course, the provisions in some instruments require the performance of something other than the payment of money, and are therefore non-negotiable. This was the holding in the case of *Holladay State Bank v. Hoffman*[6] where the note provided that additional security should be furnished by the maker in case of depreciation of collateral. In the absence of such a reason there seems little basis for the general distinction heretofore pointed out.

Courts are likewise in conflict as to the effect upon negotiability of a provision for extension. In a recent case a note payable to the maker and indorsed by him in blank contained the provision: "The makers and indorsers . . . agree that this note may be extended in whole or in part without their consent." *Held,* the note was not rendered non-negotiable by this provision.[7] Sections 1 and 184 of the

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[4] *Nickell v. Bradshaw,* 183 Pac. 12.

[5] 8 C. J. 138.

[6] (Kas.) 116 Pac. 239, 35 L. R. A. N. S.

[7] *McCormick & Co. Bankers v. Nielson* (Utah 1925) 233 Pac. 122.

N. I. L. provide that a negotiable instrument "must be payable on demand, or at a fixed or determinable future time."

A provision similar to the one set out in the case reported above is often inserted to avoid any contention upon the part of sureties that they are released by a binding agreement of the holder to extend the time of payment. The word "maker" is used to prevent misunderstanding or failure to distinguish between makers, indorsers, sureties, etc.

Logically, the fact that the holder enters into a binding agreement to extend the time should not affect negotiability. Of course, a provision for extension after maturity cannot affect negotiability, because at maturity the instrument ceases to be negotiable by operation of law.[8]

The *Utah case* reported above is in accord with the majority rule in that respect. The provision for the extension in such case prevents the operation of the rule of suretyship which otherwise would release the sureties thereon. Some courts, however, adopt a literal construction of the clause, and hold the note non-negotiable on the theory that the provision permits the holder or any one of the parties authorized to extend the time without the other's consent, thus rendering the time of payment not fixed or determinable. This is the established rule in Indiana, the decisions both before and after the adoption of the N. I. L. reaching that result.[9]

In some of the cases there is a provision that "the payee, or his assigns, may extend the time of payment thereof from time to time indefinitely." In such a case if the payee and maker were the same person, the maker would have the power to extend his own note indefinitely. Therefore such a note was held clearly non-negotiable.[10] But the same rule has been followed in Indiana without regard to whether or not the payee and maker were the same person.[11]

As has been pointed out, one would suppose the purpose in inserting such a provision was to prevent discharge of sureties in case the holder enters into a binding agreement to extend time and courts should so construe it. But regardless of the rule elsewhere, the rule is settled in Indiana, and possibly Iowa and Michigan courts, that such a provision renders the note non-negotiable.[12]

The tendency of the recent decisions is toward that construction which will sustain negotiability. Such an interpretation is reasonable and desirable from a business and commercial standpoint.

C. SEVERIN BUSCHMANN.

Of the Indianapolis Bar.

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[8] *Navajo County Bank v. Dolson* 163 Cal. 485, 41 L. R. A. N. S. 787.

[9] *Wayne County Natl. Bank v. Cook* 73 Ind. App. 404; *Merchants' and Mechanics' Savings Bank v. Fraze* 9 Ind. App. 161; *Evans v. Odem* 30 Ind. App. 207; *Oyler v. McMurry* 7 Ind. App. 645.

[10] *Woodbury v. Roberts* 59 Iowa 348.

[11] *Glidden v. Henry* 104 Ind. 278. *Rosenthal v. Rambo* 28 Ind. App. 265.

[12] For a general discussion see 8 C. J. 140; 24 Mich. L. Rev. 64 L. R. A. 1916 D. 1280 (note).