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Article 8—Investment Securities

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ARTICLE 8 INVESTMENT SECURITIES

Winthrop B. Lane*

INTRODUCTION[1]

Since the Code does not become effective until September 1, 1965, it seemed to me that a general resume of this article would be more helpful than a critical examination of its more technical provisions. Therefore, I will only attempt to sketch some of the more important provisions and point out the reasoning back of the Act. This will not take the place of a careful study of each section of the article.[2]

This article is sometimes referred to as the Negotiable Instruments Law of Investment Securities. It does not supersede the Blue Sky Laws nor the Federal Securities Exchange Act or the various tax laws affecting securities. It does not cover corporate law or municipal corporation law authorizing the issuance of securities. It takes the security when issued and deals with the handling of the security on the market.

The article covers in part certain sections of the Negotiable Instruments Law,[3] the Uniform Stock Transfer Act, and Uniform Act on Simplification of Fiduciary Security Transactions. The N. I. L. and Uniform Stock Transfer Act are both repealed and completely superseded by the Code, but the Uniform Act of Simplification of Fiduciary Security Transactions is preserved so that fiduciary transfers may be made either under the Code or under the Uniform Act. Nebraska, not being primarily a commercial state, has relatively little case law on the subject covered by article 8. Hence, this article will be helpful in Nebraska in that it will make certain a number of matters now not touched by legislation or case

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[1] This Article is found in Neb. Laws c. 544, p. 1876 (1963). The sections are numbered the same as in the Uniform Code of 1958 and the Uniform Code numbering will be used. In the interest of uniformity the 1958 Code was followed without deviation although the Code Commission in 1962 recommended certain amendments.

[2] A two-volume work with pocket supplements entitled UNIFORM LAWS ANNOTATED (N. L. A.) published by Edward Thompson Company, Brooklyn, New York, contains not only the official comments of the Commission but also annotations of cases decided to date, a list of law review articles and references to texts. It also shows the proposed amendments.

[3] The NEGOTIABLE INSTRUMENTS LAW will be hereinafter referred to as the N. I. L.

law and will avoid the necessity of trying to weave our way among the conflicting decisions of other jurisdictions.

The primary purpose of this article is to facilitate the marketability on the free market of the instruments that come within the definition of investment securities. This should be kept in mind to understand the reason for some of the provisions. Where a compromise is necessary, the Code chooses the path that will promote marketability. This end is accomplished by making investment securities negotiable instruments and eliminating many of the defenses of both the issuers and persons having adverse claims.

The Code uses a new vocabulary which must be learned by the older practitioner. Definitions are scattered throughout the Act. In addition to the definitions found in article 8, attention is particularly called to article 1, section 201, which contains a number of definitions.

So much by way of introduction. Now let us take a look at some of the provisions of the Act.

The article is divided into four parts, and is one of the shorter and perhaps less controversial articles of the Code. Part 1 contains certain definitions and a number of general matters. Part 2 deals with the rights and responsibilities of the issuer. Part 3 deals with the rights and obligations of successive purchasers. Part 4 deals with the registration and authenticating of securities.

DEFINITIONS

Investment Securities

In the first place we must see what securities are covered by this article.[4] The definition is found in section 102 and is referred to as a functional definition. It provides in part that if the security "is of a type commonly dealt in upon securities exchanges or markets or commonly recognized in any area in which it is issued or dealt in as the medium for investment,"[5] it is covered by this article. This does not mean that the security must be listed on a market or traded in over the counter, but, if it is of the "type" that could be listed or traded in, it is covered by this article. Without attempting to enumerate the securities that might qualify, in general it covers stocks, corporate, municipal and governmental bonds, debentures, certificates of participation and so forth. The securities that might come under the Act may vary from time

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[4] Uniform Commercial Code § 8-102 (Hereinafter cited as the U.C.C.).
[5] U.C.C. § 8-102(1) (a) (ii).

to time and be enlarged as new media for investments develop. These new media would necessarily have to become more or less accepted forms of investments to qualify. Thus, there would be a twilight zone in which it is uncertain whether a particular security would qualify.

One writer makes the statement that the Act "will apply to stock of even the smallest family corporation as well as securities of a larger corporation." In so stating, he places the emphasis on the word "type" without giving consideration to the likelihood of the stock ever being traded in the market. I would think there might be some argument on this point. It should also be noted that the words "investment securities" have no implication as to the soundness of the investment. In other words an investment security might qualify under this Act and still not be considered as a proper investment for the average investor.

The functional definition is subject to certain limitations. First that the security, when issued, must be in "bearer or registered form."[6] Thus, an instrument payable to a named person does not qualify even if it is later endorsed to "bearer." I do not know the reason for this limitation, except possibly to differentiate it from commercial paper covered by article 3 of the Code. The words "registered form" have been liberally construed. The stock records of a corporation have been held sufficient to make a stock certificate in "registered form."

The second limitation is that the security must be "one of a class or series or by its terms is divisible into a class or series of intruments."[7] Thus, a bearer bond for a large sum of money which provides that the holder may require the maker to issue in lieu thereof a number of individual bonds of smaller denominations would qualify.

An instrument that evidences a share or participation or other interest in property can be an investment security. Thus, investment trust certificates and interim certificates providing for the issuance of bonds or other securities in exchange therefor, when issued, would qualify. Money is excluded from this article. An instrument which might come within the definition of "commercial paper" under article 3 is governed by article 8 if it also qualifies under article 8.[8]

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[6] U.C.C. § 8-102(1)(a)(i).

[7] U.C.C. § 8-102(1)(a)(iii).

[8] U.C.C. § 8-102(1)(b).

ISSUER'S LIEN[9]

The Code provides that no lien or limitation will be recognized unless "noted conspicuously on the security."[10] The word "noted" does not mean that the entire text of the instrument referred to must be spread at large upon the security. However, it is clear that a bona fide holder without notice of the limitations would not be bound by the instruments referred to beyond the limitation noted on the face of the security.[11] This is to avoid the necessity of a purchaser making an examination of the contents, for example, of trust indentures to which reference is made.

The word "conspicuous" is defined in section 1-201 (10) to mean that "it is so written that a reasonable person . . . ought to have notice of it." It cannot be concealed in fine print. Ordinarily, setting it up in capital letters should be sufficient compliance. The obvious purpose of this provision is to prevent the big print on the face of the security being whittled down by a 100-page trust indenture that the average purchaser never sees.

SECURITIES ARE NEGOTIABLE INSTRUMENTS[12]

Section 8-105 states that the securities governed by this article *are* negotiable instruments. Therefore, if the security is covered by the article it *is* a negotiable instrument. This is important and will supersede much learning on whether the instrument is or is not a negotiable instrument. The section then proceeds to state what defenses may be raised against the instrument. I am not going into these matters for they follow much the same pattern as now covered under the N. I. L. However, the Code has the effect of making these provisions applicable to many instruments not now covered by the N. I. L.

EFFECT OF OVER-ISSUE[13]

I am quite sure that most of us never had to deal with the problem of over-issue of securities. Over-issue can arise in a number of different ways as, for example, the issuance of a new stock certificate to replace one claimed to have been lost. If the old certificate turns up in the hands of a bona fide purchaser, the corpo-

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[9] U.C.C. § 8-103.
[10] U.C.C. § 8-103.
[11] U.C.C. § 8-204.
[12] U.C.C. § 8-105.
[13] U.C.C. § 8-104.

ration might have outstanding more stock than it was authorized to issue. If a municipality by mistake issued more bonds than authorized by law, this would constitute over-issue. There are only two examples of over-issue. Under section 8-104 the issuer is in no event required to issue any instrument that would result in over-issue. This point will be noted under other sections of article 8. If an over-issue would result, the issuer must do one of two things:

1. If the security is available on the market, the issuer must purchase the securities on the market and deliver the same to the person entitled thereto.[14]

2. If the security is not available on the market, then the issuer is liable in damages, which damages are defined as "the price he or the last purchaser for value paid for it with interest from date of his demand."[15] The case law in the various jurisdictions had fixed different measures of damages. The Code thus makes a single standard for all states operating under the Code.

Issue and Issuers

Part 2 is entitled "Issue and Issuers" and deals with the relationship between the issuer and the purchaser or subsequent purchaser. Section 1-201(32) and (33) defines a "purchaser" to include a person who acquires an interest in property by almost any kind of a voluntary transaction. For example, a pledgee or mortgagee is a "purchaser."

Section 8-201 defines who are issuers, Registrars and transfer agents for the purposes of part 2 are excluded from the definition but a guarantor is included to the extent of his guaranty.

Validation[16]

Section 8-202 is referred to as the validation section and some of the writers call it the most important provision of part 2. It makes certain instruments enforcible against the issuer which were formerly considered invalid. This, again, is in the interest of marketability.

The section separates securities into two classes: (a) non-governmental securities and (b) governmental securities.

As to non-governmental securities the security in declared valid in the hands of a bona fide purchaser for value even if issued

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[14] U.C.C. § 8-104(1)(a).

[15] U.C.C. § 8-104(1)(b).

[16] U.C.C. § 8-202.

with a defect that goes to its validity *unless* the defect violates a constitutional provision and is valid in the hands of a *subsequent* purchaser for value even if the defect violates a constitutional provision. Thus, the burden is placed upon the issuer to see that a valid instrument is issued rather than upon the purchaser to ascertain the validity thereof. The distinction between a purchaser and a subsequent purchaser should be noted. The Code defines "purchaser" as a person who obtains the security from the issuer; in other words, the original purchaser.[17] A subsequent purchaser is one who obtains the security other than by original purchase.[18] The defects cured under this section do not include over-issue which is covered exclusively by section 8-104. The effect of this section is to make instruments valid as against the issuer instead of giving the purchaser a cause of action for damages for the issuance of an invalid security.

As regards securities issued by a government or governmental agency, they are validated if

1. there has been a substantial compliance with the law, or

2. (a) if the issuer has received a substantial consideration for the security, plus

(b) the stated purpose of the security is one which the issuer has the power to borrow money or issue securities.

Nebraska has no comparable statute, but there are several cases that indicate that substantial compliance is sufficient.[19]

The second basis of validation provides, in effect, that if a municipality can, for example, borrow money to pave streets and has received the moneys on the bonds issued for that purpose, it cannot deny liability even though it has not complied with some jurisdictional step. We have no statute or case law on this point. It should be also noted that in regard to governmental securities

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[17] U.C.C. § 1-201(32) (33).

[18] U.C.C. § 8-102(3).

[19] For example: In Haggard v. Misko, 164 Neb. 778, 781, 83 N.W.2d 483, 486 (1957), the Court said: "The provisions of statutes which affect the mode and manner of conducting the details of an election are directory only and not mandatory, and a departure from the prescribed method will not vitiate the ballot of a voter who has complied with the mandatory provisions of the statute applicable to him."

In Greathouse v. School District, 155 Neb. 883, 887, 54 N.W.2d 58, 61 (1952), the second Syllabus reads: "It is the policy of the law to prevent the disfranchisement of qualified electors who have cast their ballots in good faith by requiring only a substantial compliance with the election laws of the state."

the Code makes no distinction between violation of constitutional provisions and statutory provisions. In theory, this may be hard to justify. The Code is only a statute. This raises the question of how can a statute change or amend the Constitution. At least one writer says that the Code might be sustained on the theory of estoppel. Can a state or municipality be estopped from claiming the protection of the Constitution? There is substantial authority to the effect that a municipality may be estopped to deny the truth of recitals contained in its bonds. Hence, we always include in municipal bonds a statement of full compliance, etc. Does this apply to constitutional requirements? The United States Supreme Court in the case of *Hedges v. County of Dixon*,[20] held "[r]ecitals in bonds issued under legislative authority may estop the municipality from disputing their authority as against a *bona fide* holder for value, but when the municipal bonds are issued in violation of a constitutional provision, no such estoppel by reason of any recital contained in the bonds can be had." The *Hedges* case was discussed in *Gunnison County Commissioners v. Rollins*.[21] Syllabus 2 is as follows:

> A recital in county bonds that the debt thereby created does not exceed the limit prescribed by the state Constitution estops the county from asserting, as against a bona fide holder for value, that the contrary is the fact.

Thus, the certificate of an officer who has the duty of determining the fact may estop the municipality from questioning compliance with even constitutional limitations. Thus, a lot of fine distinctions have been made in applying estoppel to bond issues.

Nebraska also has several statutes that require bonds to be approved by the Court before being issued.[22] Our Court has not passed on the question of whether this so-called order of "validation" is subject to collateral attack.

The Code may go beyond the present law, at least in Nebraska, but, again, I think it is a step in the right direction.

It should also be noted that section 8-202 wipes out the defense of non-delivery or conditional delivery. Lack of genuineness is still a defense unless the forgery is committed by an employee or a person entrusted to perform certain duties as more fully set out in section 8-205. Thus, the issuer is made responsible for the acts of faithless employees or misplaced confidence. This, in my opinion, is as it should be.

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[20] 150 U.S. 182, 187 (1893).

[21] 43 L. Ed. 689 (1899).

[22] NEB. REV. STAT. §§ 31-717, 31-756, 39-1628, 46-1, 46-104 (Reissue 1960).

STALENESS OF NOTICE[24]

There is a good deal of law to the effect that to be a holder in due course a person must acquire the security befor maturity. The Code takes note of the fact that securities are frequently traded after call or maturity and a bona fide purchaser should not on that account alone be charged with notice of defects of which, in fact, he had no knowledge. Hence, the Code provides that if a purchase is made within one year after maturity, the purchaser is not charged with notice of the defect.[24] If no provision has been made for the payment of the security, the purchaser who purchases it within two years after maturity is not charged with notice of defects.[25]

RESTRICTIONS ON TRANSFER[26]

Section 8-204 provides that restrictions on transfers imposed by the issuer are ineffective unless "noted conspicuously" on the instrument as to all persons who obtain the instrument without actual knowledge of the restriction. I have already called attention to the definition of the words "noted" and "conspicuously."[27] This provision is to give effect to the general assumption that most securities are free from restrictions. It is, therefore, proper to require notice or actual knowledge of the restriction to overcome this presumption.

This section is a rephrasing of section 15 of the *Uniform Stock Transfer Act* and only refers to restrictions imposed by the issuing corporation. It was pointed out in the case of *Peter Kiewit Sons' co. v. County of Douglas,*[28] that section 15 did not affect statutory restrictions or liens as, for example, the lien of the corporation on its stock for taxes paid on behalf of the stockholder. I assume section 8-204 of the Code would not change this decision.

FORGERY[29]

As previously pointed out, the lack of genuineness of a signature is still a defense available to the issuer. Section 8-205 makes two exceptions to this rule. The issuer is bound:

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23 U.C.C. § 8-203.

24 U.C.C. § 8-203(1) (a).

25 U.C.C. § 8-203(1) (b).

26 U.C.C. § 8-204.

27 See discussion under U.C.C. § 8-103.

28 161 Neb. 93, 72 N.W.2d 415 (1955).

29 U.C.C. § 8-205.

(1) If the security is forged by a person entrusted with the preparation of the instrument,[30] and

(2) If the security is forged by an employee of the issuer or an employee of the person entrusted with the preparation of the instrument.[31]

This is a change from section 23 of the N. I. L. The N. I. L. did not specify what would estop the issuer from setting up the defense of forgery. The Code clears up this point.

COMPLETION AND ALTERATION OF INSTRUMENT[32]

Section 8-206 provides that if all necessary signatures are affixed to an otherwise incomplete instrument

(1) Anyone can fill in blanks in an incomplete instrument as authorized,[33] and

(2) Even if blanks are incorrectly filled in it is enforcible as completed in the hands of a bona fide purchaser for value without notice of such incorrectness.[34]

The defense of non-delivery is eliminated. In case of an alteration of a completed instrument it is enforcible by *any* holder, not merely a holder in due course, in accordance with the original terms. This changes the corresponding provisions of the N. I. L. and *Uniform Stock Transfer Act* and eliminates the question as to what are material alterations and who are holders in due course.

LIABILITY OF TRUSTEE, REGISTRAR AND TRANSFER AGENT[35]

If you represent a bank or trust company that acts as trustee, registrar or transfer agent of various securities, your clients may ask you as to the liability assumed by them in so acting. There is no statute in Nebraska at the present time on this point and there is no uniform statutory provision.

Section 8-208 now answers this question and provides that an authenticating trustee, registrar or transfer agent warrants three things:

1. That the security is genuine and in proper form.

2. That he has capacity to act and is acting within the scope of his authority.

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[30] U.C.C. § 8-205(a).

[31] U.C.C. § 8-205(b).

[32] U.C.C. § 8-206.

[33] U.C.C. § 8-206(1)(a).

[34] U.C.C. § 8-206(1)(b).

[35] U.C.C. § 8-208.

3. That he has reasonable grounds to believe that the instrument is not an over-issue.

The Code further provides that the authenticating trustee, registrar or transfer agent is not responsible for the validity of the security in any other respect. Thus, a bank or trust company assumes some responsibility that requires skill and investigation and should have trained personnel to handle these matters. However, the requirements are not too burdensome for the compensation received for acting in these capacities.

PURCHASE

Part 3 is entitled "Purchase" and deals with the transfer of securities and the rights of successor holders as distinguished from the relationship of the purchaser to the issuer. As under the N. I. L. a bona fide purchaser without notice acquires the security free of adverse claims. The time the purchaser becomes a bona fide purchaser is fixed as the time of delivery.[36] Hence, whether adverse claims are cut off raises two questions: Was there delivery and was there notice?

DELIVERY

Delivery is defined in section 8-313. Delivery can occur in any one of four ways:

1. By the purchaser getting physical possession of the security. However, under section 8-307 where the security is in registered form without the necessary endorsements, delivery is not complete except against the transferor, until the necessary endorsements are supplied.

2. By purchaser's broker obtaining the security specially endorsed to or registered in the name of the purchaser.

3. By purchaser's broker sending confirmation and identifying the specific security on his records as belonging to the purchaser.

4. By third party who is in possession of the security acknowledging that he holds the security for the purchaser.

The Code further provides that there is no delivery by merely indicating that the security is part of a fungible bulk.[37] In other words, the particular security must be identified for a good delivery.

It is usually to the advantage of the purchaser to have the delivery completed at the earliest possible date. However, the pro-

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[36] U.C.C. § 8-301.

[37] U.C.C. § 8-313(2).

vision that the security must be specifically identified and not merely a part of a fungible bulk may be to the disadvantage of the purchaser, as we understand brokers frequently hold a large amount of a given security in bulk for their various customers. As to such securities the purchaser would not be protected by the Code for lack of delivery. Section 60(e) of the *Bankruptcy Act* recognizes a fungible bulk of securities held for customers is distributable solely to the customers for whom the securities are held. I assume the Code does not change the bankruptcy rule as far as bankruptcy proceedings are concerned. However, it might be held that by virtue of the Code the securities were the property of the bankrupt and the general creditors would participate therein.

The proposed 1962 amendments amend section 8-313(2) by stating that the purchaser is the *owner* of the securities held for him but is not the *holder* unless the provisions of section 8-313, sub-section (1) (b) or (c) have been complied with. It also states the purchaser is the owner of a proportionate property interest in the fungible bulk. The distinction between "holder" and "owner" is important for certain sections of the Code and the change in fungible goods should eliminate the bankruptcy and federal tax lien questions suggested above.

NOTICE

On the question of notice several different situations should be considered. The Code provides a purchaser is charged with notice by a restrictive endorsement such as "for collection" or "for surrender" or in case of a bearer instrument by an unambiguous notation that the security is the property of a named individual.[38] In case of a transfer by a fiduciary the purchaser has no duty to inquire into the authority of the fiduciary.[39] This provision is similar to the provisions of the *Uniform Act for Simplification of Fiduciary Security Transfers*. Of course, if the purchaser has actual knowledge of the breach of trust or adverse claim he is bound by such knowledge and must act accordingly.

In considering the question of notice and knowledge we should not overlook the provisions of section 1-201. Sub-paragraph 25(b) provides that a person has notice when "he has received a notice or notification of it." Sub-section 26(b) provides a person "receives" a notice or notification when "it is duly delivered at the place of

[38] U.C.C. § 8-304.

[39] U.C.C. § 8-304.

business. . . ." Sub-section 27 provides that notice to an organization "is effective for a particular transaction from the time when it is brought to the attention of the individual conducting that transaction, and in any event from the time when it would have been brought to his attention if the organization had exercised due diligence." These provisions leave banks, brokerage houses and other large organizations in an uncomfortable position. Suppose, for example, the organization receives a list of stolen securities. What constitutes due diligence in getting this information around to every officer or employee who might have some connection with the transaction? How long does the organization have to have to pass this information on to all employees? How long does the notice remain effective—for one month, one year or perpetually? The Code does not answer these questions. An organization may act in good faith and still be charged with notice and liable on account thereof. The same result is probably true under the present case law so the Code does not leave the large organization in any worse position than it was in before the adoption of the Code. In other words, the Code was not written solely for large organizations. We should also point out that the requirement of good faith as defined in section 1-201 (19) probably applies to notice and knowledge.

STALENESS OF NOTICE OF ADVERSE CLAIM[40]

Section 8-305 is not to be confused with section 8-203. Section 8-203 only refers to defenses of the issuer against the holder. Section 8-305 refers to notice of adverse claims, that is, the rights of others than the issuer. Section 8-305 provides about one-half the length of time as htat provided for in section 8-203. This is on the theory that the purchaser has more reason to suspect adverse claims of ownership than to suspect that the issuer has some defense.

WARRANTIES ON PRESENTATION AND TRANSFER[41]

The N. I. L. and the *Uniform Stock Transfer Act* contain various provisions as to implied warranties resulting from certain transactions. Section 8-306 of the Code has rephrased and extended these warranties.

Under the Code the warranties differ, pending upon the person and the transaction.

FIRST: A person other than an bona fide purchaser in presenting the security to the issuer warrants that he is entitled to registra-

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[40] U.C.C. § 8-305.

[41] U.C.C. § 8-306.

tion, payment or exchange. On the other hand a bona fide purchaser for value only warrants that he has no knowledge of any unauthorized signature in the necessary endorsements.[42]

SECOND: A person transferring a security warrants three things and only three things:[43]

1. The transfer is effective in writing.
2. The security is genuine and without material alteration.
3. He knows of no fact which might impair the validity of the security.

An intermediary warrants only his own good faith.[44] A pledgee returning securities to the pledgor or his nominee acts only as an intermediary.[45] However, if the pledgee sells the securities, he may stand in an entirely different position. Another example of an intermediary is a bank that receives for collection securities with a draft attached. The bank usually knows nothing about the securities so should not be held to any warranties.

A broker gives and receives all warranties provided for by section 8-306 except he cannot claim the protection of an intermediary.[46] The proposed 1962 amendment strikes the last sentence of sub-section (3) which reads "a broker is not an intermediary within the meaning of this sub-section."

GUARANTEE OF SIGNATURES[47]

There has been a good deal of confusion as to what a bank's or broker's liabilities may be when he guarantees a signature. There is no uniform statute or Nebraska decision covering this point. What is covered by the guarantee and the liabilities of the guarantor are settled by the Code. Under section 8-312 the guarantor warrants three things and nothing more:

1. the genuineness of the signature,
2. the signer is an appropriate person to endorse,
3. the signer had legal capacity.

The guarantor does not guarantee the instrument nor the rightfulness of the transfer. The guarantee speaks as of the time the

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[42] U.C.C. § 8-306(1).

[43] U.C.C. § 8-306(2).

[44] U.C.C. § 8-306(3).

[45] U.C.C. § 8-306(4).

[46] U.C.C. § 8-306(3). The proposed 1962 amendment strikes the last sentence of sub-section (3) which reads "a broker is not an intermediary within the meaning of this sub-section."

[47] U.C.C. § 8-312.

signature is guaranteed and not necessarily at the time of the delivery of the instrument. There may be a considerable lapse of time between the guarantee and the delivery of the instrument and in this interim the executor or person whose signature is guaranteed may no longer be in office. Therefore, it is wise for the bank or broker to date their guarantee so they can prove that the guarantee was correct when made. I do not believe that dating the guarantee is in accordance with the present practice.

Since the guarantor guarantees that the signer is "an appropriate person to endorse"[48] in the case of a fiduciary signer the guarantor must ascertain at his peril that the fiduciary has been appointed and is still acting. If the guarantor does not have personal knowledge of this fact, he, as well as the transfer agent, may require that the signer produce an up-to-date copy of his letters of appointment.

I believe many persons in guaranteeing signatures think they are only guaranteeing the genuineness of the signature. We, again, point out that under the Code he guarantees more than the genuineness of the signature. The Code is beneficial in that it makes certain what is guaranteed and the extent of the guarantor's liability. Under some case law the guarantor was held to a greater liability than under the Code.

The guarantor may, of course, not only guarantee the signature but also the "endorsement" in which event he also warrants the rightfulness of the transfer.[49] The issuer cannot require such a guarantee and in practice I believe few such guarantees are made.

ENDORSEMENTS[50]

Section 8-308 covers endorsements. The Code authorizes either blank or special endorsements. The endorsements speak as of the date made and a subsequent change in circumstances, such as the death or resignation of the endorser, does not affect its validity. The Code also authorizes an endorsement of part of the securities. For example: 25 shares out of a 100 share certificate. This is a change from the provisions of the N. I. L.[51]

The Code defines who is an appropriate person to endorse a security. It also provides that the failure of the endorser to comply

[48] U.C.C. § 8-312(1)(b).
[49] U.C.C. § 8-312(2).
[50] U.C.C. § 8-308.
[51] UNIFORM NEGOTIABLE INSTRUMENTS LAW §§ 31-37, 64-69 (1943).

with the state law or the instrument under which he is acting as, for example, the failure to get a court order authorizing the endorsement, does not render his endorsement unauthorized. This must necessarily be the case as otherwise an issuer or transfer agent would have to examine the will or trust agreement or court records under which the fiduciary is acting. Under both the Code and the *Uniform Act for Simplification of Fiduciary Security Transfers* the examination of such instruments is no longer required.

Section 8-315 retains the common law right to reclaim a security wrongfully transferred against any person except a bona fide purchaser. If the wrongful transfer is due to a forged endorsement the exception in favor of a bona fide purchaser does not apply unless the purchaser has received a new, reissued or reregistered security. This section must be read with section 8-311. A distinction is apparently made between an unauthorized signature of an issuer and an endorser.[52]

Section 8-317 provides there can be no valid attachment or levy upon the security unless the security is actually seized by the officer. This is a change from our present statute which permits a levy by notice to the corporation without seizure of the certificate.[53]

Section 8-318 provides that an innocent agent or bailee who acts in good faith shall not be liable for conversion even though the principal has no right to dispose of the security. This is a more sweeping provision than contained in Section 7 of the Simplification Act. It is only proper that an innocent agent who does not knowingly participate in a breach should not be held liable for such breach.

It will be noted that I have not discussed several sections of Part 3. Most of these sections follow rather closely the corresponding sections of the N. I. L. except to make them applicable to all investment securities.

REGISTRATION

Part 4 is entitled "Registration." In general, it deals with the rights, duties and liabilities of the issuer including transfer agents and registrars in connection with the transfer and registration of securities.

There are no corresponding Nebraska Statutes and no Uniform Acts except Section 8-403 modified Section 3 of the Uniform

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[52] See U.C.C. § 8-205.

[53] See NEB. REV. STAT. § 25-1520 (1960).

Fiduciary Act which Nebraska has not adopted and Section 8-405 modified Section 17 of the Uniform Stock Transfer Act covering lost or destroyed securities.

TRANSFER OF SECURITIES[54]

I, again, want to call attention to the fact that article 10-101 of the Code, as adopted in Nebraska, keeps the Uniform Act on Simplification of Fiduciary Security Transfers in effect and a fiduciary may proceed under the Code or under the Simplification Act.

The Code is not limited to transactions by fiduciaries but covers transfers in general. The provisions of the Code and the Simplification Act are not identical but are quite similar. Both the Code and the Fiduciary Simplification Act have eliminated many headaches for executors, trustees, brokers and attorneys assisting in the administration of estates and trust. Broadly speaking, all a fiduciary needs to do to transfer a security by sale or distribution to the beneficiary is:

1. Sign the transfer on the back of a registered security or a separate stock power.
2. Have the signature of the assignor guaranteed.
3. Have Letters of Appointment certified not more than sixty days prior to presentation.
4. Obtain an Affidavit as to the residence of the decedent or incompetent.
5. Transmit enough funds to pay both the Federal and local transfer taxes and in some cases obtain a tax waiver.

Formerly it was usually necessary to obtain certified copies of the will or trust agreement and in some instances certified copies of court orders directly authorizing the transfers. The transfer agent may require these instruments, but if he does so he is bound by the information so obtained and must decide all questions of adverse claims and the rightfulness of the transfer at his peril. He would, therefore, be foolish to make unnecessary requirements. Section 8-402 sets out what assurances the issuer or transfer agent may require at its option.

ADVERSE CLAIMS[55]

If the issuer (transfer agent) receives written notice of an adverse claim or has obtained notice from examination of the will,

[54] U.C.C. §§ 8-401-402.

[55] U.C.C. § 8-403.

trust agreement or other instrument which he has required to be produced, he may give the adverse claimants notice that, unless within thirty days he receives a restraining order or injunction or a federal indemnity bond, he will proceed to register the transfer. In so doing he assumes no liability. Again, I should point out that under section 8-402 in absence of notice the issuer has no duty to inquire into matters which might restrict the transfer including court orders or the absence thereof.

LIABILITY FOR REGISTRATION[56]

Basically, the issuer is not liable to the true owner for registering any instrument that appears to be properly endorsed. Where the issuer has made a mistake the issuer must deliver like securities to the true owner unless this would result in an over-issue. The owner cannot elect to demand damages in lieu of accepting the like securities. I think this provision is a change from the rule established by case law in some jurisdictions.

LOST, DESTROYED AND STOLEN SECURITIES[57]

Section 8-405 makes several changes in the provisions of Section 17 of the Uniform Stock Transfer Act. The Code provides three things:

1. If the owner does not give to the issuer notice in a reasonable time of the alleged loss or theft of the securities and the issuer registers a transfer before receiving such notice, the owner has no claim against the issuer.

2. That the issuer must issue new securities in place of the original securities if the owner so requests before the issuer has notice that the lost securities had been acquired by a bona fide purchaser and the owner gives an indemnity bond and complies with other reasonable requirements of the issuer.

3. If, after the replacement securities are issued, the old securities are presented by a bona fide purchaser, they must be honored and transferred unless this would result in an over-issue in which event section 8-104 applies. The issuer may also recover the new securities unless they are in the hands of a bona fide purchaser.

This section has no bearing on the question as to whether a theft can pass good title to a bona fide purchaser. This question

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[56] U.C.C. § 8-404.

[57] U.C.C. § 8-405.

would come under part 3 and particularly section 8-301. Nebraska has held that a bona fide purchaser can acquire title to stolen bonds.[58] I do not see that the Code changes this rule.

DUTY OF TRUSTEES, TRANSFER AGENTS, AND REGISTRARS[59]

Under section 8-406 the authenticating trustees, transfer agents and registrars are required to exercise good faith and due diligence in the functions they perform and notice to them is notice to the issuer. In regard to their particular function, they have the same obligations and privileges as the insurer. Thus, they may become separately liable to the owner and to the issuer for nonfeasance or malfeasance.

CONCLUSION

I, again, want to repeat that this paper was not intended as an exhaustive, critical discussion of article 8. It is sketchy at best. The adoption of Article 8 is a progressive step. In my opinion it enacts the better thinking and will aid the marketability of investment securities.

Changes can be made by amendment to keep the Code abreast of changing commercial practices. One such change is the proposed addition of section 8-320 to cover transfers and pledges within a central depositary system.

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[58] State *ex rel.* Sorensen v. Nebraska State Savings Bank, 127 Neb. 262, 155 N.W. 52 (1934).

[59] U.C.C. § 8-406.

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