The risks related to use of promissory notes in European and Anglo-American law systems

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Abstract: Lack of a uniform law regulating the promissory notes in international trade has led to different statutory rules and principles applicable to this payment instrument. Excessive flexibility of Anglo-American system law, and the rigid formalism of European standards led to the creation of a complex payment instrument, and its usage raised different problems at international level. Although there have been efforts of international organizations to bring near the existing legal systems, so to eliminate the risk of use of promissory notes under different conditions, they have been without result, but they are still raising great interest.

Key-Words: bill of exchange, underwriter, unconditional promise, beneficiary, security, payment

1 Introduction

Apparently, promissory notes would not require special attention and that is either due to the fact that it is not characterized by increased movement on commercial market, either that it is subject to the same rules as the bill of exchange, or that it does not raise great issues considering the fact that it is a simplified form of the bill of exchange.

In fact, the promissory note is a commercial security similar to the bill of exchange, that has its characteristics and that raises many problems, especially at international level.

In continental right, its regulation is common to that of the bill of exchange and makes the object of the Convention Providing a Uniform Law for Bills of Exchange and Promissory Notes, Geneva 1930. In Title II (articles 75-78), this law specifically regulates promissory notes. Concurrently, article 77 of the Convention settles the principle according to which the provision regarding the bill of exchange also apply to promissory notes, if they are not inconsistent with the nature of this title.

Geneva law counterpart in Anglo-American law is the Bills of Exchange Act 1882 [1](England) and Uniform Commercial Code [2] (USA) that refer to it as promissory note.

One of the differences between the two legal systems is the fact that promissory note is an independent security and not only a type of the bill of exchange, as in continental right.

Not of little importance is its regulation within the United Nations Convention on International Bills of Exchange and International Promissory Notes, New York 1988. Even though not in force, this Convention represents the outcome of many years of activity of U.N.C.I.T.R.A.L. in its attempt to harmonize the existing law systems in what commercial securities are concerned and to create uniform law in this respect. Thus, promissory notes still raises a great deal of interest, being the object of international attention.

In Romanian law, promissory notes are regulated together with the bill of exchange within Law no. 58/1934, especially in Title II, articles 104-107, as modified by Government Ordinance no. 39/2008. For supporting its application, the National Bank of Romania has issued Norm no. 7 of June 5th, 2008 that modifies Norm-frame no. 6/1994 regarding trade drafted by banking companies and other finance companies, with promissory notes and bills of exchange and Technical Norms no. 10/1994 regarding bills of exchange and promissory notes.

2 Definition of promissory note

In Geneva law, as well as in Romanian law, the legal text does not define this payment instrument. Its definition is deduced on the basis of mandatory
mentions enumerated in the Convention, respectively in Law no 58/1934 regarding bills of exchange and promissory notes. Thus, promissory notes are documents through which a person, named drawee, undertakes to pay at due term an amount of money, to another person, named beneficiary, or to his order.

According to B.E.A., promissory notes are an “unconditional promise in writing made by one person to another signed by the maker, engaging to pay, on demand or at a fixed or determinable in future time, a sum certain in money, to or to the order of, a specified person or to bearer”.

From both definitions, it can be ascertained that, unlike the bill of exchange, that implies legal relations between three persons (drawer, drawee and beneficiary), promissory notes refer to legal relations between two persons (maker and beneficiary). In this respect, there are no differences between the two legal systems, the maker and the beneficiary being distinct persons.

From the content of the Convention of Geneva it can be ascertained that the person who issues the promissory note is not referred to neither as drawee, nor as drawer, but as maker (fr.souscripteur), however conferring him the situation de jurei of a drawee of a bill of exchange. Thus, the promissory note is practically a payment promise of payment, an acceptance of a debt by its debtor to his creditor [3].

The issuer of the promissory note, in his quality of debtor, undertakes to pay a certain amount of money at the due date. The security beneficiary, in his right to receive the payment or the payment is made at his order.

Unlike the Convention of Geneva, English Law allows the promissory note to be issued by two or more persons or to be payable to two or more beneficiaries [4].

Differences between promissory notes and bills of exchanges:
- The promissory note refers to a legal relation between two parties, maker and beneficiary, whereas in the case of the bill of exchange, the legal relation concerns three parties: the drawer, the drawee and the beneficiary.
- The promissory note is a promise of payment, an acceptance of the debt towards the creditor, whereas the bill of exchange is an obligation of payment at order.
- The rules that govern the payment of the bill of exchange are also applied to the payment of the promissory note, with the difference that in the case of the promissory note, having no drawee, the payment is made by the maker. As a consequence, the law does not stipulate the formality of presenting the promissory note at the acceptance and at the due date, the promissory note is presented to the maker for payment.

3 Form conditions of the promissory note

According to Geneva system, the promissory note is a formal title that must have a written form and contain mandatory stipulations provided by article 75 of the Convention. Norm-frame of the National Bank of Romania stipulates the fact that the promissory note is a formal title that in order to be valid must fulfill certain conditions expressed in official formulae of text draw up that expresses clauses with strict legal value. In all draw ups, the promissory note must contain mandatory stipulations provided by the law that satisfy the requirements of sufficient information that is implied by the title, as well as the requirements of the certainty of reflecting the obligations undertaken by the parties through the respective title (points 493-496 of the Norms of the National Bank of Romania no. 6/1994 supplemented by Norm no. 7/2008).

In English law, formalism is not very rigorous, so that no text form is essential for the validation of the promissory note provided that requirements stipulated in section 83 (1) are observed.

English doctrine considers that it is not sufficient for a text of the document to fall in the definition of the law (which specify the essential conditions for a promissory note), to become a promissory note if the parties did not intend to draw it up as a negotiable instrument.

For example, in the case Sibree versus Tripp, a document in the form: „Memorandum. M. Sibree has deposited today, together with me, £500 of the goods sold in the amount of £10300 with £3 Spanish percentage, to be returned at request” was not considered a promissory note, due to the fact that it is only apparently an instrument that records the agreement of the parties, being rather an agreement than a promissory note [1].

Promissory notes differs from commercial agreement concluded between the parties, comprising documents whose content is mainly made up of an undertaking of payment of an amount of money and nothing more. If applied ad literam the definition in section 83 (1) B.E.A., it would apparently cover a series of documents out of which none could be normally considered a promissory note, bill of exchange or commercial bill (for example, the legal tax on land that contains the usual
mortgager obligation for payment at fix term or at request).

In section 5 (2), B.E.A. regulates the case in which in a bill of exchange, the drawer and the drawee are the same person. In this case, the holder can treat the instrument at his own will, either as a bill of exchange or as a promissory note. This type of instrument is not actually a bill of exchange, due to the fact that it is not addressed by a person to another. The advantage of treating it as a promissory note is that usually it is not necessary to be presented at payment to make the drawer liable.

Moreover, a holder can consider the instrument either a promissory note or a bill of exchange, when the drawee is a fictitious person or a person who does not have contracting capacity.

According to Anglo-American law, when a bill of exchange is not addressed to anyone, but a person writes his agreement on it, that person can be liable for the instrument as the maker of a promissory note.

The main conditions of English promissory note correspond to the main conditions of the continental promissory note, with the following differences, that shall be further analysed:

3.1 The use of the term “promissory note”

This is a mandatory condition specific only to the Genovese system. B.E.A. does not consider the usage of the term promissory note in the document as being mandatory.

In article 75 point 1, L.U requests the term promissory note to be inserted in the body of the instrument and to be expressed in the language employed in drawing up the instrument, just as in the case of the bill of exchange.

3.2 The unconditional promise to pay a determinate sum of money

Unlike the bill of exchange which contains the order given to another person to make the payment, in the case of the promissory note, given the absence of the drawee, the maker undertakes himself to pay the sum of money specified in the document.

The obligation undertaken by the drawer must be unconditioned and is expressed usually by the words „I will pay...” or similar syntagm.

This condition is also found in English law; the obligation to pay contained in a promissory note must be unconditioned.

Just as in the case of the bill of exchange, an instrument payable in a certain situation is not a promissory note and the occurrence of the event does not remove the inconformity. The fact that the promissory note is payable in a certain place does not make it conditioned.

Moreover it is considered just as in the Romanian law that it is not necessary to use the word “promise”, any other words clearly stating an obligation to pay being sufficient. Concurrently it is considered that a simple acceptance of an amount owed, even if it involves an obligation to pay, is not a promissory note.

3.3 The statement of the time of payment

In both legal systems the time of payment must be specified in the instrument, reflecting in principle the rules stipulated for the bill of exchange [6].

The initiators of the Geneva Convention don’t get back on the time of payment for the promissory note, indicating the regulations for the bill of the exchange which are applicable to the promissory note.

The English law specifically regulates the time of payment for the promissory note, taking into account certain particularities of the instrument.

The definition of the promissory note found in B.E.A. stipulates that the payment will be done “on demand or at a fixed or determinable future time”. “On sight” payment type is not applicable to English promissory notes, as opposed to L.U provisions, article 76, paragraph 2: “a promissory note in which the time of payment is not specified is deemed to be payable at sight”.

The notes payable on demand are different from checks and bills of exchange in the way that a check is an instrument for immediate payment and a bill of exchange payable on demand is meant to be presented and paid in a short period of time.

The English promissory note is often issued as a permanent guarantee or as an additional guarantee for the fulfilment of other obligations involving payments and it is meant to stay that way for a long period of time.

The notes payable on demand are frequently issued to generate interest until the payment date and are not meant to be presented for payment soon after the issue date.

Section 86 (1) stipulates that when a promissory note has been indorsed it must be presented for payment within a reasonable time of the endorsement.

In order to determine the “reasonable time” one must take into account the nature of the instrument, the usage of trade and the facts of the particular case. [s. 86 (2)].

Since the maker is liable for the promissory note it is not absolutely necessary for the instrument to be presented for payment within a reasonable time or
even to be presented at all in order to render liability of the maker. However, the presentation for payment is necessary in order to render the endorser of the note liable and it must be done, in the case of a note payable on demand, within a reasonable time of the endorsement. If such a note is not presented as specified, the endorser is discharged. The reason for the stipulation of this rule is that the endorser has the right to avoid prejudice by unjustified delay as he is interested to know earlier if the maker will pay the note.

According to section 86, paragraph 3 of the English law, when a promissory note payable on demand is negotiated, it is not deemed to be overdue by reason that a reasonable time for presenting it for payment has elapsed, if the holder did not know about this. This reasoning is based on the fact that the promissory notes are or can be permanent guarantees and consequently they should remain entirely negotiable as long as they remain in circulation [1].

3.4 Statement of the place where payment is to be made
The Geneva Convention expressly provides that the note must show the place where the maker must pay and in the case of an omission the place where the instrument is made is deemed to be the place of payment and at the same time the place of the domicile of the maker. (art. 76 par. 2)

According to the English law, the place of payment must be specified in the body of the note, but a promissory note is not considered invalid by reason that it doesn’t specify the place of payment. At the same time if a promissory note is made payable at a particular place, presentment at that place is necessary in order to render the maker liable. A note is made payable at a particular place only if it specifies a complete address not just a country or city (e.g. England or Salt Lake City).

The declaration of a payment place at the edge of the note or below the signature or written on the face of the note is to be treated only as a note and not as part of the payment obligation.

If an instrument supposed to be a bill of exchange is drawn by a subsidiary of the drawer and the drawee is another subsidiary of the same entity, then according to section 5(2) of the B.E.A., the holder may treat the instrument, at his option either as a bill of exchange or as a promissory note.

Section 87 (3) stipulates that for a promissory note made payable at a particular place, presentment at that place is necessary in order to render an endorser liable. Moreover, the endorser is liable even if the payment place is indicated by memorandum only, presentment at that place being sufficient [7].

3.5 The name of the person to whom or to whose order payment is to be made
No matter the legal system, in order for a document to fulfil the characteristics of a promissory note, it must also comprise the name of the beneficiary, i.e. of the person who shall receive payment. In the case of endorsement conveyance, the title must comprise the name of the person at whose order the payment must be made (endorsee). (art. 75 point 5 of L.U. on the bill of exchange and on the promissory note).

Section 85 of the English Law shows that a promissory note is inchoate and incomplete until it is delivered to the payee or bearer. The delivery to the beneficiary or bearer is necessary for “the conclusion of the contract contained in the promissory note”. Through the word “delivery” it is understood the transfer of the tenure, real or implicit, from one person to another.

When the note is a promise made by the maker to pay to himself it has no value for other persons. Once indorsed, the note becomes payable to someone else (special endorsement) or to the bearer (blank endorsement) and from that moment on, the note shall act as an usual promissory note (section 83 point 2 of B.E.A.).

3.6 Statement of the date and of the place where the promissory note is issued
Regarding these statements, the promissory note follows the rules related to the bill of exchange to determine the date and place of issue.

Art. 76 paragraph 3 of Geneva L.U. stipulates that, if the title does not mention the locality where it was issued, the place where the promissory note was drawn up is the place near the maker’s name.

As we have also shown in the case of the bill of exchange, English law does not mention anything regarding with respect to this condition, the absence of this mention having no effect on the title.

3.7 The signature of the person who issues the instrument (maker).
The maker’s signature is an obligatory condition without which the title will not have any legal effects and that is why it is mandatory in all legal systems.

The maker of a promissory note is the party who, by signing the note, undertakes to pay it according to its content, being the main debtor of the title [8].

Requirements regarding the signatures on the bill of exchange are settled by the Government Ordinance.
no. 39/2008 that modifies art. 8 of the Law no. 58/1934, showing that “any signature on a bill of exchange must contain the name and surname in print of the natural person and the name of the legal person or of the entity undertaking; the handwritten signature of the natural person and of the legal representatives or delegates legal persons that undertake; or of the legal representatives or delegates of other type of entities that use this type of instruments”. Thus, by modifying the law it is attempted to eliminate any confusion regarding the signature on the bill of exchange, and thus of any person that enters in the legal bill of exchange report, due to the fact that as presented before the modification of the law, Courts decisions were different.

4 Conclusion

Regulatory differences between the two systems of law existing in the field of bills of exchange and promissory notes - European and Anglo-American - involves the risk of the instrument’s inefficiency, instrument which the parties intend to use it in order to realize the payment in a commercial operations. Elimination of this risk can be made following the example of United Nations Convention on international bills of exchange and international promissory notes, New York 1988, which aimed at limiting at the minimum the fundamental divergences existing between the main above mentioned systems. Adoption of such a convention does not aim to replace national rules on the issue, but to find those rules which are built on principles tending to harmonize the solutions in the field of bills of exchanges and promissory notes, avoiding the risk of using the promissory notes in payment execution.

References:
[2] Uniform Commercial Code, §3-104-3-112
[5] Bills of exchange Act s. 83, s. 85, s.7(2), s. 32(3)
[8] Decision no. 1 of 3 February 2003 of the Supreme Court of Justice - Joint Sections