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THE EFFECT OF FLUCTUATING RATES OF INTEREST ON THE NEGOTIABILITY OF AN INSTRUMENT

It is a well-settled rule of statute that a negotiable instrument must be for a sum certain.¹ The effect of discounts and changing interest rates on the "sum certain" requirement has, however,³ bothered the courts for some time. By the terms of the Negotiable Instruments Law itself, this question must be solved by the rules of the Law Merchant.⁴ An attempt will be made to classify certain instruments which provide for changing rates of interest, and to discover, if possible, a standard which can be used to determine whether or not such instruments satisfy the requirement that a negotiable instrument be for a sum certain.

I

The simplest class of instruments involving a changing interest rate may be divided into two types. The instruments comprising the first type bear one rate of interest on the principal until the maturity of the note, and a higher rate on the principal from maturity of the note until the obligation is discharged. Instruments of the second type are free of interest until the maturity of the principal, but bear interest on the principal after maturity until the note is paid. An example of the first type of instrument is found in *Citizens' Savings Bank v. Landis*.⁵

1. N. I. L. sec. 1 (2), R. S. Mo. (1929) sec. 2630 (2): "An instrument to be negotiable must conform to the following requirements: * * * (2) Must contain an unconditional promise or order to pay a sum certain in money." N. I. L. sec. 2, R. S. Mo. (1929) sec. 2631: "The sum payable is a sum certain within the meaning of this act, altho it is to be paid: 1) with interest; or 2) by stated instalments; or 3) by stated instalments, with a provision that upon default in payment of any instalment or of interest the whole shall become due; or 4) with exchange, whether at a fixed rate or at the current rate; or 5) with costs of collection or an attorney's fee, in case payment shall not be made at maturity." N. I. L. sec. 184, R. S. Mo. (1929) sec. 2812: "A negotiable promissory note within the meaning of this act is 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 future time, a sum certain in money to order or to bearer. Where a note is drawn to the maker's own order, it is not complete until indorsed by him."

2. Omitted.

3. *First Nat. Bank of Iowa City, Iowa v. Watson* (1916) 56 Okl. 495, 511, 149 Atl. 21, 23, where the court said that section 2 of the N. I. L. would have expressly so provided if it had been intended that a discount provision giving the maker an option to discharge the instrument within 30 days of its date should not affect the certainty.

4. N. I. L. sec. 196; R. S. Mo. (1929) sec. 2827: "In any case not provided for in this act the rules of the law merchant shall govern."

5. *Citizens' Savings Bank of Columbus, Ohio v. Landis* (1913) 37 Okl. 530, 132 Pac. 1101.

The instrument was dated March 6, 1906, and the promise was to pay \$1200 with interest at 6% per annum before maturity, and 10% per annum after maturity, until paid. Interest was payable annually. Most courts have held that such a provision does not render the amount uncertain, nor render the instrument non-negotiable,⁶ although the provision for a higher rate of interest after maturity has been held to violate the usury laws and therefore to work a forfeiture of the entire interest.⁷ An instrument dated June 4, 1890, and due 90 days after date, with interest at 8% per annum payable only after maturity is characteristic of the above-mentioned second type.⁸ The instruments of this type do not differ materially from those of the former type, and it would seem, on principle, that they should be negotiable. A majority of the courts have so held.⁹

II

In another group of instruments the rate change is brought about by failure to pay the principal at maturity, but the increased rate applies not from maturity until paid, but from the

6. *Hutson v. Rankin* (1922) 36 Idaho 169, 213 Pac. 345; *Towne v. Rice* (1876) 122 Mass. 67; *Goedhard v. Folstad* (1923) 156 Minn. 454, 195 N. W. 281; *Kendall v. Selby* (1902) 66 Neb. 60, 92 N. W. 178; *Hollinshead v. John Stuart & Co.* (1898) 8 N. D. 35, 77 N. W. 89; *Citizens' Savings Bank of Columbus, Ohio v. Landis* (1913) 37 Okl. 530, 132 Pac. 1101; *Merrill v. Hurley* (1895) 6 S. D. 592, 62 N. W. 958; *contra* *Second National Bank of Richmond v. Wheeler* (1889) 75 Mich. 546, 43 N. W. 963; *Cornish v. Wolverton* (1905) 32 Mont. 456, 81 Pac. 4; *Bracken v. Fidelity Trust Co.* (1914) 42 Okl. 118, 141 Pac. 6, L. R. A. 1915B 1216. Other cases supporting the majority view but involving other provisions in addition to the typical ones are: *Allen v. Cooling* (1924) 161 Minn. 10, 200 N. W. 849; *Lister v. Donlan* (1929) 85 Mont. 571, 281 Pac. 853; *Moore v. Interstate Mortgage Trust Co.* (1935) 172 Okl. 471, 45 P. (2d) 485; *Sharpe v. Schoenberger* (1921) 44 S. D. 402, 184 N. W. 209; *Continental & Commercial Nat. Bank of Chicago v. Jefferson* (1927) 51 S. D. 477, 215 N. W. 533; *De Hass v. Roberts* (C. C. W. D. Pa. 1894) 59 Fed. 853, *rev'd* (C. C. A. 3, 1895) 70 Fed. 227.

7. *Allen v. Cooling* (1924) 161 Minn. 10, 200 N. W. 849; *Goedhard v. Folstad* (1923) 156 Minn. 454, 195 N. W. 281. This result was reached under Minn. G. S. (1913) sec. 5805; Minn., *Mason's Stats.* (1927) sec. 7036, which provides that contracts must bear the same rate of interest after they become due as before. The question whether provisions such as those under discussion provide for penalties is beyond the scope of this article.

8. *Farmers' Nat. Bank v. Sutton Mfg. Co.* (C. C. A. 6, 1892) 52 Fed. 191, 17 L. R. A. 595.

9. *Dorsey v. Wolff* (1892) 142 Ill. 589, 32 N. E. 495; *Houghton v. Francis* (1862) 29 Ill. 244; *Kuhn v. National City Bank* (1918) 187 Ind. 726, 119 N. E. 145; *Millikan v. Security Trust Co.* (1918) 187 Ind. 307, 118 N. E. 568; *Bunting v. Mick* (1892) 55 Ind. App. 289, 31 N. E. 378; *Hatch v. Bank of Dexter* (1900) 94 Me. 348, 47 Atl. 908; *Farmers' Nat. Bank of Valparaiso, Indiana v. Sutton Mfg. Co.* (C. C. A. 6, 1892) 52 Fed. 191, 17 L. R. A. 595; *contra* *Farmers' Loan and Trust Co. v. McCoy & Spivey Bros.* (1912) 32 Okl. 277, 122 Pac. 125, 40 L. R. A. (N. S.) 177; *Dickerson v. Higgins* (1905) 15 Okl. 588, 82 Pac. 649.

date of the instrument until paid. These instruments may also be divided into two types: first, those which bear interest at one rate until maturity, but if not paid at maturity bear a different and higher rate from the date of the instrument; second, those which bear no interest until maturity, but if not paid at maturity bear interest from date. The first type is illustrated by a note with the following clauses: "with interest at the rate of 6% per annum from date, if not paid when due 8% from date."¹⁰ A different way of phrasing this type of instrument, with the same legal effect is by a stipulation that the principal be payable with interest at the rate of 9% per annum, payable annually, from date until paid; but if the note be not paid on or before maturity, interest should only be 7%.¹¹ The court, in the latter instance, held that the provision with respect to interest was equivalent to one saying that interest on the principal was payable from date until maturity at 7% per annum, but if the note was not paid when due, it should bear interest at the rate of 9% per annum from date.¹² The majority holding is that this type of instrument, expressed in either form, meets the requirement of certainty of sum.¹³

An example of an instrument representing the second type considered in this section was one dated May 1, 1905, in which the maturity date was November 1, 1905.¹⁴ The maker promised to pay \$500 with interest at 8%, payable annually from the maturity date until discharged. Interest, however, was to be paid from date, if the note was not paid when due. The instruments falling into this division are practically indistinguishable from those in the first division, and a majority of courts have logically held that such provisions do not destroy negotiability.¹⁵

10. *Farm Mortgage & Loan Co. v. Martin* (1927) 51 S. D. 424, 214 N. W. 816.

11. *Union Nat. Bank of Massillon, Ohio v. Mayfield* (1918) 71 Okl. 22, 174 Pac. 1034, 2 A. L. R. 135.

12. See *Smith v. Crane* (1885) 33 Minn. 144, 22 N. W. 633, 53 Am. Rep. 20.

13. *Clark v. Skeen* (1900) 61 Kan. 526, 60 Pac. 327, 78 Am. St. Rep. 337; *Crump v. Berdan* (1893) 97 Mich. 293, 56 N. W. 559, 37 Am. St. Rep. 345; *First Nat. Bank of Port Huron v. Carson* (1886) 60 Mich. 432, 27 N. W. 589; *Smith v. Crane* (1885) 33 Minn. 144, 22 N. W. 633, 53 Am. Rep. 20; *Union Nat. Bank v. Mayfield* (1918) 71 Okl. 22, 174 Pac. 1034, 2 A. L. R. 135; *Farm Mortgage & Loan Co. v. Martin* (1927) 51 S. D. 424, 214 N. W. 816; *contra Cayuga County Nat. Bank of Auburn v. Purdy* (1885) 56 Mich. 6, 22 N. W. 93 (instrument held non-negotiable, but interest clause not specifically attacked); *Hegeler v. Comstock* (1890) 1 S. D. 138, 45 N. W. 331, 8 L. R. A. 393 (overruled by *Farm Mortgage & Loan Co. v. Martin* (1927) 51 S. D. 424, 214 N. W. 816).

14. *Security Trust & Savings Bank v. Gleichman* (1915) 50 Okl. 44, 150 Pac. 908, L. R. A. 1915F. 1203.

15. *Reeves v. Stipp* (1879) 91 Ill. 609; *Parker v. Plymell* (1880) 23 Kan. 402; *Citizens' Bank v. Booze* (1898) 75 Mo. App. 189; *Hope v. Barker*

III

The litigated discount provisions may be divided into two general classes: (1) discount provisions which are to take effect before maturity, and (2) "discount" provisions which are to take effect either "at maturity" or "on or before maturity." An example of the first class is found in *Waterhouse v. Chouinard*,¹⁶ which involved a promissory note payable in installments, (the first installment becoming due 6 months after date, and the second and last installment 12 months after date) with interest at 6% per annum on overdue payments. The maker had the privilege of discharging the indebtedness by payment of the principal less a discount of 5% *within 30 days of the date* of the note. The court decided that this discount provision rendered the sum uncertain, and held the note non-negotiable. There has been a conflict of authority as to the effect of such a discount provision on the certainty of the note.¹⁷

The second class of instrument involving a discount has previously been noted.¹⁸ Illustrative of this type is an instrument in which the principal bore interest at the rate of 9% per annum, payable annually, from date until paid. It contained a provision that if the note were paid *on or before maturity*, the interest

(1892) 112 Mo. 338, 20 S. W. 567, 34 Am. St. Rep. 387; *Christian County Bank v. Goode* (1891) 44 Mo. App. 129; *Jackson v. Fennimore* (1924) 104 Okl. 134, 230 Pac. 689; *Security Trust & Savings Bank v. Gleichman* (1915) 50 Okl. 441, 150 Pac. 908, L. R. A. 1915F 1203; *Commercial Credit Co. v. Nissen* (1926) 49 S. D. 303, 207 N. W. 61, 213 N. W. 943; *contra Randolph v. Hudson* (1903) 12 Okl. 516, 74 Pac. 946, which was overruled by *Security Trust & Savings Bank v. Gleichman* (1915) 50 Okl. 441, 150 Pac. 908, L. R. A. 1915F 1203.

16. *Waterhouse v. Chouinard* (1930) 128 Me. 505, 149 Atl. 21.

17. The following cases have held that such a provision renders the sum uncertain: *Waterhouse v. Chouinard* (1930) 128 Me. 505, 149 Atl. 21; *Way v. Smith* (1873) 111 Mass. 523; *Lamb v. Storey* (1881) 45 Mich. 488, 8 N. W. 87 (1884) 52 Mich. 525, 18 N. W. 248; *Fralick v. Norton* (1851) 2 Mich. 130, 55 Am. Dec. 56 (agreement that payment of \$50 on a \$60 note, 10 days before maturity would cancel the note); *Lambert v. Harrison* (1918) 69 Okl. 172, 171 Pac. 45; *First Nat. Bank of Iowa City v. Watson* (1916) 56 Okl. 495, 155 Pac. 1152; *Farmers' Loan & Trust Co. v. McCoy & Spivey Bros.* (1912) 31 Okl. 433, 122 Pac. 125, 40 L. R. A. (N. S.) 177; *Nat. Bank of Commerce v. Feeney* (1899) 12 S. D. 156, 80 N. W. 186, 46 L. R. A. 732, 76 Am. St. Rep. 594; *Farmers' Loan & Trust Co. v. Devear* (1911) 2 Tenn. C. C. A. 366; *contra First Nat. Bank of Iowa City v. Rooney* (1913) 11 Dom. L. R. 353; *Seymour & Co. v. Artz* (1926) 5 La. App. 556; *Russell v. Klink* (1884) 53 Mich. 161, 18 N. W. 627 (discount provision of 7%, allowed from the time of payment until maturity, appeared on the back of the note); *Farmers' Loan and Trust Co. v. Planck* (1915) 98 Neb. 225, 152 N. W. 390, L. R. A. 1915E 564; *Stevens v. Baldy* (1917) 67 Pa. Sup'r Ct. 145, where lower court held the instrument negotiable but superior court reversed the decision on another ground; *Harrison v. Hunter* (Texas 1914) 168 S. W. 1036.

18. See section II of this article.

should only be 7%.¹⁹ The majority rule seems to be that such a provision does not destroy the certainty of sum required by the Law Merchant and the Negotiable Instruments Law.²⁰

IV

The courts have used different tests to determine whether the above types of varying-interest rate provisions satisfy the requirement as to "sum certain."

A. A provision which required payment of 6% interest from the date of the instrument if not paid at maturity was said to make the amount uncertain and contingent, thereby rendering the paper non-negotiable.²¹ The court, however, held that this provision did not make the amount uncertain, saying that "the spirit of the rule requiring precision in the amount of negotiable instruments applies rather to principal amount than to ancillary and incidental additions of interest or exchange."²² The above language, however, dealt with the effect of exchange provisions on the certainty of the amount. Altho it would be strong persuasive authority, it does not furnish direct support for the decision. This test, if applied literally, would dispense with an examination of the interest provisions, and would favor the negotiability of instruments such as those under consideration.

B. A Kansas court enunciated a test that has many adherents.²³ The maker promised to pay interest at the rate of 12% after maturity, but there was another provision to the effect that if the note was not paid at maturity, it should bear the 12% interest rate from date. The court held the instrument negotiable stating that these provisions as to interest came into effect only

19. *Union Nat. Bank v. Mayfield* (1918) 71 Okl. 22, 174 Pac. 1034, 2 A. L. R. 135.

20. *Loring v. Anderson* (1905) 95 Minn. 101, 103 N. W. 722; *Union Nat. Bank of Massillon, Ohio v. Mayfield* (1918) 71 Okl. 22, 174 Pac. 1034, 2 A. L. R. 135; see *Capital City Bank v. Swift* (D. C. E. D. Okl. 1923) 290 Fed. 505 (a trade acceptance with provision "if paid when due a discount of \$156.73 may be deducted reducing the face of this acceptance to \$3,142.92"); *Smith v. Crane* (1885) 33 Minn. 144, 22 N. W. 633, 53 Am. Rep. 20 ("with interest at 10% per annum from date until paid; 7% if paid when due"); *Mansfield Savings Bank v. Miller* (1887) 2 Ohio C. C. 96, 1 Ohio C. D. 383, 53 O. S. 666 ("if this note is paid in full when due, a discount of \$39.78 is to be made from the amount then due"); *Commercial Credit Co. v. Nissen* (1926) 49 S. D. 303, 207 N. W. 61 (1927) 51 S. D. 357, 213 N. W. 943; contra *Edwards v. Ramsey* (1882) 30 Minn. 91, 14 N. W. 272; *Third Nat. Bank of Syracuse v. Armstrong* (1870) 25 Minn. 530; see also *Hegeler v. Comstock* (1890) 1 S. D. 138, 45 N. W. 331, 8 L. R. A. 393 ("8% if paid when due").

21. *Christian County Bank v. Goode* (1891) 44 Mo. App. 129.

22. 1 *Daniels, Negotiable Instruments* (3rd ed. 1882) 58, sec. 54a. See 1 *Daniels, Negotiable Instruments* (7th ed. 1933) 70, sec. 60.

23. *Parker v. Plymell* (1880) 23 Kan. 402.

after the notes were dishonored and had lost their negotiability, and there was no uncertainty in the manner and extent of their operation. Therefore they should not affect the negotiability of the instrument. A federal court has said that this is not the best test of certainty, since it would not be applicable to provisions for exchange.²⁴ The Kansas test is also objectionable in its application to a discount provision such as was involved in *Waterhouse v. Chouinard*.²⁵ It has, however, been used many times²⁶ by courts desiring to uphold the negotiability of an instrument which would be non-negotiable under the next test to be discussed.

C. The test applied by a South Dakota court²⁷ has frequently been responsible for holding an instrument non-negotiable when it contained a provision involving a fluctuating rate of interest. That court said that it is not sufficient that the amount necessary to liquidate the note on the day it is due is certain and can be determined, but that the certainty must continue until the obligation is discharged.

There should be such a degree of certainty that the exact amount to become due and payable at any future date should be clearly ascertainable at the date of the note, uninfluenced by any condition not certain of fulfillment.²⁸

Courts have applied this test to all the types of cases so far considered with the result that they have frequently found that particular interest provisions did not meet the requirements of certainty.²⁹ This would seem to be too stringent a test, and one

24. *Cudahy Packing Co. v. State Nat. Bank* (C. C. A. 8, 1904) 134 Fed. 538. This case involved the effect of a stipulation for attorney's fees on the certainty of the sum. It was decided before the enactment of the N. I. L.

25. See section III of this note.

26. *Mansfield Savings Bank v. Miller et al.* (1887) 2 Ohio C. C. 95, 1 Ohio C. D. 383, 53 O. S. 666; *Capital City State Bank v. Swift* (D. C. E. D. Okl. 1923) 290 Fed. 505; see concurring opinion in *Hegeler v. Comstock* (1890) 1 S. D. 138, 45 N. W. 331, 8 L. R. A. 393. See also Bigelow, *Negotiable Instruments* (Lile) (3rd ed. 1928) 71, sec. 114, where it is stated that "the consideration that such stipulations do not affect the time of maturity, and are not operative during the currency of the instrument, but become effective only after dishonor, when the instrument has ceased to be negotiable in the full sense, has influenced the majority of courts, following the better principle, to interpret such stipulations as not violative of the rule of certainty of sum, nor otherwise affecting negotiability."

27. *Hegeler v. Comstock* (1890) 1 S. D. 138, 45 N. W. 331, 8 L. R. A. 393.

28. *Waterhouse v. Chouinard* (1930) 128 Me. 505, 511, 149 Atl. 21, 23.

29. *Waterhouse v. Chouinard* (1930) 128 Me. 505, 149 Atl. 21; *Lamb v. Story* (1881) 45 Mich. 488, 8 N. W. 87 (1884) 52 Mich. 525, 18 N. W. 248; *Lambert v. Harrison* (1918) 69 Okl. 172, 171 Pac. 45; *First Nat. Bank v. Watson* (1916) 56 Okl. 495, 155 Pac. 1152; *Bracken v. Fidelity*

that would not be applied by the very people who most frequently use negotiable instruments. It has been disapproved by the very judges bound to follow it by *stare decisis*.³⁰ On the other hand it was adopted as a preferable view, after a thorough resume of the discount cases in *Waterhouse v. Chouinard*.³¹

D. A test more nearly in accord with the policy of holding instruments negotiable if possible³² and more closely coinciding with the commercial notion of certainty was applied where the instrument provided for payment of principal with interest at 7%, and contained a further stipulation that if the principal was not paid when due, the maker would pay 10% interest from the date of the instrument until paid.³³ The court said that there was no date at which the precise amount due on the note could not have been determined by an inspection of the instrument itself. Courts applying this test merely require that at any given date, the amount due on the instrument can be ascertained, unaided by any information not appearing on the instrument.³⁴ In *Cudahy Packing Co. v. State National Bank*,³⁵ which dealt with the formerly very troublesome question of the effect of a stipulation for attorney's fees on the certainty of the instrument, it was said

The rule requiring certainty in commercial paper was a rule of commerce before it was a rule of law. It requires commercial, not mathematical certainty. An uncertainty which does not impair the functions of negotiable instruments in

Trust Co. (1914) 42 Okl. 118, 141 Pac. 6, L. R. A. 1915B 1216; *Farmers' Loan & Trust Co. v. McCoy & Spivey Bros.* (1922) 31 Okl. 433, 122 Pac. 125, 40 L. R. A. (N. S.) 177; *Randolph v. Hudson* (1903) 12 Okl. 516, 74 Pac. 946; *National Bank of Commerce v. Feeney* (1899) 12 S. D. 156, 80 N. W. 186, 46 L. R. A. 732, 76 Am. St. Rep. 594; *Merrill v. Hurley* (1895) 6 S. D. 592, 62 N. W. 958.

30. *Merrill v. Hurley* (1895) 6 S. D. 592, 62 N. W. 958.

31. *Waterhouse v. Chouinard* (1930) 128 Me. 505, 149 Atl. 21.

32. *International Finance Corp. v. Philadelphia Wholesale Drug Co.* (1933) 312 Pa. 280, 167 Atl. 790; *Williamson et al. v. Craig et al.* (1927) 204 Iowa 555, 215 N. W. 664.

33. *Crump v. Berdan* (1893) 97 Mich. 293, 56 N. W. 559, 37 Am. St. Rep. 345.

34. *First Nat. Bank of Iowa City v. Rooney* (1913) 11 Dom. L. R. 358; *Hatch v. First National Bank of Dexter* (1900) 94 Me. 348, 47 Atl. 908, 80 Am. St. Rep. 401; *Crump v. Berdan* (1893) 97 Mich. 293, 56 N. W. 559, 37 Am. St. Rep. 345; *Loring v. Anderson* (1905) 95 Minn. 101, 103 N. W. 722; *Farmers' Loan & Trust Co. of Iowa City, Iowa v. Planck* (1915) 98 Neb. 225, 152 N. W. 390, L. R. A. 1915 E 564. See *Commercial Credit Co. v. Nissen* (1926) 49 S. D. 303, 207 N. W. 61, 51 S. D. 357, 213 N. W. 943; *Merrill v. Hurley* (1895) 6 S. D. 592, 62 N. W. 958 (see personal opinion of judge, but not the holding).

35. *Cudahy Packing Co. v. State Nat. Bank* (C. C. A. 8, 1904) 134 Fed. 538, 67 C. C. A. 662.

the judgment of business men ought not to be regarded by the courts.³⁶

The case further commented on the fact that whenever an instrument was presented, varying in some of its features from the ordinary promissory note or bill of exchange, the English courts would call in business men for their guidance. If, from their evidence, it appeared that the instrument in question was by the general custom and practice of the business world treated as a negotiable instrument, the courts would give effect to that usage and hold the instrument negotiable.³⁷ The rule of commercial certainty suggested by the aforementioned case and universal adoption of the English practice would obviate much of the conflict that has arisen over fluctuating interest rates. This rule has been successfully applied to an interest provision more complicated than any yet considered.³⁸

V

The instruments considered, thus far, have involved changing interest rates on the principal,³⁹ but there are also instruments which involve "secondary" interest on "primary,"⁴⁰ in addition to the features considered in the first two sections. The simplest type of instrument to be considered in this section is illustrated by a promissory note, due in one year, bearing 6% interest per annum, payable *annually*, with principal and interest not paid when due bearing interest at 10% per annum until paid.⁴¹ The Montana Supreme Court held that such a provision did not render the amount uncertain. The effect of the provision for increase of interest on the principal, if not paid when due, has already been considered,⁴² and the only new problem is whether or not the stipulation for "secondary"⁴⁰ interest on interest renders the sum uncertain. In the first place, it seems well settled that a mere provision for compound interest does not render the sum uncertain.⁴³ It has previously been shown that a provision

36. *Cudahy Packing Co. v. State Nat. Bank* (C. C. A. 8, 1904) 134 Fed. 538, 542.

37. *Id.* at 543.

38. *Continental & Commercial Nat. Bank of Chicago v. Jefferson* (1927) 51 S. D. 477, 215 N. W. 533.

39. See sections I, II, and III of this note.

40. For the purpose of convenience, interest on the principal will be referred to as "primary" interest, and the higher rate of interest on the primary interest will be called "secondary" interest. This note does not discuss the common type of compound interest, where the secondary and primary interest are at the same rate.

41. *Lister v. Donlan* (1929) 85 Mont. 571, 281 Pac. 348.

42. See sections I and II of this article.

43. *Fox v. Crane* (1919) 43 Cal. App. 559, 185 Pac. 415; *Glenn v. Rice* (1917) 174 Cal. 269, 162 Pac. 1020; *Gilmore v. Hurst* (1896) 56 Kan. 626,

for increase of interest on the principal at maturity of the principal has generally been held not to render the amount uncertain. If that is true, it seems that the same result should follow in the present case. In the above instrument, it will be noticed that no interest payment is due until the maturity of the principal, *i. e.*, there can be no "secondary" interest before the maturity of the principal.⁴⁴ Applying the tests discussed in the previous section, it is evident that the same result would be reached whenever test "A," "B," or "D" is used.⁴⁵

Another variation of the "interest on interest" problem is illustrated by *Continental & Commercial National Bank of Chicago v. Jefferson*,⁴⁶ in which it was held possible to have "secondary" interest *before* maturity of the principal. There the instrument matured in one year from its date, and the maker promised to pay the principal with interest at the rate of 8% per annum, payable *semi-annually*, from date until due. There was another provision to the effect that if any of the principal or interest was not paid when due, it (principal or interest) should bear interest at the rate of 10% per annum, payable semi-annually, until paid. It was argued that the instrument did not call for a sum certain, since it was impossible to tell in advance whether the maker would pay the semi-annual interest payment when it came due at the end of the first 6 months' period, and if it was not paid, then the amount necessary to retire the note at its maturity would be quite different from the amount necessary to retire the note if the semi-annual interest installment had been paid. It was held, however, that the provision did not render the instrument uncertain in amount. The court applied the test of "commercial certainty,"⁴⁷ and said that in a note of this kind, if the maker complies with his contract, there is no question about the amount necessary to pay the note at maturity, and if he does not so comply, the matter is one of simple computation.

44 Pac. 603; *Brown v. Vossen* (1905) 112 Mo. App. 676, 87 S. W. 577; *Barker v. Sartori* (1911) 66 Wash. 260, 119 Pac. 611. In the latter case there was interest on interest, but the court did not specifically deal with that point.

44. See also *Cherry v. Sprague* (1904) 187 Mass. 113, 72 N. E. 456, 67 L. R. A. 33, 105 Am. St. Rep. 381; *contra* *Dickerson v. Higgins* (1905) 15 Okl. 588, 82 Pac. 649. This instrument involved a stipulation for attorney's fees in addition to the interest provision. It is difficult to tell which factor was responsible for the decision.

45. Under test "C" the instrument would probably have been held non-negotiable.

46. *Continental & Commercial Nat. Bank of Chicago v. Jefferson* (1927) 51 S. D. 477, 215 N. W. 533.

47. See section IV, test "D" of this note.

The court overruled dictum in *Sharpe v. Schoenberger*,⁴⁸ which had involved a promissory note dated April 8, 1920, due Oct. 9, 1920, and payable with interest at the rate of 8% per annum, payable semi-annually, until fully paid, but with interest at the rate of 12% per annum on overdue interest. There was dictum in that case to the effect that if the note had been made payable one or two years after date, this provision would have made the instrument non-negotiable by reason of the uncertainty of the promise. There would then be a possibility of "secondary" interest before the maturity of the principal. But in the *Schoenberger* case there was no possibility of this because the instrument was only a six months' note.

In a recent case⁴⁹ the note was dated July 29, 1930, and was to bear 6½% interest per annum until maturity, August 1, 1937, payable semi-annually. After maturity the principal sum was to bear interest at the rate of 10% per annum. The 6½% interest was payable by means of coupons in the form of promissory notes, which after their maturity bore interest at the rate of 10% per annum. If one considers the principal note and the interest notes together, the entire obligation could be classified as one in which there would be a possibility of "secondary" interest before the maturity of the principal, and in that aspect like the obligation in the *Continental Bank* case.⁵⁰ The court, however, regarded it merely as a case of an increased rate of interest on the principal at the maturity of the principal and held it negotiable without considering the "interest on interest" problem. This method of using separate instruments for the principal and the interest would seem to be a possible way to avoiding the argument in the *Continental* case,⁵¹ and still secure the same advantages for the holder.

The Montana case of *Cornish v. Woolverton*⁵² involved a note due five years from date with interest at the rate of 6% per annum from date until maturity, payable *semi-annually*, according to the tenor of interest notes. The note and the interest coupons were to draw interest at the rate of 12% per annum after their maturity. The court held the instrument uncertain in sum, because it was not certain that the condition referred

48. See *Sharpe v. Schoenberger* (1921) 44 S. D. 402, 404, 184 N. W. 209, 209.

49. *Moore v. Interstate Mortgage Trust Co. et al.* (1935) 172 Okl. 471, 45 P. (2d) 485.

50. *Supra*, note 46.

51. *Supra*, note 46.

52. *Cornish v. Woolverton* (1905) 32 Mont. 456, 81 Pac. 4, 108 Am. St. Rep. 598.

to would be fulfilled, and because the instrument contained a contract other than that authorized by statute.⁵³ An opposite result was reached where there was⁵⁴ an instrument having similar interest clauses, plus an additional provision that the notes were secured by a mortgage which provided that if any of the interest coupons were not paid at maturity, the principal debt would become due, and the unpaid coupon, first matured, would become part of the principal, and the whole principal debt and the first unpaid coupon would bear interest at 12% per annum from maturity of said coupon until paid. In each of these cases it was possible to have "secondary" interest before the maturity of the principal, and if the courts had used the rule of "commercial certainty," the instruments would have been held negotiable in each case. The court in the latter situation⁵⁵ reached its result with little reasoning, relying on a case⁵⁶ which expressed the theory that provisions which come into effect only after maturity do not affect negotiability.⁵⁷ The Montana court later⁵⁸ said that the *Woolverton* case⁵⁹ was largely based on a South Dakota case,⁶⁰ and upon a statute⁶¹ similar to that involved in the latter case in which the court had demanded the standard of certainty required by test "C."⁶²

An instrument that has caused quite a bit of conflict is found in *First National Bank of Miami v. Bosler*.⁶³ The instrument was dated March 16, 1925, payable on or before 18 months after date, with interest at the rate of 8% per annum from date until fully paid. Interest was payable semi-annually. Deferred payments were to bear interest from maturity at 10% per annum payable semi-annually. The court held that this instrument did not call for a sum certain because there were two irreconcilable

53. Montana Civil Code (1895) sec. 3991: "A negotiable instrument is a written promise or request for the payment of a certain sum of money to order or bearer, in conformity to the provisions of this article." Sec. 3993: "A negotiable instrument must be made payable in money only, and without any condition not certain of fulfillment." Sec. 3997: "A negotiable instrument must not contain any other contract than such as specified in this article."

54. *DeHass v. Roberts* (C. C. W. D. Pa. 1894) 59 Fed. 853, aff'd (C. C. A. 3, 1895) 70 Fed. 227, 30 L. R. A. 189.

55. *Supra*, note 54.

56. *Parker v. Plymell* (1880) 23 Kan. 402.

57. See section IV, test "B" of this article.

58. *Lister v. Donlan* (1929) 85 Mont. 571, 281 Pac. 348.

59. *Supra*, note 52.

60. *Hegeler v. Comstock* (1890) 1 S. D. 138, 45 N. W. 331, 8 L. R. A. 393.

61. *Supra*, note 53.

62. See section IV, test "C" of this note.

63. *First Nat. Bank of Miami v. Bosler* (1929) 297 Pa. 353, 147 Atl. 74.

clauses in respect to interest payable after maturity.⁶⁴ On the other hand, a New York court in ruling on the same type of instrument held that there was no lack of certainty and that the instrument was negotiable.⁶⁵ The court criticized the holding of the *Bosler* case.

It was reasoned in that case [Bosler case] that the notes carried 8% interest on the principal sum secured up to the time when the principal or any part thereof was paid, whether at or after maturity, that "deferred payments" bearing 10% interest referred to payments of principal as well as interest, and that thereby uncertainty of amount to be paid resulted. We disagree with that reasoning.⁶⁶

The New York court said that the 8% interest provision covers all the principal unpaid and as long as it is unpaid, whether at or after the maturity date of the notes. It was further stated that "deferred payments" refers only to payments of *interest* accrued and unpaid *at and at anytime after* the maturity date of the note. The notes construed in this manner presented no ambiguity or inconsistency to the court. While the result in this case is probably desirable, there is no reason why the construction of "deferred payments" should be limited to "payments of interest accrued and unpaid *at and at any time after the maturity date of the notes.*"⁶⁷ It would seem that "deferred payments" should refer to any overdue interest payment whether before or after the maturity of the principal, and if such were the case, the instrument would have "secondary" interest before the maturity of the principal, which, according to the *Continental* case,⁶⁸ is not objectionable.

In a recent United States Supreme Court case⁶⁹ the instrument bore interest on the principal sum at the rate of 7% per annum, payable semi-annually, from date until fully paid. Deferred *interest* payments were to bear interest from maturity at 10%, payable semi-annually. The Supreme Court said that the instrument was free of ambiguity and held it negotiable. The only difference between the phrasing of this instrument and that of the New York case is that this instrument said "deferred *interest* payments," instead of merely "deferred payments." It was

64. See also *New Miami Shores Corporation v. Duggan* (1931) 9 N. J. Misc. Rep. 620.

65. *Lessen v. Lindsey* (1933) 264 N. Y. S. 391.

66. *Id.* at 392.

67. *Ibid.* (Italics supplied).

68. *Supra*, note 46.

69. *Burns Mortgage Co. v. Fried* (1933) 292 U. S. 487, 54 S. Ct. 813, 78 L. ed. 1380.

thought obvious that by "maturity" the draftsman meant maturity of the interest, rather than maturity of the principal. After adopting this construction, the court was faced with an instrument resembling that in the *Continental Bank* case⁷⁰ since there was thus created a possibility of "secondary" interest before the maturity of the principal. If, as admitted, the court of last resort of the state held that a provision for payment of interest in installments prior to the maturity of the principal did not create an uncertainty in the sum payable, an added stipulation that overdue interest should bear interest at a named rate until paid would not call for a different decision. The result reached is perfectly in line with the "commercial certainty" test, but would hardly have been reached with tests "B" and "C."⁷¹

VI

There are, of course, some instruments which through inadvertence or ignorance are so written that they cannot be held to meet the requirement of "sum certain," even by application of the most liberal rules. A case of this kind was presented where the instrument was dated June 15, 1893, and was payable November 1, 1895, with interest from date until fully paid at the rate of 10% per annum, payable annually on the principal and all overdue unpaid interest.⁷² Another provision stipulated that if the interest was not paid when due it should become part of the principal and draw interest at 12% per annum until paid. The court rightly held the instrument non-negotiable because it did not call for a sum certain. There were two conflicting rates of interest applying to overdue interest, and an inspection of the instrument would not disclose whether overdue interest should be paid at 10% per annum, or 12%. It was not clear whether the principal plus the first overdue interest installment should be carried at 12%.

Another example is found in a note which provided for payment of interest at 8% interest per annum until paid, and at the same time provided for payment of 10% interest on any deficiency resulting after the sale of collateral securities.⁷³ Such an instrument would not be negotiable even under the "commercial certainty" test because there cannot be commercial certainty in the face of hopelessly conflicting interest clauses.

70. *Supra*, note 46.

71. See section IV of this note.

72. *Davis v. Brady* (1903) 17 S. D. 511, 97 N. W. 719.

73. *Ashcraft v. Bream* (D. C. M. D. Pa. 1932) 2 F. Supp. 344.

CONCLUSION

None of the tests, which have been considered, may be applied to every situation with a pristine clear result. There is no test which is so infallible that it will automatically produce the proper result if applied by a court unfamiliar with, or heedless of the needs and common practices of the business world. The test of "commercial certainty" is undoubtedly the standard that should be applied to every case, but the test itself does not disclose just what commercial certainty is. To define commercial certainty as that degree of certainty which would be sufficient to satisfy a business man of average business intelligence, is but to generalize. Such a definition, however, has one virtue: it should cause the courts to look to the business world for guidance. If the definition does that, it has accomplished its purpose. If the rule that an instrument is sufficiently certain if at any given date an inspection of the instrument will reveal data from which the exact amount due on that date can be computed, and the policy of the law in favor of the free circulation of commercial paper are considered together, there will result practical tests which may be employed to advantage as supplementing the rule of "commercial certainty."

If a rationale of the apparent majority rules were desirable it might be phrased as follows: The sum is sufficiently certain if the only factor which will upset the certainty is a provision containing either or both of the following features: (1) a promise by the maker or primary party to pay either a fixed additional sum, or interest at a definite additional rate, if he defaults on the payment of the principal, an installment of the principal, or any interest installment; or (2) an option of the maker to discharge the obligation by payment in full either within a specified time after the date of the instrument, or at, on, or before the maturity of the principal.

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