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ACCOMMODATING SPOUSES: REGULATION B AND  
REVISED ARTICLE 3—THE SURETYSHIP LAW  
COMPLICATION

*Sarah Howard Jenkins\**

Congress enacted the Equal Credit Opportunity Act<sup>1</sup> in 1974 to insure fairness and impartiality in the extension of credit. Congress found that economic stability and competition among financial institutions would be enhanced if credit decisions were made without discrimination on the basis of sex or marital status.<sup>2</sup> The Act and its implementing regulation, Regulation B, were designed “to promote the availability of credit for all creditworthy applicants without regard to . . . marital status” and to prohibit practices that discriminate on that basis.<sup>3</sup> Later, the scope of the Act was extended to include other classes of discrimination such as race, color, religion, national origin, sex, age, income—if derived from public assistance, or the good faith exercise of any right under the Act.<sup>4</sup> Although the scope of the Act extends beyond discrimination on the basis of marital status, this article is limited in scope to the impact of the Act and Regulation B on guaranties<sup>5</sup> by spouses with special emphasis on spousal guaranties on negotiable instruments.

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1. Equal Credit Opportunity Act of 1974 § 503, 15 U.S.C. §§ 1691-1691f (1995).

2. 15 U.S.C. § 1601(a) (1995).

3. Regulation B (Equal Credit Opportunity), 12 C.F.R. § 202.1-202.7 (1994) [hereinafter Reg. B].

4. 15 U.S.C. § 1691(a) (1995).

5. Guaranty or its plural form, guaranties, is the noun form and guarantee or guarantees is the verb form used throughout this article.

The law governing negotiable instruments in thirty-eight jurisdictions is Revised Article 3.<sup>6</sup> Former Article 3 is the applicable law in the thirteen remaining jurisdictions. Revised Article 3, promulgated by the National Conference of Commissioners on Uniform State Laws and the American Law Institute in 1990, is an attempt to modernize the substance of the Article and to conform its style to that of the other articles.<sup>7</sup> Because Revised Article 3 contains suretyship rules more favorable to creditors' interests than those of the Restatement of Suretyship,<sup>8</sup> the common law,<sup>9</sup> former Article 3,<sup>10</sup> and other state suretyship statutes,<sup>11</sup> creditors may be more inclined in the future to request guarantors of credit to make their guaranties on the principal debtor's promissory note rather than in a separate document.<sup>12</sup> Guarantors or sureties whose undertaking appears on a negotiable instrument are called accommodation parties.<sup>13</sup> This article addresses the special implications that result from the interface of Revised Article 3 and Regulation B because of actions taken by creditors in complying with the Act. The Act exempts from liability any act or omission by a creditor

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6. U.C.C. COMMITTEE UPDATE 12-13 (June 1995).

7. UNIFORM COMMERCIAL CODE CURRENT PAYMENT METHODS PROJECT PROGRESS REPORT 4 (ALI 1988); see also D. Fenton Adams, *Problems With the 1990 Revision of Articles 3 and 4 of the Uniform Commercial Code*, 15 U. ARK. LITTLE ROCK L.J. 665 (1993).

8. RESTATEMENT (THIRD) OF SURETYSHIP §§ 13-20 (Tentative Draft No. 1, 1992).

9. See generally RESTATEMENT (FIRST) OF SECURITY (1941).

10. U.C.C. § 3-606 (1989). See generally Neil B. Cohen & Sarah H. Jenkins, *Suretyship Issues Concerning Secured Lenders*, in ALI-ABA COURSE OF STUDY MATERIALS, THE EMERGED AND EMERGING NEW UNIFORM COMMERCIAL CODE (1993).

11. Only a few states have comprehensive suretyship statutes. See CAL. [CIV.] CODE §§ 2787-2855 (West 1993 & Supp 1996); LA. CIV. CODE ANN. arts. 3035-3070 (West 1994); N.D. CENT. CODE §§ 22-01-01 to 22-01-21, 22-03-01 to 22-03-15 (1991); OKLA. STAT. ANN. tit. 15, §§ 371-85 (West 1993); S.D. CODIFIED LAWS ANN. §§ 56-1-1 to 56-2-17 (1988).

12. See *infra* notes 77-91 and accompanying text for a discussion of the distinctions between suretyship principles under Revised Article 3 and the Restatement of Suretyship.

13. INSTRUMENTS SIGNED FOR ACCOMMODATION, U.C.C. § 3-419 (1990):

If an instrument is issued for value given for the benefit of a party to the instrument ("accommodated party") and another party to the instrument ("accommodation party") signs the instrument for the purpose of incurring liability on the instrument without being a direct beneficiary of the value given for the instrument, the instrument is signed by the accommodation party "for accommodation."

*Id.* § 3-419(a).

if done in good faith in conformity with any official rule, regulation or interpretation by the Federal Reserve Board or authorized official or employee.<sup>14</sup>

### I. REGULATION B: IMPERMISSIBLE CONDUCT

In the context of a guaranty on a negotiable instrument, two primary acts create potential liability and problems for creditors: requiring a spouse's signature and failing to release the guarantor upon renewal. Regulation B prohibits a creditor from requiring the signature of the spouse of any applicant who meets the creditor's standards of creditworthiness.<sup>15</sup> If an additional party's personal liability is necessary to support the extension of credit, a creditor may, as always, request a cosigner or guarantor. The creditor may not require the applicant's spouse to serve as the additional party.<sup>16</sup> The spouse may, however, voluntarily serve as the additional party.<sup>17</sup> At least one commentator suggests that such voluntary action should be well documented in writing.<sup>18</sup>

These prohibitions are inapplicable if the spousal signature is necessary or reasonably believed by the creditor to be necessary to enable the creditor to reach property used as a basis for the extension of unsecured or secured credit.<sup>19</sup> A creditor's reasonable belief should be supported by a thorough review of statutory and decisional law or attorney general's opinions. To otherwise require a spouse's signature violates the Act and gives an

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14. 15 U.S.C. § 1691e(e) (1991); Official Staff Interpretations, 12 C.F.R. pt. 202, supp. I, Introduction, para. 1 (1994).

15. Reg. B, 12 C.F.R. § 202.7(d) (1994).

16. *Id.* § 202.7(d)(5).

17. *United States v. Meadors*, 573 F.2d 950 (7th Cir. 1985) (ECOA not implicated because wife acted voluntarily).

18. See Kevin A. Palmer, *ECOA, Regulation B, and the Spousal Guaranty*, 110 *BANKING L.J.* 342, 350 (July-August 1993).

19. Reg. B, 12 C.F.R. § 202.7(d)(2)(3)(4) (1994); Reg. B, Official Staff Interpretations; 12 C.F.R. Pt. 202, supp. I, para. 7(d)(4) (1994); see, e.g., *Evans v. Centralfed Mortgage*, 815 F.2d 348 (5th Cir. 1987) (creditor did not violate ECOA by requiring husband's signature in the warranty deed and deed of trust in community property state when wife applied for loan to purchase non-residential real property); *McKenzie v. U.S. Home Corp.*, 704 F.2d 778 (5th Cir. 1983) (creditor's denial of loan subject to applicant's divorce becoming final or husband's signing of the deed of trust to insure valid lien on the property not a violation).

applicant a right to seek affirmative relief<sup>20</sup> including actual damages,<sup>21</sup> punitive damages,<sup>22</sup> and reasonable attorney's fees.<sup>23</sup>

At first blush, these principles may appear innocuous. The original narrow definition of "applicant" under former Regulation B excluded non-borrowers such as guarantors and their spouses and limited the right to seek affirmative relief to the borrower-applicant, often a corporate entity.<sup>24</sup> Furthermore, a married non-corporate borrower who received funds and enjoyed the benefit of credit was unlikely to complain. Revising Regulation B to increase the regulation's effectiveness in controlling and motivating creditor compliance, the Federal Reserve Board expanded the definition of "applicant" and clarified the scope of those included within the term "creditor."

Any person who requests or receives an extension of credit from the creditor, including one who is or may become contractually liable regarding an extension of credit, such as guarantors, sureties, indorsers, and accommodation parties, is now an applicant.<sup>25</sup> Each of these parties to an extension of credit, whether commercial<sup>26</sup> or consumer, is empowered under

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20. 15 U.S.C. § 1691e (1995).

21. Actual damages may include out-of-pocket monetary losses, injury to credit reputation, mental anguish, humiliation, or embarrassment. *Anderson v. United Fin. Co.*, 666 F.2d 1274, 1277 (9th Cir. 1982); *see, e.g.*, *Bhandari v. First Nat'l Bank*, 808 F.2d 1082 (5th Cir. 1987) (applicant awarded \$1.35 for postage, \$1000 for private, momentary and personal affront when creditor provided notice of denial of credit that failed to give a complete list of the reasons for adverse action).

22. Punitive damages are limited to an amount not greater than \$10,000 except in the case of a class action. The total recovery for punitive damages in a class action is the lesser of \$500,000 or one percent of the creditor's net worth. 15 U.S.C. § 1691e(b) (1995). Punitive damages may be awarded regardless of proof of actual damages. *See Fischl v. General Motors Acceptance Corp.*, 708 F.2d 143 (5th Cir. 1983); *Shuman v. Standard Oil Co.*, 453 F. Supp. 1150 (N.D. Cal. 1978) (award of punitive damages requires a threshold finding of a reckless disregard for the requirements of the law).

23. 15 U.S.C. § 1691e(d) (1995).

24. *See, e.g.*, *Comas v. Equibank*, No. 80-00288, 1989 WL 69857 (Bankr. W.D. Pa. 1989) (corporate borrower); *Douglas County Nat'l Bank v. Pfeiff*, 809 P.2d 1100 (1991) (individual borrower for business purposes).

25. Notes or other obligations issued or signed before the effective date of revised Regulation B are immune from attack by guarantors on the basis of an ECOA violation. *See Mayes v. Chrysler Credit Corp.*, 37 F.3d 9 (1st Cir. 1994); *Boatmen's First Nat'l Bank v. Koger*, 784 F. Supp. 815 (D. Kan. 1992); *Marine Am. State Bank v. Lincoln*, 433 N.W.2d 709 (Iowa 1988).

26. The 1985 revisions to Regulation B clarified that the Act and Regulation B

the Act to seek affirmative relief.<sup>27</sup> The expanded definition grants standing to all makers, indorsers, guarantors, and *their spouses*, greatly increasing the creditor's potential liability and the Regulation's sting if violated.

Moreover, this liability is not limited to the institution lending the funds. Any person who influences the credit decision, whether they are an assignee, subrogee, or potential purchaser of the instrument or paper, is by definition a creditor.<sup>28</sup> Under the revised Regulation B, the term "creditor" also includes a person who, in the ordinary course of business, regularly refers applicants or prospective applicants to creditors or selects or offers to select creditors to whom requests for credit may be made.<sup>29</sup> Those who make an initial assessment of an applicant's creditworthiness, set the standards for determining creditworthiness, or apply a financing institution's standards to a prospective applicant should also be deemed to be a "creditor" for the purposes of Regulation B. This broadened scope effectively reaches wrongful conduct at all levels of the credit decision. However, the wrongful conduct of one "creditor" or arranger in the transaction does not result in the liability of another "creditor" unless the other knew or had reasonable notice of the act, policy, or practice that constituted the violation before becoming involved in the credit transaction.<sup>30</sup>

Assuming the spousal guaranty is obtained without violating the statute, upon renewal of the borrower's obligation the creditor must determine whether the additional parties, guarantors or indorsers, are still warranted. If not, the additional parties must be released.<sup>31</sup> At least one court has concluded that the

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applied to business credit and the 1989 revisions to Regulation B eliminated prior exceptions for inquiries relating to marital status and credit reporting in business credit transactions. Equal Credit Opportunity; Revision of Regulation B; Official Staff Commentary, 50 Fed. Reg. 48018, 48019 (1985); Equal Credit Opportunity Business Credit, 54 Fed. Reg. 50482 (Dec. 7, 1989); Official Staff Interpretations, 12 C.F.R. 202, Supp. I, § 202.1, para. 2(g), 2(j) (1994).

27. Official Staff Interpretations, 12 C.F.R. pt. 202, Supp. I, § 202.1, para. 1 (1994).

28. Official Staff Interpretations, 12 C.F.R. pt. 202, Supp. I, § 202.2, para. 2(1) (1994).

29. 12 C.F.R. § 202.2(l).

30. *Id.*

31. Official Staff Interpretations, 12 C.F.R. pt. 202, Supp. I, para. 7(d)(5), ¶3 (1994).

Regulation imposes an affirmative duty on the creditor to re-evaluate the need to have a guarantor.<sup>32</sup> Failure to reassess a borrower's creditworthiness and the need for secondary parties is a violation of the Act.<sup>33</sup> However, in releasing a guarantor to comply with the Regulation, the creditor risks, under suretyship principles, the possibility of discharging other sureties, if any, and discharging all obligations on the first instrument.<sup>34</sup> Consequently, the creditor must not only be concerned with complying with the Regulation but must also consider the effects of his or her actions under the applicable negotiable instrument law including the suretyship principles.

#### A. *Enforcing the Statutory Rights—A Conundrum*

The potential penalties under Revised Regulation B provide the incentive needed to motivate creditor compliance with the Act. The broadly defined "applicant" and "creditor" terms extend the scope of the Regulation to achieve increased effectiveness in minimizing discriminatory conduct.<sup>35</sup> However, the applicable statute of limitation may render meaningless the relief granted by the Act. A two-year statute of limitations is applicable to any claim for affirmative relief<sup>36</sup> unless an agency that has responsibility for administrative enforcement commences an enforcement proceeding, or the attorney general commences an action within the applicable two year period.<sup>37</sup> Then, an applicant may commence a civil action within one year after the

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32. *Stern v. Espirito Santo Bank*, 791 F. Supp. 865 (S.D. Fla. 1992); see also Paul H. Schieber, *Spousal Signatures Revisited (There's Good News and Bad News)*, 47 CONSUMER FIN. L.Q. REP. 364 (1993) (because the facts in *Stern v. Espirito Santo Bank* did not show that husband's creditworthiness was re-evaluated, the author argues that the court required the re-evaluation of borrower's creditworthiness upon renewal).

33. Paul H. Schieber, *Attention Lenders: Re-evaluate Spousal Signature Policies and Procedures*, 5 LOY. CONSUMER L. REP. 68 (1993); *Stern*, 791 F. Supp. at 869 (citing 12 C.F.R. pt. 202, Supp. I, para. 7(d)(5) (Supp. I. 1992)).

34. See *infra* notes 77-91 and accompanying text.

35. See 50 Fed. Reg. 48018, 48019, Official Comments, para. 2 (Nov. 20, 1985).

36. 15 U.S.C. § 1691e(f) (1995).

37. *United States v. Blake*, 751 F. Supp. 951 (W.D. Okla. 1990) (FTCA five-year limitations period controlling when action based on ECOA violation commenced under FTCA).

commencement of either the agency proceeding or the attorney general's action.<sup>38</sup>

With the short statutory period, the primary concern for litigants is the accrual of the action. Courts addressing the issue have held that the action accrues on the date the creditor requires the spousal guaranty and not when the spouse is required to perform.<sup>39</sup> This view of the accrual of the spouse's cause of action is consistent with the general view that an action accrues when the wrongful act occurs or when the plaintiff can first maintain an action to a successful conclusion because all of the elements constituting the harm have occurred.<sup>40</sup>

Consequently, unless the maturity of the obligation is less than two years or the underlying obligation is accelerated, the right to assert the violation, affirmatively, may have lapsed for many spouses before discovery of the right after conferring with independent legal counsel. Many spouses who are otherwise entitled to relief may only become aware of such rights when pursued on his or her guaranty by the creditor after maturity upon default by the principal debtor. The 1973 amendments to the Act enlarged the statute of limitations from the previous one year period, one year being deemed too short for violations of anti-discrimination legislation, especially where violations were not readily ascertainable from the face of the contracts.<sup>41</sup> Congress assumed individual rights would be asserted in private actions commenced as a result of publicity surrounding agency actions after the agency developed and investigated the facts within the two year statutory period.<sup>42</sup> Under Congress' assumption, a private party had, in effect, a three-year statute of limitations.

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38. 15 U.S.C. § 1691e(f) (1995).

39. See *Farrell v. Bank of New Hampshire*, 929 F.2d 871 (1st Cir. 1991); *Riggs Nat'l Bank v. Webster*, 832 F. Supp. 147 (D. Md. 1993). *But see* *Pierce v. Citibank*, 856 F. Supp. 1451 (D. Ore. 1994) (applying a discovery rule for commencing of the statute of limitations when creditor fails to give notice of adverse action—canceling of credit card—as required by ECOA).

40. *Von Schrader v. Board of Comm'rs*, 103 P.2d 930 (Okla. 1940).

41. S. Rep. No. 94-589, 94th Cong., 2d Sess. (1976).

42. *Id.*



While this rationale does not justify judicial enlargement of the limitations period to three years, in light of the express statutory language, when the private action is commenced without the prior agency or attorney general action, the use of equitable tolling and estoppel principles are even more appropriate given Congress' assumption. Historically, statutes of limitations were subject to waiver, estoppel, or equitable tolling. These equitable principles should also be recognized in the context of spousal guaranties. Some of the equitable principles recognized under Title VII for the filing of charges<sup>43</sup> for employment discrimination provide a basis of analogy in the context of credit discrimination. As in the employment discrimination context, for example, if a spouse is reasonably unaware of facts<sup>44</sup> that constitute a violation of the Act, a tolling of the statute of limitations should be recognized by the court. Assume a creditor informs the applicant husband that wife's voluntary guaranty is necessary. If a husband, for example, requests his wife's voluntary guaranty without disclosing to her the creditor's prior request for her guaranty, the running of the statute should be tolled until the wife learned or should have learned of the fact of the creditor's request.

Additionally, if the creditor makes positive misrepresentations or disguises the facts<sup>45</sup> that constitute a violation, an estoppel to plead the statute of limitations as a defense should be recognized as within the broad equitable powers granted the courts under the Act.<sup>46</sup> If the creditor misrepresents the need for a spousal signature or offers a discount in points for joint applications, or deems an application a joint application as a matter of policy if joint assets are reflected in the application, the creditor should be estopped from asserting the statutory period until that time when the applicants are able to determine or gather facts of the ECOA violation.

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43. See generally MACK A. PLAYER, EMPLOYMENT DISCRIMINATION LAW § 5.73 (1987).

44. See, e.g., *Wolfolk v. Rivera*, 729 F.2d 1114, 1117 (7th Cir. 1984).

45. See *Meyer v. Riegel Prod. Corp.*, 720 F.2d 303 (3d Cir. 1983); see also *Bailey v. Glover*, 88 U.S. 342 (1874) (statute of limitations tolled until the plaintiff discovers the cause of action, provided the plaintiff was not negligent and the defendant actively concealed the violation).

46. 15 U.S.C. § 1691e(c) (1995).

Given the short statute of limitations, several guarantors have sought to raise the ECOA violation defensively or as a counterclaim in recoupment.<sup>47</sup> Asserting the statutory violation as an illegality defense, the guarantors argue the violation rendered their obligation on the guaranty void and unenforceable.<sup>48</sup> Courts are divided on whether the violation is a permissible defense.<sup>49</sup>

### B. *Illegality as a Defense to the Guarantor's Liability*

In general, a contract whose formation or performance is illegal is void and unenforceable.<sup>50</sup> Not only is enforcement of the contract denied but restitution for any benefits conferred under the contract may also be foreclosed.<sup>51</sup> A court, in some instances, may raise the illegality on its own motion.<sup>52</sup> Currently, courts are divided on whether a violation of the Act may be asserted as an effective illegality defense to the guarantor's liability.<sup>53</sup> Some rejecting the defense permit the violation to

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47. Characterizing an ECOA violation as a compulsory counterclaim may, more often than not, preserve the guarantor's ability to limit its liability on the obligation. See Richard J. Wirth & Jonathan B. Alter, *Spousal Defenses Based in Equal Credit Laws*, 99 COM. L.J. 93, 101 (1994). But see, *Riggs Nat'l Bank v. Webster*, 832 F. Supp. 147 (D. Md. 1993) (two-year statute of limitations is applicable to an ECOA violation asserted in recoupment).

48. See *Integra Bank v. Freeman*, 839 F. Supp. 326 (E.D. Pa. 1993); *CMF Virginia Land v. Brinson*, 806 F. Supp. 90 (E.D. Va. 1992).

49. See *infra* note 53.

50. *Sirkin v. Fourteenth St. Store*, 108 N.Y.S. 830 (App. Div. 1908).

51. RESTATEMENT OF RESTITUTION § 140. See generally *Takeuchi v. Schmuck*, 276 P. 345 (Ca. 1929) (restitution of deposit for land purchase in violation of Alien Land Law denied); *Chapman v. Haley*, 80 S.W. 190 (Ky. 1904) (restitution denied to participant in scheme to purchase counterfeit money). Although restitution is at law, the action is equitable in nature and the illegality operates as "unclean hands" to prevent restitution. *West Los Angeles Inst. for Cancer Research v. Mayer*, 366 F.2d 220 (9th Cir. 1966) (whether plaintiff's wrongful conduct (unclean hands) bars equitable relief of rescission must be based upon an examination of all circumstances and a balancing of relevant factors including the relative strength of the policy infringed by the plaintiff); *Myers v. Smith*, 208 N.W.2d 919 (Iowa 1973) (prayer for specific performance denied where contract sued on was tainted with scheme to evade the law or bilk third parties). Edward N. Fadeley, *The Clean-Hands Doctrine in Oregon*, 37 OR. L. REV. 160, 186-87 (1958). John W. Wade, *Restitution of Benefits Acquired Through Illegal Transactions*, 95 U. PA. L. REV. 261 (1947).

52. *Waring v. Lobdell*, 387 P.2d 979 (Wash. 1964); *Williams v. Burrus*, 581 P.2d 164 (Wash. App. 1978).

53. The guaranty was held void and unenforceable in *Integra Bank v. Freeman*, 839 F. Supp. 326 (E.D. Pa. 1993); *Shammas v. Merchants Nat'l Bank*, No. Civ. 90-

be raised by way of counterclaim in recoupment.<sup>54</sup> The Act does not, in express terms, prohibit the enforcement of agreements made in violation of its provisions. Courts rejecting the illegality defense do so because of the absence of language authorizing this result in the statute.<sup>55</sup> This conclusion is contrary to persuasive authority on illegal contracts or agreements.

The Restatement of Contracts recognizes that legislation infrequently provides that a contract made in violation of its provisions is unenforceable.<sup>56</sup> The conclusion that a term or agreement is unenforceable must be reached by the court from its own perception of the need to protect public welfare or its own perception of the goals of the legislation despite the absence of explicit language.<sup>57</sup> Factors to be weighed against enforcement include: the strength of the policy as manifested by legislation; the likelihood that a refusal to enforce will further that policy; the seriousness of any misconduct; the extent to which the conduct was deliberate; and the directness of the connection between the misconduct and the term. Conversely, factors to be weighed in the interest of enforcing the obligation are: the parties' justified expectations; any forfeiture that results if enforcement is denied as well as any resulting enrichment; and, any special public interest in enforcing the term.

In the context of a Regulation B violation, application of the relevant factors tips the scale in favor of holding the guaranty

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1221-N, 1990 WL 354452 (D. Mass. Nov. 9, 1990) (dictum); *FDIC v. Allen*, No. Civ. 88-361-W, 1988 WL 361044 (W.D. Okla. Nov. 3, 1988); *Eure v. Jefferson Nat'l Bank*, 448 S.E.2d 417 (Va. 1994). However, several courts have reached the opposite result. See *CMF Virginia Land v. Brinson*, 806 F. Supp. 90 (E.D. Va. 1992); *Diamond v. Union Bank & Trust*, 776 F. Supp. 542 (N.D. Okla. 1991) (signature on note); *Citibank v. Norkin*, No. 12994/92, 1993 WL 590130 (N.Y. Sup. Ct. Nov. 24, 1993).

54. See *CMF Virginia Land v. Brinson*, 806 F. Supp. 90 (E.D. Va. 1992) (ECOA violation a compulsory counterclaim entitling the victim to recoupment damages). When the violation is asserted as a claim in recoupment, courts are divided on whether the two-year statute of limitations is applicable. A recoupment claim is effective until the statute of limitations runs on the creditor's cause of action. See *Integra Bank v. Freeman*, 839 F. Supp. 326 (E.D. Pa. 1993); *Marine Am. State Bank v. Lincoln*, 433 N.W.2d 709 (Iowa 1988); *FDIC v. Notis*, 602 A.2d 1164 (Me. 1992). *But see Riggs Nat'l Bank v. Webster*, 832 F. Supp. 147 (D. Md. 1993) (two-year statute of limitations is applicable to an ECOA violation asserted in recoupment).

55. *Riggs Nat'l Bank v. Lynch*, 829 F. Supp. 163 (E.D. Va. 1993); *Citibank v. Norkin*, 1993 WL 590130 (N.Y. Sup. Ct. Nov. 24, 1993).

56. RESTATEMENT (SECOND) OF CONTRACTS § 178 cmt. b (1979).

57. *Id.* § 179.

void and unenforceable. The Act and its Regulation represent a strong public policy against discriminatory conduct or conduct that minimizes competition among creditors. Refusal to enforce a guaranty acquired in violation of the Act will implement the underlying policy concern reflected in the Act and serve as a disincentive for conduct that violates the Act. Requiring a spousal guaranty when the applicant meets the creditor's standards of creditworthiness or needs the credit enhancing presence of a guarantor is a direct violation of the express terms of the statute and its regulation. The creditor's conduct is deliberate rather than inadvertent. Furthermore, in the absence of a voluntary guaranty by the spouse, the creditor's conduct is the sole cause of the guaranty.

The countervailing considerations do not justify enforcing the guaranty. Although the spouse reasonably expects to perform his or her undertaking at the time of the engagement, the creditor's expectations of such performance is unjustified given the statute's prohibition. While the creditor may forfeit the opportunity to enforce a collateral promise of performance, the guarantor is not enriched. As a guarantor on a negotiable instrument, an accommodation party is one who does not receive a direct benefit from the loan transaction.<sup>58</sup> The creditor's forfeiture on the collateral undertaking is offset by his or her ability to enforce the borrower's obligation. The creditor's deliberate violation of the statutory mandate negates any public interest in enforcing the guaranty obtained in violation of the Act. Likewise, refusing to enforce the guaranty gives effect to the broad equitable and declaratory powers conferred upon the courts by the Act.

However, while the illegality defense should be available to the guarantor, the defense should not be extended to the underlying obligation of the borrower.<sup>59</sup> If the borrower (husband) suffers actual damages as a result of the violation, recourse is available under the statute. If actual damages are suffered, these should be recovered along with attorneys' fees. In the

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58. U.C.C. § 3-419(a) (1990).

59. A court may sever or limit the effect of an illegality to a portion of the contract and enforce the balance. *See, e.g.*, *Hemmen v. State*, 710 P.2d 1001 (Alaska 1985); *Brokaw v. Brokaw*, 398 N.E.2d 1385 (Ind. App. 1980). *But see In re Marilyn v. Remington*, 19 B.R. 718, 721 (Bankr. D. Colo. 1982).

absence of actual damages, punitive damages and attorneys' fees should be permitted for the husband if the creditor's conduct warrants such a result.<sup>60</sup> In the absence of actual harm to the borrower, if both the husband and wife are permitted to assert the illegality defense, the creditor who has extended value cannot recover on the borrower's contract and cannot recover in restitution the funds loaned.<sup>61</sup> This results in a substantial forfeiture for the creditor who has given value and the unjust enrichment of the borrower. Limiting the scope of the illegality defense balances the equities between the parties, discourages conduct by creditors that is inconsistent with the Act's underlying policy concern for the extension of credit without regard to marital status, and does not result in a substantial forfeiture by the creditor.

### C. *Illegality Defense and Negotiable Instruments*

Assuming the engagement of the guaranteeing spouse—the accommodation party—appears on a negotiable instrument, recognition of an ECOA violation as an effective illegality defense may result in a real defense, a defense that is effective against a holder in due course.<sup>62</sup> If under the particular jurisdiction's law the illegality of a transaction nullifies the obligation of the obligor, a subsequent purchaser who gives the wrongdoing creditor value in good faith for the instrument without notice of the ECOA violation takes subject to the illegality defense if successfully raised.<sup>63</sup> Consequently, a creditor cannot remove the taint of the ECOA violation from the

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60. In *Marine American State Bank v. Lincoln*, 433 N.W.2d 709 (Iowa 1988), the wife did not have standing to assert the violation under former Regulation B and the husband was the aggrieved applicant. No actual damages were established but the husband recovered \$5000 in recoupment in punitive damages and \$5000 in attorneys' fees.

61. See *supra* note 50 and accompanying text.

62. Holder in due course, a phrase coined by JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 14-1 (3d ed. 1988), places one in the position of a superplaintiff who takes free of personal defenses but is subject to real defenses.

63. DEFENSES AND CLAIMS IN RECOUPMENT, U.C.C. § 3-305 (1990). Subsection (a) states that "except as stated in subsection (b), the right to enforce the obligation of a party to pay an instrument is subject to the following: (1) . . . (ii) duress, lack of legal capacity, or illegality of the transaction which, under other law, nullifies the obligation of the obligor. . . ." *Id.*

guarantor's engagement by transferring the negotiable paper to an innocent third party.

Furthermore, principles of *jus tertii* should limit the availability of the defense to other applicants.<sup>64</sup> Section 3-305 prohibits the obligor on an instrument from asserting against the person entitled to enforce the instrument a defense of another person unless the other person is joined in the action and personally asserts the defense.<sup>65</sup> Thus, the borrower-applicant cannot assert the guarantor's illegality defense thereby preventing the substantial forfeiture that would result if a violation of the Act as to a spouse was extended to another party in the absence of actual damages.<sup>66</sup>

However, the principle of *jus tertii* is inapplicable to an accommodation party who desires to assert a defense available to the accommodated party. Excluding the real defenses of discharge in insolvency, infancy, and lack of capacity, Revised Article 3 expressly authorizes the use of an accommodated party's defense by the accommodation party.<sup>67</sup> The limited exclusion of the insolvency, infancy, and lack of capacity defenses is justified by the very nature of the accommodation party's en-

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64. See, e.g., *Warren Fin., Inc. v. Barnett Bank*, 552 So.2d 194 (Fla. 1989); *Thompson v. Wright*, 187 S.E. 311 (Ga. Ct. App. 1936).

65. U.C.C. § 3-305(c) (1990):

Except as stated in subsection (d), in an action to enforce the obligation of a party to pay the instrument, the obligor may not assert against the person entitled to enforce the instrument a defense, claim in recoupment, or claim to the instrument (section 3-306) of another person, but the other person's claim to the instrument may be asserted by the obligor if the other person is joined in the action and personally asserts the claim against the person entitled to enforce the instrument. An obligor is not obliged to pay the instrument if the person seeking enforcement of the instrument does not have rights of a holder in due course and the obligor proves that the instrument is a lost or stolen instrument.

*Id.*

66. See *supra* note 59 and accompanying text for a discussion on limiting the scope of the illegality defense.

67. U.C.C. § 3-305(d) (1990):

In an action to enforce the obligation of an accommodation party to pay an instrument, the accommodation party may assert against the person entitled to enforce the instrument any defense or claim in recoupment under subsection (a) that the accommodated party could assert against the person entitled to enforce the instrument, except the defenses of discharge in insolvency proceedings, infancy, and lack of legal capacity.

*Id.*

gagement. The goal of the engagement is to protect the person entitled to enforce the instrument, the creditor or its transferee, from the risks of the principal obligor's inability or unwillingness to perform. Permitting the accommodation party to raise these defenses would render the accommodation party's engagement valueless.<sup>68</sup> The accommodation party assumes the risk of these real defenses.

However, permitting the accommodation party to raise other defenses held by the accommodated party prevents devaluation of the accommodated party's defenses, avoids a multiplicity of actions, and discourages conduct by creditors that increase the risk of the accommodated party's non-performance.<sup>69</sup> Furthermore, no *jus tertii* problem results.<sup>70</sup> The accommodated party's defense is being raised to the duty owed by the accommodated party.<sup>71</sup> The accommodation party's duty is co-extensive with that of the accommodated party's duty. Consequently, although the accommodated party may not assert the accommodation party's rights under the Act, the accommodation party should be permitted to assert any rights available to the accommodated party by way of defense or recoupment under the Act or its regulation.

## II. PERMISSIBLE CONDUCT: RENEWAL OF OBLIGATION

Regulation B and the Official Staff Interpretations provide a safe harbor for creditors who comply in good faith with the terms of the Interpretations. Compliance negates the possibility of a violation of the Act. However, two recommended courses of action, while not violative of the Act, may result in loss or harm to the creditor's interest under other law. First, the Regu-

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68. See RESTATEMENT (THIRD) OF SURETYSHIP § 30 cmt. b (Tentative Draft No. 2, 1993); Neil B. Cohen, *Suretyship Principles in the New Article 3: Clarifications and Substantive Changes*, 42 ALA. L. REV. 595, 605 (1991).

69. RESTATEMENT OF SECURITY § 126 cmt. a (1941).

70. See *Lewis & Queen v. N.M. Ball Sons*, 308 P.2d 713, 722 (Ca. 1957); *Gamel v. Hynds*, 125 P. 1115 (Okla. 1912) (stating the general rule of *jus tertii* but reversing and remanding for a determination of whether the makers were accommodation parties and thereby exempt from the rule); RESTATEMENT OF SECURITY § 117 cmt. d (1941).

71. See PERMANENT EDITORIAL BOARD COMMENTARY No. 11, FINAL DRAFT (1994) (amendment to U.C.C. § 3-605 cmt. 3).

lation has been interpreted to require the release of guarantors whose engagements become unnecessary because of a change in the borrower's creditworthiness. This action creates possible suretyship defenses that may be raised by remaining sureties. Second, the Staff Interpretations suggest that a legend may be used on an integrated document to reflect that a spouse's limited undertaking is for the purpose of granting an interest in jointly held property. Of concern for creditors desiring the favorable rules of Revised Article 3 is whether such a legend will render the writing not negotiable.<sup>72</sup>

#### A. *Release of Unnecessary Guarantors Upon Renewal*

At maturity of the borrower's obligation, the borrower may seek a renewal of the obligation to postpone payment to some later definite time. Upon renewal of the borrower's obligation, if the creditor re-evaluates the borrower's creditworthiness, the creditor must determine whether additional parties, guarantors or indorsers, are still warranted and, if not, release the additional parties.<sup>73</sup> The court in *Stern v. Espirito Santos Bank of Florida*,<sup>74</sup> concluded that the Act imposed an affirmative obligation upon the creditor to re-evaluate the need for a guarantor when the credit obligation was renewed.<sup>75</sup> Should the creditor determine that the borrower's creditworthiness now meets his or her standards, one or more accommodation parties must be released. At early common law, such a release or other change, no matter how slight, in the original obligation among the parties discharged any other party having a right of recourse against the party released.<sup>76</sup> At early common law and under the Restatement of Security,<sup>77</sup> in the absence of an agreement

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72. While parties may by agreement appropriate Article 3 rules to govern their transaction and any transferee who takes with notice of these contract terms, a writing that fails to meet the requirements of negotiability cannot by agreement be deemed negotiable. U.C.C. § 3-104 cmt. 2 (1990).

73. Official Staff Interpretations, 12 C.F.R. pt. 202, Supp. I, para. 7(d)(5), ¶3 (1994).

74. 791 F. Supp. 865 (S.D. Fla. 1992).

75. See Schieber, *supra* note 32. Because the facts did not show that the husband's creditworthiness was re-evaluated, the author argues that the court requires the re-evaluation of the borrower's creditworthiness upon renewal. *Id.* at 365.

76. See generally William H. Loyd, *The Surety*, 66 U. PA. L. REV. 40, 53 (1917).

77. RESTATEMENT OF SECURITY § 146 (1941).



or unequal equities that establish a subsuretyship relationship, multiple sureties for the same obligation were deemed to be co-sureties, sharing the loss caused by the default of the principal debtor and had a right of contribution among themselves.<sup>78</sup> Thus, if the multiple sureties were co-sureties and one was released, the remaining surety would have had a right of recourse against the one discharged and would, therefore, be discharged from its obligation.<sup>79</sup>

A subsuretyship relationship exists between multiple sureties if they agree that as between themselves, one rather than the other should perform or bear the cost of performance.<sup>80</sup> If the relationship was one of subsuretyship and the surety with the obligation of performance (principal surety) was released, the remaining surety (subsurety), having a right of reimbursement from the released surety, would be discharged. However, if the subsurety was released, the principal surety would not be discharged because the principal surety would not have a right of recourse against the subsurety.

Revised Article 3 and former Article 3 vary this outcome at early common law but in substantially different ways. For obligations of guarantors appearing in a guaranty separate from the negotiable instrument, the Restatement of Suretyship approach is also distinguishable. A creditor releasing an accommodation party upon renewal of the obligation in a jurisdiction that has not adopted Revised Article 3 must expressly reserve his or her rights against any remaining accommodation parties or obtain their consent to the release to prevent the discharge of remaining accommodation parties to the extent of the release granted by the creditor.<sup>81</sup> The express reservation preserves the creditor's rights against remaining accommodation parties and the remaining accommodation parties' rights against the released accommodation party.<sup>82</sup>

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78. RESTATEMENT OF SECURITY § 144 (1941).

79. RESTATEMENT OF SECURITY §§ 122, 135, & 145 cmt. c (1941).

80. RESTATEMENT OF SECURITY § 145 (1941); RESTATEMENT (THIRD) OF SURETYSHIP § 47 (Tentative Draft No. 3, 1994).

81. U.C.C. § 3-606(1)(a) (1989).

82. *Id.*

Similarly, under the Restatement of Suretyship,<sup>83</sup> without preservation of rights by language or circumstances, a creditor discharges a secondary obligor (surety) to the extent of loss suffered by the secondary obligor upon release of any other secondary obligor rather than the extent of release as permitted under former Article 3. This is an important substantive change for professional sureties given the allocation of the burden of persuasion under the Restatement of Suretyship.<sup>84</sup> Professional secondary obligors (sureties) are allocated the burden of persuasion as to the amount of loss incurred from the creditor's release of any party against whom the secondary obligor (surety) had a right of recourse.<sup>85</sup>

Under Revised Article 3, release of an obligation of any party to the instrument does not discharge the obligation of any party having a right of recourse against the released party.<sup>86</sup> The comments to Revised Article 3 initially abrogated the doctrine of reservation of rights,<sup>87</sup> but under the amended commentary the reservation of rights happens "automatically."<sup>88</sup> Furthermore, the revised article does not impose an obligation of obtaining the consent of the other accommodation parties. Consequently, creditors in jurisdictions that have adopted Revised Article 3 are afforded the greatest ease in complying with their duty to release unnecessary guarantors upon renewal, without apprehension of inadvertently discharging another accommodation party. To illustrate, consider the following facts:

John and Ron are shareholders of Corporation, a newly formed business entity. Corporation desires loan funds to obtain a necessary piece of equipment. Lender agrees to make the loan if John and Ron will sign the note as accommodation makers along with two additional accommodation parties. Mary, John's wife, and Paula, Ron's wife, both

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83. RESTATEMENT (THIRD) OF SURETYSHIP § 35 (Tentative Draft No. 2, 1993, as modified by Council Draft No. 4, 1994); RESTATEMENT (THIRD) OF SURETYSHIP § 48 (Tentative Draft No. 3, 1994).

84. RESTATEMENT (THIRD) OF SURETYSHIP § 43 (Tentative Draft No. 2, 1993).

85. *Id.*

86. U.C.C. § 3-605 (1990).

87. U.C.C. § 3-605 cmt. 3 (1990). *But see*, PERMANENT EDITORIAL BOARD COMMENTARY No. 11.

88. U.C.C. § 3-605(b) cmt. 3 (1990); PERMANENT EDITORIAL BOARD COMMENTARY No. 11, FINAL DRAFT amendment to U.C.C. § 3-605 cmt. 3 (1994); Cohen & Jenkins, *supra* note 10.

voluntarily agree to serve as accommodation makers. Six months later, Corporation's successes are less than predicted. Lender, aware of the Corporation's poor cash position, its continued sluggish revenues, and unlikely short term turnaround, agrees with John and Ron not to exercise its rights under the note to accelerate payment for the presence of an additional accommodation party. Ron's long time golfing partner and successful surgeon, Stanley, signs as an accommodation indorser. At maturity, the Corporation desires to renew the note. Corporation's cash position and revenues have improved. Under Lender's standards of creditworthiness, Mary's and Paula's engagements are unnecessary given Stanley's engagement. Attempting to comply with the Act, Lender releases both Mary and Paula.

Under Section 3-116 of Revised Article 3, Ron, John, Mary, and Paula are parties with the same liability if the drafters intended in using the phrase "same liability" to limit the concept to the type of engagement made. "Same liability" might reasonably include consideration of the facts and circumstances existing at the time an engagement is made in order to distinguish co-sureties and subsureties.<sup>89</sup> If a broader definition is intended, "same liability" entails more than the kind of engagement made. Assuming the drafters intended the more limited scope of "same liability," Ron, John, Mary, and Paula have a right of contribution from one another and are deemed co-sureties.<sup>90</sup> Stanley, however, does not have the "same liability" since he has signed as an indorser. Consequently, as an indorser, Stanley has a right of recourse against Mary and Paula for indemnification.<sup>91</sup> Under the Restatement of Suretyship, Stanley would be deemed to be a subsurety even if he had signed as an accommodation maker given the timing of his engagement, the relationship among the four other accommodation parties, Stanley's knowledge of the wives' prior engagements, and his reasonable belief that as between himself and the other accommodation makers, they rather than he ought to pay.<sup>92</sup> Howev-

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89. RESTATEMENT (THIRD) OF SURETYSHIP § 47 cmts. g-h (Tentative Draft No. 3, 1994).

90. U.C.C. § 3-116 cmt. 1 (1990).

91. U.C.C. §§ 3-412, 3-419(b) (1990).

92. RESTATEMENT (THIRD) OF SURETYSHIP § 47 cmts. g-h (Tentative Draft No. 3, 1994).

er, if Revised Article 3 is the applicable body of law, Stanley is not discharged by the release of the wives from their obligation to pay, even if he suffers loss as a result of the release.

Under former Article 3, Stanley, Ron, and John are discharged to the extent of the release and under the Restatement of Suretyship, they are discharged to the extent of loss suffered by Mary's and Paula's release unless, under both provisions, the remaining accommodation parties consented to the releases or Lender preserved its rights against the two women.

### B. *Renewal and the Underlying Obligation*

At maturity, if the obligation is renewed and one or more guarantors are released, are the obligations of all parties to the first instrument discharged, especially those who were parties to the first instrument who are not also parties to the second? In the absence of an agreement on the effect of the second instrument, the obligations represented in the first note are suspended and are not discharged.<sup>93</sup> The agreement among the parties is determined by all the facts and circumstances<sup>94</sup> such as whether the creditor knows that one party is unwilling to renew the obligation; fraudulent conduct by a party inducing the surrender of the original note; the creditor's handling of the first note—was the note marked "paid," torn, or destroyed with the intent to discharge the obligations therein; or was the first instrument surrendered.<sup>95</sup> If the creditor re-evaluates and de-

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93. U.C.C. § 3-310(b) (1990).

94. DISCHARGE AND EFFECT OF DISCHARGE, U.C.C. § 3-601(a) (1990). ("The obligation of a party to pay the instrument is discharged as stated in this Article or by an *act or agreement* with the party which would discharge an obligation to pay money under a simple contract.") (emphasis added). DISCHARGE BY CANCELLATION OR RENUNCIATION, U.C.C. § 3-604(a) (1990) states:

A person entitled to enforce an instrument, with or without consideration, may discharge the obligation of a party to pay the instrument (i) by an intentional *voluntary act*, such as surrender of the instrument to the party, destruction, mutilation, or cancellation of the instrument, cancellation or striking out of the party's signature, or the addition of words to the instrument indicating discharge, or (ii) by agreeing not to sue or otherwise renouncing rights against the party by a signed writing.

(emphasis added).

95. See, e.g., *Security Pac. Fin. Corp. v. Grove*, 73 B.R. 590 (Bankr. Minn. 1987) (unintentional cancellation induced by fraud); *Cipra v. Seeger*, 529 P.2d 130 (Kan. 1974) (circumstances at time of renewal indicated an intent to discharge the first

termines that a spouse's accommodation is no longer necessary for the renewal note, an agreement to discharge both the spouse and the first note should be found in the absence of contrary facts. If the discharge of the original note is not established, the obligation reflected by the first note remains suspended until the second note is dishonored or paid.<sup>96</sup> Upon dishonor, the creditor may enforce either the first or the second note.<sup>97</sup> If the first instrument is discharged, no right of recovery remains on the instrument upon dishonor of the second.<sup>98</sup>

Because renewal of a note is equivalent to an extension in time, a creditor must determine under the applicable suretyship rule whether a renewal will discharge any accommodation party who does not consent to the extension. Under section 3-605(c), if the accommodation party proves that an extension in time for payment caused loss with respect to its right of recourse, the extension discharges the accommodation party to the extent of the loss proven. Under former Article 3, the analysis of the effect of an extension in time is identical to that for determining if a release discharges an accommodation party with a right of recourse under former Article 3.<sup>99</sup>

### C. *Renewal and the Statute of Limitations*

Finally, the effect of the renewal of the obligation on the statute of limitations must be considered. Does the statute of limitations for the ECOA violation on the original note "revive" upon renewal of the obligation and issuance of a second note? The answer should be no. Regulation B defines "credit" as a right granted to an applicant to defer the payment of a debt.<sup>100</sup> The granting of credit in any form including "refinancing or other renewal of credit"<sup>101</sup> is an extension of credit. Thus, the renewal of an obligation is a separate granting of credit covered by Regulation B. Requiring a spousal signature

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note); *American Cement Corp. v. Century Transit Mix, Inc.*, 3 U.C.C. Rep. Serv. (Callaghan) 424 (N.Y. Sup. Ct. 1966).

96. U.C.C. § 3-310(b)(2) (1990).

97. U.C.C. § 3-310(b)(3) (1990).

98. U.C.C. § 3-604(a) (1990).

99. *See supra* notes 80-84 and accompanying text.

100. Reg. B, 12 C.F.R. § 202.2(j) (1994).

101. *Id.* § 202.2 (q).

on a renewal obligation results in a second violation of ECOA and the commencing of a new two year period on the second violation.<sup>102</sup> The statute of limitations for the first violation is not revived.

D. *Use of Legend on an Integrated Writing and Negotiability*

Requiring a spousal's signature when the applicant meets the creditor's reasonable standards of creditworthiness or when the application needs the enhancing presence of a guarantor violates the Act. However, a creditor may require a spousal signature to an instrument or other documents if under the applicable state law the signature is necessary or reasonably believed by the creditor to be necessary to enable the creditor to reach the property used as a basis for the extension of unsecured or secured credit.<sup>103</sup> The Official Staff Interpretations further provide that a spouse cannot be required to sign an integrated agreement that combines a note and the security agreement but could be asked to sign an integrated instrument that contains a legend next to the spouse's signature which limits the effect of the spouse's signature to the granting of a security interest in the collateral without liability on the instrument.<sup>104</sup> Of concern is whether, in a good faith attempt to comply with the Interpretations, a creditor will destroy the negotiability of the note by including such a legend and, thereby, negate the applicability of Revised Article 3 to the obligation.<sup>105</sup>

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102. See *Silverman v. Eastrich Multiple Investor Fund*, 857 F. Supp. 447, 453 (E.D. Pa. 1994) (distinguishing a reorganization plan in bankruptcy from a creditor's renewal in the ordinary course of business).

103. Official Staff Interpretations, 12 C.F.R. pt. 202, Supp. I § 202.7, para. 7(d)(4), ¶3 (1994).

104. *Id.*

105. See, e.g., *All Lease Co., Inc. v. Bowen*, 20 U.C.C. Rep. Serv. (Callaghan) 790 (Md. Cir. Ct. 1975) (writing containing maker's promise to insure collateral and to obtain seller's consent to transfer of collateral not negotiable); *Woodworth v. The Richmond Indiana Venture*, 13 U.C.C. Rep. Serv. 2d 1149 (Ohio Com. Pl. 1990) (writing not negotiable because of provision resulting in a forfeiture of partnership interest and payments in the event of default).

Revised Article 3 is only applicable to written promises<sup>106</sup> or orders<sup>107</sup> to pay that satisfy the requirements of section 3-104(a).<sup>108</sup> Of importance, here, is the limitation imposed by section 3-104(a) on the inclusion of any "undertaking or instruction" beyond the unconditional promise to pay a fixed sum of money. Although Revised Article 3 authorizes the inclusion of an undertaking to give, maintain, or protect collateral for securing the payment of the note or other obligations,<sup>109</sup> the section does not expressly authorize including the granting or creating of a security interest in collateral. However, comment 1 to section 3-104 provides that the intent of the revised article is to maintain the same goals and meanings recognized under former Article 3 for the exceptions on promises regarding collateral. Comment 1 to section 3-112 of former Article 3 states that cross collateral provisions, a provision securing obligations not reflected in the note,<sup>110</sup> do not destroy negotiability. Such statements do not minimize the certainty of the obligation undertaken by the maker.<sup>111</sup> Consequently, the creditor's use of

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106. U.C.C. § 3-103(a)(9) (1990). "Promise" means a written undertaking to pay money signed by the person undertaking to pay. An acknowledgment of an obligation by the obligor is not a promise unless the obligor also undertakes to pay the obligation. *Id.*

107. U.C.C. § 3-103(a)(6) (1990). "Order" means a written instruction to pay money signed by the person giving the instruction. *Id.*

108. NEGOTIABLE INSTRUMENT, U.C.C. § 3-104 (1990).

(a) Except as provided in subsections (c) and (d), "negotiable instrument" means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it:

(1) is payable to bearer or to order at the time it is issued or first comes into possession of a holder;

(2) is payable on demand or at a definite time; and

(3) does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money, but the promise or order may contain (i) an undertaking or power to give, maintain, or protect collateral to secure payment, (ii) an authorization or power to the holder to confess judgment or realize on or dispose of collateral, or (iii) a waiver of the benefit of any law intended for the advantage or protection of an obligor.

*Id.*

109. U.C.C. § 3-104 cmt. 1 (1990).

110. U.C.C. § 3-112 cmt. 1 (1989); THOMAS D. CRANDALL, ET AL., UNIFORM COMMERCIAL CODE § 14.10.2 (1993).

111. FREDERICK M. HART & WILLIAM F. WILLIER, COMMERCIAL PAPER § 2.10[1][b], at 2-100 & n.9 (1995).

an integrated agreement containing the note and the granting of a security interest to secure the note being issued should not destroy negotiability.

Of most importance, the restrictions of section 3-104(a) limiting the kinds of promises or undertaking are only imposed on the person promising to pay, the maker, or ordering payment, the drawer.<sup>112</sup> Undertakings otherwise prohibited by the maker when made by a spouse who is not a maker of the note do not destroy negotiability. Hence, the use of a legend limiting the spouse's undertaking to the granting of a security interest should not destroy negotiability.

### III. CONCLUSION

The goals of the Act and its revised regulation are to promote the availability of credit without regard to marital status and to prohibit practices that discriminate on the basis of marital status. To implement these goals, a guarantor's engagement obtained in violation of the Act and Regulation B should be subject to the defense of illegality. However, to avoid a substantial forfeiture by the wrongdoing creditor, the scope of the illegality defense should not be extended to the borrower's engagement. Only if actual damages are sustained by the borrower or punitive damages are warranted as a result of obtaining the guarantor's engagement in violation of the Act should the borrower's liability be limited or damages be otherwise recovered. However, should a violation occur when the borrower's engagement is obtained, suretyship law authorizes the guarantor to employ its borrower's defenses. No exception to this rule should be recognized in the context of an ECOA violation.

Because Revised Article 3 contains suretyship rules more favorable to creditors' interests than those of the Restatement of Suretyship, the common law, former Article 3, and other

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112. U.C.C. § 3-104(a)(3)(1990) "does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money. . . ." (emphasis added). See *Universal C.I.T. Credit Corp. v. Ingel*, 196 N.E.2d 847 (Mass. 1964) (promise by holder to obtain insurance does not destroy negotiability).



state suretyship statutes, creditors may request guarantors of credit to make their guarantees on the principal debtor's promissory note rather than in a separate document. Revised Article 3 will facilitate a creditor's compliance with the Official Staff Interpretations of Regulation B when a renewal of the borrower's obligation is contemplated without placing the creditor at risk under the revised article's suretyship principles. Under former Article 3 and the Restatement of Suretyship, care must be taken to comply with the preservation of rights rules to avoid discharging any remaining surety upon renewal.