

BILLS OF EXCHANGE UNDER THE SECURITIES LAWS:
MACANDREWS & FORBES CO. v. AMERICAN BARMAG CORP.

The facts of the case indicated a conventional commercial transaction: plaintiff, a textile manufacturer, had purchased certain machinery that proved to perform disappointingly. That claims were brought on theories of common law fraud and of breach of both expressed and implied warranties was hardly unusual. But in invoking the federal securities laws,¹ on the theory that the bills of exchange² serving as partial payment for the machinery constituted securities, plaintiff urged a novel, if not far-fetched, position. Still more surprisingly, the court in *MacAndrews & Forbes Co. v. American Barmag Corp.*³ accepted that theory in denying defendants'⁴ motion to strike the securities law claims.

MacAndrews, this Comment will argue, was erroneously decided on the narrow issue whether bills of exchange employed as payment media in a commercial transaction are embraced by the federal securities laws; if followed by other courts, the precedent would bring about substantial changes in the conduct⁵ and outcome⁶ of commercial litiga-

¹ The complaint alleged violations of § 17 of the Securities Act of 1933, 15 U.S.C. § 77q (1970) (making unlawful fraud "in the offer or sale" of securities) [hereinafter cited as 1933 Act], and of § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j (b) (1970) [hereinafter cited as 1934 Act], and rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5 (1972) (making unlawful fraud "in connection with the purchase or sale of any security").

² A bill of exchange (or "draft"), the reader will recall, is a negotiable instrument by the terms of which the drawer (here, the seller of the machinery) orders the drawee (in this case, the buyer-plaintiff) to pay a sum certain either to the bearer or (as was the case here) to the order of a named payee. UNIFORM COMMERCIAL CODE § 3-104 [hereinafter cited as UCC]. The most commonly encountered form of draft is the check—a draft payable on demand and having a bank named as drawee, *see id.* § 3-104(2) (b); other drafts are either payable on demand (sometimes known as "sight drafts") or at a definite time ("time drafts"), *see id.* §§ 3-104(c), -108, -109. The case under discussion involved a time draft that named the seller's parent company as payee. *See note 4 infra.* By his "acceptance" of the draft, *see* UCC § 3-410, the drawee-buyer engaged to honor the instrument, *see id.* § 3-413(1). Such an accepted time draft on a buyer is sometimes called a "trade acceptance." *See generally* Farnsworth, *Documentary Drafts Under the Uniform Commercial Code*, 22 BUS. LAW. 479, 488-89 (1967).

³ 339 F. Supp. 1401 (D.S.C. 1972).

⁴ Named as codefendant with American Barmag was the company's German parent, Barmag Barmer Maschinenfabrik A.G., to whom the bills delivered to American Barmag had been made payable.

⁵ Jurisdiction, venue, and service of process could all be affected by the presence of a securities law claim. A federal forum would become available (indeed, mandatory, in cases under the 1934 Act) irrespective of diversity of citizenship or the amount in controversy; further advantages would ensue, even as against other litigants with federal claims, since the introduction of the securities laws would bring considerably enhanced venue and worldwide service of process. *Compare* 1933 Act § 22(a), 15 U.S.C. § 77v(a) (1970), and 1934 Act § 27, 15 U.S.C. § 78aa (1970), with 28 U.S.C. § 1332 (1970) (jurisdictional amount for diversity actions), *id.* § 1391 (venue), and FED. R. CIV. P. 4(f) (service of process). *See also* 28 U.S.C. § 1331 (1970) (jurisdictional amount for federal-question cases generally), *id.* § 1337 (jurisdiction over commerce-power cases without regard to amount). And, of course, plaintiffs with no claim whatsoever to a federal forum might find their venue and service-of-process options still more restricted.

tion. But rather more disturbing, in a larger sense, than the facts that an error may have been made in this isolated case or that its practical ramifications may be grave, is *MacAndrews'* deeper significance as an object lesson in contemporary understanding of the federal securities laws (and, especially, of rule 10b-5⁷) on the part of judges and litigants alike. The case may be read as symptomatic of widespread mystification and overexpectation—mystification in the absence of a clear, workable guideline from the Supreme Court as to the appropriate breadth of the securities laws,⁸ and overexpectation bred of self-fulfilling prophecy as to rule 10b-5's ubiquity of application.⁹ When a court not be-

In *MacAndrews* itself, plaintiff might well have found such procedural advantages to be valuable, if not essential. If, as seems reasonable, the German equipment manufacturer would more likely be capable of satisfying a judgment than its American sales subsidiary, a premium may have been put on securing the former's presence in the suit. However, litigation of a simple contract claim in federal court (on diversity grounds) would have forced plaintiff to rely for service of process on a state long-arm statute and, since it had enjoyed no direct contact with the German parent, it would be required to argue that the American subsidiary had served simply as an agent for the other company. It is not difficult to understand why plaintiff probably preferred to press a securities-law claim, with its readily available procedural benefits.

⁶ Such differences in result might be particularly obvious where the greater venue authorized under the securities laws, see note 5 *supra*, makes available statutes of limitation (taken from the forum states, see A. BROMBERG, *SECURITIES LAW—FRAUD: SEC RULE 10b-5*, § 2.5(1) (1968)) more generous than those obtaining in the (presumably) more limited number of states where a state-law claimant might find a forum.

Subtler (and more limited) substantive differences may exist between common-law and securities-law fraud claims. Under the latter, proof of scienter may be more readily satisfied or held unnecessary, compare *id.* § 2.6(1) with Jennings, *Insider Trading in Corporate Securities: a Survey of Hazards and Disclosure Obligations under Rule 10b-5*, 62 N.W. U.L. REV. 809, 817-19 (1968), and mere nondisclosure qualifies as misrepresentation, see, e.g., *List v. Fashion Park, Inc.*, 340 F.2d 457 (2d Cir.), *cert. denied*, 382 U.S. 811 (1965), although, of course, it is unlikely in any event that a seller of goods would have been completely silent as to the qualities of his merchandise. Yet, however uncertain the substantive advantages of alleging a securities-law claim, a plaintiff would at least have nothing to lose thereby. He can do no worse than under a common-law fraud claim, and (even if the substantive result on the merits, objectively considered, would be precisely the same) might well benefit intangibly, if he is able to establish his claim to the favored status of one suing under the aegis of federal securities law.

Finally, the buyer-plaintiff who can successfully invoke the securities laws in a commercial context may enjoy certain advantages over the buyer relying on the Uniform Commercial Code. Where oral misrepresentations have been made, the latter (but not the securities-law plaintiff) may find the parol evidence rule an obstacle, compare UCC § 2-202 with *Davidson v. Amos Treat & Co.*, [1961-1964 Transfer Binder] CCH FED. SEC. L. REP. ¶ 91,350 (S.D.N.Y. 1964). The question of damages, relatively unsettled under rule 10b-5, could well give rise to much confusion and commercial uncertainty, compare, e.g., Weiskopf, *Remedies Under Rule 10b-5*, 45 ST. JOHN'S L. REV. 733 (1971), with Peters, *Remedies for Breach of Contracts Relating to the Sale of Goods Under the Uniform Commercial Code*, 73 YALE L.J. 199 (1963); this factor, if no other, should prompt serious doubt whether the federal securities laws should be allowed to encroach upon a code intended to bring uniformity and predictability to commercial law and planning, cf. UCC § 1-102.

⁷ 17 C.F.R. § 240.10b-5 (1972), promulgated under 1934 Act § 10(b), 15 U.S.C. § 78j(b) (1970).

⁸ See generally 1972 DUKE L.J. 465, 474-85, noting Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6 (1971). See also notes 29-30 *infra* & accompanying text.

⁹ Cf., e.g., A. BROMBERG, *supra* note 6, § 2.5(b) ("by now such a dominant factor . . . that one is surprised when it does not turn up"); 4 L. LOSS, *SECURITIES REGULATION* vii (Supp. 1969) ("the veritable explosion of Rule 10b-5 in the 'insider trading' area"); 1972 DUKE L.J. 465, 465 ("the ubiquitous 10b-5").

numbered by repeated and heavy exposure to the securities laws can offhandedly extend their application as was done in *MacAndrews*, the time is ripe to replace gentle sarcasm or amused tolerance¹⁰ with outspoken indignation.¹¹

This Comment will leave the farther-ranging criticism to others; it will narrow its focus at this point to the specific issue presented in *MacAndrews*: are bills of exchange "securities" under the 1934 Act?¹² It should be noted at the outset that although substantially the same question could arise under the 1933 Act's definitions,¹³ that act would ultimately be unavailable to plaintiff in any event. In order to maintain its action under either section 17¹⁴ or [had it been alleged] 12,¹⁵ plaintiff

¹⁰ See, e.g., R. JENNINGS & H. MARSH, CASES AND MATERIALS ON SECURITIES REGULATION 1060 & n.9 (3d ed. 1972).

¹¹ To date, probably the loudest (certainly, the most persistent) voice crying in this wilderness has been that of Professor Ruder. See, e.g., Ruder, *Civil Liability Under Rule 10b-5: Judicial Revision of the Legislative Intent*, 57 Nw. U.L. REV. 627 (1963).

¹² This Comment will not, of course, consider the validity of the claims of misrepresentations as to the performance of the machinery and as to the safety of plaintiff's accepting bills payable in deutschemarks (which defendant allegedly knew would soon be substantially revalued upward). It may be worth observing, however, that—assuming *arguendo* that the bills were securities—the latter fraud would go to the value of the security itself and hence would not raise the fraud-in-the—"consideration" problem posed with respect to the former. Cf. note 21 *infra* & accompanying text.

¹³ Section 3(a)(10) of the 1934 Act, 15 U.S.C. 78c(a)(10) (1970), defining "security," in effect combined the 1933 Act's definition (§ 2(1), 15 U.S.C. § 77b(1) (1970)) with a section exempting certain short-term "securities" (known, for the most part, as "commercial paper," cf. note 27 *infra*) from that act's registration, but not its antifraud provisions (§ 3(a)(3), 15 U.S.C. § 77c(a)(3) (1970)).

In the course of the combination, the draftsmen narrowed the earlier definition's reach in at least one respect relevant here: they no longer included the term, "any . . . evidence of indebtedness." Although the relatively few cases dealing with this language typically concern instruments and writings somewhat more exotic or less formalized than bills of exchange, see, e.g., *Llanos v. United States*, 206 F.2d 852 (9th Cir. 1953), *cert. denied*, 346 U.S. 923 (1954), and while it is possible Congress intended that its application be limited to such unusual items, the phrase, plainly read, would instead appear to have been intended as the broadest possible generic reference, embracing not only peculiar evidences of indebtedness but also more conventional notes, bonds, debentures—and, quite possibly, bills of exchange. (It might well be argued that only "promise," not "order," instruments, cf. note 32 *infra*, serve to evidence indebtedness, but one hesitates to rely on this distinction where, as in *MacAndrews*, the order instrument has been accepted by the drawee. See also notes 16, 33 *infra*.) Wrote the *MacAndrews* court: "Initially, it cannot be denied that the bills of exchange were 'certain evidences of indebtedness.'" 339 F. Supp. at 1406.

In other words, a literal reading of the 1933 Act would probably result in our considering bills of exchange to be securities (a conclusion which a careful reading of the 1934 Act would not support, see notes 22-35 *infra* & accompanying text). But careful literalism cannot be relied upon to produce the best interpretation of the federal securities laws. It is thought that the introduction of a modicum of situation-sense, cf. K. LEWELLYN, *THE COMMON LAW TRADITION* 60, 268-69 ("What is not necessity is that the courts should wind up accepting any particular legal category as the controlling pattern unless it proves to be a category with sense-significance as well as doctrinal significance . . ."), 371-82, *et passim* (1960), will lead us to conclude that under the 1933 Act, as under the 1934 Act, bills of exchange should only in rare circumstances be deemed securities. See notes 36-44 *infra* & accompanying text.

¹⁴ 15 U.S.C. § 77q (1970). See note 1 *supra*.

¹⁵ 15 U.S.C. § 77l (1970) (providing civil remedies for purchasers of securities, with respect to which the act's registration requirements were violated, or as to which any misrepresentations were made in certain types of written or oral communications); this would appear about equally useful as § 17 for plaintiffs in a *MacAndrews* context. Some courts, however, would refuse to imply a private right of action under § 17, thus leaving § 12

would be required to characterize defendant as the seller of a security. Defendant had, to be sure, drawn the bills of exchange, but—the bills being payable to the defendant's parent—their acceptance by the plaintiff is of far greater legal and economic significance.¹⁶ Assuming for the sake of argument that the bills were securities, it would seem much more reasonable to say that defendant had purchased from plaintiff the bills in accepted form, giving the machinery as consideration,¹⁷ than to say that defendant had sold the bills. At no time did plaintiff acquire title to the bills;¹⁸ at no time, therefore, could it have acquired, as a purchaser of "securities," a cause of action under the 1933 Act. However, section 10(b) of the 1934 Act¹⁹ and rule 10b-5 are not as limited in their application. They may be invoked when fraud is perpetrated "in connection with the purchase or sale"²⁰ of any security, and the case law countenances their application whether the alleged fraud goes to the value of the security or [as in *MacAndrews*] of the "consideration."²¹ The relevant inquiry at this juncture, then, is whether the 1934 Act's definition of a "security" embraces bills of exchange.

as the only basis for suit under the 1933 Act; see *Dyer v. Eastern Trust & Banking Co.*, 336 F. Supp. 890, 903-05 (D. Me. 1971).

¹⁶ The drawer's liability on the draft arises only upon its dishonor by the drawee, see UCC § 3-413(2), and where, as here, the payee in whose favor that liability would arise is the drawer's parent company, this liability, it must be conceded, is relatively inconsequential in the normal course of events. The drawee, for his part, is not liable on the instrument until he accepts it. See *id.* § 3-409(1). Unless accepted, then, the practical import of such a draft is minimal. Upon acceptance, however, the drawee-acceptor becomes liable on the instrument, see *id.* § 3-413(1), with the result, in this case, that a more significant movement of funds can be contemplated. See note 2 *supra*.

¹⁷ Granted, this would be a peculiar way of describing the transaction; indeed, this Comment will submit that this sense of peculiarity is itself a factor militating against application of the securities laws, see note 21 *infra*. The immediate point nevertheless appears valid, that this characterization of the transaction—however eccentric it may sound—is more sensible than the alternative approach that plaintiff would be required to pursue.

¹⁸ More precisely (and more sensibly), one would say that plaintiff had never been a "holder" of the bills. See UCC § 1-201(20).

¹⁹ 15 U.S.C. § 78j(b) (1970).

²⁰ *Id.*; 17 C.F.R. § 240.10b-5 (1972) (emphasis added).

²¹ See *Errion v. Connell*, 236 F.2d 447 (9th Cir. 1956) (U.S. treasury bills used in payment for land misrepresented as to value), noted in 9 STAN. L. REV. 589 (1957); cf. *Hooper v. Mountain States Secs. Corp.*, 282 F.2d 195 (5th Cir. 1960) (issuance of new shares fraudulently induced). See also *Superintendent of Ins. v. Bankers Life & Cas. Co.*, 404 U.S. 6 (1971), noted in 1972 DUKE L.J. 465 and *The Supreme Court, 1971 Term*, 86 HARV. L. REV. 1, 260-67 (1972).

Save where capital structure is undermined by the issuance of new shares for inadequate consideration, cf. *Fleischer, "Federal Corporation Law": An Assessment*, 78 HARV. L. REV. 1146, 1161 (1965), one is strongly tempted to disapprove application of the securities laws to fraud-in-the-"consideration" cases (or, generally speaking, to cases where securities are only incidentally present in a transaction), even if on policy grounds alone, cf. 9 STAN. L. REV. 589, 593-97 (1957). Yet most would probably conclude that no basis for such criticism can be found in the statute itself; the "in connection with" language seems inconsistent with drawing lines between strong and tenuous connections. And many courts, rightly, would be disinclined to adopt a policy-oriented interpretation in the absence of an arguable statutory basis, cf. *K. LEWELLYN, supra* note 13, at 374-75.

It might be useful, however, to examine the language, "purchase or sale of a security." It would seem not an unreasonably strict construction to read this as requiring that a security be the subject matter, and not merely the consideration, in a purchase or sale transaction. (This position, of course, would be untenable if the language were broader—

The draftsmen of section 3(a)(10)²² were not sparing of words:

The term "security" means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, pre-organization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit, for a security, or in general, any instrument commonly known as a "security"; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; . . .

as, for example, "purchase or sale involving a security.") Lest it appear too great a burden is being placed on a single two-letter word, it should be noted that the argument is also altogether consistent with the use of the disjunctive phrase, "purchase or sale." One conventionally understands each party's status as purchaser or seller to be determined with respect to a transaction's subject matter alone. It would be nonsense, in an ordinary sales transaction (not a barter) to speak of one party as, say, "purchaser" of the subject matter and (at the same time) "seller" of the consideration, or vice versa, *cf.* note 17 *supra* & accompanying text. Although such conceptualization may have an element of intellectual appeal, it would tend both to frustrate language and to impede understanding of a deal's essence. (Note, by way of comparison, that article 2 of the Uniform Commercial Code, applying to "transactions in goods," *see* UCC § 2-102, defines both "buyer" and "seller" with reference to the goods involved, *see id.* § 2-103(1).) The phrase "purchase or sale," then, serves to make the rule applicable to both parties in a transaction having securities as the subject matter—not to ensure that one or the other categorization can be applied whenever securities figure only remotely in a transaction.

An appropriate analytical approach should be readily apparent: in any given case, the factfinder should consider whether both parties would as likely have proceeded with the transaction, and whether it would have made economic sense, were cash (assuming, for purposes of this inquiry, its availability) to be substituted for the securities in an amount equivalent to their agreed-upon value (a value different from their true value, obviously, where there has been fraud as to the securities' worth—in which event, the would-be defrauding party would hardly agree to substitute cash).

Where the determination under this analysis is affirmative (as it would be in a *MacAndrews* context), the securities may be considered not the subject matter of a purchase or sale, and the transaction will therefore be held to fall outside the coverage of rule 10b-5. Where the answer is negative (as it would be in most conventional transactions in securities), the pertinence of rule 10b-5 will be clear. (Note that the latter conclusion would also obtain in cases—corporate acquisitions being, probably, the most obvious examples—that involve securities as an essential, but not the sole, subject matter of the transaction. Additionally, the test would appear adequate to allow proceeding under rule 10b-5 with the case where the alleged misrepresentations concern the value of readily-marketable securities purporting to be only "consideration" in a sales transaction, for here the misrepresenting party—whether he seeks to purchase or to sell the securities—should not be supposed indifferent to substitution of cash in the misstated amount.) Finally, it should by now be apparent that this approach, though it may seem to be based upon an over-literal reading of the statute, simply represents an attempt to bring consideration of context to this matter in a principled way. *Cf.* text accompanying notes 41-42 *infra*.

The opinion in *MacAndrews* does not clearly indicate that the court deliberately held rule 10b-5 to be violated where fraud affects the subject matter of a transaction involving securities only as consideration, or even that the court was squarely confronted with the issue. Litigators would be ill-advised, the foregoing analysis should suggest, to consider the question unworthy of exploration in future cases. For present purposes, nevertheless, this Comment will accept, as given, the current state of the case-law on this point. It will proceed on the assumption that if rule 10b-5 does not apply in a *MacAndrews* situation, it must be either because the bills of exchange involved are not "securities," as that term is used generally in the 1934 Act, *see* notes 22-35 *infra* & accompanying text, or because they at least should not be considered "securities" in the commercial-payment situation, *see* notes 36-44 *infra* & accompanying text.

²² 15 U.S.C. § 78c(a)(10) (1970).

A fairly comprehensive definition. Still, it would not do to characterize it (as the *MacAndrews* court described the 1933 Act's counterpart definition²³) as "all-embracing." For one thing, it makes no mention of bills of exchange. Though the general rule²⁴ may be that such definitions must be read as nonexclusive,²⁵ there appears good reason to regard the omission as significant, and not merely inadvertent, in this case. Congress, it is clear, was not unacquainted with bills of exchange; it in fact went on to refer specifically to them (and, perhaps redundantly, to "drafts") in the next clause of section 3(a)(10):²⁶

. . . but [the term "security"] shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.

The express exclusion from a definition, of something not included within that definition in the first place, can most easily be attributed to an excess of caution²⁷—a trait no more foreign to the draftsmen of the securities laws²⁸ than to securities practitioners today. To treat the

²³ 339 F. Supp. at 1406, citing *Movielab, Inc. v. Berkey Photo, Inc.*, 321 F. Supp. 806 (S.D.N.Y. 1970), *aff'd per curiam*, 452 F.2d 662 (2d Cir. 1971). In *Movielab*, Judge Mansfield referred to the 1934 Act's definition as "unequivocal and all-embracing," and felt bound by its "plain language, literally read." 321 F. Supp. at 808. There, however, long-term promissory notes were involved, with the result that plainer language availed, and a more literal reading sufficed, than in *MacAndrews*.

Parenthetically, it should be noted that the *MacAndrews* court commonly referred to the 1933 and 1934 Acts, taken together, as "the Securities Act," see, e.g., 339 F. Supp. at 1404-05 & n.5; this, however, may have been occasioned by like confusion apparent in paragraph 21 of the complaint (quoted, *id.* at 1403-04 n.2).

²⁴ Perhaps the "general rule," however, should be that no rules of statutory construction can appropriately be called "general." See K. LLEWELLYN, *supra* note 13, at 371-75, 520-35. Cf. *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 350-51, 353-55 (1943).

²⁵ Cf. *Llanos v. United States*, 206 F.2d 852, 854 (9th Cir. 1953), *cert. denied*, 346 U.S. 923 (1954): "In defining the word 'security' in Section 2(1) of the [1933] Act, Congress intended to include all interstate transactions which were the legitimate subject of its regulation and the section should not be construed narrowly."

²⁶ 15 U.S.C. § 78c(a)(10) (1970).

²⁷ Here, there is also reflected the urgency of the commercial-paper lobby—and the Federal Reserve Board—in distinguishing investment instruments from temporary instruments and, accordingly, in calling for the clear exemption of short-term notes from the registration provisions of the 1933 Act, see Comment, *The Commercial Paper Market and the Securities Acts*, 39 U. CHI. L. REV. 362, 381-85 (1972). The resultant provision, § 3(a)(3) of the 1933 Act, 15 U.S.C. § 77c(a)(3) (1970), formed the basis for the exclusory clause quoted from § 3(a)(10) of the 1934 Act. "Commercial paper," though it had earlier included bills of exchange, see N. BAXTER, *THE COMMERCIAL PAPER MARKET* 2 (1966), by 1933—as today—was a term essentially limited to promissory notes, see *id.* 7, of substantial face-amount value and short-term maturity, placed—whether directly or through intermediaries—with large financial institutions (principally banks) in order to fund current operations. Though one might argue that recent changes in the commercial-paper market—particularly, the sale, increasingly, of commercial paper to non-banks as short-term investment media—call for reassessment of § 3(a)(3)'s desirability, see, e.g., Comment, *supra*, no such shift appears to have taken place so far as the discounting of bills of exchange is concerned, cf. Farnsworth, *supra* note 2, at 485-86, 488-89. And, certainly, *MacAndrews* does not itself present a case of accepted bills of exchange having been held out as possible investments. Cf. note 43 *infra* & accompanying text.

²⁸ Indeed, supererogatory drafting—giving rise, on occasion, to possible misleading

exclusion as containing a negative pregnant (here, to the effect that bills with a maturity exceeding nine months, as those in *MacAndrews*, are securities) would appear methodologically suspect in light of the highly specific definition with which the exclusion is conjoined.

The *MacAndrews* court, however, did not feel required to decide whether any inference could be drawn from the omission of the term "bill of exchange" from the definition, or—on the other hand—whether a negative pregnant could be inferred from the qualified nature of the exclusion. Rather, the court simply observed that the securities laws "are to be read flexibly and broadly,"²⁹ and that the terms of section 3(a)(10) "are to be given a very broad definition."³⁰ The court went on, nevertheless, to find specific language in the definition to support its conclusion that the bills of exchange were "securities." It wrote: "A bill of exchange, of course, is merely a form of note. Upon acceptance it is a promise to pay to the order of a certain person and it is negotiable."³¹

This characterization seems less than obvious in light of the Uniform Commercial Code's sharp distinction between notes and bills of exchange,³² although it is true that acceptance, under the Code, substantially eliminates the differences in legal effect.³³ The Uniform Negotiable Instruments Act, a predecessor of the Code, drew a similar distinction³⁴ and was in effect in every American jurisdiction when the federal securities laws were enacted.³⁵ And, finally, Congress' definition of a security, in juxtaposing the words, itself reflects an appreciation of the bills-notes distinction. It would seem most rea-

negative implications—abounds in the area of exemptions from the 1933 Act (and it is, of course, on such an exemption that the 1934 Act's exclusory clause was based). See 1 L. Loss, *supra* note 9, at 496-97, 570-72, 584-85 (1962).

²⁹ 339 F. Supp. at 1406, citing *Superintendent of Ins. v. Bankers Life & Cas. Co.*, 404 U.S. 6 (1971).

³⁰ *Id.*, citing also *Tcherepnin v. Knight*, 389 U.S. 332 (1967).

³¹ *Id.*

³² Compare UCC § 3-104(2)(a) ("order" instruments) (bills or drafts) with *id.* § 3-104(2)(d) ("promise" instruments) (notes).

³³ Cf. note 16 *supra* & accompanying text. The contract of the acceptor of a bill is the same as that of the maker of a note, see UCC § 3-413(1), and the secondary liability of a bill's drawer is very nearly similar to that of an indorser of any negotiable instrument, compare *id.* § 3-413(2) with *id.* § 3-414(1). The instrument, once accepted, see *id.* § 3-410(1), must almost certainly be considered an "evidence of indebtedness," cf. note 13 *supra*, but that does not make it a "note." It is worth recalling that notes, unlike bills of exchange, are frequently employed as a means of raising funds in the commercial-paper market or of creating significant debt (or, at times, disguised equity, cf. INT. REV. CODE OF 1954, § 385) interests in corporations; Congress' exemption of the former notes, see note 27 *supra*, serves only to emphasize that its regulatory attention was focused on the latter—investment—notes, cf. note 42 *infra*. The fact that a bill of exchange, once accepted, may resemble a note in the legal relationships it entails does not mean that it resembles a note also in those functional characteristics that justify regulation under the federal securities acts.

³⁴ See UNIFORM NEGOTIABLE INSTRUMENTS ACT § 191 (act withdrawn 1951, as superseded by the UCC) ("'Bill' means bill of exchange, and 'note' means negotiable promissory note."); see also *id.* §§ 126, 184.

³⁵ See NATIONAL CONF. OF COMM'RS ON UNIFORM STATE LAWS, HANDBOOK 590 (1932).

sonable, then, to hold on the basis of a careful reading of the statutory definition that bills of exchange are not embraced by the 1934 Act, unless the "economic reality" in which such bills figured might lead one to conclude otherwise in a particular case.

The *MacAndrews* court failed entirely to consider the commercial context in which the alleged securities figured. The applicability of each of the 1934 Act's definitions is limited by an introductory phrase, as follows: "When used in this chapter, *unless the context otherwise requires*—[the term *X* means *Y*, etc.]."³⁶ Although authority for resort to such clauses is relatively slim,³⁷ it appears clear that "context" invites reference not only to the textual environment of words in a statute,³⁸ but also to the real-world factual situation within which the definitional question arises.³⁹ It having been conceded that the securities acts' definitions should be liberally construed, even the most latitudinarian interpreter must be prepared to stop short of absurdity.⁴⁰ More concretely put, even though one might conceive of circumstances in which bills of exchange were the subject matter of investment transactions and could fairly be considered securities by the law as well as by the parties,⁴¹ at the same time one is hard

³⁶ Section 3(a), 15 U.S.C. § 78c(a) (1970) (emphasis added). The same language introduces the 1933 Act's definitions, see § 2, 15 U.S.C. § 77b (1970).

³⁷ See *Schillner v. H. Vaughan Clarke & Co.*, 134 F.2d 875, 877-78 (2d Cir. 1943) (drawing on the 1933 Act's parallel clause), *approved*, 3 L. Loss, *supra* note 9, at 1698; Comment, *The Application of Section 17 of the Investment Company Act of 1940 to Portfolio Affiliates*, 120 U. PA. L. REV. 983, 986 & n.12 (1972) (dealing with parallel language introducing § 2(a) of the Investment Company Act of 1940, 15 U.S.C. § 80a-2(a) (1970)). See generally 1 L. Loss, *supra* note 9, at 460 & n.17.

³⁸ Cf. *Helvering v. Gregory*, 69 F.2d 809, 810-11 (2d Cir. 1934) (L. Hand, J.), *aff'd*, 293 U.S. 465 (1935):

[I]t does not follow that Congress meant to cover such a transaction, not even though the facts answer the dictionary definitions of each term used in the statutory definition. It is quite true, as the Board has very well said, that as the articulation of a statute increases, the room for interpretation must contract; but the meaning of a sentence may be more than that of the separate words, as a melody is more than the notes, and no degree of particularity can ever obviate recourse to the setting in which all appear, and which all collectively create. Such an approach is in order with respect to the definition of a "security" under consideration, which appears, on the whole, intended to embrace investment media of all forms. Cf. notes 27, 33 *supra*.

³⁹ See, e.g., *Movielab, Inc. v. Berkey Photo, Inc.*, 321 F. Supp. 806 (S.D.N.Y. 1970), *aff'd per curiam*, 452 F.2d 662 (2d Cir. 1971). Long-term notes had been taken in exchange for corporate assets, and Judge Mansfield (still sitting as a district judge) felt thoroughly constrained by the language of the definition to hold that "securities" were involved. 321 F. Supp. at 809. He did go on to observe, however, with apparent satisfaction, that notes of the type concerned "are frequently discounted, purchased for investment, hypothecated, or otherwise made the subject of dealings in the market place." *Id.* Cf. K. LLEWELLYN, *supra* note 13, at 60 *et passim* (calling on judges to decide cases in the light of "situation-sense"). See also the authorities cited note 37 *supra*.

⁴⁰ One might expect that point to be the more nearly approached, the further the situation departs from the securities-market context identified as having necessitated passage of the 1934 Act; see 1934 Act § 2, 15 U.S.C. § 78b (1970).

⁴¹ Cf. *Sanders v. John Nuveen & Co.*, 463 F.2d 1075 (7th Cir.), *cert. denied*, 409 U.S. 1009 (1972) (1934 Act's commercial-paper exclusion held inapplicable to notes offered to the public as investment media). See also Comment, *supra* note 27.

pressed to suppose bills employed commercially as payment media are considered securities by any party to the transaction.⁴²

Attention to context further implies attention to consequences. Where bills of exchange are traded as securities, application of the securities laws may be beneficial, if not in fact necessary, in order to prevent fraudulent dealing.⁴³ But where, as in *MacAndrews*, bills of exchange function as substitutes for cash, application of the securities laws hardly appears necessary, and in fact would very likely be disruptive of the commercial environment.⁴⁴ On the further ground that interpretation must appreciate context, then, *MacAndrews* appears wrongly decided.

In summary, *MacAndrews* can teach a great deal to judges and lawyers generally. Its lesson, in essence, is that careful analysis is not rendered superfluous by policies of broad application of remedial legislation, and, further, that analysis is surer when illuminated by context. Finally, it should be plain how dangerous it is to suppose the securities laws to be either ubiquitous or all-embracing.⁴⁵ Congress, in its concern for the investor, appears to have neither contemplated nor desired a fundamental alteration in the fabric of commercial law; courts and litigators, in consequence, would do well carefully to take the full measure of their actions.

⁴² Cf. 1 L. Loss, *supra* note 9, at 546 (arguing, on the basis of the "context" clause, that long-term promissory notes given to obtain personal loans ought not be considered subject to antifraud liabilities under the securities acts).

⁴³ Cf. *Sanders v. John Nuveen & Co.*, 463 F.2d 1075 (7th Cir.), *cert. denied*, 409 U.S. 1009 (1972).

⁴⁴ See notes 5-6 *supra* & accompanying text.

⁴⁵ See note 9 *supra* & accompanying text. One is reminded of Lord Denman's observation: "[T]he mere statement and restatement of a doctrine,—the mere repetition of the *cantilena* of lawyers, cannot make it law, unless it can be traced to some competent authority, . . . if it be irreconcilable to some clear legal principle." *O'Connell v. The Queen*, 8 Eng. Rep. 1061, 1143 (H.L. 1844).