

# Commercial Paper

Commercial paper serves two important functions. It is a substitute for cash and it is a way to loan money. This makes it an essential part of the business environment.

# Types of Commercial Paper

There are four types of commercial paper. All can be either negotiable or nonnegotiable.

1. Drafts
2. Checks
3. Notes
4. Certificates of Deposit

# Drafts & Checks

Referred to as three-party paper because there are three parties to the instrument.

- Drawer – Person who orders the payment to the payee through an order instrument (draft or check).
- Drawee – The bank, who the payment is drawn from.
- Payee – Person who receives payment.

# Notes

Known as two-party paper because there are two-parties involved, the maker and the payee.

- Maker – Person who says “I promise to pay” on the face of the note.
- Payee – Person to be paid.

# Certificates of Deposit

Type of two-party paper issued by a bank or other financial institution.

When you invest in a certificate of deposit you are lending the bank money under the terms specified by the CD. The bank issues you its promise to repay you , at a stated time in the future, the principal plus interest at a specified rate. It also sets forth penalties for failing to comply with the terms.

# Negotiability Requirements

Article 3 of the UCC requires that to be negotiable all forms of commercial paper must meet certain criteria.

- It must be in writing
- It must be signed by the maker or drawer
- It must contain an unconditional promise or order to pay a sum certain in money
- It must contain no other promise or obligation
- It must be payable on demand or at a definite time
- It must be payable to order or bearer unless it is a check