The "Good Heart, Empty Head" Test

The parties to a contract cannot always envision every possibility when spelling out what circumstances should enable one party to declare the other in default of the contract. Thus, lenders are in the habit of inserting language in their notes to the effect that they may accelerate and declare the entire balance due on a note not otherwise in default if the lender "deems itself insecure" for any reason.

The standard under which such an acceleration by a lender is measured is "good faith," and the standard by which the lender's good faith has been tested bears the sobriquet among commercial lawyers of the "good heart, empty head" test.

UCC 1-201(19) defines "good faith" to mean "honesty in fact in the conduct or transaction concerned."

To show how this concept works, suppose a bank has a note not due for another 90 days when its loan officer, John Lender, learns that the bank's customer, the owner of a local pharmacy, is about to begin a federal sentence for drug related crimes. John Lender in good faith believes that unless he accelerates the note immediately, the debtor's ability to pay will suffer considerably. John Lender therefore accelerates the note and makes demand for payment in full prior to his customer's pending incarceration.

So long as John Lender reasonably believed that the bank was insecure due to the debtor's pending imprisonment, he should be able to accelerate the note in reliance upon the "deems itself insecure" clause, and it should not matter if John Lender is mistaken in his good faith belief. That is, so long as he *believes* the bank is insecure and has a demonstrable reason for so believing (clearly the case here), then John does not have to be correct in his conclusion.

The debtor defending against such an acceleration bears the burden of proof to show that the creditor did not act in good faith, which means that he must show that John Lender did not have a reasonable belief that the bank was insecure at the time of the acceleration. This is a much more difficult task than proving, for example, that the debtor's impending imprisonment did not really lessen the chances of repayment.

Traditionally the "good heart, empty head" standard has given some consolation to creditors who are nervous about the status of accounts even when their debtors are not past due. It remains to be seen how the present commercial climate and its shower of "lender liability" cases will test the strength of this traditional good-faith standard.

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