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# Payees As Holders in Due Course of Negotiable Instruments

# LEGISLATION

## PAYEES AS HOLDERS IN DUE COURSE OF NEGOTIABLE INSTRUMENTS.

### *Meaning and Scope of the Term Holder in Due Course*

It is a basic and venerable rule of the law of property that a "purchaser for value and without notice" of a legal title takes it free of outstanding equities.[1] This classic concept, far from being outmoded, finds a formidable place in the law of today, for modern business, with its need for credit financing, requires that one who buys the goods or written obligations of another in reliance upon the title of the seller receive some measure of protection. The importance of the bona fide purchaser in our law is evidenced by the fact that he is incorporated as a highly favored personality in such legislation as factors acts,[2] recording acts,[3] and the Uniform Laws governing negotiable instruments,[4] sales of goods,[5] conditional sales,[6] trust receipts,[7] bills of lading,[8] warehouse receipts,[9] and stock transfers.[10] Though the precise elements going into the makeup of this personage are not identical in all of the above statutes, it is generally true that he must have taken for value, and in good faith;[11] and where the thing bought is a written obligation, the transfer must also have been before maturity, and the instrument must have been complete on its face.[12]

Long before the courts had begun to look with particular favor upon purchasers of other types of commercial paper,[13] the bill of exchange and the

1. United States v. Des Moines Navigation and Railway Co., 142 U. S. 510, 530 (1892); Alden v. Trubee, 44 Conn. 455, 459 (1877); Dunham v. Day, 15 Johns. 555, 568 (N. Y. 1818); "So in this principal case, if the bill of exchange had been afterwards assigned for a valuable consideration, the honesty of this assignment had purged the original canker and rendered it good enough. As where a fraudulent conveyance is assigned upon a valuable consideration, the fraud is purged." Hussey v. Jacobs, 1 Ld. Raym. 87, 88, 91 Eng. Reprints 954, 955 (K. B. 1696). ". . . an equity, being in its nature a claim in personam and not in rem, can be enforced only against a party to the transaction in which the equity arises, or some one in privity with that party. (Langdell, Summary of Equity Pleading § 141.) The transfer of bills and notes, by virtue of their negotiability, is governed by the same principle." 2 AMES, CASES ON BILLS AND NOTES (1894) 866.

2. N. Y. PERS. PROP. LAW (1909) § 43. "This statute was intended to protect subsequent bona fide purchasers. . . ." *In re* James, 30 F. (2d) 555, 558 (C. C. A. 2d, 1929); "That act was to protect persons dealing in good faith with the apparent owners of property." Dorrance v. Dean, 106 N. Y. 203, 205, 12 N. E. 443, 444 (1887).

3. N. Y. REAL PROP. LAW (1909) § 291; N. Y. LIEN LAW (1909) § 230.

4. UNIFORM NEGOTIABLE INSTRUMENTS LAW, 5 UNIFORM LAWS ANN. (1896) § 52. This statute will hereafter be cited U. N. I. L.

5. UNIFORM SALES ACT, 1 UNIFORM LAWS ANN. (1907) § 38.

6. UNIFORM CONDITIONAL SALES ACT, 2 UNIFORM LAWS ANN. (1919) § 9.

7. UNIFORM TRUST RECEIPTS ACT, 9 UNIFORM LAWS ANN. (1934) § 9.

8. UNIFORM BILLS OF LADING ACT, 4 UNIFORM LAWS ANN. (1910) § 42.

9. UNIFORM WAREHOUSE RECEIPTS ACT, 3 UNIFORM LAWS ANN. (1907) § 13.

10. UNIFORM STOCK TRANSFER ACT, 6 UNIFORM LAWS ANN. (1911) § 4.

11. See *supra* notes 3-10.

12. See *supra* note 4.

13. Shaw v. Railroad Co., 101 U. S. 557 (1879) (rule permitting bona fide purchaser of bill or note to recover thereon not applicable to bill of lading); Stollenwerck v. Thacher,

promissory note had attained all the indicia of negotiability.[14] This early development arose from the need of the business world for a readily circulable credit medium, which could be used as a means of liquidating indebtedness without transmitting actual cash from place to place.[15] Bills and notes would obviously not serve that purpose if an obligor, in defending an action brought by a bona fide purchaser, could plead that the paper in suit had been executed under fraud or duress, or without a binding consideration. The possibility of this undesirable consequence was fully realized by the early English courts which held that a party who had taken a bill or note complete on its face, before maturity, for value, in good faith, and in the regular course of business, was not subject to defenses other than those that were deemed to create a defect in the *res*, the paper itself.[16] These requirements, excepting the one that the purchase must have been in the regular course of business, were first embodied in the Bills of Exchange Act, enacted in England in 1882,[17] and were later included in the Uniform Negotiable Instruments Law,[18] which has now been made a part of the statutory law of all the states of the Union and has also been enacted in the District of Columbia and in many American territories. Under the Bills of Exchange Act the "bona fide holder for value and without notice" became, by name, the "holder in due course,"[19] and that term found favor also in this country.[20]

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115 Mass. 224 (1874) (purchaser of order bill of lading from agent lacking authority to sell not permitted to recover against drawer); Gardiner v. Suydam, 7 N. Y. 357 (1852) (delivery of warehouse receipts not sufficient to pass title though such was intention); ". . . a more modern . . . invention . . . for the transfer . . . of personal property, is the indorsement or assignment of bills of lading or warehouse receipts." McNeil v. Hill, 16 Fed. Cas. No. 8,914, at 325 (C. C. D. Minn. 1865).

14. In these early cases bills and notes were held negotiable: Jenys v. Fawler, 2 Strange 947, 93 Eng. Reprints 959 (K. B. 1760); Price v. Neal, 3 Burr. 1355, 97 Eng. Reprints 871 (K. B. 1762); Anonymous, 1 Ld. Raym. 738, 91 Eng. Reprints 1393 (K. B. 1792) (purchaser in good faith of lost bill not required to surrender it upon trover being brought by rightful owner). Ames, *Purchase for Value Without Notice*, 1 HARV. L. REV. 1 (1887).

15. See Aigler, *Payees as Holders in Due Course* (1927) 36 YALE L. J. 608, 621; NORTON, BILLS AND NOTES (4th ed. 1914) 6; for cases discussing the origin of the negotiability of bills and notes see: Buller v. Crips, 6 Mod. 29, 87 Eng. Reprints 793 (K. B. 1794) (courts recognized the custom of merchants as law); Brown v. Harraden, 4 T. R. 148, 100 Eng. Reprints 943 (K. B. 1797) (notes placed on equal footing with bills of exchange).

16. Smith v. Livingston, 111 Mass. 342 (1873); see Bennett v. Semmes, 287 Fed. 745, 748 (D. C. Ark. 1923) (statute construed according to law merchant and regarded as declaratory thereof). First Nat. Bank in Brownwood v. First Nat. Bank of Coleman, 264 S. W. 1020, 1024 (Tex. Civ. App. 1924); 2 AMES, CASES ON BILLS AND NOTES (1894) 811.

17. BILLS OF EXCHANGE ACT, 1882, 45 & 46 VICT. c. 61, § 29.

18. U. N. I. L. (1896) § 52.

19. Lewis v. Clay, 76 L. J. Q. B. 224, 228 (1898); ". . . the bona fide holder for value without notice, or the holder in due course as he is now called. . . ." Herdman v. Wheeler [1902] 1 K. B. 361, 370.

20. See Blumenthal & Bickart v. City of Columbia, 175 Ala. 398, 57 So. 814, 815 (1912); Davis v. National City Bank of Rome, 46 Ga. App. 194, 167 S. E. 191, 192 (1932); ". . . a holder in due course . . . or, as more familiarly termed, an innocent purchaser for value." Newburg State Bank v. Heflin, 189 Mo. App. 292, 296, 175 S. W. 297, 298 (1915).

To guard the holder in due course from defenses personal to former owners of the paper, the Uniform Law declares that he ". . . holds the instrument free from any defect of title of prior parties, and free from defenses available to prior parties among themselves. . . ."[21] In order that his good faith may not easily be impeached it is provided that notice of infirmities or defects means ". . . actual knowledge of the infirmity of defect, or knowledge of such facts that his action in taking the instrument amounted to bad faith."[22] Should the defense be raised that the paper had failed of delivery, or had been delivered subject to a condition, the holder in due course may avail himself of a provision to the effect that ". . . where the instrument is in the hands of a holder in due course, a valid delivery . . . is conclusively presumed."[23] In sharp contrast to this favored status is the position of a holder other than one in due course, who holds the instrument ". . . subject to the same defenses as if it were non-negotiable."[24]

In view of the significant consequences ensuing from the fact that a person is a holder in due course, both courts and legislatures may be expected to discriminate with care in determining who may assume that status. No doubt exists that a party other than a payee, who has taken order paper by indorsement and delivery, or who has received bearer paper by delivery, is eligible to stand in the position of a holder in due course; indeed, it is by protecting such parties as these, that the present English and American statutes seek to give to bills and notes certain attributes of currency.[25] Whether, on the other hand, the nominal payee of negotiable paper can be a holder in due course is a question not easily answered. It is complicated by the fact that considerations of commercial expediency come in conflict with the niceties of statutory construction; and additional difficulty is occasioned by the need for uniformity of interpretation among the several jurisdictions. Suits by payees are many in number and situations are exceedingly common in which the results of these actions depend entirely upon the question of whether the payee is a holder in due course. The problem is, therefore, one of considerable practical importance.

*The Rule at Common Law*

It was the well settled and generally accepted rule at common law that the right of a payee to be a holder in due course was co-extensive with that of any other holder of a negotiable instrument.[26] The cases wherein this rule

21. U. N. I. L. (1896) § 57.

22. U. N. I. L. (1896) § 56.

23. U. N. I. L. (1896) § 16.

24. U. N. I. L. (1896) § 58.

25. Gruntal v. National Surety Co., 254 N. Y. 468, 173 N. E. 682 (1930); Employers' Liability Assurance Corporation v. Greenfield, 316 Pa. 477, 175 Atl. 403 (1934); Wakem v. Schneider, 192 Wis. 528, 213 N. W. 328 (1927). "The law merchant is essentially the creation of the business world, whose practices have hardened into principles, and these principles have been shaped and polished for centuries by the lapidaries of the law—all to one supreme end, viz., the protection of a bona fide holder for value who has acquired a negotiable instrument in the due course of trade or business." *Ex Parte* Goldberg & Lewis, 191 Ala. 365, 366, 67 So. 839, 842 (1914).

26. Armstrong v. American Exchange Nat. Bank, 133 U. S. 433 (1889); Steadwell v. Morris, 61 Ga. 97 (1878); Lucas v. Owens, 113 Ind. 521, 16 N. E. 196 (1888) (maker's

was established were, for the most part, those in which an intermediate party, in the regular and customary course of business, came into possession of paper by taking it from the maker, and then transferred it to the payee, who subsequently brought suit. This occurred, for example, when a debtor bought a bill payable to his creditor, intending to turn it over to the payee in satisfaction of a debt which he owed the latter; or a debtor, at his creditor's request, drew a note naming as payee the bank where the creditor expected to pledge the instrument, which was turned over to him for that purpose; or, as often happened, an accommodation maker drew paper payable to the bank where it was to be discounted by the accommodated party to whom it was entrusted.[27] Had it been held under the common law that a payee who took from an intermediate party was subject to personal defenses existing between the latter and the maker, these useful three-way transactions would have become valueless to the commercial world. Apparently desirous of averting that unfavorable result, the early courts gave immunity from personal defenses to one, whether named payee or not, who had taken from such an intermediary for value and without notice.[28] Indeed, the great majority of courts went even further and extended similar protection where the intermediate party was an agent or bailee of the maker, or a wrongdoer in possession of the paper, provided always that, in selling the same to the payee, he had feigned the appearance of a rightful owner.[29]

There are also classes of cases where no third party handles the document during its transfer from the maker to the payee and in which the present problem arises most interestingly. For example, a maker fraudulently obtains

surety sued by payee and not permitted to prove fraud practiced by maker); Poirier v. Morris, 2 El. & Bl. 89, 118 Eng. Reprints 702 (Q. B. 1853); See Nelson v. Cowing, 6 Hill 336 (N. Y. 1844) (payee not presumed to be a holder in due course but may prevail over personal defense by proving transfer before maturity and payment of value).

27. The most common of these situations is the first one mentioned, wherein a party purchases a bill payable to another before the latter has received it. The intermediary in this transaction is known as the purchasing remitter. Boston Steel & Iron Co. v. Steuer, 183 Mass. 140, 66 N. E. 646 (1903). See Moore, *The Right of the Remitter of a Bill or Note* (1920) 20 COL. L. REV. 749, 756; Beutel, *Rights of Remitters and Other Owners Not Within the Tenor of Negotiable Instruments* (1928) 12 MINN. L. REV. 584. "Where there are four parties to such a bill, namely, the drawer, the drawee, the payee, and the remitter or purchaser, the usual course of business is for the drawer to deliver it to the remitter or purchaser, and for the latter to deliver it to the payee." Armstrong v. American Exchange Nat. Bank, 133 U. S. 433, 453 (1889).

28. Gagle v. Lane, 49 Ark. 465, 5 S. W. 790 (1887) (failure of consideration from intermediary to maker no defense to payee's action against maker); South Boston Iron Co. v. Brown, 63 Me. 139 (1873); American Exch. Nat. Bank v. Ulm, 21 Mont. 440, 54 Pac. 563 (1898) (payee taking note as collateral from co-maker not bound to inquire whether other makers had agreed to such use of note); Lookout Bank v. Aull, 93 Tenn. 645, 27 S. W. 1014 (1894) (delivery of note in violation of condition not valid defense to suit by payee against maker's sureties).

29. Hoffman & Co. v. Bank of Milwaukee, 12 Wall. 181 (U. S. 1878) (failure of consideration between drawer and acceptor no defense to suit by bona fide payee even where acceptor was defrauded by drawer); Brown v. Weldon, 27 Mo. App. 251 (1887). Some courts went so far as to protect the payee where the intermediary had posed as a borrower of the paper, Jordan v. Jordan, 78 Tenn. 124 (1882); Bank v. Goss, 31 Vt. 315 (1858).

the signature of an accommodator and then transfers the paper to an innocent payee; or, obtaining the signature honestly but subject to a condition, he transfers the bill or note free of the condition to a payee unaware thereof. It was well settled at common law that even in these situations the payee could claim the favored status of a purchaser for value without notice.[30]

*Effect of the N. I. L. and the Bills of Exchange Act*

Soon after the enactment of the Bills of Exchange Act and the Negotiable Instruments Law the English and American courts encountered the difficulty that these statutes, substantially similar in pertinent part,[31] were susceptible of conflicting constructions on the question of whether a payee could be a holder in due course.[32] The provisions that are generally involved when a payee claims to be a holder in due course are as follows:

"§191. *'Holder' means the payee or indorsee of a bill or note, who is in possession of it, or the bearer thereof.*

*'Bearer' means the person in possession of a bill or note which is payable to bearer.*

*'Issue' means the first delivery of the instrument, complete in form, to a person who takes it as a holder.*

*'Delivery' means transfer of possession, actual or constructive, from one person to the other.*"

"§52. *A holder in due course is a holder who has taken the instrument under the following conditions: . . . (4) That at the time it was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it.*"

"§30. *An instrument is negotiated when it is transferred from one person to another in such manner as to constitute the transferee the holder thereof. If payable to bearer it is negotiated by delivery, if payable to order it is negotiated by the indorsement of the holder completed by delivery.*"

The procedure of the courts in seeking a solution to the problem has been to consider at the outset whether the party claiming to be a holder in due course is a "holder" at all, under the definition of that term in Section 191. Since this definition expressly includes payees among those who may be holders, all divergence of judicial opinion on this point has been forestalled, no contrary

30. Tischhauser v. Prentice, 30 Cal. App. 699, 159 Pac, 226 (1916) (co-maker having agreed to transfer paper to payee subject to condition transferred it free thereof); Anderson v. Warne, 71 Ill. 20 (1873); *cf.* Kulenkamp v. Groff, 71 Mich. 675, 40 N. W. 57 (1888).

31. For the sake of convenience in making reference to particular sections of the statutes, the numbers used will be those of the UNIFORM NEGOTIABLE INSTRUMENTS LAW. For cross-citations into corresponding sections of the English Act see BRANNAN, NEGOTIABLE INSTRUMENTS LAW (5th ed. 1932) 1149.

32. In England it was first held that a payee was not a holder in due course, Herdman v. Wheeler [1902] 1 K. B. 361; and later the same court reached the opposite result in Lloyd's Bank v. Cooke [1907] 1 K. B. 794. Soon after the adoption of the N. I. L. a divergence of opinion appeared among our courts. The first case to be decided held in favor of the payee. Boston Steel & Iron Co. v. Steuer, 183 Mass. 140, 66 N. E. 646 (1903); but this case was disapproved in Vander Ploeg v. Van Zuuk, 135 Iowa 350, 112 N. W. 807 (1907).

construction being taken even in the cases where our ultimate question is answered in the negative.[33] Having decided that the payee is a holder, the next inquiry of the courts has been to ascertain whether he is one in due course under the language of Section 52, the evident function of which is to prescribe the requisites for that status. In this connection the principal source of difficulty has been subdivision (4) of Section 52 which requires that a holder in due course be one to whom the paper has been negotiated.[34] To determine whether this requisite has been satisfied some courts turn again to Section 191 where the first delivery of an instrument to a holder is defined as its issuance. Here the question presents itself whether this first delivery being the issuance, can at the same time be a negotiation so as to comply with Section 52 (4).[35]

In deciding whether the transfer to the payee is a negotiation the courts in all states refer to Section 30 which is entitled "What Constitutes Negotiation."[36] The structure of this section has been a prolific source of trouble for the courts. In the first sentence it is stated very broadly, that a transfer from *one person* to another, who thereby becomes a holder, is a negotiation. Reading this alone, it appears that the transferror in a negotiation may be *any person* and that the transfer need merely be such as to constitute the recipient a holder. Thus, if a maker or an intermediary transfers paper to a payee the latter becomes a holder under Section 191 and the transfer is a negotiation within the meaning of the first sentence of Section 30. The conclusion follows that the payee may be a holder in due course. However, the second sentence of Section 30 very clearly provides that bearer paper is negotiated by delivery, and order instruments by *indorsement* plus delivery. The crux of the difficulty with this provision is the question of whether it excludes all methods of negotiation other than the two mentioned. If that is its meaning the conclusion follows that a payee who has taken order paper from a maker or an intermediary without indorsement, as is the usual practice, has not received it by a negotiation, and so cannot be a holder in due course under Section 52 (4), which requires a negotiation.

This construction, the theory of which is that the payee did not take by

33. Liberty Trust Co. v. Tilton, 217 Mass. 462, 105 N. E. 605 (1914); Merchants Nat. Bank v. Smith, 59 Mont. 280, 196 Pac. 523 (1921); American Nat. Bank v. Kerley, 109 Ore. 155, 220 Pac. 116 (1923).

34. It is generally held that a transfer to a payee can be a negotiation. Drumm Const. Co. v. Forbes, 305 Ill. 303, 137 N. E. 225 (1922); Snyder v. McEwen, 148 Tenn. 423, 256 S. W. 434 (1923); *contra,* Southern Nat. Life Realty Corp. v. People's Bank, 178 Ky. 80, 198 S. W. 543 (1917).

35. In these cases it was decided that an issuance could not be a negotiation: Southern Nat. Life Realty Corp. v. People's Bank, 178 Ky. 80, 198 S. W. 543 (1917); First Nat. Bank v. Allen, 88 Okla. 162, 212 Pac. 597 (1923). "'Issue' is therefore the usual first step towards 'negotiation,' which results, under Section 30, when the first or a later holder passes the note to another person in such manner as to constitute the latter a holder." J. I. Case Threshing Co. v. Howth, 116 Tex. 434, 438, 293 S. W. 800, 802 (1927).

36. The following cases offer analyses of this section: Davis v. National City Bank of Rome, 46 Ga. App. 194, 167 S. E. 191 (1932) (court of opinion that since negotiation of order paper requires indorsement, transfer to payee by mere delivery cannot be negotiation); Maurer v. Hahn, 105 N. J. L. 494, 145 Atl. 316 (1929); Belt v. Smith, 264 S. W. 1027 (Tex. Civ. App. 1924).

negotiation because there was no indorsement to him, applies, of course, only to order paper. However, since bearer instruments are very rarely found in cases where our question arises, the conclusion that is reached in reference to paper payable to order disposes of the problem in its more important aspect. Moreover, the question of whether the payee can be a holder in due course presents little difficulty where the paper is of the bearer type. A bearer is one in possession of a bill or note payable to bearer and such a party is also a holder. This holder can easily show that he took by negotiation, for bearer paper is negotiated by a mere delivery which is defined in Section 191 as a transfer of possession by one person to another. Thus, the payee can satisfy Section 30 and 52 (4) by proving simply that another person transferred to him the possession of the paper.

*The Negative View*

Stepping now from the statute to the cases which interpret it, the fact appears that a small minority of courts, while not disputing that another view would be preferred by the business world, find it impossible, within the Act, to protect the payee. The difficulties involved in seeking to conform the statutory language to a commercially desirable result were revealed for the first time when the Court of King's Bench, departing from its earlier liberal position,[37] denied recovery in the leading case of *Herdman v. Wheeler*.[38] Here the payee-plaintiff, acting in good faith, took a note from the maker's agent who had fraudulently filled in an amount in excess of his authority. The court, it seems, could have disposed of this case on the ground that the payee, knowing he was dealing with an agent, should have inquired as to the extent of the authority given.[39] Instead, however, the holding was based on the broader ground that the plaintiff was not a holder in due course because the transfer to him as payee could not be a negotiation under the Bills of Exchange Act.[40]

Though the *Herdman* case did not long remain the law in England it has undeniably had a great influence on the authorities in our country. This is shown by the fact that those American cases which take the negative view, have in every instance adopted the narrow construction of the corresponding English statute.[41] In reaching the conclusion that a payee cannot be a holder in due course, the *Herdman* case necessarily held that a transfer to the

37. The leading common law cases in favor of the payee are: Munroe v. Bordier, 8 C. B. 862, 137 Eng. Reprints 747 (C. P. 1849); Poirier v. Morris, 2 El. & Bl. 89, 118 Eng. Reprints 702 (Q. B. 1853); Watson v. Russell, 3 B. & S. 34, 122 Eng. Reprints 14 (Q. B. 1862). For a discussion of the historical background of the first two of the above cases see Aigler, *Payees as Holders in Due Course* (1927) 36 YALE L. J. 608, 610.

38. [1902] 1 K. B. 361.

39. *Id.* at 373.

40. *Id.* at 372.

41. Vander Ploeg v. Van Zuuk, 135 Iowa 350, 112 N. W. 807 (1907) (here, however, court denied that payee could never be holder in due course); Long v. Shafer, 185 Mo. App. 641, 171 S. W. 690 (1914); Miller v. Campbell, 173 App. Div. 821, 160 N. Y. Supp. 834 (1st Dep't 1916) (recovery denied with express reservation that in proper case payee would prevail); Britton Milling Co. v. Williams, 45 S. D. 274, 187 N. W. 159 (1922) (court apparently of opinion payee can never be holder in due course).

payee by a maker or an intermediate third party is not a negotiation.[42] To justify this contention the courts of the minority view in the United States set forth almost verbatim the three chief points made in *Herdman* v. *Wheeler,* which are the following: (1) The word "negotiation", as used in Section 52 (4), means a transfer of paper after it has left the hands of the immediate parties of which the nominal payee is one.[43] (2) The first transfer of the paper to one who is thereby constituted the holder of it is its issuance and is, hence, not a negotiation.[44] (3) The enumeration in Section 30 of two types of negotiation excludes all other methods whereby such a transfer may be effected.[45] On the basis of the first two of these points the rule has been formulated that in order to have a negotiation the parties must be successive holders.[46] Consequently, since a maker is not a holder he is held not to negotiate when he transfers to the payee.[47] An intermediate party in possession, not being a payee or indorsee in possession, is also not a holder and so his transfer to the payee falls short of a negotiation.[48] The Court of King's Bench in the *Herdman* case expressly denied that a payee would never be protected, and this denial has been reiterated in this country. However, the exclusion of transfers by a maker or an intermediary leaves no practical significance to the statement that in certain cases a payee can be a holder in due course.

42. Builders' Lime and Cement Co. v. Weimer, 170 Iowa 444, 151 N. W. 100 (1915); Harrington First National Bank v. Lyons Exchange Bank, 100 Kan. 194, 164 Pac. 137 (1917); Bolton v. Wharton, 163 S. C. 242, 161 S. E. 454 (1931); Kimball-Krough Pump Co. v. Judd, 88 S. W. (2d) 579 (Tex. Civ. App. 1935).

43. Kinder v. Fisher's Nat. Bank, 93 Ind. App. 213, 177 N. E. 904 (1931) (plaintiff-payee not holder in due course because an "original party"); Britton Milling Co. v. Williams, 45 S. D. 274, 187 N. W. 159 (1922); see Herdman v. Wheeler [1902] 1 K. B. 361, 373.

44. ". . . as plaintiff was the payee to whom the note was issued . . . the note was never negotiated. . . ." Southern Nat. Life Realty Corp. v. Peoples' Bank, 178 Ky. 80, 85, 198 S. W. 543, 546 (1917); see Foster v. Security Bank & Trust Co., 288 S. W. 438, 440 (Tex. Comm. App. 1926); Herdman v. Wheeler [1902] 1 K. B. 361, 376.

45. Carter v. Butler, 264 Mo. 306, 174 S. W. 399 (1915); "To constitute a holder in due course the instrument must be negotiated; that is, must be held by indorsement if payable to order, or by delivery if payable to bearer." First Nat. Bank v. Lyons Exch. Bank, 100 Kan. 194, 197, 164 Pac. 137, 138 (1917); "In the case of a note payable in ordinary form to a person's order, the statute explicitly requires something further to accomplish its negotiation . . . , to wit, indorsement by such payee, followed by delivery by the payee to another." J. I. Case Threshing Co. v. Howth, 116 Tex. 434, 438, 293 S. W. 800, 801 (1927).

46. Vander Ploeg v. Van Zuuk, 135 Iowa 350, 112 N. W. 807 (1907); Rice v. Jones, 102 Okla. 30, 225 Pac. 958 (word "course" held to require more than one transfer); see Herdman v. Wheeler [1902] 1 K. B. 361, 376.

47. Long v. Mason, 273 Mo. 266, 200 S. W. 1062 (1918); Strother v. Wilkinson, 90 Okla. 247, 216 Pac. 436 (1923); Marion Sav. Bank v. Leahy, 200 Iowa 220, 204 N. W. 456 (1925) (question not discussed but decision reached that transfer from maker not such as to permit payee to be holder in due course).

48. Jones v. Citizens' State Bank, 39 Okla. 393, 135 Pac. 373 (1913); Tripp State Bank v. Jerke, 45 S. D. 448, 188 N. W. 314 (1922); Kincaid v. Lee County State Bank, 4 S. W. (2d) 310 (Tex. Civ. App. 1928).

A further development of *Herdman v. Wheeler* has arisen from the fact that the paper in that case was not complete when it left the hands of the maker, who authorized another person to fill in the blanks. In reference to such instruments Section 14 provides: "But if any such instrument, after completion, is negotiated to a holder in due course, it is valid and effectual for all purposes in his hands, and he may enforce it as if it had been filled up strictly in accordance with the authority given and within a reasonable time." Under their construction of this section the courts of a few jurisdictions, while permitting an *indorsee* to be a holder in due course regardless of whether the paper was complete when it left the maker[49] are willing to extend this right to a payee only where the maker left no blanks on the paper.[50] For the acceptance of this distinction in the United States the leading case of *Vander Ploeg v. Van Zuuk*, decided in Iowa in 1907,[51] is largely responsible. Here the factual situation was substantially the same as that in the *Herdman* case which was cited and followed as the chief authority in point.[52] The defendant signed a piece of paper and gave it to X whom he authorized to fill it up as a note not in excess of two hundred dollars. X fraudulently wrote in two thousand dollars and made it payable to the plaintiff, who took in good faith. Following the *Herdman* decision, the Iowa tribunal held that under Section 14 a payee could not enforce a bill or note which had been completed by a third party unless the latter had done so in accordance with the authority given by the maker.[53] To support this conclusion the court argued that X, the intermediary, was no holder because as the paper was delivered to him it was not a note at all, but merely a blank form with the makers' names affixed. Section 14 permits the enforcement of an instrument such as the one at bar only if " . . . after completion, [it] is negotiated to a holder in due course. . . ." The court then reasoned that as a negotiation requires successive holders and X was not a holder, he could not negotiate to the payee within the mean of that Section.

This approach to the problem is open to attack on the following grounds: First: In determining whether X was a holder the logical procedure was to look to the definition of that term in Section 191, which clearly excludes X who was not the ". . . payee or indorsee . . . in possession . . . or the bearer. . . ." The court might thus have reached its conclusion as to X without any refer-

49. Windahl v. Vanderwilt, 200 Iowa 816, 203 N. W. 252 (1925); Stanley v. Davis, 32 Ky. Law Rep. 1135, 107 S. W. 773 (1908); Baumeister, Vollmer & Scott Bank v. Talbott, 129 Wash. 509, 225 Pac. 238 (1924); Rusmissell v. White Oak Stave Co., 80 W. Va. 400, 92 S. E. 672 (1917).

50. Consolidated Wagon & Machine Co. v. Housman, 38 Idaho 343, 221 Pac. 143 (1923) (recovery denied because paper wrongfully filled in by third party); *cf.* Redfield v. Wells, 31 Idaho 415, 173 Pac. 640 (1918) (recovery allowed in favor of payee where maker completed instrument); Vander Ploeg v. Van Zuuk, 135 Iowa 350, 112 N. W. 807 (1907) (court said payee could have recovered had maker completed instrument); Bank of Commerce & Savings v. Randell, 107 Neb. 332, 186 N. W. 70 (1921) (payee permitted to recover, but that right restricted to cases where maker left no blanks).

51. 135 Iowa 350, 112 N. W. 807 (1907).

52. *Id.* at 808.

53. *Id.* at 809.

ence whatever to the fact that the maker had left blanks in the instrument. Had the court pursued this course it would have appeared that X could not be a holder even if the paper was complete when he took it, and that, therefore, no particular difficulty was raised by the insertion of the factor "incompleteness" into the question of "negotiation by an intervening third party." Second: The *Vander Ploeg* decision and those that follow it concede that an indorsee is a holder in due course when he purchases paper that was filled in by the payee.[54] This conclusion, undeniably a correct one and everywhere the law, is justified by Section 14 which is properly held to mean that a holder in due course to whom paper is negotiated after its completion may enforce it as if it had been filled in according to the authority given. If, however, we consistently apply the rule that one must take completed paper in order to be a holder, this manifestly desirable end cannot be reached. A transferror-payee would not be a holder of an incomplete instrument, and under the rule that a negotiation requires successive holders, he could not negotiate to an indorsee. It is, therefore, at a sacrifice of consistency that the payee is denied recovery where the reason given is that the intermediary was not a holder because there were blanks on the paper when he took it. It is submitted that neither the statute nor the equities of the question can be said to support the distinction made by the Iowa court between the *Vander Ploeg* situation and the supposed case of an indorsee.

The practice is quite common for negotiable paper to be delivered to an intermediary conditionally or for a particular purpose and the question arises whether the payee takes subject to the limitation. Parties defending suits by payees in such cases often invoke Section 16 which says that "As between immediate parties, and as regards a remote party other than a holder in due course, the delivery . . . may be shown to have been conditional or for a special purpose only. . . . But where the instrument is in the hands of a holder in due course, a valid delivery thereof . . . is conclusively presumed." The defendants assert that the payee, being an immediate party, may not rest on the conclusive presumption of valid delivery and in a small number of cases the courts have agreed.[55] This contention is rejected by the prevailing weight

54. Johnston v. Hoover, 139 Iowa 143, 117 N. W. 277 (1908); Hornstein v. Cifuno, 86 Neb. 103, 125 N. W. 136 (1910) (indorsee permitted to recover where maker had not completed paper). See L. R. A. 1915B 1064 for a collection of cases gathered from all states and holding that in an action by an indorsee it is no defense that the party who filled in blanks exceeded his authority.

55. Bronson v. Stetson, 252 Mich. 6, 232 N. W. 741 (1930); Williams v. Jones, 52 S. W. (2d) 256 (Tex. Com. App. 1932); Kimball-Krough Pump Co. v. Judd, 88 S. W. (2d) 579 (Tex. Civ. App. 1935). In Vander Ploeg v. Van Zuuk, 135 Iowa 350, 356, 112 N. W. 807, 809 (1907), the court, though not citing Section 16, used the following significant language: ". . . the check was not delivered by the drawer as a valid and complete instrument . . . but it was given into his hands only for delivery to the payee in extinguishment of the drawer's debt to the payee." Referring to Section 21 of the English statute, which corresponds to our Section 16, the court in Herdman v. Wheeler wrote that "Payees and holders not in due course are . . . put on the same footing as regards proof of the authority of the person handing them the bill. In the present case, therefore, the delivery of the note to the plaintiff must, in order to enable him to recover, be under the authority of the defendant." [1902] 1 K. B. 361, 374.

of authority which holds that if the payee is a holder in due course under Sections 52, 30, and 191, he is not an immediate party within the meaning of Section 16.[56] As was said in *Liberty Trust Co. v. Tilton*,[57] the leading case in point, " . . . 'immediate parties' excludes a party who is a holder in due course. . . . These words must be confined to parties who are immediate to the conditions or limitations placed upon the delivery in the sense of knowing or being chargeable with notice of them. A payee who is a holder in due course is not an immediate party in the sense of that section." This test of immediacy seems sound in principle and is also likely to do justice in cases where harm would result if it were held that a payee is always an immediate party.

*The Affirmative View*

By the great preponderance of authority a payee of a negotiable instrument is elegible to be a holder in due course, and his right to occupy that status is not subject to any qualifications which do not apply to an indorsee.[58] This conclusion is reached by giving to the word negotiated in Section 52 (4) not the narrow interpretation of a transfer between successive holders, but by construing it in the light of the broad first sentence of Section 30. The consequences of this approach are twofold: any transfer is a negotiation if it is made " . . . in such manner as to constitute the transferee the holder . . . ";[59] and "An instrument is negotiated when it is transferred from one person to another . . ." regardless of whether the transferror is a holder.[60]

56. Liberty Trust Co. v. Tilton, 217 Mass. 462, 105 N. E. 605 (1914); National Investment & Security Co. v. Corey, 222 Mass. 453, 111 N. E. 357 (1916); Bank of Commerce & Savings v. Randell, 107 Neb. 332, 186 N. W. 70 (1921) (citing and following Tilton case); see BRANNAN, NEGOTIABLE INSTRUMENTS LAW (5th ed. 1932) 489 for a discussion of Section 16 in reference to this problem. "The obligation of all makers . . . is to pay to the holder for value according to the terms of the bill or note. Their obligation is primary and absolute. . . . The act makes no provision for the proof of another and different relation than that expressly undertaken and defined by the tenor of the instrument signed." Price v. Klett, 255 Mich. 354, 358, 238 N. W. 253, 254 (1931). *Cf.* Portland Morris Plant Bank v. Winckler, 127 Me. 306, 143 Atl. 173 (1928) (court of opinion payee can be holder in due course when not immediate to conditions under which paper was drawn); see Empire Trust Co. v. Manhattan Co., 97 Misc. 694, 697, 162 N. Y. Supp. 629, 631 (1st Dep't 1916).

57. 217 Mass. 462, 464, 105 N. E. 605 (1914).

58. "If a payee cannot be a holder in due course, the universal mercantile custom and the overwhelming weight of authority have been upset by the act. . . . But no such construction of the act is warranted." BRANNAN, NEGOTIABLE INSTRUMENTS LAW (4th ed. 1926) 120. Boston Steel & Iron Co. v. Steuer, 183 Mass. 140, 66 N. E. 646 (1903); Drumm Const. Co. v. Forbes, 305 Ill. 303, 137 N. E. 225 (1922) 26 A. L. R. 764 (1923); Ann Arbor First Nat. Bank v. Wuerth, 262 Mich. 691, 247 N. W. 784 (1933).

59. Thorpe v. White, 188 Mass. 333, 74 N. E. 592 (1905); Maurer v. Hahn, 105 N. J. L. 494, 145 Atl. 316 (1929); Howard Nat. Bank v. Wilson, 96 Vt. 438, 120 Atl. 889 (1923); see Pan-American Bank & Trust Co. v. National City Bank, 6 F. (2d) 762, 767 (C. C. A. 2d 1925).

60. For cases holding a maker's transfer to a payee to be valid negotiation, see *Ex Parte* Goldberg & Lewis, 191 Ala. 356, 67 So. 839 (1914) L. R. A. 1915 F 1157; Colonial Fur

Only rarely, however, do these opinions venture an explanation as to the reason why two particular types of negotiation were enumerated in the second sentence of Section 30. The most cogent argument yet to be made on this point is that the second sentence prescribes the methods by which a person who is a holder may negotiate, but that one other than a holder is not thereby precluded from effecting such a transfer.[61]

An abundance of common law decisions in favor of the payee has had much to do with bringing about the general acceptance of that conclusion under the present enactments in England and the United States.[62] By way of proof of the fact that the statutes were not intended to change the prior law on our question it is shown that Chalmers, the draftsman of the Bills of Exchange Act, has cited[63] as an illustration of a holder in due course, *Watson v. Russell*,[64] a leading English common law case wherein the payee was held to occupy that status. This opinion of Chalmers is set forth with emphasis in *Boston Steel & Iron Co. v. Steuer*, the first case under the N.I.L. wherein our question arose.[65] *Herdman v. Wheeler* is rejected by the Massachusetts tribunal which decided this case, and one of the reasons given is that *Watson v. Russell* " . . . does not seem to have been before the court . . . " in the argument on the *Herdman* controversy.[66] It is further contended in the *Steuer* case that the result of *Herdman* decision is commercially inexpedient and that the court had not " . . . taken into consideration the practice of a check being procured drawn by another to be used in paying a debt due from the person procuring the check to the person to whom the debtor has had the check made payable. The practice is recognized in the case of foreign bills of exchange, and the person procuring the bill is known technically as the 'remitter' of it. . . . In our opinion, a check received by the payee named in

Ranching Co. v. First Nat. Bank of Boston, 227 Mass. 12, 116 N. E. 731 (1917); American Nat. Bank v. Kerley, 109 Ore. 155, 220 Pac. 116 (1923); Johnson v. Knipe, 260 Pa. 504, 105 Atl. 705 (1918). In these cases the transfer by an intermediary was a valid negotiation to a payee: McLaughlin's Store v. Copeman, 50 Idaho 214, 294 Pac. 523 (1930); Farmers' State Bank of Craig v. Lydick, 112 Neb. 586, 200 N. W. 50 (1924); Brown v. Brown, 91 Misc. 220, 154 N. Y. Supp. 1098 (N. Y. City Ct. 1915) (third party had stolen paper); Gulf Live Stock Ins. Co. v. Love, 181 S. W. 766 (Tex. Civ. App. 1915); Helper State Bank v. Jackson, 48 Utah 430, 160 Pac. 287 (1916).

61. Liberty Trust Co. v. Tilton, 217 Mass. 462, 105 N. E. 605 (1905); Merchants' Nat. Bank v. Smith, 59 Mont. 280, 196 Pac. 523 (1921).

62. The common law rule in favor of the payee is stressed in Boston Steel & Iron Co. v. Steuer, 183 Mass. 140, 145, 66 N. E. 646, 647 (1903); "It is inconceivable that it was the purpose of the act to work a change in the law so radical without an express declaration to that effect, and we ought not to draw the inference that such a result was contemplated unless compelled by the weightiest considerations." Merchants' Nat. Bank v. Smith, 59 Mont. 280, 296, 196 Pac. 523, 527 (1921); Brown v. Brown, 91 Misc. 220, 222, 154 N. Y. Supp. 1098, 1099 (N. Y. City Ct. 1915); American Nat. Bank v. Kerley, 109 Ore. 155, 192, 220 Pac. 116, 128 (1923); Snyder v. McEwan, 148 Tenn. 423, 428, 256 S. W. 434, 436 (1924).

63. CHALMERS, BILLS OF EXCHANGE (5th ed. 1889) 89.

64. 3 B. & S. 34, 122 Eng. Reprints 14 (Q. B. 1862).

65. 183 Mass. 140, 144, 66 N. E. 646, 648 (1903).

66. *Ibid.*

it, in payment of a debt due from the remitter of the check, is a holder in due course. . . . "[67] As an additional reason for denying recognition to *Herdman v. Wheeler,* the opinions point out the fact that that decision was substantially overruled in England before a single American court followed it.[68] The contention that the payee, though he is a holder, cannot be one in due course because he took by issuance and not by negotiation is ably answered in the decisions of the majority. Section 59 says that "Every holder is deemed prima facie to be a holder in due course." Apparently, then, a payee in possession, being a holder is potentially one in due course in spite of the fact that the transfer to him was an issuance.[69] Section 50 lends color to the view that the transfer to the payee, even though it is defined as an issuance, may also be a negotiation. It provides: "Where an instrument is negotiated back to a prior party, such party may . . . reissue and further negotiate the same." Under this provision when paper is reacquired by a former owner he may transfer it to another party. That transfer operates as a reissuance and, at the same time, is a negotiation. Thus the terms issuance and negotiation are not mutually exclusive.[70]

One notices, upon examining the cases on the question, that the conclusions may be classified in the following manner: (1) In a few jurisdictions the payee can never be a holder in due course because the transfer to him is not a negotiation within the meaning of Section 52 (4); (2) A small number of other courts are of the opinion that a payee is eligible to be a holder in due course, provided that he purchases the bill or note from an intermediary who had taken it as a complete instrument; (3) In the great majority of states the payee's right to be a holder in due course is not subject to any qualifications which do not apply to an indorsee. Admittedly, the ambiguities of the applicable statute are responsible for the divergence of opinion. However, it is interesting to note that the statutory constructions unfavorable to the payee are confined almost exclusively to those states where commerce and credit financing are present, if at all, only on a small scale.[71] If it is true

67. *Ibid.*

68. Before Vander Ploeg v. Van Zuuk was decided in this country, Herdman v. Wheeler was disapproved in England in Lloyd's Bank v. Cooke [1907] 1 K. B. 794. Since the latter decision the Herdman case has not been followed by the English courts. Glenie v. Bruce Smith [1908] 1 K. B. 263; Talbot v. Von Boris [1911] 1 K. B. 854. See *Ex Parte* Goldberg & Lewis, 191 Ala. 356, 363, 67 So. 839, 841 (1914); Howard Nat. Bank v. Wilson, 96 Vt. 438, 120 Atl. 889, 891 (1923); Hening, *The Uniform Negotiable Instruments Law* (1911) 59 U. OF PA. L. REV. 471, 479.

69. See Merchants' Nat. Bank v. Smith, 59 Mont. 280, 293, 196 Pac. 523, 526 (1921); F. S. Royster Guano Co. v. Sherman, 151 Atl. 382, 383 (Sup. Ct. N. J. 1930); Belt v. Smith, 264 S. W. 1027, 1029 (Tex. Civ. App. 1924); Howard Nat. Bank v. Wilson, 96 Vt. 428, 449, 120 Atl. 889, 893 (1923).

70. This point is discussed at length in Moore, *The Right of the Remitter of a Bill or Note* (1920) 20 COL. L. REV. 749, 762.

71. The payee's right to be a holder in due course is either denied or qualified in Florida, Georgia, Indiana, Iowa, Kansas, Kentucky, Missouri, Nebraska, North Carolina, Oklahoma, South Dakota and Texas. For a separate treatment of the law of each state see BRANNAN, NEGOTIABLE INSTRUMENTS LAW (5th ed. 1932) 487-502. See also Feezer, *Payee as a Holder in Due Course* (1925) 9 MINN. L. REV. 101.

that the courts which take the prevailing view do so in regard for the needs of the business community, that factor may play an important part in the trend of the decisions that are to follow.

*The Law in New York*

In a commercial and financial center such as New York our question is of unusual importance, and since this jurisdiction is not as yet finally committed to a choice between conflicting views, the present state of the case law merits attention. The proposition has apparently been accepted by the lower courts that where an instrument is delivered conditionally to a third party, who transfers it free of the condition to a bona fide payee, the latter may be a holder in due course.[72] From these decisions it seems fair to assume that protection would be given the payee in the more common situation where the paper involved was that of a commercial firm and the payee's transferror was or had purported to be an intermediate purchaser.

In another case a thief stole an instrument and, by representing himself as the maker's agent, obtained certain stamps from the payee, giving the stolen check in payment. The thief then absconded with the stamps. An action on the check was brought by the payee, which claimed to be a holder in due course.[73] In its defense the maker argued that the plaintiff was not a holder in due course but was an immediate party under Section 16 and could not recover because the paper had not been validly delivered to it. The court, following *Liberty Trust Co. v. Tilton,* held that an immediate party is one who knows or is chargeable with knowledge of the conditions or limitations placed upon the delivery of the paper. Applying this test, the court said that the plaintiff was an immediate party because it knew that the maker did not intend to part with the check unless it received the stamps in return.[74] The court then denied recovery on the ground that the check had never been delivered, conditionally or absolutely, by any party to it. There having been no delivery, it follows that the plaintiff did not take by a negotiation and so could not be a holder in due course. Although the court refused to permit the payee to recover, this case cannot fairly be regarded as supporting the minority rule. On the contrary, the refusal to hold that a payee is, as a matter of law, an immediate party, indicates that the court did not mean to rule that a payee can never be a holder in due course.

The courts have been confronted also with the situation in which a wrongdoer, W, forged on a note the names of Y as maker and Z as payee and, representing himself to be the agent of Y used the note as security to obtain a loan from Z in behalf of his alleged principal. Z gave the loan in the form of a check payable to Y and entrusted it to W for delivery. W then gave Y the check, not for the authorized purpose but in satisfaction of his own debt. Z was permitted to recover from Y the amount of the check on the

72. Brown v. Brown, 91 Misc. 220, 154 N. Y. Supp. 1098 (City Ct. 1915); see Empire Trust Co. v. Manhattan Co., 97 Misc. 694, 699, 162 N. Y. Supp. 629, 632 (Sup. Ct. 1916).

73. Empire Trust Co. v. Manhattan Co., 97 Misc. 694, 162 N. Y. Supp. 629 (Sup. Ct. 1916).

74. *Id.* at 701, 162 N. Y. Supp. at 634 (Sup. Ct. 1916).

theory that it had been paid under a mistake of fact.[75] To all appearances it would seem that the case squarely raised the question of whether Z, payee, could defend by claiming to be a holder on due course under the N.I.L. Instead, the court proceeded on the theory that Y, seeing W in the ambiguous position of one in possession of paper that on its face bore no evidence of his right, was on notice to inquire into the history of the instrument and, taking without inquiry, had been unjustly enriched.[76] Although the payee was charged with constructive notice of defects in the paper, the decision does not indicate that New York's highest court will construe the statute to mean that a payee always takes subject to personal defenses. No such inference should be predicated upon this case, for the statute was neither pleaded in bar nor cited by the court.[77] Moreover, although the decision preceded most of the lower court cases on our question and would, therefore, be controlling if it were in point, it has not been cited in a single one of them. So far as now appears the only relation which this case can possibly bear to the problem of whether a payee can be a holder in due course is that on facts such as those he is deemed to have taken in bad faith.

The opinions of the New York cases show, on the whole, a marked tendency to abandon the N.I.L. as a possible source of a solution. Since the statute did not contemplate a situation involving an intermediary[78] and in view of what experience other jurisdictions have had with arguments based on construction this departure may not be unwise. One notices also an inclination to view the facts from the standpoint of how they appeared to the payee, and to let him recover where, from a business point of view he was quite as far removed from the origin of the paper as an indorsee would be.[79] It is probably true, that the chief inquiry of the courts has been directed to the matter of bad faith. Contrary to what is the situation in most other states, the approach that the New York courts have taken augurs well for a solution which, if not conformable with the language of the ill-suited statute, will at least provide protection where commercial expediency so requires.

### *Conclusion*

As might be expected, a number of attempts have been made in the interest

75. Hathaway v. County of Delaware, 185 N. Y. 368, 78 N. E. 153 (1906) 13 L. R. A. (N. S.) 273.

76. *Id.* at 373, 78 N. E. at 155 (1906).

77. Professor Brannan believes that because the *Hathaway* case did not cite the N. I. L. it may have rested on its special facts. BRANNAN, NEGOTIABLE INSTRUMENTS LAW (5th ed. 1932) 496. The case is also disapproved in (1912) 23 BANKING L. J. 595.

78. ". . . The exceptional status of a payee is a casus omissus." *Ex Parte* Goldberg & Lewis, 191 Ala. 356, 367, 67 So. 839, 843 (1914).

The statute was framed with the thought of protecting the innocent indorsee and does not deal with the signer's duty to the payee; see Moore, *The Right of the Remitter of a Bill or Note*, 20 COL. L. REV. 749, 754 (1920).

79. "It may be that the payee named in a note is so separated from the consideration of the note that he may still have the right of a purchaser for value of commercial paper." Miller v. Campbell, 173 App. Div. 821, 824, 160 N. Y. Supp. 834, 841 (1st Dep't 1916); see Empire Trust Co. v. Manhattan Co., 97 Misc. 694, 699, 162 N. Y. Supp. 629, 632 (Sup. Ct. 1916); Bergstrone v. Ritz-Carlton Restaurant and Hotel Co., 171 App. Div. 776, 780, 157 N. Y. Supp. 959, 962 (1st Dep't 1916).

of certainty and practical efficacy to set forth categorical statements of possible solutions to the problem. The legislature of West Virginia, for example, has altered Section 52 so that it now reads: "A holder in due course is a holder *including a payee* who has taken the instrument under the following conditions:"[80] In the absence of judicial interpretation the true effect of this change is, of course, highly conjectural, but its apparent effect is to place the payee on an equal footing with an indorsee. Such a rule may be regarded as too broad. An indorsee is assumed to look upon commercial paper as currency, and thus his good faith is not easily impeached. There is less reason, however, to look upon a payee in this light. Only where the paper is that of a business institution does an intermediary, in the usual course of business, obtain possession of it. Ordinarily the payee deals directly and exclusively with the maker and in such a situation he can easily avail himself of facts concerning the history of the instrument, which an indorsee, however diligent, could never discover. It is advisable, therefore, that a payee be subject to more exacting obligations of good faith and due care than are applied to those whose names do not appear upon the face of the instrument.

Professor Chafee has submitted the suggestion that the first clause of Section 52 be changed to read: "A holder in due course is a *payee or other holder* . . ." And that (4) be amended as follows: "that at the time he *became a holder* he had no notice of any infirmity in the instrument or *that* the title of the person *negotiating* it *was defective or that the delivery to* himself was wrongful."[81] Possibly these modifications might solve the problem, but not without difficulty, for any holder, including an indorsee, would face the new task of establishing that he did not know the delivery to himself was wrongful. Besides, much diversity of interpretation would be invited by the use of language requiring the courts to determine what is a wrongful delivery.

In a most ably written paper Professor Aigler proposes that a payee be held a holder in due course when he takes the instrument as a "purchaser", that is, when he buys it from one who does not appear to be an obligor on the face of the paper itself; but that protection be denied to a payee who takes paper as a "promisee", having bought it from a promisor, *e.g.*, the maker.[82] Under this rule a payee could not recover in an action against an accomodator who pleaded the maker's fraud as a defense, where the plaintiff had taken the instrument from the maker himself. Here, very likely, the maker would be a "promisor" and yet to deny recovery might seriously impair the negotiability of commercial paper.

In view of the hazardous nature of the undertaking, no concrete solution of the problem will herein be attempted. All that can be ventured with any firmness of conviction is that the payee's relationship, from a business point of view, to the transaction in which the paper is drawn seems to be a proper basis on which to discriminate between cases where he should be protected and those in which a knowledge of personal defenses ought to be imputed to him.

80. OFFICIAL CODE W. VA. 1931 § 46-4-2.

81. BRANNAN, NEGOTIABLE INSTRUMENTS LAW (4th ed. 1926) 361.

82. Aigler, *Payees as Holders in Due Course* (1927) 36 YALE L. J. 603.