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THE NEGOTIABLE INSTRUMENTS LAW.

(A REVIEW OF THE AMES-BREWSTER CONTROVERSY.)

Second Paper.

In the August number of the REGISTER I commenced a review of the interesting articles published in the *Harvard Law Review* and in the *Yale Law Journal* by Professor James Barr Ames, Dean of the Harvard Law Faculty, and Judge Lyman D. Brewster, President of the Conference of Commissioners on Uniform State Laws, discussing certain sections of the Negotiable Instruments Law. The present article proceeds with the discussion.

Section 22:

"The indorsement or assignment of the instrument by a corporation or by an infant *passes the property therein*[1] notwithstanding that from want of capacity the corporation or infant may incur no liability thereon."[1]

[1] The italics are inserted by the reviewer.

Professor Ames says, "Does this section, like the corresponding section of the English act,[2] mean merely that the indorsee has the right to enforce payment from all parties prior to the infant, or does it mean that the indorsee becomes absolute owner of the instrument, so that he and his transferees, whether with or without notice of the infancy, may retain the instrument even against the infant? If it was intended to reproduce the effect of the English act on this point, it is unfortunate that the unambiguous language of that act was not retained. If, on the other hand, it was intended to make the infant's transfer of negotiable paper irrevocable, the section introduces a radical change in the law as to the rights of infants, and one that goes unnecessarily far in protecting an indorsee who knows that he is dealing with an infant."

There are two criticisms here. The first is that the language is ambiguous and may mean that the infant's indorsee takes an *indefeasible* title. As a proof of this, Professor Ames states that some members of Judge Brewster's committee assured him that this was the purpose of the section. Judge Brewster replies that the American and English acts mean the same thing and that he never heard of any other interpretation.

It is to be regretted that Professor Ames does not indicate the reasoning by which this section could be interpreted as giving an indefeasible title. It is the practically universal rule with us that an infant's acts are voidable merely and not void.[3] Of course then, when he indorses a note he "passes the property therein." That is simply stating what has been the law for years. Without discussing whether he is or ought to be permitted later to annul his act, it is clear that his indorsement, which certainly is not void,

[2] English Bills of Exchange Act, Sec. 22 par. 2: "Where a bill is drawn or indorsed by an infant, minor, or corporation having no capacity or power to incur liability on a bill, the drawing or indorsement entitles the holder to receive payment of the bill, and to enforce it against any other party thereto."

[3] In England by the Infant's Relief Act, 37 and 38 Vict., Ch. 62 (1874) the common law rule is abrogated to the extent of making the contract of an infant absolutely void. But throughout the United States the common law rule that it is voidable merely, prevails universally.

"passes the property" in the note. As to his right to revest the title in himself, the act is silent. Now, a statute which decides one point and leaves another point untouched, is not ambiguous. Nor does Professor Ames tell us why the English act is any different from ours. The language there used is that the infant's indorsement "entitles the holder to receive payment of the bill, and to enforce it against any other party thereto." But to enforce payment the holder must have title to and possession of the bill. Therefore the English act provides that the indorsement "passes the property." Moreover, that is all it does provide. It does not provide that the holder may enforce it only until the infant avoids his act and reclaims the instrument. On that point, it is as silent as our act. Yet the critic would have us believe that under the English act the infant clearly may reclaim the instrument, but that our act is ambiguous on this point. Both acts provide exactly the same thing, and since it appears never to have been specifically decided whether an infant may reclaim a negotiable instrument that he has indorsed, both acts are precise codifications of existing law.

In the absence of authority on that point, the framers of the American and English acts did well to leave the question untouched. Whether they did so unintentionally or not is of small moment. Professor Ames is of opinion that the infant should be allowed to reclaim the instrument as against a holder with notice, but not as against a holder in due course.[4] Probably all would agree that the title of the holder in due course should be indefeasible. The importance of preserving the untrammelled negotiability of bills and notes leads some to conclude that even a holder with notice should be protected as against the infant. The point is that this question is within the province of a judge and not within the province of those engaged in *codifying* the law.

Section 23:

"When a signature is forged or made without the

[4] See also Ames' Cases on Bills and Notes, Vol. 2, title "Infancy" p. 840, and title "Transfer" (18) on p. 881.

> authority of the person whose signature it purports to be, it is wholly inoperative and no right to retain the instrument, or to give a discharge therefor, or to enforce payment thereof against any party thereto, can be acquired through or under such signature, unless the party against whom it is sought to enforce such right is precluded from setting up the forgery or want of authority."

In a supplementary note, published subsequently to the articles in the *Harvard Law Review,* Professor Ames says that the need of amending Section 23 is shown by the case of *Tolman* v. *American National Bank,*[5] decided by the Supreme Court of Rhode Island in March, 1901.

An interesting line of cases is involved in the discussion of this section. Suppose A., falsely representing himself to be B., a citizen of X. town, goes to C. for a loan. C. makes inquiry concerning B., and finding him to be a prosperous and responsible merchant of X. town, hands A. a check payable to the order of B., whom he supposes that A. is. A. indorses the check in B.'s name and A. or his indorsee has it cashed. The question then comes up between the bank and C. (the drawer) as to who shall bear the loss. This set of facts, with strikingly few variations, has been presented in numerous cases, all of them, prior to the case of *Tolman* v. *American National Bank,* holding that C. must bear the loss.[6]

[5] 48 Atl. R. 480.

[6] *U. S.* v. *Nat. Bank,* 45 Fed. R. 163; *Meyer* v. *Indiana Bank,* 61 N. E. Rep. 596; *Emporia Bank* v. *Shotwell,* 35 Kan. 360; *Robertson* v. *Coleman,* 141 Mass. 231; *First Bank* v. *American Bank,* 49 N. Y. App. Div. 349; *Merch. Bank* v. *Metropolitan Bank,* 7 Daly, 137; *Land Title and Trust Co.* v. *N. W. Bank,* 196 Pa. 230; *Metzger* v. *Franklin Bank,* 119 Ind. 359.

And see *Meridian Bank* v. *First Bank,* 7 Ind. App. 322; *Elliott* v. *Smitherman,* 2 Dev. & B. (N. C.) 338; *Frebis* v. *Espy,* 21 Oh. 474, in which, though the name adopted by the swindler appears to have been really fictitious, the loss is thrown on the drawer for the same reason as that which governed the former cases.

The same rule prevails as to the sale of chattels: *Edmonds* v. *Merch. Co.,* 135 Mass. 283; *Samuel* v. *Cheney,* 135 Mass. 278; *Dunbar* v. *Boston F. R. Co.,* 110 Mass. 26; *Alexander* v. *Swackhamer,* 105 Ind. 81.

This result may be reached in several ways; none of which are without difficulty.

1. You may hold that A., albeit he is representing himself by a name falsely assumed for the purpose of deceiving C., is the real payee, the person to whom C. intended that the check should be paid. Under this view, any question as to C.'s negligence becomes immaterial. He must bear the loss, not because he has negligently trusted a stranger, but because the physical person who stood before him and with whom he dealt is the person whom he intended the bank should pay. The difficulty with this view is that although C. intended that the money should be paid to the person standing before him, it is equally true that he intended that it should be paid to B. of X. town.

2. You may hold that the drawer is liable because he has negligently trusted a stranger, but this view is unsatisfactory because none of the cases in point go on this ground, and because the loss is thrown on C., even when he has admittedly exercised all reasonable diligence.

3. You may hold that the payee is fictitious, and that the check is therefore payable to bearer; but such an instrument is payable to bearer only when the drawer knows that the payee is fictitious. Moreover, if B., of X. town, is in existence and known to the drawer, such a view is clearly untenable.

4. You may hold that C. is estopped to deny that A., to whom he gave the check, is the real payee. But *estoppel* cannot operate unless the fact represented be known to and acted on by the bank, and where the swindler indorses the check to a bona fide holder who cashes it (and this is what

A case interesting (though not quite in point) in connection with the rule here discussed is *Gravis* v. *The American Exchange Bank,* 17 N. Y. 205, which holds that if a check be made payable to one person and another person of precisely the same name or initials, so far as these are written out in the check, comes wrongfully or accidentally into possession of the same, indorses it, and obtains the money on it from the bank, still the bank is liable to make good the amount to the drawer. Possibly this carries the bank's liability to an excessive point. It would seem that the drawer, having represented that any man named John Smith is the payee, should be estopped to deny that the particular John Smith who indorsed the check and had it cashed is the payee.

happened in most of the cases) the bank knows nothing of the delivery to A. and does not rely on the drawer's representation that he is the payee.[7]

As a matter of fact, the courts base their decision on the first ground, namely, that the bank has merely carried out the drawer's intent. Here and there an expression may be singled out which seems to countenance one or more of the other views, but a fair reading of the opinions shows that one idea dominates nearly all of them, namely, that the money has been paid to the person for whom it was really intended. The reasoning is briefly this: A man's name is the verbal designation by which he is known, but the man's visible presence affords a surer means of identification. C. was deceived as to the man he was dealing with, but he dealt with and intended to deal with the visible man who stood before him, identified by sight and hearing. Thinking that this man's name was B., he drew the check to B.'s order intending thereby to designate the person standing before him; so the bank has simply paid the money to the person for whom it was intended.

Such was undoubtedly the law prior to the act. By Section 23, when a signature is forged or made without the authority of the person whose signature it purports to be, it is wholly inoperative except as against the person who "is precluded from setting up the forgery or want of authority." In the light of the cases above referred to, the meaning of this section, as applied to the point under discussion, seems reasonably clear. The drawer (C.) "is precluded from setting up the forgery or want of authority" and so the signature is not inoperative as to him and the law remains unchanged.

[7] However, in an interesting note to *Land Title and Trust Co.* v. *Bank*, 50 L. R. A. 83, the above objection to the estoppel theory is claimed to be invalid, the argument being: When the bank pays a check upon a forged indorsement it acts on the belief that the person who indorsed it was the person whom the drawer intended to designate as payee. This belief is largely—and when the person who presents the check is not identified—is solely induced by the fact that the check is, or was at the time of indorsement, in the impostor's possession. The drawer—by delivering the check to the impostor in the belief that he is the person named as payee—creates the appearance on which the bank acts.

In 1899, Rhode Island adopted the Negotiable Instruments Law and in 1901 the case of *Tolman* v. *American National Bank* arose in that state.

In that case, one Louis Potter, representing himself to be Ernest A. Haskell, went to the plaintiff (Tolman) for a loan of money, giving the occupation and residence of Haskell as his own. The plaintiff made inquiry, and finding that Haskell was employed and was living as represented, gave Potter his check on the defendant bank payable to the order of Haskell. Potter indorsed Haskell's name and delivered the check to one A. R. Hines, who had it cashed at the bank. In an action by Tolman to compel the bank to credit him with the amount of the check, the court held that the bank must bear the loss.

As Professor Ames remarks, "the decision is a surprising one, both from the standpoint of common law principles, and of Section 23 of the act. All the reported cases on the point of fraudulent impersonation are against the decision. As a statutory question, but for this decision, the liability of the drawer would seem clear under the last clause of the section."

It is worth while to analyze the opinion of the court. It divides itself into three parts, and the reasoning of the learned Chief Justice Stiness may be summarized as follows:

1. When a bank receives money, it is to be paid out only as the depositor shall order. Therefore, if it pays on a forged indorsement, it bears the loss, unless the depositor is estopped by negligence from alleging the forgery. Therefore, *since Tolman intended that the money should be paid to the order of Haskell, and since Haskell has not indorsed the check, and since the plaintiff has not misled the defendant, the bank must bear the loss.*

2. The above reasoning represents what the law was "when, a few years ago, it seems to have been switched off on a fallacy in some places." To show that this formerly was the law, the learned judge cites three English and four American cases, not one of which presents the point involved in *Tolman* v. *The Bank*. Coming, then, to the line of cases involving substantially the same facts as *Tolman* v. *The*

Bank, in all of which the drawer was held liable, the learned judge says that these are based on a manifest fallacy and ignore the distinction between fictitious and real payees.

3. Section 23 brings the law back to where it was before it was "switched off on a fallacy." An application of this section to the case at bar shows this. The signature here is clearly one "made without the authority of the person whose signature it purports to be." Therefore, it is wholly inoperative except as against a person who "is precluded from setting up the want of authority." But Tolman is not precluded, for he has been guilty of no conduct which misled the bank and so is not estopped from showing that the bank did not pay as directed.

Judgment for Defendant.

Three observations may be made on this opinion:

1. In stating what the law was before it was "switched off on a fallacy" the learned judge is really stating what in his opinion the law should have been. There is no case in point to sustain him. Prior to the cases against his view, there are no cases in point at all.

2. As to "the manifest fallacy" in which the uniform current of authority has its source, the learned judge says that it is caused by ignoring the distinction between real and fictitious payees—that in the latter case, there can be no one in the mind of the drawer other than the person with whom he is dealing—but that *"in the case of a real person, one party having him in mind satisfies himself about the responsibility of such party and supposes that he is dealing not with the person who is in fact before him, but with the one whom he has in mind."* But the numerous cases which oppose the learned judge go on the ground that *the real person whom the drawer has in mind is the man standing before him.* True, this ignores the fact that the drawer supposed him to be B., of X. town, but the other view ignores an equally important fact, *i. e.* that he intended to deal with and lend the money to the person standing before him. One view is about as satisfactory as the other in interpreting the drawer's real intention. Moreover, the view which holds the drawer liable, in case B., of X. town, does not exist, even though the drawer made all reasonable inquiry and

was deceived into believing that he did exist, but protects him in case B., of X. town, is in existence, makes a distinction which does nothing to increase the actual justice meted out.

3. When a *code* is, as here, entirely in accord with a settled rule of law, what justification is there for holding that it meant to upset that rule and establish one which never was the law?

Judge Brewster replies, "The exact point in *Tolman* v. *Bank* was simply this: was it 'precluding' negligence for Tolman to trust the stranger Potter, with no further inquiry than that stated in the opinion? On this precise point as to a 'stranger payee' there are but two exact precedents.[8] The first is *National Bank* v. *Nolting*.[9] This case holds the bank liable, saying, 'To hold that giving a check to a stranger . . . was sufficient . . . evidence to excuse the bank . . . would be to relieve the bank from a just responsibility.' The second case is *Smith* v. *Mech. Bank*.[10] This case, by a divided court, held the bank not liable."

Of this defence, it may be observed first, while the lack of negligence may have been the ground on which the decision in *Tolman* v. *Bank* was based, it was not, according to all the cases in point, the question really involved. The well-settled rule applicable to these facts renders the question of negligence wholly immaterial because it declares that Potter was the real payee. Admit that he is not the payee, then the drawer is liable only in case he is estopped. But the latter view has never been the law. Thus it is that in the numerous cases which are exact precedents on this point, though the degree of care exercised by the drawer differs, the decisions are the same, for the very reason that they proceed on a ground which renders negligence immaterial.

Second, the two cases cited by Judge Brewster are not precedents at all. *National Bank* v. *Nolting* was a case of the *alteration* of a check, and the point decided was that

[8] 5 Amer. and Eng. Ency. of Law, Second Edition, 1066.
[9] 94 Va. 263.
[10] 6 La. Ann. 610.

the check, having been properly drawn, the mere fact that it was delivered to a stranger did not estop the drawer from showing that it had been raised from ten dollars to five hundred dollars. *Smith* v. *The Mech. Bank* comes somewhere nearer being in point, though it differs from *Tolman* v. *The Bank* in at least one vital particular. In the former case, the swindler did not represent himself to be P. & W., the firm in whose favor the check was drawn. It was made payable to P. & W., who were known to the drawer, for the very purpose of compelling the stranger concerning whom the drawer realized that he knew nothing, to go to P. & W. and get their indorsement. Of course, then, when the stranger forged their signature, the drawer could not be held liable on the ground that the stranger was the man to whom he intended to make the check payable.

Judge Brewster further remarks, "The theory of the Dean as to the drawer's expectation that the 'physical person before him' would indorse the note had already been shown to be a fallacy." Where and by whom? Not in any of the cases in which the question was raised and not in the two articles which Judge Brewster cites as bearing out his assertion.[11]

It is perfectly evident, then—and indeed this is Professor Ames' position—that the trouble is not with Section 23, but with the case of *Tolman* v. *The Bank.* Undoubtedly it is unfortunate that the only judicial interpretation that this section has received should serve only to throw doubt on what was previously well settled.[12] But the blame does not

[11] The admirable little article on "Loss by Check Delivered to Impostor," Case and Comment, Vol. I, No. 7, December, 1900, p. 75, cites no authorities, and although ably stating the difficulty of the "intention" theory, *i. e.*, that "The imposture make it impossible that both parts of his intent can be carried out," admits that most courts have adopted this view. Moreover, though agreeing with the result of the decisions, it advances no more satisfactory ground on which to base it, the estoppel theory being as open to objection as the intention theory. As for Judge Brewster's negligence theory, the article disposes of that in convincing fashion.

To the same effect is the note in 50 L. R. A. 83. Moreover, both of these articles agree that the *drawer* should bear the loss.

[12] It is not denied that much might be said in favor of the result

belong to the Negotiable Instruments Law. Section 23—copied from the English act—was, at the time of its adoption, an accurate statement of existing law, and in view of the unanimity that exists among the cases on which it is based, the doubts raised by *Tolman* v. *The Bank* will probably soon be dispelled and this section will be interpreted as having merely affirmed a well-settled rule.

Section 29:

> "An accommodation party is one who has signed the instrument as maker, drawer, acceptor, or indorser, *without receiving value therefor,* and for the purpose of lending his name to some other person. Such a person is liable on the instrument to a holder for value, notwithstanding such holder at the time of taking the instrument knew him to be only an accommodation party.[13]

The criticism is, "By this definition, one who has received a commission, which is certainly value, for lending the credit of his name, would not be an accommodation party. But no business man or good lawyer would sanction such a distinction. . . . To take a concrete case. A. offers B. ten dollars if he, B., will sign a note of $1,000 for A.'s accommodation. B. accepts the ten dollars and signs the note. Can anyone seriously doubt that B. is an accommodation party? If he is, the definition in this section is erroneous."

Judge Brewster's answer is that the definition of an accommodation party given in Section 29 is the same as the definition given by "all the cases, all the text writers, and all the encyclopedias, the law dictionaries and the ordinary English lexicons.[14] . . . The only reason given for the

reached in *Tolman* v. *The Bank,* did the question arise *de novo.* The point is that when once so difficult and doubtful a point is clearly settled, mischief and not good results from reopening the matter and involving it in doubt. As matters stand to-day, no lawyer could advise a client, with any certainty, on this point.

[13] This is a copy of Section 29 of the English Act.

[14] Judge Brewster refers to Amer. and Eng. Ency. of Law, Vol. I., pp. 335-36; I Daniel, 189; Tiedman, Sec. 158; Byles on Bills, Star, p. 131; II Randolph, 472; Norton's Horn-Book (1900), 176; Bigelow, Second Edition, cites the definition given by the Negotiable Instruments Law as the true definition; Standard and Webster Lexicons.

overthrow of all these authorities is an illustration intended apparently to demonstrate the difficulty of showing what is value and what is not, but which in reality indicates value on its face."

Professor Ames replies that Judge Brewster's answer only shows "that he and his colleagues erred in good company."

The last sentence quoted above from Judge Brewster leaves something to be desired from the standpoint of clearness, but apparently the judge thinks that under Section 29 B. (in the case supposed) is not an accommodation party.[15] A moment's reflection shows the error of this. B. ought to be regarded as an accommodation party. Though doubtless partially induced by the ten dollars to sign his name, his real purpose in signing (however that purpose may have been induced) was to lend credit to A. B. received nothing *for the note.* He did not become a holder for value of it. On the contrary, what he did receive came from his *transferor* (assuming that B. ever became the holder of the note at all) and the note was negotiated solely for A.'s benefit; who received the consideration paid for it. Moreover, B. is an accommodation party under Section 29. Mr. Cohen hits the nail squarely in stating the meaning of this section. " 'Without receiving any value therefor' means without receiving any value for the bill, and not *without receiving any consideration for lending his name.*" Thus B. is an accommodation party because he has received no value for the instrument, though he did receive ten dollars for signing his name to it.

Probably no harm would have resulted had the Commission adopted Professor Ames' suggestion and omitted the words "without receiving value therefor and," but since their insertion requires merely that proper care be exercised in interpreting the word "therefor," no difficulty need be anticipated on this point. It may be added that the same words used in the English act have proved entirely satisfactory.

[15] Mr. John L. Farrell also thinks that B. is not an accommodation party. See article in Brief of Phi Delta Phi, Vol. III, No. 20, Quarter (1901). But Mr. Farrell, like Judge Brewster, ignores the meaning of the word "therefor."

Section 34:

> "A special indorsement specifies the person to whom, or to whose order, the instrument is to be payable; and the indorsement of such indorsee is necessary to the further negotiation of the instrument. An indorsement in blank specifies no indorsee, and an instrument so indorsed is payable to bearer, and may be negotiated by delivery."

"This," says Professor Ames, "is an inadequate definition" because "it is nowhere stated that an indorsement, like the drawing of a bill, is an order. If the payee writes "I assign this note to B.," or "I guarantee to B. the payment of this note," is he liable as indorser on his assignment or guarantee? Is his transferee an indorsee, and therefore within the rule that gives a holder in due course title free from equitable defences? There are numerous but conflicting decisions on these points,[16] and it is unfortunate that the new code does not secure uniformity here as it does in the matter of notes payable with exchange or attorneys' fees."

Judge Brewster answers that "The liability of a party on a peculiar indorsement, which is outside of negotiability, must be settled by a court."

But, as Professor Ames replies, "The very point in controversy is one of negotiability." Some states hold that language such as that referred to above amounts to an indorsement—others hold that it does not—Professor Ames' point is that the code should have settled this disputed question as to negotiability and that it could have done so by

[16] "In ten states a payee who transfers a note by writing on the back, 'I assign this note to X.,' assumes the liability of an ordinary indorser. In six states such an assignor is not an indorser. In thirteen states the assignee, like an indorser, acquires title free from equities good against the assignor. In two states the assignee takes subject to such equities.

"In three states a payee who transfers a note by writing on the back, 'I guarantee the payment of this note to X.,' is liable as an indorser. In ten states he is not so liable. In thirteen states the transferee, like an indorsee, acquires a title free from equities good against the transferor. In three states and in the Supreme Court of the United States, the transferee takes subject to such equities."

stating in Section 34 that an indorsement, like the drawing of a bill, is an order.

Undoubtedly much would be gained by deciding once for all as to what expressions constitute an indorsement. But the question cannot be settled by enacting that an indorsement is an order. No one ever denied that an indorsement is, among other things, a direction to the maker or acceptor to pay the amount of the instrument to the indorsee, but some states hold that the words "I assign this note to B." amount to such a direction, while others hold that they do not. This is where the courts differ. Therefore, Professor Ames has merely shown that here is a disputed question left unanswered, without showing how it could have been answered by any provision sufficiently brief and accurate and comprehensive to be inserted in a code.

Section 36:

> "An indorsement is restrictive, which either (2) constitutes the indorsee the agent of the indorser; or (3) vests the title in the indorsee in trust for or to the use of some other person."

Professor Ames says, "Since the so-called 'agent of the indorser' has, under Section 37, the right to sue in his own name on the instrument, but for the benefit of the indorser, he is in truth a trustee, and not a mere agent. The Sub-section 2 and 3 should therefore be consolidated as follows: 'An indorsement is restrictive which vests the title in the indorsee in trust for the indorser or some third person.'"

Judge Brewster replies that although all agents are trustees in the sense that they are ultimately accountable to the principal, all agents are not technically trustees, and that the distinction between an agent and a trustee is embodied in Section 36 to relieve the plaintiff from proving an actual trust.

Of course the criticism of this sub-section deals simply with its form. Professor Ames does not mean that any difficulty can possibly arise under the language as it stands. He means merely that the substitute he offers is somewhat

shorter than the act and more technically correct. When A. indorses a note "Pay to B. for the use of C.," B. has always been termed a *trustee,* as of course he is. When A. indorses a note "Pay to B. for my use" or indorses "for collection" to B., B. has always been termed an *agent.* Professor Ames' point is that "agent" is no longer a correct word to use in describing B. in the latter case, *because* he can now, under Section 37, sue *in his own name* on the instrument, though for the benefit of the indorser. Thus Section 37 vests the legal title in the indorsee, and therefore, says the critic, he is in truth a trustee.

Possibly—though nevertheless it is not clear that the suggested change could have been made without the risk of some misunderstanding. An indorsement for collection has always been regarded as creating a mere agency. Title remains in the indorser, who may terminate the agency at any time before collection and reclaim the instrument. In most states, prior to the act, the agent, not having title, could not sue in his own name. In some, however, he could[17]—the indorsement being deemed to have conferred this authority—but the latter states, though deeming the agent to have received the legal title to an extent sufficient to enable him to sue in his own name, still speak of him and regard him as an *agent* whose authority may be revoked at any time. It is extremely unlikely that Section 37 intended to accomplish anything more than a procedural change. The indorsee for collection was to be allowed to sue in his own name; it was not intended to make any further change in his rights and duties—not intended to alter in any way the legal conception of the relationship that exists between him and his indorser. Was it not, therefore, the wise and safe course to retain the words whose meaning long use and repeated construction have rendered unmistakable? Why introduce a word which has never been used to describe an indorsee for collection even by courts which conferred on him the right to sue in his own name?[18]

[17] *Wilson* v. *Tolson,* 79 Ga. 137; *Boyd* v. *Corbitt,* 37 Mich. 52; *Moore* v. *Hall,* 48 Mich. 143.

[18] It may be added that by Section 35 of the English Bills of Exchange

Section 37: . . .

This section confers upon the indorsee under a restrictive indorsement the right to bring any action that the indorser can bring.[19] "Inferentially," says Professor Ames, "such an indorsee cannot sue his indorser. This is just, if the instrument was transferred to the indorsee for the benefit of the indorser. But unjust, if the indorsement was for value to the indorsee in trust for a third person." For instance, "A., the holder of a note payable to his order, sells it to B. and is about to indorse it to him, but, at B.'s request, indorses it to X. in trust for B., instead of to B. directly. At maturity of the note, the maker is insolvent, but A. is solvent. By this section, X., the indorser, may sue anyone that his indorser can sue. In other words, he may sue the insolvent maker, but he cannot sue the solvent indorser, A."

The ground upon which Judge Brewster finally rests his defence of this section is "the fact that no trouble has arisen under it in England sufficiently indicates that the immunity the Dean claims for the solvent indorser 'A.' does not exist. Equity would take care of that."

It is too plain for discussion that X., in the case supposed, should have a right of action on the note against the solvent indorser A. How "equity would take care of that" does not appear. Unless X. has his action under a proper construction of this section it is difficult to see how equity could mend matters.

Mr. Farrell makes a useful contribution on this point. He says, "The language of Section 37 is used in a permissive and not in a restrictive sense. Section 36 defines a restrictive indorsement, which limits and circumscribes the utility of the instrument so indorsed as compared with paper which does not bear this qualified indorsement. The following section (37) states the effect of such an indorsement, and

Act, a restrictive indorsement, although it confers on the indorsee the right to sue in his own name, is, nevertheless, regarded as a mere authority to deal with the bill and not as a transfer of the ownership thereof.

[19] Section 37: "A restrictive indorsement confers upon the indorsee the right, (1) To receive payment of the instrument; (2) To bring any action thereon that the indorser could bring."

the rights of the indorsee, notwithstanding the restrictive feature, and says that it '*confers* the right to bring any action that the indorser can bring.' That does not imply that he could bring no action other than that which his transferor might have brought, and the phraseology of the opening clause shows that the framers undoubtedly had this in mind when drafting the section."[20]

This argument—while not wholly convincing—makes out the best case that can be presented in defence of the act on this point. Undoubtedly this section could be improved upon, but since it would be gross injustice to refuse X. the right to sue A. and since the real purpose of Subsection 37, par. 2, was simply to permit an indorsee under a restrictive indorsement to sue in his own name, the reasoning suggested by Mr. Farrell is sufficient to enable the courts to reach a just result.

Section 40:

Professor Ames criticises Section 40 as being repugnant to Section 9-5. A discussion of this criticism and of Judge Brewster's reply thereto will be found in the August number of the REGISTER.[20a]

Section 49:

> "Where the holder of an instrument payable to his order transfers it for value without indorsing it, the transfer vests in the transferee such title as the transferor had therein, and the transferee acquires, in addition, the right to have the indorsement of the transferor. But for the purpose of determining whether the transferee is a holder in due course, the negotiation takes effect as of the time when the indorsement is actually made."

Professor Ames criticises the first sentence of this section. He agrees that if an indorsement was intended, but

[20] Article on the Negotiable Instruments Law by John L. Farrell, Brief of Phi Delta Phi, Vol. III, No. 2, First Quarter (1901).

[20a] AMERICAN LAW REGISTER, Vol. 41, N. S., No. 8, August, 1902. "The Negotiable Instruments Law. First Paper." See pages 454 to 461 inclusive.

omitted through inadvertence, it is obviously just that the transferor should be required to indorse subsequently. But he says that if the omission to indorse was intentional, it is as obviously unjust to compel the transferor to assume the liability of an indorser.

The obvious answer is that the transferor may indorse "without recourse" whenever such an indorsement will carry out the intention of the parties. But Professor Ames thinks that this section does not permit of a qualified indorsement in any case. "In Section 44," he says, "it is provided that any person under obligation to indorse in a representative capacity may indorse in such terms as to negative personal liability. But there is no similar provision for a qualified indorsement in Section 49. Such a provision should be added to this section." The critic's reasoning does not convince. It certainly does not follow that Section 49 requires an unqualified indorsement in every case, simply because Section 44 provides that one under obligation to indorse in a representative capacity may use terms which negative personal liability. Section 49 does not specify any one kind of indorsement. In every case the transferee must go into a court of equity to compel an indorsement. Obviously he will be given the kind of an indorsement to which he is entitled. If the parties agreed that the transferor was not to assume personal liability, an indorsement "without recourse" gives the transferee all that he is entitled to by common sense, by equity or by Section 49.[21]

Professor Ames makes a further objection to this section. "If the transferee by delivery merely of an instrument payable to the order of the transferor always acquires only the rights of the latter, such a transferee of a note made for the accommodation of the payee could not enforce it against the maker, even though he might have given to the payee the money which it was the object of the maker

[21] The Colorado Legislature added to the sentence requiring an indorsement the words "if omitted by accident or mistake," but for the reason given above the addition was unnecessary, and Judge Brewster refers to Mr. J. Warner Mills, page 23, the annotator of the Colorado act, who says, in speaking of the two forms of expression, "But either form of expression establishes the equitable rule of law."

to procure for the payee on the credit of his own name. Such a result would be a reproach to the law, even if due to the action of the courts. But this section, so far from codifying, actually nullifies the judicial precedents in this country."[22]

Judge Brewster makes no reply to this criticism.

Let us see. A. makes his note for $1,000 payable "to the order of B." for B.'s accommodation. B. transfers it by

[22] Of the four American cases cited by Professor Ames, only one can be regarded as supporting his position, viz., *Hughes* v. *Nelson*, 39 N. J. Eq. 547. (For a convincing argument which expressly disapproves of that case and cites numerous authorities the other way, see *Goshen National Bank* v. *Bingham*, 23 N. E. Rep. 181.)

In *Matthias* v. *Kirsch*, 87 Me. 523, the accommodation note in suit, which was unindorsed by the payee, had been given in renewal of a prior note which had been properly indorsed. It was held that the rights of the parties were established by the first note. The plaintiff could have enforced the first note and having taken the second merely as a renewal of the first, should be allowed to recover. The court expressly based its decision on this ground, stating that but for the transaction previous to the giving of the note in suit, the defendant would have prevailed on the well-settled rule that the delivery of a note before maturity without the indorsement of the payee is a mere assignment and carries with it only the rights of the assignor.

Meggett v. *Baum*, 57 Miss. 22, went entirely on a Mississippi statute, on reasoning which is not applicable in other states.

Freund v. *National Bank*, 76 N. Y. 352, is a poor case with which to sustain any proposition. The court mistook the point and then reasoned incorrectly on what it supposed to be the point. The plaintiff drew his check on the defendant bank payable to O. for the latter's accommodation. O. transferred it unindorsed to B. for value. Then B. took it to the defendant bank and had it certified. Later the bank paid the check and the plaintiff (drawer) who, prior to the payment but after the certification, had notified the bank to stop payment of the check, sought to compel the bank to credit him with the amount of it. Judgment for defendant. The opinion first established at some length that B. was an assignee *who succeeded merely to the payee's rights.* Then it reasoned that *since B. could have enforced the check against the drawer,* the bank was justified in paying him or in certifying at his instance.

Two later New York cases (*Goshen National Bank* v. *Bingham*, 23 N. E. Rep. 181, and *Lynch* v. *First National Bank*, 13 N. E. Rep. 775) based the decision in the Freund case solely on the ground that the bank certified the check *while it was in the hands of B., the transferee by delivery of the payee*—that under these circumstances the bank

delivery, without indorsement, to C. for value. Under Section 49, C. may go into equity, compel B. to indorse, and may then recover against the maker. But until C. gets B.'s indorsement, he is merely B.'s assignee and so cannot recover against the maker. This, says Professor Ames, is a "reproach to the law."

It would not be, if A., induced by B.'s fraud, had executed

took, as it had a right to take, the risk of the title which the holder claimed to have acquired from the payee, and entered into a contract with the holder by which it accepted the check and promised to pay the amount of it to the holder, notwithstanding the lack of indorsement.

The precise point involved in the Freund case was this: Is a bank justified in paying a check to one who is merely the transferee by delivery of the payee If that question be answered in the affirmative, the bank wins regardless of whether the check was an accommodation one or not. If that question be answered in the negative, the drawer wins. Why? Once admit that payment to the payee's transferee by mere delivery is within the scope of the drawer's order, then the bank is justified in paying the transferee whenever it would be justified in paying the payee. But it is justified in paying the payee regardless of whether the latter gave value for the check or not. Therefore the question of accommodation was wholly immaterial in the Freund case. Still more immaterial, if possible, was the question which arose out of the fact that the payee was an accommodated party, viz., the question whether the transferee by mere delivery had a right of action against the drawer. The question was as to the implied contract that exists between the drawer and the bank. If that contract permits the bank to cash checks only for the payee or his indorsee, then any payment made to the payee's transferee by mere delivery violates the drawer's order. Otherwise, if the contract allows a payment to the payee, or to his transferee by delivery or to his indorsee. (Of course, a bank may certify a check and debit the drawer with the amount of it when and only when it would be justified in cashing the check.) The Freund case decided that the defendant bank would have been justified in paying the check to the payee's transferee by delivery. It follows that it was justified in certifying it at his instance.

It is submitted that the decision is wrong for the reason that if the check should be given to the payee in payment of a debt, the drawer, if sued by the payee on the original consideration, might find it difficult, if not impossible, to prove that the debt had been paid. He must prove that B. (who had the check cashed) was the payee's assignee. But there is no written evidence of that. A check should be regarded as authorizing the bank to pay only to the *payee or his indorsee*. Moreover, this view accords with banking practice, which does not sustain the proposition laid down (though apparently unconsciously) by the Freund case.

the note for a valuable consideration. In such a case all would sanction the application of the well-settled rule that the transfer by delivery without indorsement of a note payable to order operates as a mere assignment which vests in the assignee (C.) whatever rights his assignor (B.) had. But as against B., the maker has the defence of fraud, so C. cannot recover. Why should there be a difference between the defence of "fraud" and the defence of "accommodation?"

Professor Ames' reason is that A. gave the note to B. to enable the latter to raise money on it. He lent his credit for that purpose. And since B. has in fact raised money on the note by using A's credit, A. should not be allowed to escape liability to C. That is an argument *ad hominem*. It does not contain any legal reason for holding A. liable. Of course, he meant to lend B. his credit. But he lent it to him by executing a promissory note in which he promised to pay "to the order of B." Those words have a very definite legal meaning, viz., to pay to B. or to one who holds under his indorsement. That is A.'s promise. What reason is there for saying that he intended to assume a broader liability? By what legal principle can he be held liable on any promise other than the one he has made? Why should the law be "reproached" for insisting that those who seek to avail themselves of the unusual and extraordinary protection extended to commercial paper must comply with the rules which govern commercial paper—rules universally understood and which are merely a statement of those everyday business customs which really created and govern this branch of the law? It is a fundamental and an almost universal rule of law that no one can transfer a better title than he possesses. An exception exists in favor of those who become the holders in due course of commercial paper. The proper method of becoming a holder in due course is very simple, and little authority and still less reason can be presented for protecting those who through design, carelessness or ignorance seek to dispense with that method.[23]

Section 64:

"When a person, not otherwise a party to an instru-

[23] Section 49 is copied from Section 31, par. 4, of the English act. See Chalmers' Bills of Exch., fifth ed., pp. 103 to 105.

ment, places thereon his signature in blank before delivery, he is liable as indorser, in accordance with the following rules:

"1. If the instrument is payable to the order of a third person, he is liable to the payee and to all subsequent parties.

"2. If the instrument is payable to the order of the maker or drawer, or is payable to bearer, he is liable to all parties subsequent to the maker or drawer.

"3. If he signs for the accommodation of the payee, he is liable to all parties subsequent to the payee."

Prior to the act, no part of the law of Bills and Notes was more difficult and confused than the rules regulating the liability of the anomalous indorser. This kindly individual was held liable in various states as first indorser, second indorser, joint maker, and guarantor. Even then his liability was in most cases merely "presumed," and the question, in what cases and by what evidence could the presumption be rebutted, gave rise to various answers. All agree that Section 64, which deals with this question, is a long step forward. It unifies the law and lays down rules admirably framed to carry out the intention of the parties.

Professor Ames fully appreciates the excellence of this section, but thinks that it might be improved in one particular. He says, "Section 64 is an excellent piece of codification but for one slip. One not otherwise a party to a bill payable to the order of the drawer may sign it for the accommodation of the acceptor, as in *Matthews* v. *Bloxsome*.[24] He should clearly be liable to the drawer-payee. But by Sub-section 2 he is liable only to parties subsequent to the drawer."

To illustrate: X. is willing to sell goods to A. on credit provided B. becomes surety for A. So A. makes his note payable to X., gets B. to indorse it, and delivers it to X. in exchange for the goods. By Sub-section 1, B., the surety, is liable to X. This is the correct result and the one intended by the parties. Suppose, however, that they attempt

[24] 33 L. J. Q. B. 209. For a similar case see *Young* v. *Glover* [illegible] Jurist, N. S. 6[illegible]7

to accomplish it in a different way. Suppose X. draws on A. payable to his own order, A. accepts, gets B. to indorse, and hands the bill back to X. X. sells it to Y. It is dishonored at maturity and X. is compelled to take it up. X. now has no right over against B. All intended that B. should become liable to X., yet, the bill being payable to the order of the drawer, Sub-section 2 makes B., the anomalous indorser, liable not to the drawer-payee but only to parties subsequent to the drawer-payee. Professor Ames' point is that Section 64 should be amended so as to render B. liable to X. in the latter case.[25]

Judge Brewster misapprehends Professor Ames' meaning on this point. He regards the critic as saying that the anomalous indorser should be liable to the *maker or drawer whom he has accommodated with his signature,* in cases where the maker or drawer is the payee. But Professor Ames does not say that. The case he speaks of and the hypothetical case he puts forward is a case in which the *acceptor* is accommodated by the anomalous indorser. Where the *drawer-payee* is the accommodated party, Professor Ames agrees with Sub-section 3, which renders the anomalous indorser in such case liable only to parties subsequent to the drawer-payee. To this misapprehension of the critic's meaning must be attributed Judge Brewster's statement that "The Dean's proposed substitute would defeat the purpose of the act. It would not. The proposed substitute would leave the act precisely as it is, except that an anomalous indorser who signed *for the accommodation of the acceptor,* a bill payable to the drawer's order, would be liable to the drawer-payee.[26]

[25] Professor Ames proposes to meet the difficulty by making the first two sections of Section 64 read as follows:

1. "If the instrument is a note or bill payable to the order of a third person, or an accepted bill payable to the order of the drawer, he is liable to the payee and to all subsequent parties."

2. "If the instrument is a note or unaccepted bill payable to the order of the maker or drawer, or payable to bearer, he is liable to all parties subsequent to the maker or drawer."

[26] In his second paper, Judge Brewster remarks, "As the Dean's definition of accommodation paper includes paper 'for value received, his new illustration has no meaning if the illustration makes 'B.' an accom-

In another place Judge Brewster says that by Section 64 the anomalous indorser is to be liable *to all subsequent parties.* This is the answer to Professor Ames, if any there be. Of course, the only liability that the regular indorser assumes is to subsequent parties. That is the contract created by the law merchant. But one, not otherwise a party to an instrument, who puts his signature thereon before delivery, is not a regular indorser. His position is anomalous. So far, therefore, as any technical rule goes, he could be held to the liability of a first indorser, second indorser, joint maker, or guarantor. Section 64 attempts, and with much success, to fasten on him the liability which he intended to assume. In one case, however, namely, where he signs, for the accommodation of the acceptor, a bill payable to the order of the drawer, the section makes his liability less than he intended. Professor Ames' substitute would remedy this defect without making any other change. It would seem, therefore, that admirable as Section 64 now is, Professor Ames' substitute would have been even better.

Charles L. McKeehan.

(To be concluded in the October number.)

modation indorser." A remarkable sentence. All anomalous indorsers are accommodation parties in the sense that they sign for the purpose of lending their credit. But very few accommodation indorsers are anomalous indorsers. And these are anomalous indorsers not because they received no value, but because they signed before delivery instruments to which they were not otherwise parties. Therefore, whether or not "B." in the case supposed received value, is absolutely immaterial.