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Defenses Good against Past Due Commercial Paper

Elton E. Richter

Joseph Yoch

DEFENSES GOOD AGAINST PAST DUE COMMERCIAL PAPER

Perhaps no one branch of the law of commercial paper more mystifies the student and bewilders a non-legal student and business man than the subject of defenses good against overdue paper. This fact coupled with the present economic depression which has caused much commercial paper to be defaulted are the principal reasons for the writer's selection of overdue paper as the subject of this article.

At the outset it may be stated that the legal confusion concerning defenses to which the purchaser of overdue paper is subject is due to the failure of the courts to adopt a single legal principle which would exclusively determine the rights of such a purchaser. The failure to determine the principle in turn is due to a failure on the part of the courts to classify overdue paper as exclusively a chose in action to be governed by the rules applicable to choses in action or as an ordinary chattel to be governed by the rules applicable to chattels.

Before noting the question involved in the problem of the correct classification of overdue paper either as a cause of action or as a chattel, a brief historical sketch of the law applicable to choses in action and chattels will be noted.

First as to choses in action: Perhaps no better brief outline of the historical development of the law of assignments can be given than to quote Chitty, in his work on *Bills of Exchange*:[1]

"The first peculiar privilege of a bill of exchange is its *assignable quality,* and which is in direct opposition to a very ancient rule of law, the founders of which refused to sanction or give effect to the transfer of any possibility, right, or any other *chose in action* (which is defined to be a right not reduced into possession) to a stranger; on

[1] CHITTY ON BILLS (1839) 6.

the ground that such alienations tended to increase maintenance and litigation, and afforded means to powerful men to purchase rights of action, and thereby enable them to oppress indigent debtors, whose original creditors would not perhaps have sued them. Our ancestors were so anxious to prevent alienation of *choses,* or rights in action, that we find it enacted by the 32 H.8. c. 9. (which, it is said, was in affirmance of the common law,) that no person should buy or sell, or by any means obtain any right or title to any manors, lands, tenements, or hereditaments, unless the person contracting to sell, or his ancestor, or they by whom he or they claim the same, had been in *possession* of the same, or of the reversion or remainder thereof for the space of one year before the contract; and this statute was adjudged to extend to the assignment of a copyhold estate, and of a chattel interest, as a lease for years, of land, whereof the grantor was not in possession. At what time this doctrine, which, it is said, had relation originally only to *landed estates,* was first adjudged to be equally applicable to the assignment of a mere *personal chattel not in possession,* it is not easy to decide: it seems, however, to have been so settled at a very early period of our history, as the works of our oldest text writers, and the reports, contain numberless observations and cases on the subject. Lord Coke says, that it is one of the maxims of the common law, that no right of action can be transferred, 'because, under color thereof pretended titles might be granted to great men, whereby right might be trodden down, and the weak oppressed, which the common law forbiddeth.' Accordingly we find, that judgment was arrested in an action on a bond conditioned for the performance of articles of agreement, which contained a covenant that the defendant should assign certain bonds to the plaintiff for his own use, on the ground that such condition and covenant amounted to maintenance. And although it was decided, that the king, in respect of his prerogative, might transfer a right of action, yet it was afterwards ruled, that his assignee had no such power.

"This doctrine, however strictly adhered to in our courts of law, was not adopted by our *courts of equity*: for though it is said to have been decided on the 11th James I, that the assignee of a covenant could not sue in a court of equity to enforce performance, because it was against law to assign a covenant, yet that seems to be an insulated case; and no other authority is to be found, where a court of equity has refused to give effect to the assignment of a *chose in action,* provided such assignment were made for a sufficient consideration. A court of equity having it in its power to decree according to the justice of every case, there could have been no danger of maintenance being increased by its giving effect to such assignments; we therefore find a great number of cases where decrees have been made in favor of such assignees.

"In courts of *law* the *equitable* interest of the assignee of a *chose in action* seems to have been recognized as far back as the middle of the last century, when we find it said by one of the judges, 'that if an assignee of a *chose in action* have an equity, that equity should be no exile to the courts of common law.' In another case also, the court speaks of an assignment of an apprentice, or an assignment of a bond, as things valid between the parties, and to which they must give their sanction; and an assignment of a *chose in action* has always been deemed a sufficient consideration for a promise, although the debt assigned was uncertain. So indeed it was decided, that where the obligee has assigned over a bond, and afterwards becomes a bankrupt, he might nevertheless bring an action on the bond; and that in an action upon a bond given to the plaintiff in trust for another, the defendant may set off a debt due from the person beneficially interested, in like manner, as if the action had been brought by the *cestui que trust*. A debt assigned for the benefit of creditors, is not liable to be attached for the debt of the assignor. But though courts of law have gone the length of taking notice of assignments of *choses in action,* and of giving effect to them, yet in almost every case they have adhered to the formal objection that the action should be brought in the name of the assignor, and not in the name of the assignee; the consequence of which rule is, that the defendant may give in evidence a release, declaration, or admission of the plaintiff on the record, to defeat the action, although it be evident such plaintiff is but a mere trustee for a third person. It has been observed, that the substance of the rule being done away, there can be no use or convenience in preserving the shadow of it; for where a third person is permitted to acquire the interest in a thing, whether he bring the action in his own name or in the name of the assignor, does not seem to affect the question of maintenance. However, in a subsequent case, Lord Kenyon expressed his determination not to sanction the assignment of a *chose in action,* so as to allow the assignee to sue in his own name. The consequence of this doctrine is, that if an instrument which is not assignable at law, so as to pass the legal interest, be indorsed by the person to whom it is payable to his agent to whom he is indebted generally, without any specific appropriation, the agent, in case of the death of the principal, will have no legal or equitable interest in the instrument towards satisfaction of his debt, but must restore it to the executor.

"Even at the earliest period of our history, the doctrine of relating to the assignment of *choses in action* was found to be too great a clog on *commercial* intercourse; an exception was therefore soon allowed in favor of mercantile transactions. It was the observation of the learned and elegant commentator on the English laws, that in the infancy of trade, when the bulk of national wealth consisted of

real property, our courts did not often condescend to regulate personalty; but, as the advantages arising from commerce were gradually felt, they were anxious to encourage it by removing the restrictions by which the transfer of interest in it was bound. On this ground, *the custom of merchants,* whereby a *foreign* bill of exchange is assignable by the payee to a third person, so as to vest in him the *legal* as well as the equitable interest therein, was recognized and supported by our courts of justice in the fourteenth century; and the *custom of merchants,* rendering an *inland bill* transferable, was established in the seventeenth century. In short, our courts, anxiously attending to the interests of the community, have in favor of commerce, adopted a *less technical* mode of considering *personalty* than *realty;* and, in support of *commercial transactions,* have established the *law merchant,* which is a system peculiarly founded on the rules of equity, and governed in all its parts by plain justice and good faith."

Chitty also says:

"The various advantages which commerce derives from the use of bills of exchange, have induced our courts of justice, and also most foreign courts, to allow them certain *peculiar privileges* in order to give full effect to their utility."

The one which concerns us is as follows:

". . . that although a bill of exchange is a *chose in action,* yet it may be *assigned* so as to vest the *legal* as well as equitable interest therein, in the indorsee or assignee and to entitle him to sue thereon *in his own name.*

"This privilege is of most essential importance in various points of view, and principally that a release by the drawer to the acceptor, or a set-off or cross demand due from the former to the latter, cannot affect the right of action of the payee or indorsee; because the *legal* and not the mere equitable interest is vested in such payee or indorsee, and the action is sustainable in his own name; whereas suits upon bonds, and most other *choses in action,* must be in the name of the original obligee; and though it be apparent that he sues merely as a trustee for another to whom he has assigned his interest, yet a release from him, or a set-off due from him to the obligor, may be an effectual bar to the action."

Although we may earnestly question the reason for the rule against inalienability of choses in action by Mr. Chitty, the rule itself is unquestionable. The reasons given by Dean Ames in his lecture on *The Inalienability of Choses in Action,*[2] are now accepted:

2 AMES, LECTURES ON LEGAL HISTORY (1913) 210; 211, 212.

"There were, however, a few exceptions to the rule. The king, as might be supposed, could grant or receive the benefit of a *chose* in action. So, too, a reversion or a remainder was transferable by fine in the king's court, or by a customary devise, which, when recorded in the local court, operated like a fine. Again, certain obligations, by the tenor of which the obligor expressly bound himself to the obligee and his assigns, could be enforced by a transferee. If, for instance, one granted an annuity to A. and his assigns, or covenanted to enfeoff A. and his assigns, or made a charter of warranty to A. and his assigns, the assignee was allowed to bring an action in his own name against the grantor, covenantor, and warrantor, respectively.

"The significance of this exception lies in the fact that it goes far to explain the reason of the rule which prohibits the assignment of rights of action in general. The traditional opinion that this rule had its origin in the aversion of the 'sages and founders of our law' to the 'multiplying of contentions and suits' shows the power of a great name for the perpetuation of error. The inadequacy of this explanation by Lord Coke was first pointed out by Mr. Spence. The rule is not only older than the doctrine of maintenance in English law, but is believed to be a principle of universal law.

"A right of action in one person implies a corresponding duty in another to perform an agreement or to make reparation for a tort. That is to say, a *chose* in action always presupposes a personal relation between two individuals. But a personal relation in the very nature of things cannot be assigned. Even a relation between a person and a physical thing in his possession, as already stated, cannot be transferred. The thing itself may be transferred, and, by consent of the parties to such transfer, the relation between the transferror and the thing may be destroyed and replaced by a new but similar relation between the transferee and the *res*. But where one has a mere right against another, there is nothing that is capable of transfer. The duty of B. to A., whether arising *ex contractu* or *ex delicto*, may, of course, be extinguished and replaced by a new and coextensive duty of B. to C. But this substitution of duties can be accomplished only in two ways: either by the consent of B., or, without his consent, by an act of sovereignty. The exceptions already mentioned of assignments by or to the king, and conveyances of remainders and reversions in the King's Court, are illustrations of the exercise of sovereign power. Further illustrations are found in the bankruptcy laws which enable the assignee to realize the bankrupt's *choses* in action, and in the Statute 4 and 5 Anne, c. 16, which abolished the necessity of attornment.

"When the substitution of duties is by consent, the consent may be given either after the duty arises or contemporaneously with its creation. In the former case the substitution is known as a novation,

unless the duty relates to land in the possession of a tenant, in which case it is called an attornment. A consent contemporaneous with the creation of the duty is given whenever an obligation is by its terms made to run in favor of the obligee and his assigns, as in the case of annuities, covenants, and warranties before mentioned, or to order or bearer, as in the case of bills and notes and other negotiable securities. Here, too, on the occasion of each successive transfer, there is a novation by virtue of the obligor's consent given in advance; the duty to the transferror is extinguished and a new duty is created in favor of the transferee."

The rule against inalienability of choses was not accepted with grace by the commercial interests, nor did the protection which the transferee received in equity seem to meet the commercial requirements. As a result the common law lawyers devised the so-called letter of attorney which they hoped would meet the necessities of the commercial classes.[3] By such a letter the owner of a claim appointed the intended transferee as his attorney, with power to enforce the claim in the appointor's name, but to retain whatever he might recover for his own benefit. This devise (assignment with letter of attorney)[4] for avoiding the rule against inalienability of choses was not altogether satisfactory to the transferees. For instance, the security given by the warrant of attorney might be lost in one of the following ways: 1. the assignor might revoke the power of attorney expressly, or, revocation might be effectuated by implication of law, as by

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[3] "In 1 Lilly's Abr. 125, it is said: 'A statute merchant or staple, or bond, etc., cannot be assigned over to another so as to vest an interest whereby the assignee may sue in his own name but they are every day transferred by letter of attorney, etc., ... These letters of attorney for the attorney's own use, whether borrowed from the similar *procuratio in rem suam* of the Roman law or not, are of great antiquity . . . . Know ye that I do assign and attorn in my stead E., my dear partner, to demand and receive the same rent of forty shillings with the arrears and by distress the same to levy in my name . . . and all things to do as to the same matter FOR HER OWN PROFIT as well as ever I myself could have done in my own proper person.'" AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 213.

[4] "Formerly an express power of attorney was indispensable . . . the notion of an implied power being as much beyond the conception of lawyers three centuries ago as the analogous idea of an implied promise. . . Today, of course, the power will be implied from circumstantial evidence. Formerly a deed could not be delivered in escrow without express words to that effect." AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 214 note.

death; 2. or if the assignee still remains the owner of the claim, his bankruptcy by virtue of the bankruptcy statute might be expected to give title to his assignee in bankruptcy to the exclusion of an assignee claiming under a prior assignment if that is interpreted as giving a mere power of attorney, and an attachment by garnishment of the debt by a creditor of the assignor might be expected to prevail over a prior assignment; 3. the assignor might, by other assignment, appoint other persons with authority to collect the claim, and either they or the assignor himself might collect the claim in fraud of the original assignee. These difficulties were partly met by the jurisdiction which equity assumed over assignment at an early date.[5]

The effectiveness of the power of attorney was greatly increased by equity's aid in their enforcement:

"Courts of Equity undertook as a branch of their jurisdiction to give, so far as possible, the effect to an assignment which the parties intended. As will be seen equity did not go so far as to treat the assignee as a true successor, like an assignee in bankruptcy, but it was found possible in effect to enforce specifically a covenant on the part of the assignor not to revoke the power given to the assignee, and indeed without the aid of a covenant against revocation or of any power of attorney other than that necessarily implied from the assignment itself, to hold that the assignee had an irrevocable right, commensurate with that which the parties contemplated, in any controversy between the parties themselves or with those in similar position. Accordingly, Courts of Equity held that an assignee for value would be protected against any person except one who had in good faith and for value reduced to possession the chose in action. Therefore, equity preferred the assignee of a chose in action over a creditor of the assignor who subsequently garnished the debtor as a means of collecting his claim against the assignor. Equity also held that the assignee would be protected in his right as against an assignee in a subsequent bankruptcy of the assignor; and at the end of the eighteenth century the same decision was made by a court of law, which held that it would take notice of the doctrines of equity in regard to assignments and apply them. At the present time so fully have courts of law adopted the principle that assignment of choses in action will be protected, that where an absolute and total assignment of a chose in

[5] 1 WILLISTON ON CONTRACTS (1921) § 409.

action is made, application to a court of chancery is not often necessary; and where the assignee has an adequate remedy at law, equity will not take jurisdiction to enforce his rights. The power given to an assignee to collect and keep the proceeds of the claim assigned, being wholly for the interest of the assignee may be delegated by him to another, and a sub-assignment is protected as fully as the original assignment." [6]

Although there were the enumerated defects in the assignment with power of attorney, the arrangement did meet a serious commercial need and was widely adopted by the commercial interest of its use. Dean Ames writes:

"Indeed, so effectual was the power of attorney as a transfer, that, during a considerable interval, it was thought unduly to stimulate litigation, and therefore to fall within the statutory prohibition of maintenance, unless the power was executed for the benefit of a creditor of the transferor. Powers executed for the benefit of a purchaser or donee were treated as void from the beginning of the fifteenth century if not earlier, till near the close of the seventeenth century." [7]

We have noted that as time wore on an expressed power of attorney was no longer indispensable and that by force of the assignment the assignee by implication acquired the right to enforce the chose by suit brought in the name of the assignor. Yet the assignee still proceeded, in a sense, as the agent of the assignor. The rights of the assignee are determined by the rules of equity which were worked out at a time before the common law would take notice of the assignee's rights.[8]

It is true that the procedure compelling the assignee to bring suit in the name of the assignor was sometimes questioned, as for instance, in *Master v. Miller*,[9] Buller, J., says:

"But still it must be admitted, that tho the courts of law have gone the length of taking notice of assignments of choses in actions and of acting upon them, yet in many cases they have adhered to the formal objections, that the action shall be brought in the name of the assignor,

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[6] WILLISTON ON CONTRACTS, *op. cit. supra* note 5, § 410.

[7] AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 213.

[8] Winch v. Keeley, 1 T. R. 619 (1787). In this case the assignee brought suit in the name of the assignor and therefore the question whether a chose in action might be so assigned as to give legal title to the assignee was not involved.

[9] 4 T. R. 320 (1791).

and not in the name of the assignee. I see no use or convenience in preserving that shadow when the substance is gone; and that it is merely a shadow, is apparent from the later cases, in which the courts have taken care that it shall never work injustice."

Yet the practice continued until prohibited by statutory enactment of the so-called real party in interest rule.[10]

Even under the statutes, permitting the assignee to sue the obligor in his own name, the assignee still proceeds in a real sense as a representative of the assignor. This is true because the statutes only introduced a change in procedure. In *Leach v. Greene*[11] the court held that a suit could not be maintained in the name of the assignee where the plaintiff, who had purchased a cause of action in New York, where the real party in interest statute was in effect, brought suit in his own name on the assigned cause of action in Massachusetts where the rule was that the assignee must bring his suit in the name of the assignor. It thus seems that the statute permitting a suit in the name of the real party in interest did not affect a change in the title to the assigned chose in action.

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10 In 1848, New York enacted a statute which provided that: "Every action must be prosecuted in the name of the real party in interest." England followed by the passage of THE JUDICATURE ACT (1873) § 25 (6). STAT. 36 & 37 VICT., c. 66: "Any absolute assignment, by writing under the hand of the assignor (not purporting to be by way of charge only), of any debt or other legal *chose* in action, of which express notice in writing shall have been given to the debtor, trustee, or other person from whom the assignor would have been entitled to receive or claim such debt or *chose* in action, shall be, and be deemed to have been effectual in law (subject to all equities which would have been entitled to priority over the right of the assignee if the Act had not passed), to pass and transfer the legal right to such debt or *chose* in action from the date of such notice, and all legal and other remedies for the same, and the power to give a good discharge for the same, without the concurrence of the assignor: Provided always, that if the debtor, trustee, or other person liable in respect of such debt or *chose* in action shall have had notice that such assignment is disputed by the assignor or any one claiming under him, or of any other opposing or conflicting claims to such debt or *chose* in action, he shall be entitled, if he think fit, to call upon the several persons making claim thereto to interplead concerning the same, or he may, if he think fit, pay the same into the High Court under and in conformity with the provisions of the Acts for the relief of trustees." At the present time practically everywhere the assignee sues in his own name.

11 116 Mass. 534 (1875).

For purpose of illustration, if we concede that overdue paper is a chose in action, it would seem that if A, owner of overdue paper, should sell the same to B, B would not get the legal title and his position would be an agent of A with power of attorney to collect the chose. B's rights being measured by what A's rights would have been if A had not sold the paper.

The rule pertaining to the purchase of chattels in so far as we are concerned can be briefly stated as follows:

"A court of equity will not deprive a defendant of any right of property, whether legal or equitable, for which he has given value without notice of the plaintiff's equity." [12]

The reason for this rule as stated by Dean Ames is:

"The rule just given is simply an application of that comprehensive principle which lies at the foundation of constructive trusts and other equitable obligations created by operation of law (including implied or *quasi* contracts, which are really equitable liabilities, upon which the common law assumes to give a remedy), namely, that a court of equity will compel the surrender of an advantage by a defendant whenever, but only whenever, upon grounds of obvious justice, it is unconscientious for him to retain it at another's expense. Indeed, it is not too much to say that the purchaser of a title from one who holds it subject to an equity is always charged, if chargeable at all, as a constructive trustee. If he acquired the title with notice of another's equity his acquisition was dishonest, and he must, of course, surrender it. If he gave no value, though his acquisition was honest, his retention of the title, after knowledge of the equity, is plainly dishonest. If he gave value, and had no notice of the equity, it is eminently just for him to keep what he has got." [13]

Assuming for the purpose of illustration that under the above rule overdue paper is a chattel, if A, the owner of overdue paper, sells the same to B, an innocent purchaser, B gets the legal title, and the outstanding equities which were enforceable during A's ownership are lost.

The transferee of negotiable paper brings suit thereon in his own name. If the instrument sued on is a bill, the

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12 AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 254.
13 AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 255.

right extends back to the time when foreign bills were first recognized by the common law of England at the beginning of the seventeenth century. As to promissory notes, the right dates back at least to the Statute of Anne.[14]

Was the right of a transferee of negotiable paper to bring suit on the paper in his own name a real exception to the common law rule against alienating choses in action? In Dean Ames' explanation for the rule against alienating choses, he suggests that if the instrument according to its original tender was payable to the obligee and his assigns, as in the case of annuities, covenants, and warranties, or to order or to bearer, as in the case of bills and notes, the relation created would not be personal since the obligor would be consenting in advance to a novation. However, the rule presumed to exist from the cases of annuities, covenants, and warranties does not seem to be as broad as Dean Ames' discussion would lead one to think. One might believe that whenever the obligor's promise ran in favor of the obligee or his assigns the relation created was not personal and a transferee might have brought suit in his own name. But this was not true as illustrated in the case of *Skinner v. Somes*.[15] Here suit was brought on a bond which was made by the defendant to one John Somes, his heirs, executors, administrators or assigns. The plaintiff, transferee of the obligee, brought suit upon the bond in his own name. The court in sustaining a demurrer to the declaration said:

"This is the first attempt to maintain an action of debt by the assignee of a bond in his own name. The word *assigns* has been for centuries inserted in bonds and obligations, but no one has conceived that it gave to them a negotiable property, so as to transfer the right of action upon them to the assignee."

In *Jessel v. The Williamsburgh Insurance Company*[16] the obligee of an insurance policy, with the consent of the

14 3 & 4 ANNE, c. 9-(1704).
15 14 Mass. 106 (1817).
16 3 Hill (N. Y.) 88 (1842).

Insurance Company, assigned the policy. The assignee brought suit on the policy in his own name. The court nonsuited the plaintiff saying:

"We know of no principle upon which the assignee of a policy of insurance can be allowed to sue upon it in his own name. The general rule applicable to personal contracts is, that, if assigned, the action for a breach must be brought in the name of the assignor, except where the defendant has expressly promised the assignee to respond to him. . . . The argument that the policy in question originally contemplated an assignment, would be equally cogent in all cases, for aught we see, of a promise in form to one *and his assigns;* and yet it is settled that the latter words do not impart a negotiable quality to the promise so as to enable the assignee to sue upon it in his own name."

It therefore seems that the right of the transferee of negotiable paper to sue thereon in his own name is not due to the fact that the common law did not regard the relation between obligor and obligee as personal when the promise ran in favor of the obligee and his assigns, or to the obligee or order, or bearer, but that the transferee's right to maintain suit in his own name on negotiable paper, that is, in cases where the promise ran to the obligee, or to his order, or to bearer, was as stated by Mr. Chitty, a peculiar privilege accorded these instruments by our courts of justice in aid of commerce. If the instrument was negotiable, then *ipso facto* the transferee by operation of law might sue in his own name.

The basis for the right of the transferee of negotiable paper to sue in his own name is very important. If the basis of the right is the tenor of the promise, it is conceivable that an obligation of a promisor to an obligee and his assigns would become absolute, if, as suggested by Dean Ames, such transaction amounts to a novation. This would be true at least when the instrument is in the hands of the transferee. The dealings between the parties would be similar to the following case:

A holds a claim against B. B promises C that if he, C, will purchase the claim from A, he will pay C the amount

of the claim. In reliance upon A's promise, C purchases the claim. B will have to pay C even though it should later develop that A could not have enforced the claim against B. It would seem to make no difference whether B's promise was made to C when the contract with A was executed or when C purchased.

On the other hand, if overdue commercial paper is a chose in action and the peculiar characteristics of commercial paper are based entirely on the privilege extended this paper *ipso jure* and the law extends the privilege to meet commercial requirements, then it would seem that the privilege extended should be commensurate with commercial requirements and no more.

With this survey of principles sketched, the problems involved in classifying overdue commercial paper as choses in actions or chattels will be noted. Both choses in action and chattels are property. Property implies the exclusive right of possessing, enjoying, and disposing of a thing, "when used subjunctively, it means that with respect to which this right exists, or that which is one's own." [17] According to Dean Ames, "a true property may, therefore, be shortly defined as possession coupled with the unlimited right of possession." [18]

Personal chattels are properly things movable, which may be carried about by the owner: such as animals, household stuff, money, jewels, corn, garments and everything else which can be put in motion and transferred from one place to another.[19]

A chose in action is a right not reduced into possession. It may be an interest in a contract, which, in case of nonperformance, can only be reduced into beneficial possession by an action or suit.[20] In the words of Mr. Justice Mc-

17 Vann v. Edwards, 135 N. C. 661, 67 L. R. A. 461 (1904).
18 AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 193.
19 2 KENT COMMENTARIES (14th ed.) 340.
20 2 BLACKSTONE COMMENTARIES 442.

Reynolds, "The difference between the two things seems obvious enough." [21]

As to the different modes of acquiring original ownership of tangible personalty and of intangibles: Inception of title (unlimited right to possession) to tangible personalty accrues by original acquisition.[22] Title to intangibles, where the inception of the right was not a breach of duty imposed by law, depends upon the existence of contractural facts.

As to the original inception of the rights, there would seem to be little similarity between rights in tangibles and contractual rights. To tangibles, the right depends upon original acquisition. In contracts the right depends upon the existence of contractual facts. The inception of rights on commercial paper clearly corresponds to the inception of contractual rights on non-commercial paper. On commercial paper, however, the promisor may incur a legal liability even though contractual facts did not exist at the time the instrument was issued if the holder [23] is a holder in due course. Considered from the view of inception of rights, commercial paper should be classified with choses in action rather than with tangibles. This would be true if subsequent motives of dealing with rights to tangibles and rights against an obligor on commercial paper would not justify a different classification.

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21 Farmers Loan and Trust Co. v. Minn., 230 U. S. 204, 74 L. Ed. 371 (1929).

22 Original acquisition is acquired by occupancy; by accession; by intellectual labor.

23 Section 191 of the N. I. L. states that: " 'Holder' means the payee or indorsee of a bill or note, who is in possession of it, or the bearer thereof."

Section 52 of the N. I. L. states that: "A holder in due course is a holder who has taken the instrument under the following conditions:

1. That it is complete and regular upon its face;
2. That he became the holder of it before it was overdue, and without notice that it had been previously dishonored, if such was the fact;
3. That he took it in good faith and for value;
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."

Rights to property (ownership) may be transferred by act of law.[24]

At common law the rule against transfering causes of action did not apply when the crown was a party, and a debt might have come to the Queen by attainder.[25] If the felon were the owner of commercial paper, rights thereon would also be forfeited.

As to transfer by succession, that is, the mode by which one set of persons, members of a corporation aggregate, acquire the rights of another set which preceded them, presents no special problem.

Upon marriage, ownership of personal property, tangibles, belonging to the wife vested in the husband. As to choses in action, the rule was different, the husband having the right and power during coverture to receive and reduce to his possession all choses in action belonging to the wife at the time of marriage, or which accrued to her while the coverture continued.[26] The absolute ownership vesting in the husband only when the chose was reduced to possession.[27] This rule applied to commercial paper.[28]

A judgment lien in the absence of a statute does not attach to personal property.[29] Generally speaking, however, any species of personal property properly described as a chattel is subject to execution and consequently an execution lien.[30] Choses in action are subject to execution only when made so by statute, or are voluntarily given up to be sold on execution.[31] In many jurisdictions, statutes have been enacted by which the chose in action of the debtor may be reached by process of garnishment, and in some

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24 By forfeiture; succession; marriage; judgment; insolvency; intestacy.
25 Allen's Case, Owen, 113, 74 K. B. 939 (1584).
26 Standeford v. Devol, 21 Ind. 404 (1863).
27 *Supra* note 26.
28 Rogers v. Bank of Pike County, 69 Mo. 560 (1879).
29 Ball v. Barnett, 39 Ind. 53 (1872).
30 Sumter County v. Hanes, Jones & Cadbury Co., 143 Ga. 124, 84 S. E. 425 (1915).
31 The Marion Township Union Draining Co. v. Norris, 37 Ind. 424 (1871).

jurisdictions, under certain conditions by expressed statutory authority, all choses in action of the debtor may be levied upon and sold under execution against him in the same manner as other personal property.[32] Personal property subject to execution is subject to attachment. But it is said that as a general rule an instrument evidencing a debt and providing for the payment of money, such as, promissory notes and bonds, are attachable.[33] The problems involved in subjecting rights on negotiable paper to the claims of the creditors of the holder are well summarized by Professor Campbell.[34]

In the case of tangibles, the creditors of the owner can, with the aid of the law, transfer the *res* under such circumstances that the debtors' rights thereto are completely extinguished. In cases of choses in action, including commercial paper, the obligee's rights to performance on the part of the obligor are extinguished. At the present time, there would seem to be little difference between subjecting the rights constituting ownership of chattels and rights constituting ownership of choses to a creditor's claim. Of course, there is a difference in procedure made necessary by the obvious difference between rights in *rem* and rights in *personam.* In either case the creditor can, with aid of the law, extinguish the debtors' rights and create coextensive rights in himself.

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32 Bay v. Saulspaugh, 74 Ind. 397 (1881).

33 Attachment, 6 C. J., Sec. 353.

34 "Under appropriate statutes, a creditor may reach a negotiable instrument as an asset of his debtor in either of two ways: (1) By attachment and sale of the instrument itself, in which case the only problem is whether the statute is broad enough to include this type of property (41 A. L. R. 1003); or (2) By garnishment of the maker or acceptor, and collection from him of the amount due, a process sometimes referred to as attachment, as in Kieffer v. Ehler, 18 Pa. 388 (1852).

"The process of garnishment is subject to two fundamental requirements. In the first place, it must affirmatively appear that the garnishee is indebted to the plaintiff's debtor, the defendant in the principal action. . .

"In the second place, a garnishee must never be placed in a worse position by the process; judgment must not be rendered against one liable on an instrument unless payment of the judgment will be a defense to any subsequent action on the instrument." CAMPBELL'S CASES ON BILLS AND NOTES (1928) 531.

In case of transfer by insolvency, the rights of the insolvent, whether rights to a *res* or rights in *personam*, pass to the representative of the insolvent. This was true at a time when the common law generally did not permit assigning choses in action.[35]

As to transfers by intestacy: Upon death of the owner of the right, the right passes to the representative of the deceased, whether the right be in *rem* or in *personam*.

Summarizing: Rights constituting ownership may be transferred by operation of law. The law makes no difference whether the rights are in *rem* or in *personam* except under the common law in cases of transfer by marriage.

Rights to property (ownership) may be transferred by the acts of the party.[36]

The owner of a chattel, that is, the person in possession and having unlimited right to possession, may generally do with the chattel as he pleases. He may give the chattel to another, the donee acquiring the rights to the chattel coextensive with the rights of the donor; he may sell the chattel, the vendee acquiring rights coextensive with the rights of the vendor; or by contract he may create an interest short of unlimited ownership in another, as in a bailment.

Generally, excepting transfers by act of law, the rights of the owner cannot be divested without the owner's consent. The principal exception to this exists in cases where the owner acts in such a way as to be estopped from asserting his rights against a *bona fide* purchaser. The results of a transfer by act of the party has been analyzed by Dean Ames as follows:

"The title in such cases is said to pass by transfer. For all practical purposes this is a just expression. But if the transaction be closely scrutinized, the physical *res* is the only thing transferred. The seller's right of possession, being a relation between himself and the *res*, is purely personal to him, and cannot, in the nature of things, be trans-

35 That is by gift, by contract, or by sale.

36 Fawcett, Isham & Co. v. Osborn, Adams & Co., 32 Ill. 411 (1863).

ferred to another. The purchaser may and does acquire a similar and coextensive right of possession, but not the *same* right that the seller had. What really takes place is this: the seller transfers the *res* and abandons or extinguishes his right of possession. The buyer's possession is thus unqualified by the existence of any right of possession in another, and he, like the occupant, and for the same reason, becomes absolute owner." [37]

This incident of ownership, the right to transfer, has always been favored in the common law. Attempts to limit the right have always been frowned upon as is evidenced by the English hostility to spendthrift trusts, the rule against perpetuities, and accumulations.

As to the transfer of rights to tangible personalty by acts of the party the following maxim applies: "Where there is equal equity, the law must prevail." [38] The application of the rule not only takes into consideration equal equities but maintains the right in a transferable thing.

Transfers of choses in action by acts of party:

The common law as to transfers of choses in action by acts of the party has been previously stated. We noted that at common law choses were not transferable by act of the party, the right being regarded as one entirely personal to the obligee. The right of a transferee was, however, protected in equity. The extent of the right acquired by the transferee in equity was determined by the maxim: "Where there are equal equities, the first in order of time shall prevail." [39] When the transferee proceeded under warrant of attorney, suit was brought in the name of the obligee and any defenses of the obligor to the enforcement

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37 AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 194.

38 The meaning of the maxim is: "If two parties have equal equitable claims upon or interest in the same subject-matter, or in other words if each is equally entitled to protection and aid of a court of equity with respect of his equitable interest, and one of them, in addition to his equity, also obtains the legal title to the subject-matter, then he who thus has the legal title will prevail." POMEROY'S EQUITY JURISPRUDENCE (1918) 678.

39 Pomeroy explains the maxim as follows: "As between persons having only equitable interest, if their interests are in all other respects equal, priority in time gives the best equity, or *qui prior est tempore, potior est jure.*"

of the chose were admissible. Under the real party in interest statutes, the assignee brings suit on the chose in his own name. However, strange as it may seem, his title is still equitable and his rights determined by equitable rules worked out at a time when the common law regarded the right as purely personal. At the present time, it would seem that a contract right in *personam* which is subject to no inceptional defects can no longer be regarded as personal and that therefore it should be transferred according to the same rules as a right to a chattel. It is now time for us to forget our squeamishness concerning ability to pass the legal title to an assignee and to apply the maxim, "Where there is equal equity, the law must prevail," in cases where a right can be effectively assigned.

The preceding proposition cannot claim either newness or novelty. Ames writes:

"It seems to have been a common opinion in early times that a court of equity would give no assistance against a purchaser for value without notice." [40]

Chancelor Kent was of the opinion that a purchaser for value without notice of a chose in action did not take subject to latent equities, that is, equities of persons other than the debtor party.[41] The Reporter of the Restatement of the Law of Contracts, Professor Williston, after noticing conflicts of authorities, states the desirable rule to be as follows:

"If an assignor's right against the obligor is voidable by some one other than the obligor or is held in trust for such a person, an assignee who purchases the assignment for value in good faith neither knowing nor having reason to know of the right of such person cannot be deprived of the assigned right or its proceeds." [42]

Pomeroy fears this doctrine of latent equities on the ground that it might render all choses of action negotiable

40 AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 253.
41 Murray v. Llyburn, 2 Johns. Ch. Rep. 454.
42 RESTATEMENT OF THE LAW OF CONTRACTS, § 174.

and thus affect the original debtor.[43] The doctrine does not seem to lead to any such result. Property consists of rights, whether in *rem* or in *personam*. As the owner of a right in *rem* can generally transfer no better right than he has, unless application can be made of the maxim: "Where there are equal equities, the law must prevail," so the owner of a right in *personam* can transfer no better right than he possessed unless the same maxim applies.

The vendee of a chattel must ascertain whether or not the person proposing to sell has title.[44] So the purchaser of a chose in action must ascertain whether or not the inception of the right against the debtor was complete. There would seem to be no more reason for considering that mere possession conferred title in the one case than in the other. In cases of choses in action, if the debtor has a defense it would seem that no property right ever had any existence, and transferring title to the right would therefore be impossible. Mr. Pomeroy seems to be of the opinion that once the assignee of a chose can acquire legal title then the extraordinary rule of negotiable instruments must be applied, rather than the common rules of property, a conclusion seemingly not justified. As to justness in results, there would seem to be little difference between the position of one who has equitable rights in a chattel losing those rights by sale of the chattel to a *bona fide* purchaser and the position of one who has equitable interest in a chose losing those interests by the sale of the chose to a *bona fide* purchaser. In both cases the owner of the equitable right must stand the loss as his contribution to commercial convenience.

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43 POMEROY'S EQUITY JURISPRUDENCE (1918) § 711.

44 Ballard v. Burgett, 40 N. Y. 314 (1869): "Simply intrusting the possession of a chattel to another as depository, pledgee, or other bailee, or even under a conditional executory contract of sale, is clearly insufficient to preclude the real owner from reclaiming the property in case of unauthorized disposition of it by the person so intrusted. The mere possession of chattels, by whatever means acquired, if there be no other evidence of property or authority to sell from the true owner, will not enable the possessor to give a good title."

Transfers of overdue negotiable paper by act of parties:

From an early date, as previously noted, the common law courts extended to contracts in negotiable form certain peculiar privileges in order to meet the necessities of commerce. These privileges were:

(1.) The fact that the transferee obtained the legal title and could sue at law in his on name, and

(2.) The fact that the transferee in good faith and for value took free from all equities and nearly all defenses subsisting in favor of prior parties to the paper, or equities subsisting in favor of parties who never were parties to the paper.

The difference between equities and defenses should be observed. The equities referred to are the ordinary rights, of which the owner receives protection only in equity. The equity in the contract would be comparable to an equitable interest in a chattel, ownership of which might be lost by application of the maxim: "Where there is equal equity, the law must prevail." The subject of defenses requires more consideration. The historical origin is given by Ames,[45] who first points out that the obligee who lost the specialty had no remedy at law but had to resort to equity, also shows that the obligor was just as helpless at law when sued by the obligee on the specialty. Thus the obligee would be entitled to judgment at law even though the specialty was secured by fraud; given in an illegal transaction; given for a consideration which had failed; paid; paid by accord and satisfaction; or executed for accommodation of the obligee plaintiff. In all of these cases the obligor was compelled to resort to equity where an injunction would issue against the obligee forbidding suit on the specialty at law; hence we have the term equitable defenses. The relation between specialty contracts and equitable defenses, and defenses to negotiable contracts is made clear by Ames:

[45] AMES, LECTURES ON LEGAL HISTORY, *op. cit. supra* note 2, at 104.

"By statute or judicial innovation, as we have seen, the jurisdiction of the common laws courts has been greatly extended, except in the Federal courts of this country, in the matter of defenses to actions on formal contracts. In all cases where, formerly, a defendant was obliged to apply to equity for relief against an unconscionable plaintiff, he may now defeat his adversary at law. But the change of forum does not mean any change in the essential character of the relief. The common law accomplishes, by peremptorily barring the action, the same result, and upon the same grounds, that the Chancellor effected by a permanent unconditional injunction. It is as true to-day as it ever was, that fraud, payment, and the like do not nullify the title of the fraudulent or paid obligee, but are simply conclusive reasons why he ought not to enforce his title.

"The truly equitable or personal character of these defenses at law has commonly only a theoretical value in actions upon the ancient common law specialty, the instrument under seal. But it is of the highest practical importance in actions upon the modern mercantile specialty, the bill of exchange or promissory note. For the legal title to bills and notes, by reason of their negotiability, passes freely from hand to hand, and equity would not restrain, by injunction, any holder from enforcing his title, if he came by it honestly and for value. And the plea at law being, in substance, like the bill in equity for an injunction, we see at once the reason for the familiar rule that fraud and other defenses, based upon the conduct of the payee or some other particular person, cannot be successfully pleaded against any *bona fide* holder for value." [46]

The history of defenses has sometimes led to a classification of equities to negotiable paper as equities of ownership and equitable defenses instead of merely equities and defenses.[47]

It must be noted that before the transfer of negotiable paper will cut off equities, the transferee must, according to general equitable doctrines, be a purchaser in good faith and for value. It thus appears that the common law courts, to meet commercial requirements, made the first concessions in favor of negotiable paper, conceding that the legal title could be transferred. It being conceded that the legal title to a right in *personam* could be transferred, the same as a legal title to a right in *rem*, equity could ap-

[46] AMES, LECTURES ON LEGAL HISTORY, *op. cit, supra* note 2, at 114.
[47] See Zechariah Chafee, Jr., *Rights in Overdue Paper*, 31 HAR. L. REV. 1104.

ply the maxim: "Where there is equal equity, the law must prevail." Hence we see the application of the doctrine of *bona fide* purchaser to negotiable paper. But in order to apply this doctrine, the purchaser must have no notice of equities or defenses, which may either be actual notice, that is, actual knowledge of the equity or defenses, or knowledge made by law which is imputed to him. The latter is constructive notice. In *Brown v. Davies* [48] the payee received payment of the note without delivering it to the maker and after maturity sold the note to the plaintiff. The question arose as to whether or not the evidence by which the maker, defendant, offered to prove payment to the payee was admissable. The trial court held that the evidence was not admissible on the ground that it was irrelevant unless it could be shown that plaintiff had actual knowledge of the payment. On appeal a new trial was granted. Ashhurst, J., said,

"That where a note is overdue, that alone is such a suspicious circumstance as makes it incumbent on the party receiving it to satisfy himself that it is a good one, otherwise much mischief might arise."

From the date of *Brown v. Davies* to the present it has been held in the United States [49] and in England that non-payment at maturity is constructive notice of equitable defenses in many cases and in others it is notice of equities of ownership.

In *Hinckley v. Union Pacific Railroad* [50] the court said:

"It is an elementary principle of commercial law that negotiable paper overdue carries with it, on its very face, notice of defective title sufficient to put the transferee on inquiry. . . . After maturity, a coupon, like any other negotiable security, loses the protection of the law merchant, and becomes a mere chose in action."

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48 3 T. R. 80, 100 Eng. Rep. 466 (1789).

49 Section 52 N. I. L. states: "A holder in due course is a holder who has taken the instrument under the following conditions:

1. . . .
2. That he became the holder of it before it was overdue, and without notice that it had been previously dishonored, if such was the fact."

50 129 Mass. 52 (1880).

In *British & American Mortg. Co. v. Smith*[51] the court made the following statement:

"The only question, therefore, which we are called upon to decide, is whether the assignee of a note and mortgage transferred after maturity can claim the protection of the equity rule in favor of purchasers for valuable consideration, without notice."

The conclusion was that the transferee after maturity could not claim protection of a *bona fide* purchaser. In *Bradley v. Linn,*[52] Conger, J., was of the opinion that

"A person taking a note after its maturity receives it subject to all equities existing between former parties to the instrument, whether they are, or not, apparent on the note. It is dishonored by not being taken up at its maturity. It comes to him tainted with suspicion and he is put upon inquiry as to the rights of the former holders, and the real and not the apparent liability of the makers. He takes it precisely as it was held by those from whom he acquires his title. The maxim *caveat emptor* applies in such a case."

The statement by the Massachusetts court, in *Hinckley v. Union Pacific Railroad,* that an overdue negotiable security loses the protection of the law merchant, and becomes a mere chose in action, squarely presents the problem as to the extent of the right acquired by the transferees of negotiable paper negotiated after maturity. It is submitted that the statement of the court is too broad, there being important differences between overdue commercial paper and a mere chose in action. Overdue commercial paper is still negotiable.[53] An overdue promissory note is negotiable within a statute exempting from attachment, debts secured by bills of exchange on negotiable promissory notes; hence the amount due thereon is exempt from garnishment.[54] A

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51 45 S. C. 83, 22 S. E. 747 (1895).

52 19 Ill. App. 322 (1885).

53 Section 47 N. I. L. provides: "An instrument negotiable in its origin continues to be negotiable until it has been restrictively indorsed or discharged by payment or otherwise."

54 Oakdale Mfg. Co. v. Clarke, 29 R. I. 192, 69 Atl. 681 (1908).

purchaser after maturity may sue in his own name.[55] A holder [56] who becomes such after maturity acquires the legal title and does not, like an assignee sue as agent of the assignor. In *Davis v. Miller* [57] the payee after maturity transferred the note to the plaintiff. The defendant, maker of the note, without notice of the transfer, paid the amount due on the note to the payee. The defendant stated as his defense that payment had been made before notice of transfer. In the course of the opinion, the court said:

"There is a material distinction in regard to notice, between a negotiable note, and choses in action not negotiable. Choses in action not negotiable are not designed for circulation. They may be assigned in equity, but not so as to prejudice the debtor who, until he receives notice of the assignment, may safely make payment to the original creditor."

The court gave judgment to the plaintiff. Valuable consideration was not considered necessary to a valid transfer of a negotiable instrument which may be the subject of a gift either *inter vivos* or *mortis causa.* In *Milnes v. Dawson* [58] it was held that payment by the acceptor to the drawer of a bill of exchange, after the latter had indorsed it without value to the indorsee was not a good defense to an action by the indorsee against the acceptor of the bill. Parke, B., said:

"It would be altogether inconsistent with the negotiability of these instruments, to hold, that after the indorser has transferred the property in the instrument, he may, by receiving the amount of it, affect the right of his indorsee."

In *Davis v. Miller* the judge could see no distinction between gifts made after maturity and those made before. In

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55 Section 51 of the N. I. L. provides: "The holder of a negotiable instrument may sue thereon in his own name; and payment to him in due course discharges the instrument."

Also, Ohio Valley Banking & Trust Co. v. Great South. F. Ins. Co., 176 Ky. 694, 197 S. W. 399 (1917).

56 "Holder" means the payee or indorsee of a bill or note, who is in possession of it, or the bearer thereof. N. I. L., § 191.

57 14 Gratt (Va.) 1 (1857).

58 5 Ex. 948, 155 Eng. Rep. 413.

view of the fact that the donor could not revoke the gift in either case, there probably would be none.[59] The holder's right on the instrument may be lost by renunciation.[60] In this respect the rights on the instrument would closely resemble the rights on a chattel which may be lost by abandonment. Trover may be maintained for a negotiable instrument after it is due.[61] Overdue negotiable instruments are considered as goods and chattels within the Statute of Frauds, although choses in action are not generally within the Statute.[62] From this brief review of some of the attributes of overdue paper it would seem that there are many circumstances in which past due paper is treated much as a chattel and that the statement of the Massachusetts' court in holding it to be a chose in action cannot be supported in all cases.

The holdings in a few of the cases where the indorsee acquired the instrument after maturity will be noted. First with reference to those decided before the Negotiable Instrument Act:

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59 The cases in which gratuitous assignments are revocable are set out in THE RESTATEMENT OF THE LAW OF CONTRACTS, § 158, as follows:

"(1) The right acquired by the assignee under a gratuitous assignment is revocable by the assignor's death, by a subsequent assignment by the assignor, or by notice from the assignor received by the assignee or by obligor, unless,

(a) the assignment is in a writing either under seal or of such a nature as to be capable of transferring title to a chattel without delivery thereof and without consideration; or

(b) the assigned right is evidenced by a tangible token or writing, the surrender of which is required by the obligor's contract for its enforcement and this token or writing is delivered to the assignee; or

(c) the assignor should reasonably expect the assignment to induce action or forbearance of a definite and substantial character on the part of the assignee and such action or forbearance is induced.

(2) If an assignee holding an assignment revocable because gratuitous obtains before revocation,

(a) payment or satisfaction of the obligation, or

(b) judgment against the obligor, or

(c) a new contract of the obligor by novation.

He can hold what he has thus acquired. Whatever he obtains after revocation can be recovered from him by the assignor."

60 N. I. L. § 122.

61 Miller v. Race, 1 Burr. 452, 2 Keny. 189, 97 Eng. Rep. 398 (1758).

62 WILLISTON ON SALES (1924) § 67.

The English rule is illustrated in the case of *In re European Bank. Ex parte Oriental Commercial Bank.*[63] In this case, one *Demetrio Pappa* purchased negotiable paper with funds belonging to the Oriental Commercial Bank and sold the same to the Eastern Commercial Bank after maturity. The Oriental Bank claimed the proceeds of the paper. The court adopted the statement of Sir R. Malins, V.C., as laid down in *Ex parte Swan*[64] as follows:

"It is said that the indorsee of a bill which is over due takes it subject to all the equities. Perhaps a better expression would be . . . . that he takes the bill subject to all its equities 'that is, the equities of the bill, not the equities of the parties.' . . . The indorsee of an over due bill takes it subject to all the equities that attach to the bill itself in the hands of the holder when it was due; but he does not take it subject to claims arising out of collateral matters, such as the statutory right of set-off."

The judgment was in favor of the Oriental Bank. The English rule therefore would be that maturity of a negotiable instrument operates as constructive notice, not only of equitable defenses but also of equities of ownership. There are decisions adopting the same rule in the United States. In *Mayer v. Bank*[65] a trustee of over due negotiable paper sold it to an innocent purchaser. It was held that the paper could be replevied by the *cestui.* The court held that an indorsee after maturity stands in the shoes of his indorser. In *Kernohan v. Durham*[66] the payee sold a note to the plaintiff but instead of delivering it to him he delivered a forged copy. The genuine note was sold to the defendant, a *bona fide* purchaser after maturity. The note was held subject to the plaintiff's equity in the defendant's hands. Under decisions such as these, it is plain that the courts regard past due instruments as choses in action applying the maxim: "Where there are equal equities, the first in point of time will prevail."

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63 5 Ch. App. 358, 39 L. J. Ch. 588, 22 L. T. 422, 18 W. R. 474, L. J. (1870).
64 L. R. 6 Eq. 344, 18 L. T. 230, 16 W. R. 560 (1868).
65 86 Mo. App. 108 (1900).
66 48 Oh. St. 1 (1891).

There are a few decisions contrary to those cited in next preceding paragraph. In *Sanderson v. Crane* [67] the payee who had passed through insolvency withheld a note from his assignee. After maturity of the note, he sold the same to a *bona fide* purchaser. The court held that the note was not affected with equities in favor of the assignee. In *Crosby v. Tanner* [68] a note was held by Tanner which was subject to an equity in favor of one Melhop. After maturity of the note Tanner sold the same to the plaintiff, a *bona fide* purchaser. Melhop asserted that the note was subject to his equity, but the court said:

"The position is based upon the familiar doctrine that the transfer of a negotiable instrument, after maturity, is governed by the rules applicable to the assignment of a chose in action, which divests no equity affecting it while in the hands of the assignor. But the rule is not applicable to the case before us, for the reason that the equities, which survive the assignment, are those which are between the parties to the instrument, and not those between the assignor and one not a party."

The court seemed to regard the instrument as a chose but applied Chancellor Kent's doctrine of latent equities as set out in *Murray v. Syburn.*[69] In *Moore v. Moore* [70] the indorsement of the note in question was secured by fraud, and the title came to a *bona fide* purchaser after maturity. In delivering the opinion of the court, Justice Mitchell said:

"It is familiar law that if the owner, although induced thereto by fraud, invests another with the apparent legal title to chattels, in pursuance of a contract, the person so clothed may transfer an unimpeachable title to a good-faith purchaser. . . . We are unable to discover any good reason for a distinction in that regard between chattels and such instruments as may be assigned by endorsement, so as to give the assignee a complete legal title."

In *Young Men's Christian Ass'n Gymnasium Co. v. Ford Nat. Bank* [71] negotiable notes belonging to the Christian As-

67 14 N. J. L. 506 (1834).
68 40 Iowa 136 (1874).
69 2 John. Ch. 441 (1817).
70 112 Ind. 149, 13 N. E. 673 (1887).
71 179 Ill. 599, 54 N. E. 297 (1899).

sociation were pledged as collateral security. The pledgee sold the same to the bank after maturity. The Association brought an action against the bank to establish its equity in the notes. The judgment was for the bank. The judgment was based upon the following statement of law:

"The equitable principle which underlies this doctrine, and which is universally admitted to be just and sound, is that if a loss occurs, by which one of two innocent persons must suffer, that one should sustain the loss who has most trusted the party through whom the loss came."

These cases illustrate the difficulties which the courts faced in attempting to determine the status of a purchaser of past due negotiable paper before the enactment of the Negotiable Instrument Act. As noted some courts took the position that past due negotiable paper was a chose in action and applied the rules governing assignments of choses. Other courts regarded it as a chose and accepted Kent's theory of latent equities. Other courts regarded the instrument as a chattel and applied the general property rules of a transfer. Still other courts decided the cases on the theory of estoppel.

The Negotiable Instrument Act contains the following provision:[72]

"In the hands of any holder other than a holder in due course, a negotiable instrument is subject to the same defenses as if it were non-negotiable. But a holder who derives his title through a holder in due course, and who is not himself a party to any fraud or illegality affecting the instrument, has all the rights of such former holder in respect of all parties prior to the latter."

It would seem that under this provision the Negotiable Instrument Act has adopted the English rule as explained in *In re European Bank*,[73] if defenses be construed to include equitable defenses and equities of ownership; hence overdue commercial paper either carries with it constructive notice of all equitable defenses and equities of owner-

72 N. I. L., § 58.
73 *Supra* note 63.

ship or it is treated as a chose in action. In the latter alternative, the courts would refuse to accept the theory of latent equities. In *Deuters v. Townsend* [74] Cockburn, C.J., says:

"The only consequence of indorsing a bill after it is due is, that whatever would have been a defense to an action on the bill in the hands of the transferor is equally so to one in the hands of the transferee."

The indorsee after maturity may sue on the instrument. Remembering the rule as to assigning choses in action, it would seem that the correct basis for explaining the rule in *In re European Bank* [75] is that a negotiable instrument past due carries constructive notice of all equities. A purchaser after maturity, therefore, could not be a *bona fide* purchaser.

Cases dealing with the rights of a purchaser of past due negotiable paper decided under the Negotiable Instrument Act may be considered under the following subdivisions:

Defenses existing at the time of transfer in favor of the primary obligor against the transferor.

Defenses in favor of the primary obligor arising subsequent to the transfer.

Defenses in favor of the payee indorser.

Equitable claims to ownership of the paper.

Set-offs and counterclaims.

First, as to cases where the primary obligor had a defense against the transferor at time of transfer: In *Guthrie v. Moore* [76] a note was given by the purchaser of land to the vendor, secured by a purchase money mortgage. *Held,* that an agreement that the note was not to be enforced against the maker until prior liens against the land had been discharged by the vendor could be set up against the indorsee

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74 5 B. & S. 613, 4 New Rep. 272, 33 L. J., Q. B. 301, 10 Jur. N. S. 1072 (1864).

75 *Supra* note 63.

76 108 S. E. 334 (N. C. 1921).

after maturity, the notes being past due, the defendant took the notes subject to and with notice of any equities and defenses existing in favor of the maker. The defense here it seems would be conditional delivery.

In *Farmers' and Merchants' Bank v. Siemers* [77] a payee who was trustee after maturity sold the instrument to a *bona fide* purchaser. After holding that the facts showed actual notice, the court said:

"A holder taking a note after maturity takes it subject to all equities with which it was incumbered in the hands of the transferor, whether he has notice of them or not."

In *Woulfe v. Douglas Storage Van and Express Co.*[78] a note executed by the defendant was sold to a foreign corporation in Illinois, which had not complied with the Foreign Corporation Act of this state. After maturity, the corporation sold the note to the plaintiff. The position assumed by the defendant was since the foreign corporation, which held the note at maturity, could not have recovered on the note, the plaintiff, the indorsee of the corporation could not recover. The court gave judgment for the plaintiff without referring to the Negotiable Instrument Act. The court rested its decision on *Young Men's Christian Ass'n Gymnasium Co. v. Rockford Nat. Bank* [79] and on *Justice v. Stonecipher.*[80] Quoting from the former case:

"When we speak of equities between the parties it is not to be understood by this expression that all sorts of equities existing between the parties from other independent transactions between them are intended, but only such equities as attach to the particular note, and, as between those parties, would be available to control, qualify, or extinguish any rights arising thereon."

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77 242 S. W. 417, (Mo. 1922); In Greenlees v. Chezik, 190 Pac. 667 (Colo. 1920), the indorser took after maturity. Court held that the indorsee would be subject to a defense of payment. In Graves v. Burch, 181 Pac. 354 (Wyo. 1919), the facts were such that the payee was not equitably entitled to recover the attorney's fees stipulated for in the note. *Held,* the holder taking from the payee after maturity could not collect the attorney's fees on the note.

78 232 Ill. App. 230 (1924).

79 *Supra* note 71.

80 267 Ill. 448, 108 N. E. 722 (1915).

In Illinois, it would therefore seem that Chancellor Kent's doctrine of latent equities is still the law on the subject under discussion.

In *Schlamp v. Manewal* [81] Manewal signed a note for the accommodation of Schlamp with the understanding that Schlamp was to use the note to raise money. After maturity, Schlamp transferred the note to the plaintiff as payment for stock. Judgment was rendered for Schlamp, the court holding that the plaintiff was in no better position than he would have been had he acquired the note before maturity knowing of all defenses available to defendant.

In *Robichaux v. Block*[82] Block executed a note to one Martel without consideration for the amount of $77.50. This note was secured by a mortgage with an agreement that Martel was to use the note in securing a loan from the St. Mary's Bank and Trust Company. After maturity the note was seized on a *fi. fa.* and sold to plaintiff. Court held that the defenses of want of consideration was good against the plaintiff, and that the plaintiff was subject to all equities and defenses which defendant could have urged against Martel.

In *Beneficial Loan Ass'n v. Hillery* [83] Hillery executed a note to the Continental Banking and Trust Company as payment for stock in said company. The company retained the stock as security for the note. After maturity the note and stock were transferred to plaintiff as security for a loan. The payee company failed. Judgment was for the plaintiff on the note. In the course of the opinion the court said:

"The holder of a promissory note which comes into his hands after maturity takes it subject to all legal defenses which the maker may have against its enforcement."

It will be noted that the court limited its statement to defenses, saying nothing about equities of ownership.

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81 190 S. W. 658 (Mo. 1916).
82 81 So. 371 (La. 1919).
83 113 Atl. 324 (N. J. 1921).

In *Gibson v. Gillespie* [84] the plaintiff, after maturity, acquired the note from the payee. The maker's defense was that he had executed the note for the accommodation of the payee. The court stated:

"A note assigned when overdue is subject in the hands of the assignee, to every infirmity which it had when in the hands of the payee. One who takes negotiable paper after maturity takes subject to every defense which could have been urged when the paper was in the hands of the original payee. Absence or failure of consideration is matter of defense as against any person not a holder in due course."

In *Farmers' Bank of Camarillo v. Goodrich* [85] the payee negotiated a note after maturity to the plaintiff under such circumstances that the transfer constituted a fraud on the defendant, maker. *Held,* the plaintiff was subject to all defenses that the payee was subject to.

In *Crife v. Wade* [86] the plaintiff brought suit on a note acquired by him from the payee after maturity. Defendant asked that the note be delivered up and cancelled on ground of fraud, conditional delivery, and failure of consideration. *Held,* that there was no danger that the note might come into the hands of an innocent purchaser for it was past due and subject to all the equities and defenses that might be considered as against the plaintiff. Cancellation was refused.

In *Cunning v. Locke* [87] the note was indorsed to the plaintiff after maturity. The court said:

"The plaintiff took it dishonored, but none the less it could be sold and transferred and recovery had thereon if the defenses failed. So far as the indorsement is concerned, it is sufficient to pass title."

In *First Nat. Bank in Alexandria, S.D., v. Ernst* [88] the question was whether the defendant, Rau F. Ernst, who had signed the note as surety for her husband was liable on

84 152 Atl. 589 (Del. 1928).
85 266 Pac. 550 (Colo. 1928).
86 261 Pac. 72 (Or. 1927).
87 258 Pac. 192 (Or. 1927).
88 219 N. W. 798 (Neb. 1928).

the note under the Nebraska law, the plaintiff acquiring the note after maturity. It was held that one taking a note after maturity is not an innocent purchaser. The court apparently adopting the theory of constructive notice.

In *Dunn v. Cutley* [89] the defendant executed the note in question for the accommodation of one Arthur L'Hommedieu. The holder at maturity was subject to an estopped in favor of the defendant. After maturity the note was transferred to the plaintiff for sole purpose of bringing suit thereon. *Held,* that the plaintiff was subject to the estoppel.

In *Westchester Mortg. Co. v. Newport Trust Co.*[90] the court held that a purchaser after maturity was subject to any defense available to the maker if the note had remained in the hands of the payee.

In *Bradford Realty Corporation v. Beetz* [91] the court held that a purchaser after maturity takes the instrument subject to such defenses as may have existed at the time of the transfer.

In *Pacific-Southwest Trust & Savings Bank v. Valley Finance Corporation* [92] the court clearly treats an overdue instrument as a chose in action. After referring to section 58 of the Negotiable Instrument Act, the court proceeds as follows:

"Section 1459 provided: 'A non-negotiable written contract for the payment of money . . . . may be transferred. . . . Such indorsement shall transfer all the rights of the assignor under the instrument to the assignee, subject to all equities and defenses existing in favor of the maker at the time of the indorsement.' Section 953 provided: 'A thing in action is a right to recover money . . . by a judicial proceeding.' Section 368, Code of Civil Procedure, provided: 'In the case of an assignment of a thing in action, the action by the assignee is without prejudice to any set-off, or other defense existing at the time of, or before, notice of the assignment. . . .' "

89 151 Atl. 367 (N. J. 1930).
90 146 Atl. 774 (R. I. 1929).
91 142 Atl. 395 (Conn. 1928).
92 280 Pac. 134 (Cal. 1929).

This interpretation not only subjects the purchaser after maturity to defenses and equities in the instrument but also to collateral equities, such as, a set-off.

As to cases involving defenses in favor of the primary obligor, arising subsequent to the transfer:

In England the case of *Milnes v. Dawson*[93] sets out the true situation. In this case the defendant was sued as acceptor. He set up as a defense that the payee indorsed the bill to the plaintiff without any consideration and that after maturity he had paid the bill to the payee. In the course of the opinion the court expressed its opinion as follows:

"It would be altogether inconsistent with the negotiability of these instruments, to hold, that after the indorser has transferred the property in the instrument, he may, by receiving the amount of it, affect the right of his indorsee. When the property in the bill is passed, the right to sue upon the bill follows also. . . . A bill of exchange is a chattel, and the gift is complete by delivery coupled with the intention to give."

Although the bill was not shown to have been transferred to the plaintiff after maturity, the plaintiff was, of course, not a holder in due course. So it would seem that the reasoning here would be applicable to a bill transferred after maturity.

In New York, the law was well stated in *First Nat. Bank of Champlain v. Wood.*[94] In this case the plaintiffs were donees. Speaking of the transaction the court said:

"It is admitted that the donees might at that time have maintained an action against the makers on the notes, and recovered thereon. If so, it could only be upon the ground that they had become the owners of the notes. They became such owners only by virtue of a voluntary gift, accompanied by an immediate and unconditional delivery. This, indeed, did give to the donees a perfect title and absolute ownership to and in the notes, as there were then no equities existing between the original parties. . . . How is it, then, that such ownership, although

93 155 Eng. Rep. 413, 5 Ex. 947 (1850).
94 27 N. E. 1020 (N. Y. 1891).

absolute at the time of the transfer, and giving the holders of the notes a right of action, shall nevertheless, if not acted on by collecting the money, be liable at any future time to be changed, and, indeed extinguished, by matters subsequently arising between those original parties? . . . People who receive gifts of negotiable securities take them subject to all equities then existing between the original parties, but not subject to all which may thereafter, and while they are absolute owners of such securities, exist between those parties."

As to cases decided since the Negotiable Instrument Act:

In *Greer v. Orchard* [95] one Graves, was the payee of a note. The note was purchased by the plaintiff's husband who directed Graves to transfer it to his wife, the plaintiff. Subsequently the money due on the note was paid to the plaintiff's husband. It was not shown that the husband had authority to act as the plaintiff's agent. The judgment was for the defendant. The court reasoned that the plaintiff was not a holder in due course, saying:

" 'A gift of a negotiable instrument of a third party is not such a negotiation of it in the usual course of business as to give the donee the full protection which is extended a *bona fide* holder for value.' The reason for the rule which protects a *bona fide* purchaser for value and makes it applicable to commercial paper is absent in case of a gift of such paper from one person to another, where the purchaser and donor is familiar with all of the facts affecting the condition of the note."

There seemed to be no doubt as to the husband's intention to make a gift to the plaintiff, and that the latter was the complete owner of the note against which the maker had no defense at the time of the execution and transfer to the plaintiff. The decision results in placing a power in the donor to extinguish the right of the donor against the obligor, a rather startling result in general property law. Although the preceding cases did not involve transfers after maturity, the holder was not a holder in due course and it seems that in cases of transfers after maturity the reasoning in cases would be applicable.

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[95] 161 S. W. 875 (Mo. 1913).

In *Clark v. Wheeler* [96] the payee transferred a note to the plaintiff after maturity. Subsequent to the transfer, the defendant paid the note to the payee. Judgment was for the plaintiff. The court said:

"But payment to the original payee after transfer and delivery of the note is no defense against the transferee, although he acquired the note after maturity. . . . A note, though overdue, is still negotiable. . . . The indorsee, taking it after maturity, can sue on it in his own name. The payor, having made the paper negotiable, cannot assume that it has not been transferred, although he has defaulted in his contract of payment. Paying the note, he has the right to have the note given up, or his partial payment indorsed."

The court further says that:

"Section 51 of the Negotiable Instrument Act provides that payment to a holder in due course discharges the instrument. No suggestion is found in the act that payment to any other than the legal holder will discharge it." [97]

In *Johnson v. People's Bank* [98] it was doubtful as to when the plaintiff acquired the note; however the court held "Where a promissory note is acquired by a transferee after its maturity, the transferee does not take it subject to a defense by the maker against the payee arising after the transfer of the note."

As to defenses in favor of the payee indorser:

In *Webb v. Rice* [99] Webb, the payee of a note indorsed it in blank and gave it to his bank for collection. After maturity the bank sold it to Mrs. Rice. Mrs. Rice brought suit against Webb as indorser. The court held that Mrs. Rice obtained no title to the note, the reason being that since she purchased after maturity, she took it subject to all defenses which could arise on the note, and that she got only such title as the bank had, which was only the authority

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96 121 Atl. 588 (N. H. 1923).

97 Section 88 of the N. I. L. provides: "Payment is made in due course when it is made at or after the maturity of the instrument to the holder thereof in good faith and without notice that his title is defective."

98 137 S. E. 104 (Ga. 1927).

99 97 So. 419 (Miss. 1923).

to collect the note and not to sell it. The bank, however, must have had the legal title since it was the holder and indorsee of the instrument which still remained negotiable. Title did pass to the plaintiff, even though it was defective. The statement therefore that plaintiff did not have title appears too broad.

As to equitable claims to ownership of the paper:

In *Justice v. Stonecipher* [100] Justice, payee and owner of notes, indorsed them in blank and intrusted them with Stonecipher. The latter was to collect the interest during absence of Justice. After maturity Stonecipher pledged them with the Bridgeport State Bank as security for a loan. Justice brought an action against the Bank and Stonecipher to recover the notes. The court gave judgment for the Bank. To the defendant's position that Stonecipher's title was defective under section 55 of the Negotiable Instrument Act,[101] and that, as a result, the defendant bank must, under section 59 of the Negotiable Instrument Act,[102] sustain the burden of proving himself a holder in due course under section 52 of the Negotiable Instrument Act,[103] the court answered:

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100 267 Ill. 448, 108 N. E. 722 (1915).

101 Section 55 of the N. I. L. provides: "The title of a person who negotiates an instrument is defective within the meaning of this act when he obtained the instrument, or any signature thereto, by fraud, duress, or force and fear, or other unlawful means, or for an illegal consideration, or when he negotiates it in breach of faith, or under such circumstances as amount to a fraud."

102 Section 59 of the N. I. L. provides: "Every holder is deemed *prima facie* to be a holder in due course; but when it is shown that the title of any person who has negotiated the instrument was defective, the burden is on the holder to prove that he or some person under whom he claims acquired the title as a holder in due course. But the last-mentioned rule does not apply in favor of a party who became bound on the instrument prior to the acquisition of such defective title."

103 Section 52 of the N. I. L. provides: "A holder in due course is a holder who has taken the instrument under the following conditions:

1. That it is complete and regular upon its face; or
2. That he became the holder of it before it was overdue, and without notice that it had been previously dishonored, if such was the fact; or
3. That he took it in good faith and for value; or
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."

"Such a construction of said section 59 would render it meaningless. It is apparent, when the section is read in connection with all the other sections in that article, that it means to place the burden upon the holder to prove that he, or some person under whom he claims, comes within the provision of the fourth clause of the statutory definition of a holder in due course; that is, that the burden is then upon him to show that at the time the instrument was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it."

It is hard to see on what grounds other sub-divisions of section 52 of the Negotiable Instrument Act, especially part (2), were ignored. It has been suggested that the case must either be rested upon an estoppel or in the alternative to treat sections 52 and 59 of the Negotiable Instrument Act as intending to apply only to defenses to obligations on the instrument, whether of parties primarily or secondarily liable, and leaving the cases of equitable claims to ownership to instruments to be dealt with as omitted cases under section 196 [104] of the Negotiable Instrument Act.[105]

In *Priest v. Garnett* [106] Priest, the payee and owner of the note in question indorsed it in blank and delivered it to one Garnett. After maturity, Garnett, although having no authority to sell the note, sold it to the defendant. Priest brought replevin against Wood. Judgment was for the defendant. The court said:

"If the true owner of a negotiable note overdue, or of a non-negotiable note, clothes another with the usual evidences of ownership, or with full power of disposition, and third persons are led into dealing with such apparent owner, they will be protected in their dealings."

In *Hoidale v. Cooley* [107] one Maginnis acted as agent for the Northern American Life & Casualty Company. He took a negotiable note as payment for premiums. He was en-

104 Section 196 of the N. I. L. provides: "In any case not provided for in this act the rules of the law merchant shall govern."

105 Suggested by Professor Chafee, BRANNON'S NEGOTIABLE INSTRUMENT LAW (4th ed.) 505.

106 191 S. W. 1048 (Mo. 1917).

107 174 N. W. 413 (Minn. 1919).

titled to seventy percent of the note and the company to thirty percent. After maturity of the note, he sold the same to the plaintiff. As against the company, the court held that the plaintiff did not have title to the note and judgment was for the company.

In *Bacon v. Reichardt* [108] the defendant purchased a note after maturity, after the payee had received payment. The court held that the note was discharged.

In *Wilkinson v. Love* [109] one J. L. Wilkinson was the payee of a note which was secured by a deed of trust. Mrs. M. C. Wilkinson was the maker of the note. The maker transferred the note to a bank before maturity and for value. At maturity the payee and the bank agreed that a new note, executed by the maker and secured by a deed of trust, should be taken by the bank as payment of the first note. The second note was accordingly executed and received by the bank and the first note and trust deed surrendered by the bank to the payee, but was not marked paid. The payee then, transferred the first note to M. L. Wilkinson, a *bona fide* purchaser, after maturity and for value. The question was whether the deed securing the first note or the deed securing the second note deserved priority on the maker's property. The court held that priority should be given to the trust deed securing the first note. In the opinion it was stated:

"Through the admitted gross negligence of the officials of the bank, this note and duly recorded deed of trust were placed in the hands of the payee in the instruments, without any sort of mark or notation thereon to indicate that they had been paid or in any manner satisfied or canceled, or that the lien of the deed of trust was not what it purported on its face and upon the records—a valid, subsisting, first lien on the property conveyed thereby.

"Under these facts there are two principles which we consider applicable, either of which would require a reversal of the decree of the court below.

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108 208 S. W. 24 (Mo. 1918).
109 115 So. 707 (Miss. 1928).

"The note which the bank surrendered to the payee, J. L. Wilkinson, although overdue, was negotiable, and it seems to be the settled rule that the assignee of overdue negotiable paper takes it with notice of all the equities or defenses which the maker may have, but he does not take it with notice of the secret equities of third parties, or those arising out of collateral transactions."

The court further said:

"Chancellor Kent, speaking of this rule in this class of cases, says: 'The assignee can always go to the debtor and ascertain what claims he may have against the bond or other chose in action which he is about purchasing from the obligee, but he may not be able with the utmost diligence to ascertain the latent equity of some third person against the obligee.' "

The court also held that the doctrine of estoppel was applicable, as evidenced from the following words:

"By the neglect of these officers, these instruments were placed in the hands of the payee of the note in such form and condition that he was thereby clothed with the apparent authority to negotiate the note and security. . . . we think the loss, if any, resulting from the negligence of its officers, must be borne by the bank."

As to set-offs and counterclaims:

The case of *Burrough v. Moss* [110] illustrates the common law rule as to set-offs. In this case, a promissory note was made by the defendant which was payable to one Fearn, and by him indorsed to the plaintiff. After it became due, the defendant maintained he had a right to set off, against the plaintiff's claim, a debt due him from Fearn, who held the note at the date of maturity. It was held that the defendant had no right of set-off. Bayley, J., said:

"I agree with them in thinking, that the indorsee of an overdue bill or note is liable to such equities only as attach on the bill or note itself, and not to claims arising out of collateral matters."

Parke, J. was of the opinion that: "If there is an agreement, either express or implied, affecting the note, that is an equity which attaches upon it, and is available against any person who takes it when overdue"; it can be set off. "But it does not thence follow, that a right depending en-

110 109 Eng. Rep. 558, 10 B. and C. 558 (1830).

tirely on the Statute of Set-Off is applicable to such a state of things."

In the absence of special statutes, the English rule is the general rule in the United States.

In *Pusey & Jones Co. v. Hanssen* [111] the court expressed its opinion as follows:

"The general rule, or, perhaps, the common law rule, followed by the Supreme Court of the United States, is stated by Mr. Justice Swayne as follows: 'The transferee of overdue negotiable paper takes it liable to all the equities to which it was subject in the hands of the payee, but those equities must attach to the paper itself, and not arise from any collateral transaction. A debt due to the maker from the payee at the time of the transfer cannot be set off in a suit by the endorsee of the payee, although it might have been enforced if the suit had been brought by the latter.' "

In some jurisdictions the question is covered specifically by statute. The rule in New York is an example and is as follows:[112]

"If the action is upon a negotiable promissory note or bill of exchange which has been assigned to the plaintiff after it became due, a demand, existing against a person who has assigned or transferred it, after it became due, must be allowed as a counter claim to the amount of the plaintiff's demand, if it might have been so allowed against the assignor, while the note or bill belonged to him."

In cases of counterclaims, the defendant's cause of action does not arise out of collateral matters but out of the same transaction which gave origin to the note sued on or out of an agreement affecting the note. The note is consequently subject to an equity in favor of the maker when the note is purchased after maturity. In *Parks, Campbell, Findley Motor Co. v. Wolverton* [113] Wolverton purchased a car from the payee of the check sued on. The car was not as represented by the payee and the check was dishonored. After dishonor, the check was sold to the plain-

111 279 Fed. 488 (1922).
112 N. Y. Code Civ. Proc. (1920) § 502.
113 230 Pac. 863 (Okl. 1924).

tiff, who knew of the dishonor. *Held*, that the defendant could file a cross petition in the nature of a counterclaim as a defense to an action on the check.

Conclusion: The foregoing review of the cases show that despite the uniformity of the Negotiable Instrument Act the law as to the rights acquired by a purchaser of overdue negotiable paper is not uniform. In practically all jurisdictions, equitable defenses to liabilities on the contracts, good against the holder at maturity, will be good against a purchaser acquiring after maturity. The conflict of authority arises when there are conflicting legal or equitable claims of ownership to the paper. Here one line of authorities take the position that the *bona fide* purchaser after maturity takes the instrument subject to the adverse claims to ownership. On the other hand, there is a line of cases holding that the *bona fide* purchaser, after maturity, is not subject to the adverse claims of ownership. The cases subjecting the *bona fide* purchaser to opposing claims to ownership do so on the theory that the transfer of the past due instrument is subject to the same rules as the transfer of other personal property, that is, that one who buys it, even though *bona fide*, from one having no title acquires none. The cases protecting the *bona fide* purchaser after maturity proceed upon the theory that the true owner who clothes the assignor with the usual apparent indices of title is estopped from asserting his claim against the *bona fide* purchaser.

It seems to the writer that in the ultimate solution of the question, the common law doctrines as to assignability of *choses* in action should not be permitted to have an undue influence. These doctrines were worked out largely during a non-commercial age, when the great majority of property rights were represented by rights to tangible chattels and to real estate. At the present time, a large percentage of property rights consist of contractual rights, as witness the files of any of our financial institutions. At present we are

far from the day when the contractual relation was regarded as purely personal. In the development of the law pertaining to the non-negotiable contracts, we have noticed, first, the rule as inalienability; second, the express power of attorney; third, the implied power of attorney; fourth, the real party in interest statutes; and finally, the recommendations submitted by the authors of the Restatement of the Law of Contracts. Surely the general progress of the law and commercial needs should be taken into consideration in the decision of the question under discussion. The courts subjecting the purchaser of past due paper to all equities do so on the theory that the assignee has no title. It is believed that this is error. Past due paper is still negotiable and the holder of to bearer, or indorsee of to order paper, has the title and is not merely an agent. It is therefore submitted that as an aid to alienability, always an important characteristic, and uniformity in the general property law, the title of the purchaser of past due negotiable instruments should be recognized, and, facts should be applied permitting the following maxim: "Where there is equal equity, the law must prevail." This may be done by interpreting the word, "defenses," in section fifty-eight of the Negotiable Instrument Act to include only defenses to contracts on the instrument, leaving equitable claims to ownership to be determined by the general property rules.[114]

Elton E. Richter.
assisted by
Joseph R. Yoch.

University of Notre Dame, College of Law.

114 Professor Chafee has suggested that section 58 of the N. I. L. be amended to read as follows: "A holder who has taken the instrument in compliance with the first, third, and fourth conditions of section fifty-two is under no obligation to surrender the instrument or account for its proceeds because of the defective title of any prior party, and such holder may enforce payment of the instrument for the full amount thereof against all parties thereon, except persons who have defenses of their own, or who sign for the accomodation of any person and are allowed by law to avail themselves of defenses of such accommodated person."