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CONFLICT OF LAWS - NEGOTIABLE INSTRUMENTS - SITUS OF BEARER BONDS UNDER THE TRADING WITH THE ENEMY ACT

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COMMENTS

CONFLICT OF LAWS — NEGOTIABLE INSTRUMENTS — SITUS OF BEARER BONDS UNDER THE TRADING WITH THE ENEMY ACT—In a suit on a negotiable instrument, a problem arises as to just how many

places can claim valid jurisdiction. Thus, where the domiciles of the parties to a negotiable instrument are diverse, there are several jurisdictional possibilities. For example, with regard to a negotiable bearer bond it may be said that there is sufficient contact with the parties and/or the property (1) at the place where it was issued, (2) at the present location of the certificate of indebtedness, (3) at the location of the debtor corporation's office or principal place of business, or (4) in the state of incorporation of the debtor corporation. Logically, the location of either the certificate of indebtedness or the debtor himself would seem to be the preferable choices, and the conflict between them has been a source of frequent controversy. It is generally felt that the location of the certificate itself should be allowed to govern, but the purpose for which the decision is being made has occasionally altered a court's view in this respect. The purpose of this discussion is to point to the problems inherent in specifying the situs of the property interest of a negotiable bearer bond, particularly with relation to the subjection of such property interest to the provisions of the Trading With the Enemy Act.[1]

I. *Viewing the General Problem*

The difficulty of determining the situs of intangibles has long plagued the courts. The English common law courts felt that all sealed instruments, including bonds, must be enforced by "profert" of the original. Since the obligor was entitled to "crave oyer," the obligee could not recover without producing the certificate itself. Equitable relief was available, however, in the case of lost or mutilated bonds on the grounds of hardship. The common law courts subsequently relaxed some of their original restrictive rules and allowed suit on lost or mutilated bonds without "profert," but Equity retained its jurisdiction also.[2] Both courts preferred to think of the instrument as the obligation itself and not merely evidence thereof. This view, in addition to having an ancient background, is clearly justifiable today, since it accords with modern commercial usage.[3] Thus, with regard to the determination of situs of all types of certificates of indebtedness, the location of the instrument is considered as primarily significant for a number of purposes. For example, the validity of a transfer, as between

[1] 50 U.S.C. Appx. (Supp. IV, 1951) §§1-100.

[2] See brief historical statement, McGrath, Atty. Gen. v. Cities Service Co., (2d Cir. 1951) 189 F. (2d) 744, and cases cited therein.

[3] See GOODRICH, CONFLICT OF LAWS, 3d ed., 541 (1949), for a general discussion.

the transferor and the transferee, is governed by the law where the instrument was assigned or negotiated. Attachment, execution, and the possibility of quasi-in-rem action hinge on the same law.[4] But the place of payment, whether or not differing from the location of the instrument or the location of the debtor, also assumes great significance. Generally it governs with respect to the validity of presentment, notice, days of grace, and moratorium legislation.[5] Likewise the place of issuance generally governs negotiability, while the sufficiency of performance should be tested by the law applicable where performance is required.[6]

The situs problem, with respect to the administration of decedents' estates, has had a varied history. At one time a certificate of indebtedness was thought of merely as evidence.[7] But this has changed,[8] even to the extent that some cases have allowed a representative to sue on a bearer bond in his own name in a state other than that of his appointment.[9]

Although for most purposes the present day attitude is to treat bonds as chattels,[10] there is a tendency to recognize the relative significance of the location of the debtor.[11] The idea behind this, of course, is that it is the law at the place where the debt is that actually gives the obligation validity.[12] An example of this development is the trend of

[4] For discussion of this phase of the problem and voluminous citation of authority see STUMBERG, PRINCIPLES OF CONFLICT OF LAWS, 2d ed., 246 (1951); GOODRICH, CONFLICT OF LAWS, 3d ed., 173, 209, 541-545 (1949); Pavy, "Law Determining the Status of Negotiable Paper," 10 LA. L. REV. 357 (1950). It should be noted that garnishment is traditionally refused if the garnishee is the maker of a negotiable instrument which is outside the control of the jurisdiction.

[5] See such cases as Scudder v. Union National Bank, 91 U.S. 406, 23 L. Ed. 245 (1875); Gleason v. Thayer, 87 Conn. 248, 87 A. 790 (1913); Wooley v. Lyon, 117 Ill. 244, 6 N.E. 885 (1886); Cribbs v. Adams, 13 Gray (79 Mass.) 597 (1859).

[6] See discussion, STUMBERG, CONFLICT OF LAWS, 2d ed., 250 (1951).

[7] E.g., see Wyman v. Halstead, 109 U.S. 654, 3 S.Ct. 417 (1884).

[8] Iowa v. Slimmer, 248 U.S. 115, 39 S.Ct. 33 (1918). State statutes play an important role here. See Blodgett v. Silberman, 277 U.S. 1, 48 S.Ct. 410 (1928); Jordin v. Lavin, 319 Mass. 362, 66 N.E. (2d) 41 (1946).

[9] Knapp v. Lee, 42 Mich. 41, 3 N.W. 244 (1879); Sanford v. McCreedy, 28 Wis. 103 (1871).

[10] The strongest authority for this proposition seem to be cases like the following: United States Fidelity & Guaranty Co. v. Riefler, 239 U.S. 17, 36 S.Ct. 12 (1915); Blackstone v. Miller, 188 U.S. 189, 23 S.Ct. 277 (1903); Bozant v. Bank of New York, (2d) Cir. 1946) 156 F. (2d) 787; Bacon v. Hooker, 177 Mass. 335, 58 N.E. 1078 (1900). See also 6 WILLISTON, CONTRACTS 5311 (1938).

[11] See Blackstone v. Miller, 188 U.S. 189, 23 S.Ct. 277 (1903), allowing New York to tax transfers of bank trust deposits in New York by persons domiciled elsewhere. The case was overruled in part by Farmers Loan & Trust Co. v. Minnesota, 280 U.S. 204, 50 S.Ct. 99 (1929).

[12] If this were universally so, then discharge of a negotiable instrument at the place of payment should be valid everywhere; but courts have not been in accord on this point. See discussion, STUMBERG, CONFLICT OF LAWS, 2d ed., 251 (1951).

taxation on intangibles. In the earlier decisions, such as *Case of the State Tax on Foreign Held Bonds*[13] and *Blackstone v. Miller*,[14] the United States Supreme Court supported the proposition that the bond is itself the obligation, a view thought to be required by the Fourteenth Amendment of the United States Constitution.[15] Justice Holmes, speaking for the Court in the latter case, said:

> "Power over the person of the debtor confers jurisdiction. . . . And this being so we perceive no better reason for denying the right of New York to impose a succession tax on debts owed by its citizens than upon tangible chattels found within the state at the time of the death."[16]

This reasoning, which would seem to apply to bonds as well as anything else, would appear to support the assertion of jurisdiction in reference to the debtor, but Justice Holmes specifically distinguished the case of bonds by adding:

> ". . . the debt is inseparable from the paper which declares and constitutes it, by a tradition which comes down from more archaic conditions. . . . Therefore, considering only the place of the property, it was held that bonds held out of the state could not be reached. The decision has been cut down to its precise point by later cases. . . ."[17]

But quite recently the United States Supreme Court has indicated that there are no due process limitations on the power of a state to tax intangibles and choses in action where the state has a reasonable relation to them, provided that each taxing state must offer some potential benefit or protection to the parties interested in the property being taxed.[18] This indicates that the domiciliary states of both the creditor and the debtor can tax a bond, and necessitates the conclusion that, for taxation purposes, bonds are in no different category from other choses

[13] 15 Wall. (82 U.S.) 300, 21 L.Ed. 179 (1873), denying the validity of a Pennsylvania statute taxing foreign held bonds issued by a Pennsylvania corporation.

[14] See note 11 supra.

[15] Baldwin v. Missouri, 281 U.S. 586, 50 S.Ct. 436 (1930); Blodgett v. Silbermann, 277 U.S. 1, 48 S.Ct. 410 (1928).

[16] 188 U.S. 189 at 206.

[17] Ibid. Judge Learned Hand feels that the quoted statement is really a manner of avoiding the precedent the court had decided to overrule. See McGrath v. Cities Service Co., (2d Cir. 1951) 189 F. (2d) 744 at 747.

[18] State Tax Commission of Utah v. Aldrich, 316 U.S. 174, 62 S.Ct. 1008 (1942). Brown, "Multiple Taxation of Intangibles," 40 MICH. L. REV. 806 (1942).

in action. Thus, statements such as a recent one made by Judge Learned Hand that,[19] "Bonds have never been considered only as evidence of the obligation; . . . and that notion persists," must be read in the context to which they specifically refer; for though bonds are not merely evidence of the obligations, they are not for all purposes so exclusively comparable to a chattel as to preclude judicial action by any state possessing the proper contacts.

It may reasonably be concluded that the determination of the situs of a bearer bond will depend upon the purpose for which the determination is being made.[20] If this conclusion is objectionable, then it will be necessary to admit that at times the bond seems to have partial situs in two places: the domicile of the debtor corporation and the location of the instrument. Perhaps the best manner in which to look at the problem is to say that the situs is with the instrument, but that the jurisdiction which has control of the debtor has sufficient contact with the property interests, at least for taxation purposes.[21] The extent to which the same is true for other purposes, particularly federal seizure during wartime, will be dealt with subsequently.

II. *Scanning The Statute*

For the combined purposes of weakening the enemy during wartime, making more money available for the prosecution of war, and reimbursing the United States for war expenditures, the Trading With the Enemy Act[22] authorizes the taking of all of the property of an enemy alien which is "within the United States." The first measures to effectuate this purpose were enacted on October 6, 1917. The extent to which Congress intended to subject to the act property not usually considered "located within the United States" is not exactly clear from the original Trading With the Enemy Act, but subsequent amendments[23] and executive orders pursuant thereto indicate that

[19] Bozant v. Bank of New York, (2d Cir. 1946) 156 F. (2d) 787 at 790.

[20] For the view of another writer reaching the same conclusion and citation of extensive authority, see 49 MICH. L. REV. 1064 (1951).

[21] The United States Supreme Court has been willing to go quite far in allowing jurisdiction where there is control over the debtor. See Standard Oil Co. v. New Jersey, 341 U.S. 428, 71 S.Ct. 822 (1951).

[22] 50 U.S.C. Appx. (Supp. IV, 1951) §§1-100.

[23] For a short discussion of the amendments since the original act see Scott, "The Supreme Court on Trading With The Enemy," 27 THE PHI DELTA DELTA 3 (Jan. 1949).

everything within the possible grasp of the Alien Property Custodian[24] is included.[25] Thus section 7(c) of the act authorizes that[26]

> "if the President shall so require any money or other property including . . . choses in action, and right and claims of every character and description owing or belonging to . . . an enemy . . . shall be . . . paid over to the Alien Property Custodian . . . or the same may be seized by him."

Section 7(e)[27] provides, "in case of payment to the Alien Property custodian of any debt or obligation owed to an enemy" he shall have the power to execute a valid discharge and shall "deliver up any notes, bonds, or other evidence of indebtedness or obligations . . . that may have come into his possession." Section 9(n)[28] declares, "In the case of property consisting . . . of bonded or other indebtedness . . . evidenced by bonds . . . where the right, title, and interest in the property (but not the actual . . . bond . . .) was conveyed, transferred, assigned, delivered, or paid to the Alien Property Custodian or seized by him . . .," the true owner may be indemnified as provided elsewhere[29] in the act.

Negotiable bearer bonds are clearly intended to be included within the scope of the act, since they are mentioned specifically numerous times and referred to by implication many more. Moreover, the act has been extended to include many types of interests usually not otherwise subjected to the processes of our legal system, such as the spendthrift trust,[30] and the "property interest" contained in the wife's statutory right to elect to take a percentage share of her husband's estate against her husband's will.[31] Even more significant is that the federal law on seizure overrides a state law concerning the embodiment of

[24] Executive Order 9095, March 11, 1942, established the Office of Alien Property Custodian as a part of the Office of Emergency Management of the Executive Office of the President and set out the powers of this officer. Executive Order 9193, July 6, 1942, amended his duties. On October 14, 1946 Executive Order 9788 terminated the Office of Alien Property Custodian and transferred his functions and property seized to the Attorney General.

[25] Compare HUBERICH, TRADING WITH THE ENEMY, CIVIL RIGHTS AND DISABILITIES OF ENEMY ALIENS (1918), with DOMKE, TRADING WITH THE ENEMY IN WORLD WAR II (1943) and supplement, THE CONTROL OF ALIEN PROPERTY (1947).

[26] 50 U.S.C. Appx. (Supp. IV, 1951) §7(c).

[27] Id., §7(e).

[28] Id., §9(n).

[29] Id., §§5(b)(2) and 7(e).

[30] Great Northern Railway v. Sutherland, 273 U.S. 182, 47 S.Ct. 315 (1927).

[31] Matter of Herter, 193 Misc. 602, 83 N.Y.S. (2d) 36 (1948), affd. 274 App. Div. 979, 84 N.Y.S. (2d) 913 (1948). For other interesting discussions of the scope of the Trading With the Enemy Act see: Bishop, "Judicial Construction of Trading With the Enemy Act," 62 HARV. L. REV. 721 (1949); Rabel, "Situs in Enemy Property Measures," 11 LAW AND CONTEM. PROB. 118 (1945); 9 UNIV. PITT. L. REV. 228 (1948).

corporate shares in the certificate itself, so the shares of a foreign national in an American corporation can be seized even though the Alien Property Custodian never actually has possession of the share certificates.[32] It should also be observed that cessation of hostilities does not prevent the subsequent seizure of the property of any one who satisfactorily qualified as an "enemy" during the hostilities.[33]

III. *Reconciling the Cities Service Case*

In the case of *Cities Service Company and Chase National Bank v. McGrath, Atty. Gen.*,[34] the Attorney General as Alien Property Custodian had vested[35] property interests in negotiable bearer bonds issued by the Cities Service company. The bank was the indenture trustee. Cities Service was ordered to cancel the bonds and deliver the proceeds, plus accrued interest, to the attorney general. The controversial bond certificates were in the Russian sector of Berlin at the time of the vesting order, but their present whereabouts was unknown. The federal district court held the situs of the property interest to be with the bond certificate and thus not "within the United States" as required by the Trading With the Enemy Act.[36] The court of appeals reversed,[37] indicating that situs of bearer bonds was not such a crystallized idea as to prevent the vesting here; the United States Supreme Court affirmed.

The primary argument of the bond obligors stressed the historical situs concept. Judge Learned Hand, speaking for the court of appeals, indicated that the intervention of equity into cases of lost or mutilated bonds had dispelled the concept that the actual debt was embodied in the bond certificate. He emphasized that the law where the debtor corporation is domiciled is the one giving validity to the obligation and held the proper view to be that the certificate is mere parchment, and the bond is actually no more than a chose in action. Judge Hand obviously did not mean this to apply universally,[38] because, as for some purposes discussed previously, the bond can best be treated as a chattel. Justice Clark, writing for the United States Supreme Court, classifies the "situs with certificate" theory as a fiction[39] which, though valid in

[32] Silesian American Corp. v. Clark, 332 U.S. 469, 68 S.Ct. 179 (1947); Great Northern Ry. Co. v. Sutherland, 273 U.S. 182, 47 S.Ct. 315 (1927).

[33] Woods v. Miller, 333 U.S. 138, 68 S.Ct. 421 (1948).

[34] 342 U.S. 330, 72 S.Ct. 334 (1952).

[35] Vesting Order 12960, March 29, 1949.

[36] (D.C. N.Y. 1950) 93 F. Supp. 408.

[37] (2d Cir. 1951) 189 F. (2d) 744.

[38] See his opinion in Bozant v. Bank of New York, (2d Cir. 1946) 156 F. (2d) 787.

[39] The same idea played a large part in the decision in Standard Oil Co. v. New Jersey, 341 U.S. 428, 71 S.Ct. 822 (1951). See pp. 438-439 of the opinion.

some instances, should not be applied to defeat congressional intent and the war power of the United States, when another interpretation will effectuate them. This seems to be the clearer approach to what both courts undoubtedly meant.

The *Cities Service* case, like the more recent state intangible tax cases, negatives any present attempt to settle the situs question. Actually, it raises the question as to when the general rule will be disregarded and when it will be applied. Although the case may be taken as an indication of a trend away from the "chattel" approach, it is not completely unique. No other prior United States cases have been found on the precise point, but the same result was reached by a Union of South Africa court,[40] which held that bearer shares and bearer debentures of a gold mine in Transvaal were situated and subjected to seizure as enemy property within the Union, irrespective of the place in which the certificates were to be found.[41] Moreover, a recent international agreement specifically recognizes the inherent power of the sovereign where incorporation took place to control and dictate the ownership in corporate obligations or interests in currency and commercial paper as well as in stock certificates.[42] There is no doubt that federal policy overcomes state policy, when necessary, concerning the situs of corporate shares.[43] As long as the debtor corporation is in the United States the same should be true in the case of other intangibles. The power of the federal government to influence changes in the normal concepts

[40] There are some cases which are closely significant. One is In re Central State's Power & Light Corporation, (D.C. Del. 1951) 99 F. Supp. 157, which followed the lead of Judge Hand's decision in the Cities Service case when it held that bonds of the United States company could be taken by the Alien Property Custodian although the certificates were in possession of German nationals. Another case, In re DeGheest's Estate, 360 Mo. 1002, 232 S.W. (2d) 378 (1950), went probably farther than the Cities Service case when it held that checks issued by one French resident to another French resident in payment for exchange and letters directing American drawee bank to hold sums in escrow sufficient to pay such checks on presentation were "evidence of indebtedness" within the meaning of an executive order prohibiting unlicensed transfer of enemy alien's property. Another leading case which dealt with bonds which seems closely analogous to the Cities Service case in reasoning is Badger Machinery Co. v. United States Bank and Trust Co., 166 Wis. 18, 163 N.W. 188 (1917). This case held that for purposes of determining who was a holder in due course of the bond the law of the place of issuance would govern, although the validity of a transfer would be determined by the law of the place where the transfer took place.

[41] Randfontein Gold Mining Co. v. Custodian of Enemy Property, [1923] A.D. 576 (App. Div. So. Afr.).

[42] Paris Agreement, Part I, Art. 1, and 6A, 61 Stat. L. 3157 (1947). See also Mason, "Conflicting Claims To German External Assets," 38 GEO. L.J. 171 (1950).

[43] Silesian American Corp. v. Clark, 332 U.S. 469, 68 S.Ct. 179 (1947); Great Northern Ry. Co. v. Sutherland, 273 U.S. 182, 47 S.Ct. 315 (1927).

of commercial transactions should never be underestimated.[44] That the United States has power of some sort over intangible interests owned by foreigners, but vitally connected with the United States in some manner, has been recognized for quite some time.[45] It might be argued that absolute uniformity for all cases is more desirable than altered interpretations depending upon purpose. But the nation's war power need not be impaired to foster uniformity. Other countries have probably altered their interpretive processes to benefit their own self interests to a greater extent than has the United States.[46] Most important, if there can be a duality of control for tax purposes, there is no reason why the same duality should not exist to effectuate the policy of the Trading With the Enemy Act.

IV. *Soothing the Constitutional Sting*

The obligors in the *Cities Service* case raised a second argument the validity of which cannot be questioned. They argue that although the Supreme Court's decision is binding on all courts in the United States and although sections 7(e) and 5(2)(b) of the act[47] provide for discharge upon compliance with a vesting order, it is possible that some tribunal somewhere will allow recovery on the original bonds in question in the present case. Since they both own property of various kinds located at points throughout the entire world, double liability could result, thus depriving them of property without due process of law. Being obligors, neither company has an interest which gives them the right to use section 9(n) to recover their loss. No statutory remedy being apparent, both Judge Hand and Justice Clark indicate that recoupment could be obtained through implied contract, since the United States will not be presumed to have intended to violate its own Constitution.[48] Justices Reed and Minton concurred[49] in the result of the *Cities Service* case, but disagreed concerning the declaration by the Supreme Court that there would be an action available to the parties should subsequent recovery against the obligors be allowed elsewhere.

[44] See United States v. Pink, 315 U.S. 203, 62 S.Ct. 552 (1942).

[45] Direction Der Disconto-Gesellschaft v. United States Steel Corp., 267 U.S. 22, 45 S.Ct. 207 (1925).

[46] See Rabel, "Situs in Enemy Property Measures," 11 LAW AND CONTEM. PROB. 118 (1945).

[47] 50 U.S.C. Appx. (Supp. IV, 1951) §§1-100.

[48] See Silesian American Corp. v. Clark, 332 U.S. 469, 68 S.Ct. 179 (1947).

[49] Cities Service Co. and The Chase National Bank v. McGrath, Atty. Gen., 342 U.S. 330, 72 S.Ct. 334 (1952).

Their idea was that since there would be no taking of property until then, no determination should be made until the circumstances resolve themselves. It is comforting, however, to see the Court, whichever view is taken, not only recognizing, but emphasizing, that the obligors should be allowed recompense somehow should they suffer the sting of double payment.

V. *Conclusions*

A. In the vast majority of cases the situs of the property interest of a negotiable bearer bond has been treated as being embodied in the certificate of indebtedness. This view can be applied in most instances and it has some distinct advantages. It is shrouded with historical antiquity. It represents the approach of the ordinary person, who naturally feels that a bond is more than merely evidence of the debt. It coincides with the modern commercial practice of buying and selling these property interests on an open market. It tends to aid the certainty with which a buyer may view a prospective purchase, thus fostering marketability. It has the disadvantage of being treated as a fiction by the United States Supreme Court.

B. In a number of instances the situs of this property interest has been treated as being at the domicile of the corporate debtor. Some cases have indicated that there is a duality, with partial situs in both places. Others indicate that the determination of the situs issue may be altered to effectuate a certain purpose. The influence upon the determination of governmental powers and policies, both state and federal, should not be underestimated.

C. The extent to which the situs concept will be treated as a fiction and for what other purposes the courts will determine situs to be with the corporate debtor are not presently answerable; but it is clear that for purposes of state intangible taxation and for the purpose of the Trading With the Enemy Act, control over the corporate debtor is sufficient to acquire jurisdiction over the negotiable bearer bond.

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