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CONTRACTS-BILLS AND NOTES-PRECEDENT DEBT AS CONSIDERATION IN THE LAW OF CONTRACTS AND NEGOTIABLE INSTRUMENTS

Shubrick T. Kothe S.Ed.
University of Michigan Law School

COMMENTS

CONTRACTS—BILLS AND NOTES—PRECEDENT DEBT AS CONSIDERATION IN THE LAW OF CONTRACTS AND NEGOTIABLE INSTRUMENTS

I

Today, it is established as a general rule in the law of contracts that a precedent debt cannot be consideration for a subsequent promise.[1] However, in 1588 it could be said with good reason that a precedent debt was one of the "three manner of considerations upon which an

[1] WILLISTON, CONTRACTS, rev. ed. §§ 108, 143 (1936).

assumpsit . . . [might] be grounded. . . ."[2] At this time, the courts were gradually expanding the action of assumpsit to reach obligations which formerly could be enforced only in an action of debt.[3] By the end of the sixteenth century, it was definitely established that an action of indebtitatus assumpsit would lie where a debt was acknowledged by a subsequent promise to pay.[4] This action was later extended in *Slade's Case*[5] to include promises made contemporaneously with the receipt of the consideration in case of a debt. It is apparent, then, that originally a precedent debt was held to be consideration in order that an action of indebitatus assumpsit could be maintained in situations formerly sufficient to ground an action of debt only.[6] With the decision in *Slade's Case*,[7] after which a subsequent promise need no longer be proved in assumpsit, the purpose for calling a precedent debt a valid consideration disappeared. The natural objection to it is that the precedent debt is a past consideration.[8] To say that the debt was "continuing" and therefore not past at the time the promise was made was a convenient method used by the courts to overcome this objection.[9] This, of course, is scarcely satisfactory. A standard definition of consideration in contract law is that it is some detriment to the promisee or benefiit to the promisor, given in exchange for the promise.[10] Clearly, a precedent debt cannot be fitted into this mold.

[2] Manwood v. Burston, 2 Leon. 203, 74 Eng. Rep. 479 (1588); Ames, "The History of Assumpsit," 2 HARV. L. REV. 1 at 2, 16 (1888).

[3] 3 HOLDSWORTH, HISTORY OF ENGLISH LAW 442 et seq. (1923). "If it be asked why the Courts came to admit the validity of a consideration which is obviously past, the answer is that it is due partly to that rivalry between the Courts of King's Bench and Common Pleas which led the King's Bench to favour actions of assumpsit over which they had jurisdiction, at the expense of actions of debt over which they had no jurisdiction, and partly to the procedural advantages which assumpsit possessed over debt." 39 L. Q. REV. 146 at 147 (1923).

[4] Ames, "The History of Assumpsit," 2 HARV. L. REV. 1 at 16 (1888); 3 HOLDSWORTH, HISTORY OF ENGLISH LAW 443 (1923).

[5] 4 Co. Rep. 92b, 76 Eng. Rep. 1074 (1603). This decision was forecast by earlier cases in the Queen's Bench. Ames, "The History of Assumpsit," 2 HARV. L. REV. 1 at 17 (1888). But prior to Slade's Case, it was generally necessary that the express promise be made after incurring the debt. Plaintiff "ought to have said *quod postea assumpsit* for if he assumed at the time of the contract then debt lies, and not assumpsit;" Anon. (B.R. 1572), Dal. 84, pl. 35.

[6] 2 STREET, FOUNDATIONS OF LEGAL LIABILITY 65 (1906). As Street puts it: "It is true that the action of debt was swallowed up in the action of assumpsit, and *Slade's Case* marks the point at which this event occurred. But—and here here is the whole import of that decision—the point involved was one of remedy purely. It was necessary that simple contract law should be entirely freed from the meshes of the action of debt."

[7] 4 Co. Rep. 92b, 76 Eng. Rep. 479 (1603).

[8] 8 HOLDSWORTH, HISTORY OF ENGLISH LAW 9 (1926).

[9] Hodge v. Vavisour, 3 Bulstr. 222, 81 Eng. Rep. 188 (1617).

[10] 1 WILLISTON, CONTRACTS, § 102 (1936).

But the notion that a precedent debt is consideration did not disappear from the law following *Slade's Case.*[11] Subsequent promises to pay a debt contracted during infancy,[12] a debt barred by the Statute of Limitations,[13] and a debt discharged in bankruptcy[14] were still held to be binding. In these situations today, in the absence of a statute, the law is the same.[15] However, the rationale is no longer the same,[16] although it might well be said that the present day doctrine "is a legitimate extension of the rule that a precedent debt would support an action of indebitatus assumpsit."[17] The theory that moral obligation could be consideration is another concept descended from the early cases which allowed a precedent debt to support a subsequent promise in an action of assumpsit.[18] This doctrine is the result largely of the efforts of Lord Mansfield in the eighteenth century.[19] It has been repudiated in England,[20] and most modern courts in this country have denied it as well.[21] However, there are still American courts which say moral obligation is consideration for a promise.[22] The doctrine certainly does not conform to the normal conception of consideration.

Today, there is little left of the sixteenth century rule that a precedent debt is consideration sufficient to ground an action of assumpsit.

[11] 4 Co. Rep. 92b, 76 Eng. Rep. 479 (1603).

[12] Ball v. Hesketh, Comb. 381, 90 Eng. Rep. 541 (1697).

[13] Hyleing v. Hastings, 1 Ld. Raym. 389, 91 Eng. Rep. 1157 (1699).

[14] Trueman v. Fenton, 2 Cowp. 544, 98 Eng. Rep. 1232 (1777).

[15] 1 WILLISTON, CONTRACTS, §§ 151, 158, 162. (1936).

[16] In most American jurisdictions, the theory is one of waiver. 1 WILLISTON, CONTRACTS, § 203 (1936). Pollock was of the same opinion. POLLOCK, CONTRACTS, 12th ed., 141 (1946). The American Law Institute has said simply that this is a sort of contract which is valid without consideration. 1 CONTRACTS RESTATEMENT, §§ 85, 86 (1932). See Wood & Selick, Inc. v. Compagnie Generale Transatlantique, (C.C.A. 2d, 1930) 43 F. (2d) 941 at 943 where Judge Learned Hand said: "Moreover, even in cases of contract the new promise, which is said to revive the debt, does not really do so. Rather it creates a new obligation for which the old liability is regarded as sufficient consideration."

[17] 8 HOLDSWORTH, HISTORY OF ENGLISH LAW 39 (1926).

[18] Id. 26 et seq.

[19] In Trueman v. Fenton, 2 Cowp. 544, 98 Eng. Rep. 1232 (1777), he said at page 548: "The debts of a bankrupt are due in conscience, notwithstanding he has obtained his certificate; and there is no honest man who does not discharge them, if he afterwards has it in his power to do so. Though all legal remedy may be gone, the debts are clearly not extinguished in conscience."

[20] Eastwood v. Kenyon, 11 Ad. & E. 438, 113 Eng. Rep. 482 (1840).

[21] 1 WILLISTON, CONTRACTS, § 148 (1936).

[22] See, for example, Simpson v. Williams Rural High School Dist., (Tex. Civ. App. 1941) 153 S.W. (2d) 852; Williston Sav. and Loan Assn. v. Keller, (N.D. 1946) 22 N.W. (2d) 30. It should be observed that these statements are made generally in cases where some arbitrary rule of law, for instance, the Statute of Limitations, has cut off a previously valid debt, so the doctrine is not, as a rule, used to enforce contracts which in other jurisdictions would be unenforceable.

Modern cases, such as those where a debt is barred by the Statute of Limitations or discharged in bankruptcy, where it is historically applicable, generally do not rest upon that theory. As a practical matter, it makes little difference. These cases achieve a just result, and have been confined to standard fact situations. The doctrine seems clearly at variance with the rule that consideration cannot be past,[23] and serves no useful purpose today.[24] Cases where this problem arises in the general law of contracts are rare indeed, and cause the courts no trouble.[25]

II

In the field of negotiable instruments, however, we find a different situation. Section 25 of the Negotiable Instruments Law says, under the general heading, Consideration: "Value is any consideration sufficient to support a simple contract. An antecedent or pre-existing debt constitutes value; and is deemed such whether the instrument is payable on demand or at a future time." It is probable that the framers of the N.I.L. intended to formulate the same rule as was established in the Bills of Exchange Act in England,[26] but the language is not so clear. The N.I.L. says specifically that a precedent debt shall be value. To a certain extent, value and consideration are used interchangeably in the act.[27] But they are different concepts, certainly.[28] Section 25 of the N.I.L. can definitely be said to have settled the celebrated controversy between Justice Story and Chancellor Kent over the position of a person who has taken a negotiable instrument indorsed to him as security for a debt.[29] There can be little doubt now that one who has

[23] 8 HOLDSWORTH, HISTORY OF ENGLISH LAW 13 et seq. (1926).

[24] 1 WILLISTON, CONTRACTS, § 143 (1936).

[25] Mortenson v. Knudson, 189 Iowa 379, 176 N.W. 892 (1920).

[26] "Sec. 27. (1) Valuable consideration for a bill may be constituted by—(a) Any consideration sufficient to support a simple contract. (b) An antecedent debt or liability. Such a debt or liability is deemed valuable consideration whether the bill is payable on demand or at a future time. . . . "

[27] AIGLER, CASES ON NEGOTIABLE PAPER AND BANKING 442 (1937); Wickhem, "Consideration and Value in Negotiable Instruments," 3 WIS. L. REV. 321 at 335-6 (1926). Sec. 191 of the N.I.L. says: "In this act, unless the context otherwise requires—. . . 'Value' means valuable consideration. . . . "

[28] Wickhem, id. at 330 et seq.

[29] Id. at 336-7. Chancellor Kent's decision in Bay v. Coddington, 5 Johns. Ch. (N.Y.) 54 (1821), was later taken to state the rule that where one has received a negotiable instrument as collateral security for an antecedent debt, he shall not be a holder for value. As a matter of fact, there were other factors in the particular case, and the Chancellor placed strong emphasis on the fact that this transaction was not in the normal course of business. In Swift v. Tyson, 16 Pet. (41 U.S.) 1 (1842), Justice Story, relying in a large measure on commercial practice, decided such a person was a holder for value.

taken such an instrument in payment of or as collateral security for a precedent debt is a holder for value, within the meaning of section 52.[30] A remaining question is whether a precedent debt can be consideration, and if so, is it always consideration, or only under special circumstances.

A. In the simplest situation, where a negotiable instrument is given in payment of the precedent debt of the maker, it is held that the instrument is founded on good consideration. For example, *A* gives *B* his check in payment of a debt. An action will lie on the check,[31] although in contract law, it is simply a promise to pay a debt then owing. A moment's reflection is sufficient to convince one that no other conclusion is possible. In the normal case, no controversy will arise on this point. It is a foregone conclusion that the check is supported by consideration. Various explanations have been made where the question has arisen. The reason generally assigned, where one is necessary, is that there is a forbearance during the life of the instrument. This is satisfactory where a time instrument is involved, for it may well be said that there is an implied promise to postpone enforcement of the original debt until the new instrument matures.[32] Where the instrument given is payable on demand, this rationale tends to become a rationalization. With this sort of paper, courts have said that there is a sort of implied forbearance, in that the instrument will live at least a reasonable time, and the action on the original debt is suspended for that time.[33] A simple answer to this, of course, is that one does not *have* to wait a reasonable time. Ames took the position that in the Law Merchant, no consideration was necessary to support any negotiable instrument and there would never have been any trouble in this connection if courts had not since deviated from this rule.[34] He derived this view, according to Williston,[35] from a statement found in Black-

[30] "A holder in due course is a holder who has taken the instrument under the following conditions: . . . 3. That he took it in good faith and for value. . . ."

[31] Stevens v. Park, 73 Ill. 387 (1874); Gleason v. Brown, 129 Wash. 196, 224 P. 930 (1924); BRITTON, BILLS AND NOTES 371 (1943).

[32] Baker v. Walker, 14 Mees. & W. 465, 153 Eng. Rep. 558 (1845).

[33] Currie v. Misa, L.R. 10 Ex. 153 (1875).

[34] 2 AMES, CASES ON BILLS AND NOTES 876 (1894). "It is frequently stated in the books that as between the immediate parties to a bill or note a consideration is necessary to the validity of the obligation. This notion, it is submitted, is erroneous upon principle, and also upon the authorities; for although it must be conceded that the courts have sanctioned the defense of absence of consideration in certain cases, these decisions should be regarded as anomalous exceptions to the rule that a bill, being in the nature of a specialty, is obligatory without a consideration, rather than as illustrations of the opposite doctrine, that a bill, being a simple contract, requires a consideration to support it."

[35] 1 WILLISTON, CONTRACTS 372 (1936).

stone.[36] Lord Mansfield was of the same opinion.[37] However, it seems likely historically that consideration was necessary for negotiable instruments as well as other contracts.[38] The true answer probably is that the point was not presented to the courts often enough prior to the nineteenth century to evolve a definite rule.[39] However this may be, at the time the N.I.L. was drafted, some consideration was necessary to support a negotiable instrument between the original parties thereto.[40] This rule was codified in the N.I.L.[41]

The two lines of authority in this country relative to what is necessary to constitute one a holder for value have been mentioned earlier.[42] Certainly a majority of cases held that one who took a negotiable instrument in payment of or as collateral security for a precedent debt was a holder for value.[43] Strictly speaking, the New York view, that an antecedent debt is not value, is unassailable, if the problem is considered simply as one in the law of contracts. In a very well reasoned New York case,[44] decided after *Bay v. Coddington*[45] and *Swift v. Tyson*,[46] the English precedents upon which Jutice Story relied in the latter case were reviewed and the court concluded that the New York rule was correct historically. But in *Currie v. Misa*,[47] *Swift v. Tyson*[48] was cited with approval, and the English court rejected the New York decisions. These cases, it must be remembered, were cases

[36] 2 BL. COMM. 446. "For if a man . . . gives a promissory note, he shall not be allowed to aver the want of consideration in order to evade the payment . . . and every note from the subscription of the drawer carries with it an internal evidence of a good consideration." This statement is called inaccurate in a note appended by a reporter. Wendell's ed. (1854).

[37] Pillans v. Van Mierop, 3 Burr. 1663, 97 Eng. Rep. 1035 (1765). "A *nudum pactum* does not exist in the usage and law of merchants." He reconciled this view with the common law, which he took to be the same as the law merchant, on the theory that consideration was of evidentiary value only. This doctrine was speedily overruled, at least so far as contract law was concerned. Rann v. Hughes, 7 T.R. 350 n. (a) (1778). See 8 HOLDSWORTH, HISTORY OF ENGLISH LAW 29-30 (1926).

[38] 8 HOLDSWORTH, HISTORY OF ENGLISH LAW 167 (1926); 2 STREET, FOUNDATIONS OF LEGAL HISTORY 387 et seq. (1906).

[39] 1 WILLISTON, CONTRACTS, § 108 (1936).

[40] BRITTON, BILLS AND NOTES, § 90 (1943); 8 HOLDSWORTH, HISTORY OF ENGLISH LAW 167 (1926), Wickhem "Consideration and Value in Negotiable Instruments," 3 WIS. L. REV. 322 et seq. (1926).

[41] Sec. 28.

[42] Supra, note 29.

[43] Wickhem, "Consideration and Value in Negotiable Instruments," 3 WIS. L. REV. 321 at 331 et seq. (1926); cases cited, 1 AMES, CASES ON BILLS AND NOTES 634 note 1, 650, note 1 (1894).

[44] Stalker v. M'Donald, 6 Hill (N.Y.) 93 (1843).

[45] 5 Johns. Ch. (N.Y.) 54 (1821).

[46] 16 Pet. (41 U.S.) 1 (1842).

[47] L.R. 10 Ex. 153 (1875).

[48] 16 Pet. (41 U.S.) 1 (1842).

in which the question was whether one could be a holder for value if the only value were a precedent debt. If value were coterminous with consideration, it could fairly be said that a precedent debt was good consideration for a negotiable instrument prior to the N.I.L., in the majority of jurisdictions. But this is certainly not true.[49] Consideration and value are separate and distinct problems,[50] even as in other fields.[51] Ames, in illustrating his thesis that no consideration was necessary for a negotiable instrument, asserted that a bill given in payment of a debt was valid: "A person who executes or indorses to his creditors a bill or note payable at a future day, in payment of his own debt or the debt of a third party may be sued upon the new security . . . the rule is the same when the new security is payable on demand."[52] The case where a time bill or note is given may well be resolved on a theory of forbearance,[53] although the first case cited by Ames[54] does not reveal whether or not it was a time note. The three cases dealing with demand notes do not fully support the stated proposition. In *Childs v. Monins*,[55] the decision relied strongly on the fact that the executor's notes called for interest payments which implied a forbearance by the payee to go against the estate. *Currie v. Misa*[56] is a case of a holder for value. *Sison v. Kidman*[57] holds than an accomodation party can be held liable in an action of debt. *Poplewell v. Wilson*[58] seems more in point. This was a suit on a promissory note issued by *A* to *B* in payment of a debt owed by *C* to *B*. The report reveals little more. The court held that the plaintiff could recover over the objection of the defendant that the debt of another is no consideration to raise a promise. The authority of this case with reference to the problem at hand is doubtful, however. Previously, Lord Holt had said in a suit on a note made by defendant to pay so much on the account of another: "The consideration implied in the Statute[59] is, that when the party promises upon his own account, it must be presumed he is indebted, or else he would not promise to

[49] 4 WILLISTON, CONTRACTS, § 1146 (1936); 12 Iowa L. REV. 69 (1926).

[50] Wickhem, "Consideration and Value in Negotiable Instruments," 3 WIS. L. REV. 321 at 330 et seq. (1926).

[51] 3 POMEROY, EQUITY JURISPRUDENCE, 5th ed., 19 et seq. (1941).

[52] 2 AMES, CASES ON BILLS AND NOTES 876 (1894).

[53] Balfour v. Sea Fire Life Assurance Co., 3 C.B. (n.s.) 300, 140 Eng. Rep. 756 (1857).

[54] Poplewell v. Wilson, 1 Stra. 264, 93 Eng. Rep. 512 (1719).

[55] 2 Br. & B. 460, 129 Eng. Rep. 1044 (1821).

[56] L.R. 10 Ex. 153 (1875).

[57] 3 Man. & G. 810, 133 Eng. Rep. 1365 (1842).

[58] 1 Stra. 264, 93 Eng. Rep. 512 (1719).

[59] 3 & 4 Anne, c. 9 (1704). In Clerke v. Martin, 2 Ld. Raym. 757, 92 Eng. Rep. 6 (1702), Lord Holt had held that promissory notes were not within the Law Merchant. This statute was passed to overrule that decision.

pay it; *aliter* where the promise is to pay upon account of a third person."[60] The actual decision in the *Poplewell* case appears to be that a note given in payment of the debt of another is within the statute,[61] and therefore to be treated as a negotiable instrument. This, of course, overruled Holt's earlier decision on this point.

Whatever may have been the old law, it seems clear that by the time the N.I.L. was drafted, a negotiable instrument payable on demand, signed by the debtor and given to the creditor in payment of the debt was deemed to be founded on good consideration.[62] A negotiable instrument given in absolute payment of a debt owing to the payee by one not the principal debtor was also regarded as supported by good consideration.[63] But the precedent debt of a third person was not good consideration unless the debt was cancelled.[64] Directly in line with the rule last stated, a note given as collateral security for a debt of a third person was held not to be founded on good consideration.[65] The law probably was the same where a negotiable instrument was given as collateral security for the debt of the maker.[66] The effect of the Bills of Exchange Act in England seems clear.[67] It is expressly stated that a precedent debt is consideration. In the United States, however, the codification is not so explicit. Again, it would not be unreasonable to assume from the similarity of language employed that the N.I.L. meant to establish the same rule as that set up in the English Statute.[68]

B. Since the enactment of the N.I.L., there have been a great number of cases stating in one way or another that a precedent debt is good consideration for a negotiable instrument.[69] A good example of

[60] Garnet v. Clarke, 11 Mod. 226, 88 Eng. Rep. 1005 (1709).

[61] 3 & 4 Anne, c. 9. Supra, note 59.

[62] Stevens v. Park, 73 Ill. 387 (1874); Nelson v. Lovejoy, 14 Ala. 568 (1848).

[63] Holm v. Sandberg, 32 Minn. 427, 21 N.W. 416 (1884); Seymour v. Prescott, 69 Me. 376 (1879); Henry v. Ritenour, 31 Ind. 136 (1869); Brainard v. Capelle, 31 Mo. 428 (1862).

[64] Ward v. Barrows, 86 Me. 147, 29 A. 922 (1893); Wren v. Hoffman, 41 Miss. 616 (1868).

[65] Bank of Carroltown v. Latting, 37 Okla. 8, 130 P. 144 (1913); Savage v. First Nat. Bank of Rome, 112 Ala. 508, 20 S. 398 (1896); Security Bank of Minn. v. Bell, 32 Minn. 409, 21 N.W. 470 (1884). See 44 L.R.A. (n.s.) 481.

[66] Wickhem, "Consideration and Value in Negotiable Instruments," 3 Wis. L. Rev. 321 at 331 (1926).

[67] No cases in point have been found since the act went into effect.

[68] Aigler, Cases on Negotiable Paper and Banking 442, note 1 (1937).

[69] In the following cases, § 25 of the N.I.L. was cited: Hester v. Kemper Military School, (Tex. Civ. App. 1940) 138 S.W. (2d) 833; Cinema Schools, Inc. v. Westchester Fire Ins. Co., (D.C. Cal. 1932) 1 F. Supp. 37; Drewen v. Union Discount Co., (C.C.A. 2d, 1929) 32 F. (2d) 691; Bridge v. Ruggles, 202 Cal. 326, 260 P. 553 (1927); Bank of Moberly v. Meals, 316 Mo. 1158, 295 S.W. 73 (1927); Milburn v. Miners & Citizens Bank, 101 Okla. 281, 226 P. 42 (1924); Schauer v. Morgan, 67 Mont. 455, 216 P. 347 (1923). In the following cases, that section of

what courts will say is found in *Myers v. Shinn.*[70] Although the N.I.L. was in effect in Arkansas, it was not cited. The case was a simple one in which defendant executed a note to pay a debt he owed plaintiff's testator. The Court said: "The moral obligation to pay this note was good consideration."[71] The language may become definitely misleading when the courts confuse value and consideration in applying section 25. In the case of *Flynn v. Currie,*[72] for instance, the court said: "Antecedent indebtedness constitutes value, and is sufficient consideration to support a simple contract."[73] This was a case where a promissory note was executed by defendant and indorsed by the payee to plaintiff to pay a precedent debt. Plaintiff sued defendant on the instrument and recovered. In the opinion, the court cited section 25, and apparently what it was trying to do in the language quoted above was to paraphrase that section of the N.I.L. An interesting situation is presented and a rather remarkable conclusion is reached in *Hanson v. Johnson.*[74] Here, *A* gave a demand note to plaintiff with a mortgage to secure it in 1912. Plaintiff recorded immediately. Prior to that time, *A* had mortgaged the same property to defendant, but this mortgage was not recorded until 1914. Both transactions were effected to secure precedent debts. The court held that plaintiff was a purchaser for value of the property by reference to section 25 of the N.I.L. because he took an instrument payable on demand, which brought him within the terms of the statute. The court indicated that defendant, even had he recorded, would not have been a purchaser for value since he did not receive an instrument payable on demand.

Although the cases where the question is whether one is a holder for value of negotiable paper and the cases where the debt of the maker is paid with a negotiable instrument are relatively simple insofar as they concern precedent debt, the problem becomes rather more complicated where a bill or note is executed in payment of or as collateral security for the debt of a third party. A case may arise in several ways. The easiest is where one executes a note expressly to pay the debt of another, and the creditor expressly releases the third party from his debt. This note is supported by good consideration.[75] In *Schaefer v.*

the N.I.L. was not cited: Wheeler v. Wardell, 173 Va. 168, 3 S.E. (2d) 377 (1939); Smeltzer v. McCrory, (Tex. Civ. App. 1937) 101 S.W. (2d) 850; Lucas E. Moore & Co. v. Hursey Transp. Co., 18 La. App. 56, 137 S. 630 (1931); Wade v. Johnson, 111 Ore. 468, 227 P. 466 (1924); Popp v. Exchange Bank, 189 Cal. 296, 208 P. 113 (1922).

[70] 201 Ark. 857, 147 S.W. (2d) 355 (1941).

[71] Id. at 859.

[72] 130 Me. 461, 157 A. 310 (1931).

[73] Id. at 463.

[74] 42 N.D. 431, 177 N.W. 452 (1918).

[75] Merrell v. Timmons, (Tex. Civ. App. 1940) 140 S.W. (2d) 480; In re

First National Bank of Findlay,[76] we find a variation. Plaintiff owed defendant a sum of money. In order to get his debt extended, he executed a note as collateral security for a debt owed defendant by a third party. In a suit to cancel this note, the court said there was no consideration for the second note, since defendant could still proceed against the third party. His debt was not cancelled nor was it assigned to plaintiff. The N.I.L. was not mentioned. However, even without relying on the N.I.L., it would seem that defendant should have had judgment. There appears to be sufficient consideration here to support a simple contract; namely, a forbearance to sue on the debt owed to the defendant, in consideration of plaintiff's contingent promise to pay a sum of money. On the other hand, in *In re Ciabattari*[77] defendant gave a note to plaintiff who was threatening to sue defendant's wife on another note executed by her previously. Although there was some doubt whether the second note was given as security for the wife's debt or in payment thereof, the court said it did not matter. Plaintiff was liable in either event. If the note had been given as collateral security, forbearance to sue the wife would support it. If it had been given in payment, then the wife's debt was cancelled, and the cancellation was consideration. The N.I.L. was not cited. As a matter of fact, plaintiff kept the wife's original note, so very probably it was given as security. The report does not reveal whether or not defendant's was a time note and certainly there was no agreement to forbear for a definite time.[78] If it were a demand note, there could be at best only an implied promise to forbear for a reasonable time.[79] In *Newman and Snell's State Bank v. Hunter,*[80] the original obligor's widow gave her note to his creditor, following his death. There was nothing in his estate, and the security which the creditor held for the decedent's note was valueless. In a suit against the widow, the court held her not liable, since her note was not supported by consideration. In *Neal v.*

Ciabattari, (D.C. Ky. 1939) 29 F. Supp. 573; First Nat. Bank of Athens v. Laughlin, 209 Ala. 349, 96 S. 206 (1923).

[76] 134 Ohio St. 511, 18 N.E. (2d) 263 (1938). Luing v. Peterson, 143 Minn. 6, 172 N.W. 692 (1919) is a similar case. In the latter case, two judges dissented, but did not cite the N.I.L.

[77] (D.C. Ky. 1939) 29 F. Supp. 573.

[78] Cf. Holm v. Sandberg, 32 Minn. 427, 21 N.W. 416 (1884), decided prior to the enactment of the N.I.L., where the court held it to be a jury question whether the note was given in payment of or as collateral security for the third person's debt, and based its decision on the fact that the jury found the note to have been given in payment. There was no express agreement to cancel the original debt. In this case, the court indicated that if the note had been given as collateral security, it would not have been supported by a valid consideration.

[79] 1 WILLISTON, CONTRACTS, § 136 (1936).

[80] 243 Mich. 331, 220 N.W. 665 (1928).

Wilson,[81] defendant gave a check to plaintiff as collateral security for *A's* debt to plaintiff. *A's* name did not appear on the check. The court treated defendant as an accomodation party, and held him liable, evidently on the theory that no consideration is necessary to hold an accommodation party. Section 29 of the N.I.L.[82] was cited, but no mention was made of section 25. A fairly common situation is the deposit in banks of notes made by third parties either in payment of or as security for the debts of others, for the purpose of concealing the true financial condition of the bank from the examiner.[83] These notes are usually made under a *sub rosa* agreement with the bank that they will not be enforced against the maker. The courts generally hold that a receiver of the bank can collect from the maker,[84] and some even say the bank can enforce the notes.[85] These cases are rested not on precedent debt as consideration, however, but generally on something like estoppel. Whether the notes are given in payment of or as security for the antecedent debt should not make any difference in this situation. The effect of section 25 on these cases is not discussed in the opinions.

C. In all these cases, it would seem possible, relying solely on section 25, to say that a precedent debt is consideration sufficient to support a negotiable instrument between the original parties thereto, and therefore the instruments are enforceable. Britton makes a strong argument that a precedent debt should be consideration to support a negotiable instrument given to secure the debt of another in several of these situations.[86] His position is that there is no essential difference between the case where the principal debtor and the third party both sign an instrument given as collateral security on which the third party is liable,[87] and where the third party signs alone where some courts have held him not liable,[88] or where he signs after the delivery, but not pursuant to an agreement entered into at the time the instrument was executed, where he is never held liable.[89] Where the note of a

[81] 213 Mass. 336, 100 N.E. 544 (1913).

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

[83] Cases collected, 64 A.L.R. 595 (1929). The problem is critically discussed, BRITTON, BILLS AND NOTES, § 94 (1943).

[84] Dietrick v. Greaney, 309 U.S. 190, 60 S. Ct. 480 (1940).

[85] First Nat. Bank of Tulsa v. Boxley, 129 Okla. 159, 264 P. 184 (1927).

[86] BRITTON, BILLS AND NOTES, § 94 (1943).

[87] Elgin Nat. Bank v. Goecke, 295 Ill. 403, 129 N.E. 149 (1920).

[88] Kiess v. Baldwin, (App. D.C. 1934) 74 F. (2d) 470. Contra, Neal v. Wilson, 213 Mass. 336, 100 N.E. 544 (1913).

[89] Jackson v. Lancaster, 213 Ala. 97, 104 S. 19 (1925); Northern Trust and Sav. Bank v. Ellwood, 200 Iowa 1213, 206 N.W. 256 (1925).

third party is given in payment, there should be no trouble, and there seems to be none except when for some reason or another the debt of the third party is valueless.[90] In the collateral security case, however, the courts seem loath to enforce the naked liability of a third party. Britton thinks section 25 is authority for enforcing these promises. Where a precedent debt is the only consideration, there is no difference in substance between the case where a person signs alone or subsequent to the delivery of an instrument and the one where he signs at the same time or later pursuant to an agreement entered into at the time of the execution. The consideration is the same in both cases. "Section 25 of the N.I.L. deprives, or should deprive every promisor on a negotiable instrument, no matter how or when he signed, of the defense of no consideration, so long as he signed for the purpose of paying or securing his own antecedent debt or that of another. . . . In other words, in the antecedent debt setting, the statute has made 'naked promises' respectable, however much they may be subject to arrest when they stray beyond the footlights."[91] The cases, as indicated in a previous paragraph, do not usually consider the effect of section 25 on these situations.

Where the note is executed to pay an unenforceable precedent debt, as, for instance, a debt barred by the Statute of Limitations, or discharged in bankruptcy, it is generally held that an instrument of the principal debtor is supported by good consideration,[92] but an instrument of a third party is not.[93] An interesting variation is illustrated by *Eastlick v. Hayward Lumber & Investment Co.*[94] Plaintiff corporation delivered lumber to *A*, pursuant to an agreement that the delivery was to be made on defendant's credit. At the time the lumber was delivered, plaintiff had no registered agent in Arizona, although previously it had had one there. An Arizona statute[95] provided that all contracts made by a corporation without a registered agent in the state might be declared void at the option of the interested party. An agent had been appointed and registered at the time the note was executed by defendant. The court held the original contract was merely voidable, and a

[90] Newman & Snell's Bank v. Hunter, 243 Mich. 331, 220 N.W. 665 (1928); Bradstreet v. Crosbie, 123 Okla. 269, 253 P. 63 (1926); Santikos v. Hamilton-Turner Grocery, (Tex. Civ. App. 1919) 208 S.W. 560; Sykes v. Moore, 115 Miss. 508, 76 S. 538 (1917); Citizens' Trust Co. v. McDougald, 132 Tenn. 323, 178 S.W. 432 (1915); Widger v. Baxter, 190 Mass. 130, 76 N.E. 509 (1906).

[91] BRITTON, BILLS AND NOTES 384 (1943).

[92] Ramey v. Ramey, 181 Va. 377, 25 S.E. (2d) 264 (1943); Baxter v. Brandenburg, 137 Minn. 259, 163 N.W. 516 (1917).

[93] Taylor v. Weeks, 129 Mich. 233, 88 N.W. 466 (1901); Widger v. Baxter, 190 Mass. 130, 76 N.E. 509 (1906). See 6 WILLISTON, CONTRACTS, § 1875 I (1936).

[94] 33 Ariz. 242, 263 P. 936 (1928).

[95] Ariz. Rev. Stat. (1913) ¶ 2229.

precedent debt, even though the debtor may be exempt from discharging it by law, is good consideration for a promise to pay. This was not treated as a negotiable instrument case, but rather as one of simple contract. It should not matter in this particular situation. In its essentials, it is similar to a subsequent promise to pay a debt barred by the Statute of Limitations, and even closer to the case of a debt contracted during infancy, and subsequently properly affirmed. In this case, the court hewed to the line advocated by Holdsworth[96] and indicated that if the corporation had never had a resident agent, the debt then being void by statute, and not simply voidable, the instrument would have been without consideration.[97] It is submitted that this is consistent with the law of bills and notes. If there were never any debt, and a void debt is not legally a debt, there would be no precedent debt to support the subsequent promise. A similar problem might arise under the Statute of Frauds. In *Bagaeff v. Prokopik*,[98] a note was given to pay a contract debt treated by the court as void by virtue of the Statute of Frauds. It was held to be supported by consideration. The court did not cite the N.I.L. but relied in a large measure on validity of moral obligation as consideration. In the great majority of jurisdictions, it is held that the Statute of Frauds makes a proper contract voidable;[99] under this interpretation of the Statute, it is believed the decision is correct. It is a case analogous to *Eastlick v. Hayward Lumber & Investment Co.*[100] and to the infancy cases. If the oral contract were absolutely void, it would seem the negotiable instrument should be unenforceable as between the original parties thereto. A precedent debt, to be consideration, should at least be a voidable debt, or one which was once legally binding. Precedent debts which will support negotiable instruments should include, it is believed, debts of third parties, whether still enforceable or not. Also, if a precedent debt is consideration, and the N.I.L. and many cases seem to say it is, there is no good reason why a promise by a third party to pay it either absolutely or contingently should not be enforceable regardless of whether the principal debtor or his estate could have paid. The courts talk of release of the principal debtor's obligation, in order to find consideration where the paper is given in payment of a third party's debt. In the absence of an express agreement amounting to a novation, and this is the more common case, such reasoning seems to be circular. Obvi-

[96] 8 HOLDSWORTH, HISTORY OF ENGLISH LAW 36 et seq. (1926).

[97] Contra on this point, St. Louis Union Trust Co. v. Chicot County Cotton-Alfalfa Farm Co., 127 Ark. 577, 193 S.W. 69 (1917).

[98] 212 Mich. 265, 180 N.W. 427 (1920). See 1 WILLISTON, CONTRACTS, § 199 (1936).

[99] 2 WILLISTON, CONTRACTS, § 527 (1936).

[100] 33 Ariz. 242, 263 P. 936 (1928).

ously, the creditor does not mean to release the principal debtor if he cannot collect from the promisor. And he can collect from the latter only if there is consideration for his promise to pay. We get off this merry-go-round if we say that a precedent debt is consideration in the law of negotiable instruments. It is then no problem to say that one's note is supported by consideration if it is issued to pay the debt of a decedent who has left no assets. The same rule should apply in the case of a note issued as collateral security for the debt of a third party, or that in which one not the principal debtor signs after delivery. It is perhaps a little more difficult to say the same rule should hold where one executes a note to pay a debt of a third party barred by the Statute of Limitations or discharged in bankruptcy. But the principal debtor's own note would be binding, and it is not illogical to hold another liable, since we do have a precedent debt. As has been shown, it is on the basis that a precedent debt is good consideration, even though it be uncollectible because of some rule of law which has cut off the action on it, that the principal debtor was originally held in these situations.

It is admitted that the cases do not support all these views. On the other hand, most of them do not go into the effect of section 25. *Citizens Trust Co. v. McDougald*[101] is an exception to this general practice. There the court cited section 25 but went on to say that a precedent debt of another is not good consideration when that debt was worthless at the time the new note was executed to pay it. However, in *Crane and Co. v. Hall*,[102] this case was cited and there limited. Brannan[103] suggests that the earlier case is wrong, for the reason that the payee had a right to sue and get judgment against the principal debtor, which he gave up, and this is consideration without regard to the question whether the judgment could be executed. This analysis, though probably correct, also disregards the question of the effect of section 25. It is submitted that this section of the N.I.L. sets up a ready and workable rule, governing most of the situations herein described.

Shubrick T. Kothe, S.Ed.

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[101] 132 Tenn. 323, 178 S.W. 432 (1915).
[102] 141 Tenn. 556, 213 S.W. 414 (1919).
[103] BRANNAN'S NEGOTIABLE INSTRUMENTS LAW, 6th ed., 399 (1938).