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BILLS AND NOTES-INDORSEMENT IN BLANK FOLLOWED BY SPECIAL INDORSEMENT

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RECENT DECISIONS

BILLS AND NOTES—INDORSEMENT IN BLANK FOLLOWED BY SPECIAL INDORSEMENT—Plaintiff purchased a cashier's check from *X* Bank payable to himself. He indorsed the check in blank and immediately below stamped it, "Pay to the order of Bank of America, National Savings and Trust Association, S. & R. Produce Co." Plaintiff then gave the check to one *R* with whom he had agreed to enter into business under the name of the S. & R. Produce Company. *R* took the check to *Y* Bank which at his request blocked out the special indorsement without the knowledge or consent of plaintiff. *R* then indorsed the check and deposited it to his personal account. *X* Bank paid the check on presentment. In an action against both banks to recover the amount of the check alleged to have been paid to *R* wrongfully, *held*: the status of the check as a bearer instrument from plaintiff's indorsement in blank was unaffected by the subsequent special indorsement; *Y* Bank therefore took title to it by delivery as a holder in due course, and *X* Bank was bound to pay on the presentation of *Y*. *Christian v. California Bank*, (Cal. 1946) 173 P. (2d) 318.

It is generally conceded that according to the Law Merchant a special indorsement of an order instrument controlled a prior indorsement in blank making the instrument negotiable only by further indorsement.[1] The common law, however, took a different turn when Lord Kenyon in *Smith v. Clarke* [2] held that an order bill which became payable to bearer by a blank indorsement could thereafter be negotiated by delivery even though subsequently specially indorsed. This rule became generally accepted both as to order [3] and bearer [4] paper. The doctrine of *Smith v. Clarke* was repudiated however by the English Bills of Exchange Act which included a section providing that, "A bill is payable to bearer . . . on which the only or last indorsement is an indorsement in blank." [5] Chalmers, the draftsman of the Bills of Exchange Act, stated that this section was intended to bring the law into accordance with mercantile practice by making a special indorsement control a previous indorsement in blank.[6] This provision, with

[1] McKeehan, "The Negotiable Instruments Law: a Review of the Ames-Brester Controversy," 50 AM. L. REG. (o.s.) 437 at 455 (1902); Brannan, "Some Necessary Amendments to the Negotiable Instruments Law," 26 HARV. L. REV. 493 at 501 (1913); CHALMERS, BILLS OF EXCHANGE, 5th ed., 24 (1896). Bigelow, however, was under the impression that Smith v. Clarke, infra, was expressive of the Law Merchant. BIGELOW, BILLS AND NOTES, 3d ed., § 260 (1928).

[2] Peake 225, 1 Esp. 180, 170 Eng Rep. 320 (1793).

[3] Vanarsdale v. Hax, (C.C.A. 8th, 1901) 107 F. 878; Watervliet Bank v. White, 1 Denio (N.Y.) 608 (1845); Howry v. Eppinger, 34 Mich. 29 (1876); Huie v. Bailey, 16 La. 213 (1840).

[4] Johnson v. Mitchell, 50 Tex. 212 (1878); Mitchell v. Fuller, 15 Pa. St. 268 (1850), instrument drawn payable to drawer and indorsed by him in blank; see also Savannah Natl. Bank v. Haskins, 101 Mass. 370 (1869). Contra, Meyers v. Friend and Scott, 22 Va. 12 (1821).

[5] Bills of Exchange Act, 45 & 46 Vict., c. 61, § 8 (3) (1882).

[6] CHALMERS, BILLS OF EXCHANGE, 5th ed., 24 (1896).

only slight change in phraseology, was written into section 9 (5) [7] of the N.I.L. for presumably the same reason. The N.I.L., however, contains another pertinent provision not found in the Bills of Exchange Act. Section 40 of the N.I.L. states that "Where an instrument, payable to bearer, is indorsed specially, it may nevertheless be further negotiated by delivery; but the person indorsing specially is liable as indorser to only such holders as take title through his indorsement." The first half of this section appears to be a codification of the rule of *Smith v. Clarke* and there is evidence that the draftsman of the N.I.L. so regarded it.[8] The apparent conflict between sections 9 (5) and 40 was one of the points of controversy in the Ames-Brewster debates.[9] The most satisfying construction of the two sections seems to be that first suggested by McKeehan [10] to the effect that section 40 should be construed as applying only to those instruments drawn payable to bearer,[11] and that section 9 (5) restricts an order instrument indorsed in blank and subsequently indorsed specially from being negotiated by delivery. In *Parker v. Roberts*,[12] however, there is authority for the view that section 40 enacts the rule of *Smith v. Clarke*. Since the principal case involves an order instrument indorsed in blank and then specially indorsed, it would seem that the better construction of sections 9 (5) and 40 would have the special indorsement govern. Without reference to the act, however, the court assumes that the blank indorsement is controlling. *Y* Bank's obliteration of the special indorsement at *R's* request is justified by the court on the ground that the holder of a negotiable instrument may at any time

[7] "An instrument is payable to bearer . . . when the only or last indorsement is an indorsement in blank."

[8] Crawford in his notes to § 40 states that "This section makes no change in the law" and cites Smith v. Clarke, Peake 225, 1 Esp. 180, 170 Eng. Rep. 320 (1793), and Johnson v. Mitchell, 50 Tex. 212 (1878). However, in the same note, the draftsman of the N.I.L. also states that "The section cannot apply where the paper is originally made payable to order and indorsed in blank; for by section 9, a note or a bill which, upon its face, is payable to order, becomes payable to bearer only when the *last* [sic] indorsement is in blank; and hence, when a blank indorsement is followed by a special indorsement, the instrument is not within the terms of section 9." CRAWFORD, ANNOTATED NEGOTIABLE INSTRUMENTS LAW 83 (1918). Clearly, if the latter statement is the correct interpretation of the section there has been a change in the law.

[9] See the compilation of these debates contained in BRANNAN, NEGOTIABLE INSTRUMENTS LAW, 3d ed., 423-426 (Ames), 439-442 (Brewster), 449-450 (Ames), 459-460 (Brewster) (1919).

[10] McKeehan, "The Negotiable Instruments Law: A Review of the Ames-Brewster Controversy," 50 AM. L. REG. (o.s.) 437 at 461 (1902).

[11] Brannan suggests that § 40 should apply to those instruments expressly indorsed "Payable to bearer" as well as those drawn so payable. BRANNAN, NEGOTIABLE INSTRUMENTS LAW, 3d ed., 492, note 2 (1919).

[12] 243 Mass. 174, 137 N.E. 295 (1922). A blank indorsement of a note by the payee was followed by two special indorsements. Plaintiff was in possession of the note but did not allege or prove title through any indorsement. Defendant maker pleaded want of consideration and fraud. Held, plaintiff took title by delivery and was thus a holder in due course free from the defenses.

strike out any indorsement not necessary to his title.[13] Nor was it held that the special indorsement was notice to *Y* Bank of any suspicious circumstances which would impair its status as a holder in due course. There is, however, one argument overlooked by the court which could be advanced to support the striking of the special indorsement, without assuming the point in controversy. Apparently *R* was a partner in the firm that signed the special indorsement. As such he might be entitled to strike out a partnership indorsement leaving the instrument payable to bearer. If this had been established, the court's result could be reached consistently with what seems to be the enlightened interpretation of sections 9 (5) and 40 of the N.I.L. Apparently, too, the check had never been delivered to the special indorsee. It is unfortunate that the decision should follow *Parker v. Roberts* in adding to the body of authority developing on this interesting question without the guidance of a construction of these sections.

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[13] N.I.L., § 48: "The holder may at any time strike out any indorsement which is not necessary to his title. The indorser whose indorsement is struck out, and all indorsers subsequent to him, are thereby relieved from liability on the instrument."