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BILLS AND NOTES - ACCOMMODATION PAPER - DEFENSES WHICH CAN BE ASSERTED DY MAKER AGAINST ONE NOT A HOLDER IN DUE COURSE

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BILLS AND NOTES — ACCOMMODATION PAPER — DEFENSES WHICH CAN BE ASSERTED BY MAKER AGAINST ONE NOT A HOLDER IN DUE COURSE — The defendant, at the request of her husband, signed a blank promissory note. After making the note payable to himself, the husband discounted the note before maturity at the plaintiff bank. In an action by the bank against the wife, the accommodation maker claimed that the bank took in bad faith and that the negotiation to the bank was a diversion from the intended purpose of the accommodation. The plaintiff bank sought to recover upon the ground that the defendant was liable to it as a holder for value irrespective of whether it was a holder in due course. *Held*, affirming the decision of the lower court, that the defense was not open to the defendant because the plaintiff was a holder in due course. *Madigan v. Lumbert*, (Me. 1939) 5 A. (2d) 278.[1]

Section 29 of the N. I. L. provides, "An accommodation party . . . 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." This section has given rise to some difficult questions of statutory construction,[2] particularly because superficially, at least, it conflicts with section 58 which declares that a negotiable instrument "In the hands of any holder other than a holder in due course" is subject to the same defenses as if it were non-negotiable" and with section 28 which states that "Absence or failure of consideration is matter of defense as against any person not a holder in due course." Since an accommodation party is, by definition, one who signed without receiving value, it may be plausibly argued that under sections 28 and 58 he has a good defense except as against a holder in due course. If, on the other hand, one's attention is concentrated on section 29, it may be contended with like plausibility that

[1] Maine has adopted the Negotiable Instruments Law. Me. Rev. Stat. (1930), c. 164.

[2] Greeley, "The Uniform Negotiable Instruments Law in the Light of Recent Criticism," 10 ILL. L. REV. 264 (1915); Brannan, "Some Necessary Amendments to the Negotiable Instrument Law," 26 HARV. L. REV. 493 (1913).

such accommodation party is liable to a holder for value regardless of other factors. Obviously these sections, being parts of one statute, must be construed so as to harmonize them if possible. Thus it would seem that section 29 was clearly intended to eliminate the defense of lack of consideration by an accommodation signer as against a holder for value even though he does not have the favored position of a holder in due course.[3] It would seem equally clear, however, that if sections 28 and 58 are given their due effect, other defenses are open to the accommodation party unless the claimant is, except for his knowledge of the fact of accommodation, a holder in due course. In a case where there is a claim that a negotiation after maturity is a violation of an express agreement between the accommodation and accommodated parties or where, as in the principal case, the claim is that the negotiation of the instrument is a fraudulent and material diversion from the intended purpose of the accommodation,[4] there should be no question as to the right of the accommodation party to assert the defense in order to preclude the holder, not otherwise a holder in due course, from recovering.[5] Most courts in such cases have allowed the accommodation party to assert the defense of diversion of purpose.[6] The difficulty appears in the case where there is no express agreement, the only fact being the negotiation of the instrument for the first time after the maturity date. The English courts refuse to presume that the agreement between the parties is that the accommodation paper must be negotiated before maturity or the accommodation's party liability on his accommodation is terminated.[7] The majority American view prior to the adoption of the N. I. L. was to the contrary.[8]

[3] Notwithstanding this, some courts interpret § 29 as eliminating the defense of lack of consideration *only* in those cases where the holder is a bona fide holder for value before maturity, and, if he is not, the accommodation party may assert the defense of lack of consideration to bar recovery. These courts are of the opinion that the only way in which these sections can be reconciled is to read the words of § 29, "holder for value" as "otherwise a holder in due course." Otherwise, in their opinion, a holder of accommodation paper after maturity or one who takes before maturity but in bad faith will be in a superior position to a holder in due course. See Frank L. Dittmeier Real Estate Co. v. Knox, (Mo. App. 1924) 259 S. W. 835; Pacific Southwest Trust & Savings Bank v. Valley Finance Corp., 99 Cal. App. 728, 279 P. 222 (1929), petition for rehearing denied 280 P. 134.

[4] Negotiation in breach of faith is an equity which the holder could assert against anyone except a holder in due course. Section 55 of the N. I. L. makes the holder's title defective when the instrument is negotiated in bad faith. Also when there is an express agreement between the accommodation and accommodated parties, the note is really delivered on a condition, which conditional delivery by virtue of § 16 can be asserted against anyone except a holder in due course.

[5] Parol evidence is admissible to show the oral agreement between the accommodation party and the accommodated party. See Gobles Co-op. Assn. v. Albright, 248 Mich. 68, 226 N. W. 876 (1929); Schlam v. Manewal, 196 Mo. App. 114, 190 S. W. 658 (1916).

[6] Red Wing Rubber Mfg. Co. v. Hjermestad, 176 Minn. 425, 223 N. W. 682 (1929); Hill v. May, 205 Iowa 948, 218 N. W. 946 (1928).

[7] Charles v. Marsden, 1 Taunt, 224, 127 Eng. Rep. 818 (1808).

[8] The courts were in conflict prior to the N. I. L. Early cases allowing a holder for value after maturity to recover: Miller v. Larned, 103 Ill. 562 (1882); First National

Under the N. I. L. the courts are still in conflict.[9] Although there are arguments advanced in favor of both views, it is submitted that the preferable view is the one which holds that negotiation after maturity is a breach of an implied agreement between the parties, not only because it is more in keeping with the supposed intention of the parties[10] but because the surety is one of the most favored parties known to the law.[11] In the principal case, although the court was not faced directly with this problem, its language supports this view. This decision is illustrative of the recent trend not to interpret the term "holder for value" employed in section 29 of the N. I. L. literally but consistently with the rest of the sections of the N. I. L., particularly section 58.[12]

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Bank of Salem v. Grant, 71 Me. 374 (1880). Cases refusing recovery: Chester v. Dorr, 41 N. Y. 279 (1869); Sears v. Moore, 171 Mass. 514, 50 N. E. 1027 (1898). See collection of cases pro and con in 46 L. R. A. 753 at 772 (1900). The early English cases allowed recovery: Charles v. Marsden, 1 Taunt. 224, 127 Eng. Rep. 818 (1808); Stein v. Yglesias, 1 C. M. & R. 565, 149 Eng. Rep. 1205 (1834); Sturtevant v. Ford, 4 M. & G. 101, 134 Eng. Rep. 42 (1842). See also CHALMERS, BILLS OF EXCHANGE, 8th ed., 137 (1919).

[9] Cases allowing recovery from an accommodation party after N. I. L.: Marling v. Jones, 138 Wis. 82, 119 N. W. 931 (1909) [§ 29 was construed as adoption of the English rule because it is the same as § 28 of the Bills of Exchange Act, which codified the rule of Charles v. Marsden, 1 Taunt. 224, 127 Eng. Rep. 818 (1808)]; Altfillisch v. McCarty, 49 S. D. 203, 207 N. W. 67 (1926), noted 24 MICH. L. REV. 847 (1926), 39 HARV. L. REV. 893 (1926), 10 MINN. L. REV. 613 (1926); Vernon Center State Bank v. Mangelsen, 166 Minn. 472, 208 N. W. 186 (1926).

See, however, Comstock v. Buckley, 141 Wis. 228, 124 N. W. 414 (1910). This case modifies the rule in Wisconsin at least, to the extent of preventing renegotiation after maturity.

Cases refusing recovery: Rylee v. Wilkerson, 134 Miss. 663, 99 So. 901 (1924); Weiser Nat. Bank v. Peters, 174 Ark. 984, 298 S. W. 878 (1927); Bartels v. Suter, 130 Okla. 7, 266 P. 753 (1928); 48 A. L. R. 1280 (1927).

[10] In favor of the view that the accommodation party's credit is unlimited, it is sometimes said that the burden of taking up the note at maturity rests upon the accommodated party, and if through his negligence the note is still outstanding and negotiated after maturity the accommodation party cannot object. But in opposition it has been said that the liability must be considered as being limited to the maturity of the instrument and that the taker after maturity takes at his own peril.

[11] See Whiney v. Groot, 24 Wend. (N. Y. S. Ct.) 82 (1840), for a striking example.

[12] 48 A. L. R. 1280 (1927).