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SMU Law Review

Volume 3
Issue 3 *Survey of Texas Law for the Year 1948*

Article 10

January 1949

Bills and Notes

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BILLS AND NOTES

HOLDER'S AUTHORITY TO ACCELERATE MATURITY DATE OF A PROMISSORY NOTE

A PROVISION in a promissory note in *Faulk v. Futch*[1] stated:

"... in the event any default is made in the payment of any installment of principal or interest hereon, or any part thereof, when due, such default shall at the option of the holder, at once mature the whole of this note."

The dominant question presented in this case was whether the holders of the note were authorized to accelerate the maturity date and to declare the entire amount of the principal due and payable.

The instrument provided that it was payable "in San Antonio, Bexar County, Texas," but no specific place was given at which the payment could be made. The holders of the instrument resided in Seguin, Guadalupe County, Texas, and did not maintain a place of business in Bexar County. The proper place of payment was held to be the maker's place of business in San Antonio, Bexar County, Texas. This holding is in line with the provisions of the Negotiable Instrument Law[2] and Texas decisions.[3]

Having made this determination, the court then set forth what it considered to be the well established rule that,

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[1] ..... Tex. ....., 214 S. W. (2d) 614 (1948).

[2] TEX. REV. CIV. STAT. (Vernon, 1925) art. 5937, § 73, "Presentment for payment is made at the proper place: ... (3) where no place of payment is specified and no address is given and the instrument is presented at the usual place of business or residence of the person to make payment."

[3] Parker v. Mazur, 13 S. W. (2d) 174, (Tex. Civ. App. 1928) *writ of error dism'd;* Griffin v. Reilley, 275 S. W. 242 (Tex. Civ. App. 1925; *cf.* Barnes v. Rushing 5 S. W. (2d) 777 (Tex. Civ. App. 1928); Moore v. Kenmeyer, 271 S. W. 653 (Tex. Civ. App. 1925); O'Connor v. Kirby Investment Co., 262 S. W. 554 (Tex. Civ. App. 1924) *writ of error refused.*

"... where the acceleration clause in a promissory note leaves it optional with the holder whether he shall declare the whole amount due upon failure to pay any installment of principal or interest, such holder cannot without presentment for payment, exercise his option to declare the whole amount due, if no specific place of payment is expressed in the note, until it has been presented to the payor at the latter's place of business."[4]

This rule was first announced in Texas by the court of civil appeals in *Griffin v. Reilley*,[5] although it had earlier been said in *Beckham v. Scott*[6] that in such a situation to allege the exercise of such option by the holder and to show that formal demand was made for payment, was a sufficient showing of the exercise of such option. The rule has since been set out in several other civil appeals decisions.[7]

There are decisions of the appellate courts of this state which have held that institution of suit within a reasonable time after default in payment of one of a series of notes or of an installment of principal or interest is sufficient notice of an election to exercise the option to accelerate maturity as per the terms of the instrument.[8] At first glance this seems to conflict with the

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[4] ..... Tex. ....., ..., 214 S. W. (2d) 614, 616 (1948).

[5] 275 S. W. 242 (Tex. Civ. App. 1925).

[6] 142 S. W. 80 (Tex. Civ. App. 1911).

[7] Curtis v. Speck, 130 S. W. (2d) 348 (Tex. Civ. App. 1939) *writ of error refused*; Ladd v. Anderson, 89 S. W. (2d) 1041 (Tex. Civ. App. 1936) *rev'd on other grounds*, 115 S. W. (2d) 608 (Tex. Com. App. 1938); Ross v. Isaacs, 54 S. W. (2d) 182 (Tex. Civ. App. 1932) *writ of error dism'd*; Parker v. Mazur, 13 S. W. (2d) 174 (Tex. Civ. App. 1928) *writ of error dism'd.*

[8] Natali v. Witthaus, 134 Tex. 513, 135 S. W. (2d) 969 (Tex. Com. App. 1940); Seaboard Bank & Trust Co. v. Amuny, 23 S. W. (2d) 287 (Tex. Com. App. 1930); Kyle v. Commercial Credit Co., 152 S. W. (2d) 465 (Tex. Civ. App. 1941) *writ of error dism'd* J. Corr; Chandler v. Guaranty Mortgage Co., 89 S. W. (2d) 250 (Tex. Civ. App. 1935); Barnes v. Rushing, 5 S. W. (2d) 777 (Tex. Civ. App. 1928); Moore v. Kenmeyer, 271 S. W. 653 (Tex. Civ. App. 1925); Dunkel v. Amarillo Bank & Trust Co., 222 S. W. 670 (Tex. Civ. App. 1920) *writ of error refused*; Stewart v. Thomas, 179 S. W. 886 (Tex. Civ. App. 1915); Shearer v. Chambers County, 159 S. W. 999 (Tex. Civ. App. 1913) *writ of error refused*; Coleman v. Garvin, 158 S. W. 185 (Tex. Civ. App. 1913) *writ of error refused*; Dieters v. Bowers, 37 Civ. App. 615, 84 S. W. 847 (Tex. Civ. App. 1905) *writ of error denied*; Gillispie v. Brown, 30 S. W. 448 (Tex. Civ. App. 1895); Luzenburg v. Bexar Building & Loan Assn., 29 S. W. 237 (Tex. Civ. App. 1894) *writ of error denied*; Kerr v. Morrison, 25 S. W. 1011 (Tex. Civ. App. 1894); Chase v. First Nat. Bank of Cleburne, 1 Civ. App. 595, 20 S. W. 1027 (Tex. Civ. App. 1892).

holding of the court in the *Faulk* case. But, a careful reading of these cases reveals that either a special place of payment was specified in the instruments involved or that the reports are silent as to this fact. However, there are two civil appeals cases[9] which explicitly declared that the place of payment prescribed in the instrument was not a special place of payment within the provisions of the Texas Negotiable Instrument Law,[10] but went on to hold in one of them[11] that it was not necessary to present the note for payment, and in the other,[12] that the filing of the suit operated as notice to the maker of the intention to exercise the option to accelerate maturity. It seems safe to say that these two cases are therefore overruled by the holding in the *Faulk* case.

As to this apparent conflict relative to the requisites of a holder exercising the option to accelerate maturity of the instrument as provided by its terms, it seems that the holding of the Supreme Court in the *Faulk* case can be reconciled, so long as it is limited to instruments wherein no special place of payment is specified. However, this view has not been immune from attack in other jurisdictions.[13] In looking at the decision of the Oregon Supreme Court in *Harrison v. Beals*,[14] it is interesting to note that the court criticized the case of *Bardsley v. Washington Mill Co.*,[15] which was cited in *Griffin v. Reilley* and also the *Faulk* case. The criticism was on the grounds that the court went out of its way

[9] Barnes v. Rushing, 5 S. W. (2d) 777 (Tex. Civ. App. 1928); Moore v. Kenmeyer, 271 S. W. 653 (Tex. Civ. App. 1925).

[10] TEX. REV. CIV. STAT. (Vernon, 1925) art. 5937, § 70, "Presentment for payment is not necessary in order to charge the person primarily liable on the instrument; but if the instrument is, by its terms, payable at a special place, and he is able and willing to pay it there at maturity, such ability and willingness are equivalent to a tender of payment upon his part...."

[11] Barnes v. Rushing, 5 S. W. (2d) 777 (Tex. Civ. App. 1928).

[12] Moore v. Kenmeyer, 271 S. W. 653 (Tex. Civ. App. 1925).

[13] Corbett v. Ulsaker Printing Co., 49 N. D. 103, 190 N. W. 75 (1922); Harrison v. Beals, 111 Ore. 563, 222 Pac. 728 (1924); the following cases have interpretated the rule so as to give it a very limited effect: James v. Brainard Jackson & Co., 64 Wash. 175, 116 Pac. 633 (1911); Cook v. Strelau, 127 Wash. 128, 219 Pac. 846 (1923); Hartge v. Capeloti, 136 Wash. 538, 241 Pac. 5 (1925).

[14] 111 Ore. 563, 222 Pac. 728 (1924).

[15] 54 Wash. 553, 103 Pac. 822 (1909).

to relieve a contracting party from his express obligation and that the clause in Section 70 of the N.I.L.[16] rendering presentment to the maker unnecessary makes no exception requiring presentment for enforcement of the acceleration clause.

The *Faulk* case is also important in that for the first time a Texas court set forth the rule allowing a waiver of the requirements of Article 5937, Section 74 of the Texas Negotiable Instrument Law,[17] which provision gave the makers the right to have the note actually exhibited at the time when payment was demanded. This rule has been adopted in other jurisdictions[18] and seems justified when it is remembered that the reason for the requirement is that the drawer or acceptor may be able to judge (1) the genuineness of the instrument; (2) the right of the holder to receive payment; and (3) that he may immediately reclaim possession upon paying the amount.[19] Therefore, the right to require exhibition is personal, and may be waived; and if exhibition is not requested and payment is refused on other grounds, exhibition is waived.[20]

Reference in a Promissory Note to a Collateral Instrument

Continental National Bank of Fort Worth v. Conner[21] involved certain clauses in a promissory note, which had been executed at

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[16] See Note 9, *supra*.

[17] Tex. Rev. Civ. Stat. (Vernon, 1925) art. 5937, § 74, "The instrument must be exhibited to the person from whom payment is demanded, and when it is paid must be delivered up to the person paying it."

[18] Freudenberg v. Lucas, 38 Cal. App. 95, 175 Pac. 482 (1918); Greenstein v. Kucharski, 107 Conn. 269, 140 Atl. 482 (1928); Union Bank of Louisiana v. Lea, 7 Rob. (La.) 76, 41 Am. Dec. 275 (1844); Legg v. Vinal, 165 Mass. 555, 43 N. E. 518 (1896); Porter v. East Jordan Realty Co., 210 Mich. 398, 177 N. W. 987 (1920); Porter v. Thom, 40 App. Div. 34, 57 N. Y. S. 879 (1899) *affirmed* 167 N. Y. 584, 60 N. E. 1119 (1901) memo; Hodges v. Blalock, 82 Ore. 179, 161 Pac. 396 (1916); Waring v. Betts, 90 Va. 46, 17 S. E. 739 (1893).

[19] Waring v. Betts, 90 Va. 46, 17 S. E. 739 (1893).

[20] Gilpin v. Savage, 60 Misc. 605, 112 N. Y. S. 802 (1908) *affirmed* 132 App. Div. 948 memo., 118 N. Y. S. 1108 (1909) memo., *reversed on the facts* 201 N. Y. 167, 94 N. E. 656 (1911).

[21] ..... Tex. ....., 214 S. W. (2d) 928 (1948).

the same time that the makers entered into a mechanic's lien contract with the payee of the note. The clauses read as follows:

> "Failure to pay any portion of the principal or interest hereon . . . " or failure to perform any agreement in the below mentioned lien instrument shall, at the option of the holder thereof, mature this note.
>
> "This note is secured by mechanic's lien contract of even date between Maker and Payee relating to . . . [property described] . . . to which said mechanic's lien contract reference is hereby made."

The Supreme Court was called upon to determine if the above quoted provisions rendered the note non-negotiable. Recognizing the rule in this State, that before a reference in an otherwise negotiable instrument to another agreement will make the former non-negotiable, it must appear therefrom that the paper is to be burdened with the conditions of that agreement,[22] the references to the mechanic's lien contract were said to be either a mere statement of the transaction which gives rise to the instrument or a reference to the security given for the note. If the former, such a reference is permitted by the provisions of the Texas Negotiable Instrument Law,[23] which is but a restatement of the law as announced by our courts for a number of years,[24] or if the latter, such reference is also impliedly authorized by another provision of the statute.[25] No particular phrase regarding the relationship between the note and the lien contract contained the words "burdened with," "subject to" or their equivalent, so as to bring it within the rule that would destroy its negotiability.

Relative to the provision entitling the noteholder to accelerate maturity for breach by the makers of their obligations under the contract, it was admitted that it was something different from

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[22] Arrington v. Mercantile Protective Bureau, Inc., 24 S. W. (2d) 383 (Tex. Com. App. 1930); P. J. Williams Industries Inc. v. First State Bank of Lyford, 38 S. W. (2d) 1109 (Tex. Civ. App. 1931) *writ of error dism'd*; Mountjoy Parts Co. v. San Antonio Nat. Bank, 12 S. W. (2d) 609 (Tex. Civ. App. 1928).

[23] TEX. REV. CIV. STAT. (Vernon, 1925) art. 5932, § 3.

[24] Arrington v. Mercantile Protective Bureau Inc., 24 S. W. (2d) 383 (Tex. Com. App. 1930).

[25] TEX. REV. CIV. STAT. (Vernon, 1925) art. 5932, § 5.

a mere statement of the underlying transaction, and caused the holder to have to look to the contract to see if its terms have been violated, only in the case he cares to accelerate maturity for this reason. But, it did not purport to render conditional or uncertain the maker's otherwise absolute and certain promises theretofore contained in the note. Therefore, the note was not rendered non-negotiable by this provision.

An example of a clause in an instrument having been declared to be more than a mere statement of the transaction which gives rise to the instrument, as permitted by the N.I.L.[26] is that contained in the trade acceptance involved in *Lane Co. v. Crum.*[27] The provision there declared:

> "The obligation of the acceptor arises out of the purchase of goods from the drawer, maturity being in conformity with the original terms of purchase."

The instruments containing this clause were held non-negotiable on the grounds that the obligation of the acceptor, according to the terms of the clause arose, not from the instruments themselves but from a collateral transaction.

Three years after the *Lane* decision, the Commission of Appeals in *Arrington v. Mercantile Protective Bureau, Inc.*[28] was confronted with a trade acceptance which contained the following clause:

> "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer."

On the basis of it being construed to be nothing more than a mere reference to the transaction out of which the obligation arose, the instrument was held to be negotiable. It will be noted that this clause is identical with the first part of the one involved

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[26] See Note 23, *supra.*

[27] 291 S. W. 1084 (Tex. Com. App. 1927) *reversing* 284 S. W. 980 (Tex. Civ. App. 1926).

[28] 24 S. W. (2d) 383 (Tex. Com. App. 1930) *affirming* 15 S. W. (2d) 663 (Tex. Civ. App. 1929).

in the *Lane* case. However, the court went on to specifically distinguish the provision in the *Lane* case from the one they were considering, on the grounds that the latter part of the clause there involved, which reads, "maturity being in conformity with the original terms of purchase," was susceptible of no other construction except to indicate a purpose to burden the paper with the conditions of an extrinsic agreement as to the maturity thereof. This result was reached, even though the trade acceptances that were involved in the *Lane* case were payable respectively 60, 90, and 120 days after date. The note in the *Conner* case was payable at a fixed date, just as were the above mentioned trade acceptances, yet the provision in the note which gave the holder the option to mature it on failure of the makers to perform any agreement contained in the lien instrument was held not to burden the note with the conditions of the collateral agreement. These provisions as to the maturity of the instruments involved in the *Lane* and *Conner* cases, while not the same, can possibly be considered as being of a like nature, and therefore raise the question whether the divergent result of these two cases is justified.

The *Lane* case has met with some approval in other jurisdictions,[29] but the Pennsylvania Superior Court in 1941[30] adopted what it termed the majority view and the one adopted by the jurisdictions called upon most recently to determine the question of negotiability where an identical provision to that contained in the *Lane* case was involved,[31] and declared the instrument to be negotiable. This result is reached by construing the provision as

[29] Westlake Mercantile Finance Corp. v. Merritt, 204 Cal. 673, 269 Pac. 620 (1928). (Note—There seems to be no due date plainly stated in the body of the instrument); First Nat. Bank, Statesville, N. C. v. Power Equipment Co., 211 Ia. 153, 233 N. W. 103 (1930).

[30] State Trading Corp. v. Jordan, 146 Pa. Super. 166, 22 A. (2d) 30 (1941).

[31] State Trading Corp. v. Rosen, 136 Conn. 37, 9 A. (2d) 290 (1939); State Trading Corp. v. Toepfert, 304 Mass. 473, 23 N. E. (2d) 1008 (1939); Heller v. Cuddy, 172 Minn. 126, 214 N. W. 924 (1927); State Trading Corp. v. Smaldone, 172 Misc. 367, 15 N. Y. S. (2d) 33 (1938); State Trading Corp. v. Tobias Studio, 64 Ohio App. 516, 29 N. E. (2d) 38 (1940); Levitt v. Johnson Office Supply Co., 103 Pa. Super 76, 157 Atl. 804 (1931) (instrument considered as negotiable without any discussion).

merely a statement of the transaction which gives rise to the instrument and not a reference to an extrinsic instrument affecting the time of payment. That decision listed the *Lane* case as one setting out the minority view that an instrument containing such a provision is non-negotiable.

In view of the result reached in the *Conner* case and the position other jurisdictions have taken in holding instruments which contained the identical provision to that involved in the *Lane* case to be negotiable, perhaps it can be expected that should this question be expressly presented to our Supreme Court, it may overrule the Lane case and adopt what has been termed the majority view.[32]

Liability of the Drawee Bank to the Payee on an Indorsement Made Without Authority

The plaintiff in *Strickland Transportation Co. v. First State Bank of Memphis*[33] was the payee of certain checks which had been cashed at the drawee bank by the payee's agent, who had authority only to accept the checks for the payee, but had no authority to cash them and receive payment thereon. The agent appropriated to his own use the money so paid to him, and left for parts unknown. The checks were charged against the account of the drawer by the drawee bank.

Plaintiff's action against the drawee bank was based on two theories. One, that the bank was liable for wrongful conversion of the checks, and the other, that the plaintiff as assignee of the rights and causes of action of the drawer of the checks, could recover for the breach of the bank's duty to its depositor in cashing the checks upon an unauthorized indorsement and thereafter charging them to the depositor's account.

The court was unanimous in their holding that the payee could not recover directly against the drawee bank on the theory of

[32] See Note 30, *supra*.

[33] ..... Tex. ...., 214 S. W. (2d) 934 (1948).

wrongful conversion. To sustain this result, the court relied mainly on *Fidelity and Deposit Co. of Maryland v. Fort Worth National Bank.*[34] In that case, the Commission of Appeals, without discussion, denied liability on the part of the drawee bank, where the suit had been brought on the conversion theory. However, the court in that decision expressly refused to approve earlier decisions of the courts of civil appeals allowing recovery on that theory,[35] and the Supreme Court in the *Strickland* case construed this to be a rejection of the conversion theory as a grounds of recovery. This result is not uniformly accepted in other jurisdictions,[36] and the Texas decisions have been said to follow the minority rule.[37]

In deciding if the plaintiff could recover as assignee of the drawer's rights, the Supreme Court had before it a question of first impression in this state in determining whether the drawer of these checks had any cause of action that could be assigned to the payee of these checks where the payee's agent, without authorization indorsed and cashed them, failing to account to his principal for the proceeds.

In answering this question, the court first found it necessary to determine if the liability of the drawer to the payee was discharged by the authorized delivery of the checks, to the payee's agent, and their subsequent payment by the drawee bank to the agent on his unauthorized indorsement. The conclusion of the

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[34] 65 S. W. (2d) 276 (Tex. Com. App. 1933).

[35] City National Bank & Trust Co. of Corpus Christi v. Pyramid Asbestos & Roofing Co., 39 S. W. (2d) 1101 (Tex. Civ. App. 1931) *writ of error dism'd;* Pierce Petroleum Corp. v. Guaranty State Bank of Mt. Pleasant, 22 S. W. (2d) 520 (Tex. Civ. App. 1929).

[36] A. Paul Goodall Real Estate & Ins. Co. v. North Birmingham American Bank, 225 Ala. 507, 144 So. 7 (1932); Louisville & N. R. Co. v. Citizens & Peoples Nat. Bank of Pensacola, 74 Fla. 385, 77 So. 104 (1917); Bentley, Murray & Co. v. LaSalle St. Savings Bank, 197 Ill. App. 232 (1916); James v. Union Nat. Bank, 238 Ill. App. 159 (1925); Kentucky Title Savings Bank & Trust Co. v. Dunavan, 205 Ky. 801, 266 S. W. 667 (1924); Blacker & Shepard Co. v. Granite Trust Co., 284 Mass. 9, 187 N. E. 53 (1933); State v. First State Bank of Albuquerque, 38 N. M. 225, 30 P. (2d) 728 (1934); Burstein v. Peoples Trust Co., 143 App. Div. 165, 127 N. Y. S. 1092 (1911); Hartford Accident & Indemnity Co. v. Bear Butte Valley Bank, 63 S. D. 262, 275 N. W. 642 (1934).

[37] Note, 12 TEX. L. REV. 226 (1934).

majority of the court was that the better reasoned authorities and decisions of other jurisdictions[38] supported the holding that the drawer's liability was discharged when the checks were paid to the agent. The unfortunate position in which the payee found himself was not due to any act or omission of the drawer, but arose solely from the unfaithfulness of the payee's own agent. Therefore, the drawer's liability having been discharged, he had no cause of action against the bank to assign to the plaintiff.

In a strong dissenting opinion by Jusitce Hart, in which three other justices joined,[39] it was contended that since the proceeds of the checks were never paid to the payee or any agent authorized to receive them, the drawer's obligation to the payee was not paid, and the drawer was still under an obligation to pay, with the right of a depositor to pursue its remedy against the drawee bank for the wrongful payment of the checks. Therefore, the drawer could for a valuable consideration, assign his cause of action to the payee, who may then recover against the bank.

Therefore, in summary, the majority denied the payee's ability to recover because the harm wrought by the unfaithfulness of the agent must fall on the one who selected him and sent him out to receive checks under an implied representation that he was worthy

[38] Kansas City, M. & B. R. Co. v. Ivy Leaf Coal Co., 97 Ala. 705, 12 So. 395 (1892); Mills v. Hurley Hardware & Furniture Co., 129 Ark. 350, 196 S. W. 121 (1917); McFadden v. Follrath, 114 Minn. 85, 130 N. W. 542 (1911); Morrison v. Chapman, 155 App. Div. 509, 140 N. Y. S. 700 (1913); Indemnity Mutual Marine Assur. Co. v. Powell & O'Rourke Grain Co., 216 Mo. App. 673, 271 S. W. 538 (1925); Union Home Furnishing Co. v. National Bank of Commerce in St. Louis, 53 S. W. (2d) 1067 (1932); 1 MEACHAM ON AGENCY, 687 (2d ed. 1914). It is interesting to note that in each of these jurisdictions which hold the drawer's obligation to the payee is discharged when the checks, which were indorsed and cashed without authority by the payee's agent, are paid by the drawee bank, a recovery is allowed by the payee directly from the drawee bank on the theory of conversion. A Paul Goodall Real Estate & Ins. Co. v. North Birmingham American Bank, 225 Ala. 507, 144 So. 7 (1932); Wayne Tank & Pump Co. v. Bank of Eureka Springs, 172 Ark. 775, 290 S. W. 370 (1927); Wm. Deering & Co. v. Kelso, 74 Minn. 41, 76 N. W. 792 (1898); Kansas City Casualty Co. v. Westport Ave. Bank, 191 Mo. App. 287, 177 S. W. 1092 (1915); Burstein v. Peoples Trust Co., 143 App. Div. 165, 127 N. Y. S. 1092 (1911). Recovery on this theory was expressly disapproved in the *Strickland* case. Consequently, Texas reaches a different result to that reached in these states, in that neither by going directly, or indirectly as assignee of the drawer's rights, can the payee recoup his loss.

[39] Justices Smedley, Taylor and Garwood.