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Negotiable Instruments

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NEGOTIABLE INSTRUMENTS

GOOD FAITH UNDER THE FIDUCIARIES ACT

New Mexico. The *good faith* required of a person taking a negotiable instrument in order to stand as a holder in due course under the Negotiable Instruments Law has come to be almost uniformly treated from the standpoint of *honesty*.¹ This is in contrast with the common law test of a bona fide purchaser. Freedom from negligence characterizes the common law approach in determining whether or not a transaction may be sheltered under the rights and privileges accorded a bona fide purchaser.²

Under the more recent Uniform Warehouse Receipts Act³ authority is scant and lacking in uniformity. In two cases the *honesty* test has been applied.⁴ In another case the good faith of a purchaser under this act was determined by the rule of negligence.⁵

Consistent with the purpose of achieving uniformity in dealing with commercial paper is the application of the Fiduciaries Act of New Mexico⁶ in a case of first impression, *Roswell State Bank v. Lawrence Walker Cotton Co., Inc.*⁷ The Act specifically states that a thing is done in *good faith* when it is in fact done *honestly*, whether it be done negligently or not. Further, by its terms the Act indicates exculpation of a bank when it is sought to be charged by a fiduciary's principal.

The court held a statutory right was created in favor of a bank acting in good faith against a faithless fiduciary's principal to enforce payment of an instrument dishonored by the principal. The faithless fiduciary appeared on the bill as agent-drawer, agent-acceptor, and as payee. The bill drawn on a Texas bank was de-

¹ See authorities collected in 10 C.J.S., *Bills and Notes*, § 324.

² See 27 R.C.L., *Vendor and Purchaser*, § 475.

³ §§41, 47; see TEX. REV. CIV. STAT. (Vernon, 1948) arts. 5652, 5658.

⁴ *Grauman v. Jackson*, 216 Ark. 362, 225 S. W. 2d 678 (1950); *Starkey v. Nixon*, 151 Tenn. 637, 270 S. W. 980 (1925).

⁵ *City Nat. Bank of Decatur v. Nelson*, 218 Ala. 90, 117 So. 681 (1928).

⁶ N. M. STAT. 1941 ANN. § 36-101 *et seq.*

⁷ 56 N. M. 107, 240 P. 2d 1143 (1952).

posited to the fiduciary's personal account in plaintiff bank. Withdrawal of the funds by the fiduciary was permitted by the plaintiff bank prior to clearance by the drawee bank but upon instruction from the drawee to plaintiff in a telephone communication made upon insistence by the fiduciary. Thereafter the bill was dishonored.

The parties were reversed from the positions specifically provided for by Section 9 of the Uniform Fiduciaries Act. But the court, consistent with the *good faith* provision, interpreted the Act to give the bank not only a good defense against the principal but to establish a cause of action in favor of the bank. Under this Section the bank was not bound to inquire whether the fiduciary was committing a breach of his obligation where he had authority to draw on the account of his principal and the amount drawn was credited to his personal account and later withdrawn.

SET-OFF AGAINST A NOTE

ASSIGNED AFTER MATURITY

New Mexico. In *Turkenkoph v. Te Beest*⁸ a note was assigned in good faith for value but after maturity. After maturity, but prior to the assignment, a debt arose in favor of the maker against the assignor of the note. Action was initiated by the maker against the assignor prior to notice of assignment of the note to collect the debt, which arose out of collateral matters. The assignee, a party defendant, filed a cross-action against the maker to collect the note, and as against this claim the maker of the note as cross-defendant urged his right to set-off against the note.

The court recognized that set-off and counterclaims exist by reason of statutory law only and that the apparent discord in the decisions relating to set-off and counterclaims exists only because

⁸ 55 N. M. 279, 232 P. 2d 684 (1951).

of the wide variety in statutory provisions. Section 58 of the Negotiable Instruments Law⁹ would not permit set-off against the note if the "defenses" referred to be interpreted to mean only such defenses as inhere in the negotiable paper itself. The cross-complainant-assignee urged that this Section of the Negotiable Instruments Law was exclusive and should bear the interpretation indicated. The provisions of the New Mexico statute relating to counterclaims and set-off specifically state that "in case of an assignment of a chose in action, the action by the assignee shall be without prejudice to any set-off, counterclaim or other cause of action or defense, whether matured or not, if matured when pleaded, if existing in favor of defendant against the assignor, before notice of the assignment; but this shall not apply to negotiable instruments transferred in good faith, and upon valuable consideration before maturity."¹⁰

In sustaining the right of the maker to counterclaim against the assignee under the statute the court held that Section 58 was not exclusive and did not prevent pleading other defenses not dealt with or covered in the Negotiable Instruments Law and specifically authorized by another statute governing practice and procedure in civil actions. The assignee taking the negotiable instrument after maturity did not have the protection offered a holder in due course by the counterclaim and set-off statute.

FICTITIOUS PAYEE

Texas. The Negotiable Instruments Law provides that an instrument is payable to bearer "when it is payable to the order of a fictitious or non-existing person, and such fact was known to the person making it so payable."¹¹ Where an agent draws a negotiable instrument on his principal's account, there is a division of authority as to whether under the statutory provisions the character of the paper payable to the order of a fictitious person is determined by

⁹ N. M. STAT. 1941 ANN. § 53-158.

¹⁰ N. M. STAT. 1941 ANN. § 19-412.

¹¹ § 9(3); TEX. REV. CIV. STAT. (Vernon, 1948) art. 5932.

the knowledge of the nominal maker or drawer (the principal) or by the knowledge of the agent.¹²

The precise question has not been decided in Texas. A recent opinion, the decision of which turned upon whether the doctrine of election of remedies applied, left the question open and relied upon a relatively narrow ground, namely, that the agent involved was not "the person" making the check "so payable" within the meaning of the Act, in holding that checks there in question were not bearer instruments.¹³

In the case plaintiff's employee *A* induced plaintiff to issue checks payable to fictitious claimants, which checks were endorsed by *A* in the names of the payees and cashed. The checks were actually drawn by other employees and were signed by authorized officers of plaintiff in response to *A*'s requisition. The court found Section 9(3) of the Negotiable Instruments Law inapplicable. Although *A* had the knowledge dealt with in the statute, he was not the *person making it "so payable."* The contention that the actual signer was but an automaton or instrumentality through which *A* acted was rejected.

The supreme court also declared that the question is settled in Texas that a depositor is under no duty to his bank to examine signatures of payees on his cancelled checks and that his failure to discover such signatures to be forged does not constitute negligence, citing *Liberty State Bank v. Guardian Savings and Loan Association*.¹⁴ However, the opinion does not preclude the possibility of adoption of the doctrine that a depositor owes a duty to his bank in other regards, such as reasonable supervision of employees having authority to issue or requisition checks and being careful to draw checks in a manner that does not invite material alteration or unauthorized signatures.¹⁵

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¹² See authorities cited in 10 C.J.S., *Bills and Notes*, § 129.

¹³ *Liberty Mutual Insurance Co. v. First National Bank in Dallas*, _____ Tex. _____, 245 S. W. 2d 237 (1951).

¹⁴ 127 Tex. 311, 94 S. W. 2d 133 (1936).

¹⁵ See *Young v. Grote*, 4 Bing. 253, 130 Eng. Rep. 764 (C.P. 1827).