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NEGOTIABLE INSTRUMENTS

ROBERT A. MCKENNA*

It is difficult to understand why in Florida, where real estate transactions with the usual promissory notes and accompanying mortgages are most numerous, there should be only one case on negotiable instruments decided during the period of this survey. In the same two years approximately twenty were considered in Louisiana. In any event, the author has only one decision of the Florida Supreme Court to report. I have included a decision of the U.S. District Court believing it to be of some interest to Florida attorneys. The Florida amendment to the Negotiable Instruments Law, also noted, deals with a problem which will be familiar to recent graduates from law school, but probably long since forgotten by other attorneys.

Negotiability and Rights of a Holder in Due Course

In *Wright v. Board of Public Instruction*¹ certain time warrants were issued by the defendant. Each warrant provided that it was "payable out of the Common School fund of Sumter County" and that the "full faith, credit and resources of the said Board of Public Instruction . . . are pledged for the . . . payment . . . hereof." These instruments were purchased by a Florida bank and, shortly thereafter, received by a Maryland bank, as security for a debt, without knowledge that full consideration had not been paid by the Florida bank. Subsequently, after acquiring knowledge of this defect the Maryland bank acquired complete title to the warrants by a compromise agreement with the liquidator of the Florida bank. The plaintiff then purchased those which had not been retired, having a face value of \$20,000, for \$3,600. In the lower court it was held that the instruments were not negotiable and, hence, the Board's defense of partial failure of consideration was good. A judgment for \$14,800, principal and interest, plus costs, was nevertheless rendered. On this appeal by the plaintiff it was held that the warrants were negotiable, as plaintiff contended, but that plaintiff's recovery would be limited to the amount of the debt, plus interest, owed to the Maryland bank by the Florida bank, as the former would be a holder in due course only to the extent of this lien. Since some \$5,000 of the original debt of \$15,000 had been paid off it would appear that plaintiff's appeal was not monetarily, at least, particularly successful.

Under the N.I.L. § 1,² an instrument to be negotiable must contain an *unconditional* promise or order to pay. Obviously, a promise to pay "out

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1. 77 So.2d 435 (Fla. 1955).

2. FLA. STAT. § 674.02 (1953).

of a particular fund" is conditional upon the existence of that fund, so that such a promise would render the instrument non-negotiable; it being expressly so provided.³ Under the same section "an indication of a particular fund out of which reimbursement is to be made, or a particular account to be debited with the amount" will not impair negotiability. The distinction between the two is generally determined by resolving whether or not the promissor is pledging his general credit; if he is, the promise is unconditional.⁴ In the principal case⁵ we have an indication of the County School Fund out of which payment is to be made, and a pledge of the general credit of the Board of Public Instruction. In effect the decision of the court affirms the proposition that, in certain instances, a pledge of the general credit of a non-corporate entity may not be a promise to pay out of a particular fund within the meaning of the rule that such a promise destroys negotiability. Of course the promise of a legal corporate entity which restricts the obligation to the corporate assets is clearly not conditional.⁶ The difficulty seems to be in comprehending a pledge of the general credit of a non-legal entity, like a partnership or even a huge business trust, where the promise is to pay "out of" the assets of the partnership or the trust.⁷ Here the Florida Court simply ignored the difficulty which, of course, is the easiest means of reaching a good result.

The decision affirms, without contest, the generally accepted rule, not before passed upon in Florida, that N.I.L. § 25⁸ in effect makes a negotiation *as collateral security* for an antecedent debt, a negotiation for value within the meaning of the provision that requires a holder in due course to be a holder for value.⁹ Under N.I.L. § 27¹⁰ such a holder can recover on the instrument "to the extent of his lien" free and clear of personal defenses, as he would be a holder in due course only to that extent.¹¹ Under N.I.L. § 58¹² the plaintiff, in the principal case, would get only the rights of the former holder in due course, the Maryland bank.

In *Citizens and Southern National Bank v. Stepp*¹³ the defendant, in an action brought on a promissory note, unsuccessfully based his defense of failure of consideration upon the authority of *Mutual Finance Co. v. Martin*.¹⁴ In that case the court held that the finance company, indorsee

3. FLA. STAT. § 674.04 (1953).

4. BRITTON, HANDBOOK ON THE LAW OF BILLS AND NOTES 56 (1943).

5. See note 1 *supra*.

6. BRITTON, HANDBOOK ON THE LAW OF BILLS AND NOTES 58 (1943).

7. *Lorimer v. McGreevy*, 229 Mo. App. 970, 84 S.W. 2d 667 (1935).

8. FLA. STAT. § 674.23 (1953).

9. FLA. STAT. § 674.54 (1953).

10. FLA. STAT. § 674.30 (1953).

11. FLA. STAT. § 674.59 (1953).

12. FLA. STAT. § 674.60 (1953); *Wiers v. White*, 142 Fla. 628, 196 So. 206 (1940).

13. 126 F. Supp. 744 (N.D. Fla. 1954).

14. 63 So.2d 649 (Fla. 1953); See note 8 *MIAMI L.Q.* 296.

of the note, was so closely connected as to be almost identified with the payee and hence could not be considered a holder in due course. Consequently the defense of failure of consideration interposed by the defendant was good. In the principal case, the District Court for the Northern District of Florida refused to hold that the mere providing of the note and conditional sales contract forms, with an advertisement of the plaintiff in an upper corner of the latter, established such a relationship between the payee, conditional seller, and the Citizens and Southern National Bank as would prevent the latter from being a holder in due course. The case might well be of some value to attorneys for finance companies alarmed by the decision in the *Mutual Finance Co.* case. It does constitute persuasive authority to the effect that that decision should be strictly limited to the fact situation which practically identified the payee, conditional seller and the indorsee, finance company.

Statutory Changes

In the General Session of 1955, effective June 16, Section 9, Subsection 3 of the N.I.L.¹⁵ was amended in Florida by adding the following italicized portion: "The instrument is payable to bearer . . . (3) 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 or known to his employee, or other agent who supplies the name of such payee."

N.I.L. § 9(3), the unitalicized above provision, has almost uniformly been held to also apply to instruments payable to a real existing person whom the maker or drawer does not intend to receive payment.¹⁶ The usual type of case under this section is where the treasurer of a corporation, authorized to sign checks on the corporation's account, draws a check to the order of either a fictitious or real creditor of the corporation, never intending the named payee to receive payment. Instead the treasurer forges the indorsement of the named payee and cashes the check for his own benefit. On discovering the fraud the corporation brings action against the drawee bank to force it to re-credit the corporation's account with the amount of the check on the theory that the bank did not pay out according to order but under a forged indorsement. Applying the above section of the N.I.L., the court will hold that the intent of the treasurer is imputed to the corporation and hence the instrument is payable to bearer. The drawee bank, then, is justified in paying the bearer and may debit the corporation's account.¹⁷ However, a contrary result was generally reached if the fraud was committed, not by the person who actually drew

15. FLA. STAT. § 674.11 (3)(1955).

16. BRITTON, HANDBOOK ON THE LAW OF BILLS AND NOTES 700. In *Johnson v. Exchange National Bank*, 9 So.2d 810, 152 Fla. 228 (1942) the court stated "fictitiousness does not depend upon the actual existence or non-existence of the payee, but on the intention of the drawer and the payee's right to the proceeds."

17. BRITTON, *supra* at 701.

the checks, but by another agent who supplied the name of the payee. Only the intent of the person who actually drew the check, stated the courts, controlled the character of the instrument¹⁸ and the drawee bank would have to re-credit the amount paid out under the forged indorsements. Quite naturally the banks did not appreciate this state of affairs and the American Bankers Association recommended the amendment which has been heretofore adopted in a number of states. In Florida, then, as of June 16, 1955, a genuine indorsement of the payee is not necessary to a transfer of title to a negotiable instrument either where the person executing the instrument, or his agent who supplied the name, never intended the named payee to receive payment. Such an instrument will be treated just as though it were payable to bearer on its face.

18. Robertson Banking Co. v. Brasfield, 202 Ala. 167, 79 So.651(1918); U.S. Cold Storage Co. v. Central Mfg. Dist. Bank, 343 Ill. 503, 175 N.E.825 (1931).