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Bills and Notes—Holder in Due Course—Notice of Theft

Comment on Recent Decisions

BILLS AND NOTES—HOLDER IN DUE COURSE—NOTICE OF THEFT.—An attempt by the courts to construe Sections 52 and 56 of the Uniform Negotiable Instruments Law[1] so as to conform to decisions prior to its adoption has resulted in an incorrect interpretation of these sections. Thus, in *Graham v. White Phillips Company* (1935) 56 S. Ct. 21, 296 U. S. 27, the plaintiff sought to recover negotiable bonds stolen from him and sold to defendant at a fair price in the ordinary course of its business. Defendant contended it was a holder in due course, and therefore that it took free from such defects in title. Three days after the theft plaintiff had caused printed notice thereof to be sent to bond dealers, including defendant. Because of defendant's negligence in dissemination of this information to its employees, the defendant later purchased these bonds without any recollected knowledge of the theft. Before the purchase defendant made no inquiry except as to the status of the vendor. The Supreme Court of the United States, supporting defendant's contention, held that one who purchases a stolen negotiable bond in good faith before maturity, for a valuable consideration, may be a holder in due course despite the fact that notice of the theft had previously come to him, if through forgetfulness or neglilence, he did not have it in mind when purchasing.

Lord v. Wilkinson,[2] the early leading case in point, relied on other cases decided before the present codification of the law of negotiable instruments. In the *Lord Case,* the Court of Appeals held that an instruction that "the defendants once having had notice, are bound by it, although the notice may have been forgotten" was incorrect, and said that *bona fides* must be judged as of the defendant's knowledge at the time of purchase, and that while a presumption of *mala fides* arises from prior notice, such is rebuttable by proof that notice was lost, or its existence and contents forgotten.

This doctrine is approved by dicta in other cases. In *Merchants National Bank v. Detroit Trust Company*[3] the facts were identical with the *Graham Case,* except that the purchaser testified that notice was not actually received, but the court said that assuming that notice of the theft had actually been received, if the purchaser later forgot about it or carelessly mislaid it "so that it was not in their minds at the time they acquired the bonds" the purchaser's title as holder in due course would be unaffected. In

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[1] N. I. L. Sec. 52: "A holder in due course is a holder who has taken the instrument under the following conditions: . . . 4. That at the time it was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it." Sec. 56: "To constitue notice of an infirmity in the instrument or defect in the title of the person negotiating the same, the person to whom it is negotiated must have had actual knowledge of the infirmity or defect, or knowledge of such facts that his action in taking the instrument amounted to bad faith."

[2] (1870) 56 Barb. (N. Y.) 593. New York passed the N. I. L. in 1897.

[3] (1932) 258 Mich. 526, 242 N. W. 739.

Vermilye v. Adams Express Company,[4] easily distinguishable from the *Graham Case* in that the bonds were purchased after maturity, the Supreme Court held that bankers have the duty to keep a book or other form of reference in which to preserve notices when received, which must be consulted before buying overdue negotiable paper, but "by the well established rule of the cases they may purchase such paper before due without cumbering their minds or their offices with the memoranda of such notices."

In other cases are found statements that the knowledge of a defect in title will prevent a purchaser from being a holder in due course only when such knowledge was had at the time of the purchase.[5] But in these cases the courts were not thinking of notice not recollected at the time of purchase, but were distinguishing cases in which the purchaser had notice before or at the time of purchase from cases in which the purchaser received notice after the purchase.

These cases all seem to overlook the fact that the N. I. L. provides that either bad faith or notice of defects in title may prevent the purchaser from becoming a holder in due course. They say that although the purchaser may have had notice, he was not acting in bad faith because he had forgotten all about the notice, even though the failure of memory was caused by negligence of the purchaser himself; and, furthermore, that even gross negligence is not conclusive of bad faith, but only evidence thereof, and may be rebutted by a clear showing that the purchaser actually had forgotten the notice.[6] This may be true, but by the N. I. L. the purchaser's notice alone would seem to prevent him from being a holder in due course, although he may have acted in good faith.

The better view is upheld in only one case, *Northwestern National Bank v. Madison and Kedzie State Bank*,[7] which arose in the same state as the *Graham Case*, Illinois. Here a notice of theft of bonds was mailed to one who became a subsequent purchaser in good faith before maturity. The notice, it was proved, was actually received by the mailing clerk. The Court of Appeals held that if the mailing clerk of the purchaser had authority to open the mail, the clerk's knowledge was imputed to the principal whether such knowledge was remembered at the time of purchose or not. The court correctly pointed out that the N. I. L. does not qualify the rule of notice with exceptions for forgotten or overlooked notices, and that the

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[4] (1875) 21 Wall. 138, 22 L. Ed. 609.

[5] Goodman v. Simonds (1857) 20 How. 343, 15 L. Ed. 934, 941; Mechanics American National Bank v. Helmbacher (1918) 199 Mo. App. 173, 201 S. W. 383; First National Bank v. Pennington (1899) 57 Neb. 404, 77 N. W. 1084; Mills v. Hayden (1924) 128 Wash. 67, 221 Pac. 994, 34 A. L. R. 1372.

[6] Originally gross negligence was conclusively presumptive of bad faith. Crook v. Jadis (1833) 5 Barn. and Ad. 909. But today this presumption is rebuttable. Goodman v. Harvey (1835) 4 A. & E. 870; Hall v. Wilson (1853) 16 Barb. 551; Phelan v. Moss (1870) 67 Pa. 59; Mayes v. Robinson (1887) 93 Mo. 114, 5 S. W. 611; Chapman v. Rose (1874) 56 N. Y. 137, 15 Am. Rep. 401. See also 2 Daniel on Negotiable Instruments (7th ed.) sec. 892 and cases cited in notes to 8 C. J. 503.

[7] (1926) 242 Ill. App. 22.

purchaser bank, although it may have acted in good faith at the time of purchase, could not be a holder in due course because it had been given notice prior to purchase.

The Supreme Court of the United States, referring to the Illinois Appeals case, said:[8] "The State Supreme Court denied an application for certiorari without more. The argument is that this amounted to approval of the construction placed upon the statute by the Appeals Court. The point is not well taken." Although the Supreme Court of the United States may not have been bound by the *Northwestern National Bank Case* as was thus explained, it is to be regretted that the latter case was not followed as stating the better doctrine. J. C. L. '36

FEDERAL JURISDICTION—JOHNSON ACT.—The Federal District Court for the Western District of Oklahoma had taken jurisdiction of a suit by Cary, a trustee of the Consolidated Gas Company, seeking an interlocutory injunction against the enforcement of reduced rates ordered by the Oklahoma Corporation Commission, and that court, sitting with three judges, had granted the injunction prayed for.[1] On appeal, the Supreme Court of the United States *per curiam* affirmed the decision. *Held* that the District Court did not abuse its discretion; that, in view of the uncertainty produced by "diametrically opposed" decisions of the state courts[2] as to the availability of judicial review to one contesting an order of the Corporation Commission in the state courts, and in view of certain provisions of the Oklahoma constitution,[3] there was no "plain, speedy, and efficient" state remedy as contemplated by the Johnson Act[4] and hence the District Court was not deprived of its jurisdiction.[5]

The Johnson Act, passed by Congress on May 14, 1934, after prolonged debate,[6] was designed to eliminate unnecessary interference by the Federal

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[8] Graham v. White-Pillips Co., supra, l. c. 30.

[1] Cary v. Corporation Commission of Oklahoma et al. (1935) 9 F. Supp. 709.

[2] Swain v. Oklahoma Ry. Co. (1934) 168 Okl. 133, 32 P. (2nd) 51; Pioneer Telephone and Telegraph Co. v. State (1914) 40 Okl. 417, 138 P. (2nd) 1033.

[3] Article 9, Sections 20, 22, 23, Oklahoma Constitution.

[4] 48 Stat. 775, 28 U. S. C. 41 (1). "An act to amend Section 24 of the Judicial Code." (Senate Bill No. 752.) It provides: no District Court shall have jurisdiction to restrain the enforcement of an order of an administrative board or commission of a State, "where jurisdiction is based solely upon the ground of diversity of citizenship, or the repugnance of such order to the Constitution of the United States, where such order (1) affects rates chargeable by a public utility, (2) does not interfere with interstate commerce, and (3) has been made after reasonable notice and hearing, and where a plain, speedy, and efficient remedy may be had at law or in equity in the courts of such state."

[5] Corporation Commission of Oklahoma et al. v. Cary (Dec. 23, 1935) 56 S. Ct. 300.

[6] (a) In the Senate, 78 Cong. Rec. (Part 2) 1915-1920, 2014-2024, 2238-2243; (b) In the House, 78 Cong. Rec. (Part 8) 8322-8351, 8415-8433. (c)