BILLS AND NOTES

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The field of bills and notes is outstanding in only one particular this year, that is, inactivity at the appellate level. It is hoped that the reason for this is that the Negotiable Instruments Law is our state has clarified the problems that existed prior to its adoption, and not due to the inactivity of legal practice in this field. The writer is inclined to think that the outstanding reason is the clarity of the law.

A discussion of the requirements of negotiable form and good faith purchase of the due course holder was afforded by the opinions of the court of appeals and the supreme court in the case of *Citizens & Southern National Bank v. Johnson*.[1] There, the plaintiff bank, a holder of a series of notes, sued the maker. The notes were issued to an insurance agency and the payments were applied by the agency as premiums on a policy of term insurance. The insurance company did not know that its agent was accepting notes for premium payments, and had it known, it would not have permitted such arrangements. The bank, when it bought the notes from the agency knew of the practice but did not know that the insurer was uninformed of the arrangement or unwilling to consent to it. The maker defaulted on one of the notes and the insurance was cancelled for the remainder of the term, giving rise to the maker's defense of failure of consideration. The bank, however, claimed as holder in due course with rights superior to the personal defense of the maker. The court of appeals held for the maker on the ground that the bank did not possess the claimed preferred status; first, because the notes were non-negotiable and second, because the bank had knowledge of the facts constituting the agent's fraud on the insurer and the public and thus purchased the notes in "bad faith." The supreme court reversed both rulings. The contention that the notes were non-negotiable had nothing more to commend it than that they were styled "Conditional Acceptance Notes." Because there was nothing in the terms of the instruments conditioning the promise to pay, their otherwise negotiable form was easily held not to be impaired by their heading. Equally supportable was the supreme court's rejection of the argument that the bank had purchased the notes in bad faith because of notice of the

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1. 97 Ga. App. 200, 102 S.E.2d 680 (1958). *Reversed* 214 Ga. 229, 104 S.E.2d 123 (1958).

facts which constituted the fraud of the agency on the insurer. The burden on the maker to demonstrate the purchaser's bad faith is properly a heavy one. The policy of the statute of effecting greater commercial utilization of negotiable instruments by protecting its purchasers has been consistently implemented by the courts by placing on the maker a high standard of proof on the bad faith issue; this decision is entirely consistent with the act's policy and previous authority.[2]

The indorser's suretyship remedy of exoneration was the subject of discussion in the court of appeals decision in *Glasser v. Decatur Lumber Co.*[3] The remedy as codified[4] requires that the debtor (here the maker of a note) be within the state and that the notice by the surety (the indorser) to the creditor (the note's holder) demanding that the creditor proceed against the principal debtor, contain a statement as to the county in which the debtor could be found. In this case the debtor was a foreign corporation and, naturally enough, the demand on the holder contained no reference as to the county in which the debtor might be found. On both grounds, the court of appeals concluded in favor of the holder who had failed to pursue his rights against the maker, and against the indorser who claimed a defense, in that subsequent to the demand for exoneration the maker had become insolvent.

As to the requirement that the demand on the creditor state the location of the debtor by county, where it appears that the creditor is aware of the debtor's general location, the rule operates as a trap for the unwary. As applied to a corporate, as opposed to an individual, debtor, the requirement becomes even less useful because the location of a corporation for purposes of demand and service of process is relatively fixed.[5] It must be seldom that a creditor, even a holder of a negotiable note, would be uninformed of the county in which a

2. BRITTON, BILLS AND NOTES, 443 (1943).
3. 95 Ga. App. 665, 99 S.E.2d 330 (1957).
4. GA. CODE § 103-205 (1933).
5. On historical grounds it could be urged persuasively that the legislature never intended the act to apply to situations where the debtor was a corporation. This provision requiring the surety's demand to contain a statement of the debtor's county of location came into the law in 1866 when the legislature amended the exoneration statute which was originally an act passed in 1826. In 1866 the contemporary concept of a corporation's locus was strongly influenced by judicial experience with municipal, not business, corporations and their location was felt to be rooted geographically. The manifest purpose of the provision as then enacted was to safeguard the creditor as he sought to locate a mobile, and perhaps dodging, individual debtor. The courts, however, have followed the letter of the act even though it has led to absurd results. *Cf. Sackinger v. Exchange Bank*, 38 Ga. App. 667, 145 S.E. 94 (1928).

corporation debtor is located. To the degree that the surety's remedy of exoneration is desirable, the requirement is an unfortunate technicality that defeats the legitimate expectations of the parties. Strong arguments exist for judicial avoidance of the requirement's undesirable incidents, but legislative modification is probably necessary.

As to the statute's application to foreign corporations, it would appear that when a corporation is subject to suit locally, the policy sought to be served would be satisfied as sufficiently as if it were a domestic company. As well, because in traditional conception amenability of a foreign corporation to local jurisdiction rests on the fiction that the enterprise is "present" where it "does business," it would seem that compliance would be obtained with the technical requirement that the debtor be "within" the state.

The problem of the quantum of evidence that must be produced by the party in possession of an instrument to demonstrate the authority of an indorsing agent of a prior party in order to recover from the maker was discussed in the case of *Matthews v. Griffin.*[6] This was a suit by the holder against the maker of a note where the payee was a corporation and the note was indorsed for the payee by its then president in his representative capacity. The question of the authority of the president to indorse being placed in issue by the maker's pleadings, the court of appeals affirmed a non-suit because the holder had not satisfied his burden of proving the officer's authority. However, the court said that the evidence would have been sufficient if, in addition, it had been shown that the president was at the time "in active charge of the management of (the corporation's) affairs;" as well, if the corporation's seal had appeared, there would have been a "presumption of authority."

Certain principles are elementary: the maker is usually not entitled to urge the defenses of subsequent parties; however, the defense of lack of authority to indorse for a subsequent party may properly be asserted for such an indorsement is deemed to be in the nature of a forgery, the effect of which prevents title from passing to the indorsee. Thus, rights in the instrument still reside in the principal and the party in possession is not entitled to payment. Because theoretical title is in issue, it is logically appropriate that the one in possession should have the burden of proving this authority. The question of the amount of evidence that should be deemed sufficient to establish such authority is the debatable ground.

Whatever may be the standard of proof necessary to establish au-

6. 95 Ga. App. 837, 99 S.E.2d 342 (1957).

thority in the law of agency generally, two reasons point to the desirability of a lower standard of proof for the purchaser of a negotiable instrument. First, the special policy of the negotiable instruments law which seeks to increase the utility of commercial paper by facilitating the purchaser's efforts to collect the claim it represents, and second, the fact that unless the corporation principal is made a party to the suit, its rights are not determined in the litigation by the holder against the maker. The defense of lack of authority may be frivilous and much time and expense may be necessary for the holder to overcome a heavy burden of proof. If the defense is genuine, the facts constituting it can be introduced by the maker who, as compared with the holder, probably has greater accessibility to these facts anyway. It would seem then that a showing that the officer is one that usually has authority by virtue of his position with the company, that he held such position at the time of his indorsement, and that he signed in a representative capacity should be a sufficient demonstration to place the holder beyond the pale of a nonsuit.

In the case of *Credit Equipment Corporation v. Pendley*,[7] the court of appeals adopted a rule well settled elsewhere as to the rights of a payee on a renewal note.[8] The plaintiff had purchased drafts as a holder in due course which the defendant, as drawee, had accepted. Because of the inability of the defendant to pay these on maturity, the plaintiff surrendered them in return for the defendant's notes on which the plaintiff was payee. In a suit on the notes, defendant proved breach of contract by the drawer on the sales contract underlying the transaction on the drafts. The court held that, though the plaintiff is but a payee on the notes, his rights as a holder in due course on the drafts were retained and that he was entitled to recover as against the maker's personal defense. The court said that, subsequent to the negotiation of an instrument to a holder in due course, "no act or conduct of the maker short of making payment in full or being adjudicated a bankrupt can enhance, diminish, or in any wise effect the right of a holder in due course to enforce payment of the instrument free of defenses relative to its consideration."

A review of the legislative changes since the last survey issue discloses that there have been no changes in the law of negotiable instruments in Georgia. This follows the pattern of inactivity in this particular field.

7. _____Ga. App._____, 104 S.E.2d 718 (1958).
8. BRITTON, BILLS AND NOTES p. 263 (1943).