Negotiable Instruments in California

The Negotiable Instruments Act is modeled upon the English Bills of Exchange Act, which was enacted in 1882. The first state to pass the American Act was New York, which adopted it in 1895. The Act has now been enacted in all American jurisdictions, including states, territories and insular possessions, except Georgia and Porto Rico. It became law in this state July 27, 1917.

The law of California has probably been changed as much by the adoption of the Negotiable Instruments Act as has the law of any other state. But to catalogue the changes made in this state is a task I have been unable to undertake. The character of the changes, however, may be indicated by three observations of a general character, with brief comments on the same.

My first observation is this: In England and the majority of American jurisdictions, both before and since the adoption of the acts, the law merchant has been a living organism, adapting itself to the changing needs of business; and as the commercial community treated new instruments or conventional ones with additional stipulations as negotiable, the law did likewise.

The earliest form of negotiable instrument was the bill of exchange; the next, the simple promissory note; and the next, the bank note. The negotiability of the simple promissory note was settled in 1704, but it has not been until recent times that notes with collateral stipulations designed to assure payment, such as for costs of collection and attorney fees, waiver of exemption laws, confession of judgment and acceleration of maturity, have been held negotiable. The leading case in this country holding municipal bonds negotiable was decided by the United States Supreme Court in 1863. Tested by ordinary requirements, such bonds could not have been regarded as negotiable, as they were under seal. In our own time, corporate bonds containing conditions not meeting the traditional requirements of certainty, and secured by mortgage or deed of trust, have almost without dissent been held negotiable. This development of the law merchant has been the work of the courts unaided by statute.

1 Address before Los Angeles Bar Association at first monthly dinner, November 19, 1920.
2 See article by Maurice E. Harrison, The Adoption of the Negotiable Instruments Law in California, 6 California Law Review, 23.
Turning now to my second observation: In California prior to the adoption of the Negotiable Instruments Act, the law merchant had become stereotyped; and unless instruments conformed to paper that traditionally had been held negotiable, our courts held them non-negotiable.

In 1914 for the first time, our Supreme Court held corporate bonds to be non-negotiable, although as already indicated they had been held negotiable in almost all other jurisdictions. Our courts had previously held, contrary to the great weight of authority, that notes secured by mortgage were necessarily non-negotiable and likewise as to notes with stipulations accelerating maturity or for payment of attorney fees. Commenting on the state of the law in California in 1914, Mr. A. M. Kidd of the law faculty at Berkeley, in the course of a scholarly article, said:

"The principles of negotiability were taken from the few instruments in common use in the early part of the nineteenth century. These principles were prematurely and narrowly codified, thus further restricting expansion; and the judicial construction of the Code has further confined the law merchant to its ancient bounds.

"Most notes drawn by business men are, contrary to the belief of the parties, non-negotiable. A California lawyer knows only this, that certain additions to the ancient conventional forms will surely render the instrument non-negotiable. Anything else will raise a doubt."

Coming to my third observation: The purpose of the Negotiable Instruments Act was to make the law uniform throughout the country by codifying the existing law, and where the authorities were in conflict, by adopting the majority view. In order to secure uniformity, uniformity of decision as well as of enactment is necessary. This implies that the courts will disregard their earlier decisions, where the same are inconsistent with the weight of authority, and follow the decisions of other states construing the Act, or in the absence of such decisions, look to the weight of authority before the Act.

The construction of the Negotiable Instruments Act was before

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4 Kohn v. Sacramento etc. Co. (1914) 168 Cal. 1, 141 Pac. 626.
5 Meyer v. Weber (1901) 133 Cal. 681, 65 Pac. 1110.
6 Meyer v. Weber, supra, n. 5; Chase v. Whitmore (1886) 68 Cal. 545, 9 Pac. 942.
7 Law Merchant and California Decisions, 2 California Law Review, 377 at 382, 395. I acknowledge indebtedness to this able paper.
our Supreme Court in the case of Utah State National Bank v. Smith. The question in the case was whether a note made in California before the adoption of the Act here, but payable in Utah, which had the Act at the time, was rendered non-negotiable by a stipulation giving the holder an option to advance the due date for non-payment of interest. The note being payable in Utah, its negotiability was governed by the law of that state. The Utah courts had not passed upon the question whether or not stipulations for the acceleration of maturity rendered a note non-negotiable, but there were cases in California holding notes with such stipulations non-negotiable. On the other hand, under the weight of authority both before the Act and the decisions under it the note was negotiable. The trial court and the District Court of Appeal held the note to be non-negotiable, but the Supreme Court held it to be negotiable.

In the opinion of the District Court of Appeal the matter is thus summed up:

"We can see no particular difference between the Utah statute and our own upon this question; unless, indeed, it may be said that the Utah law is more exacting than ours. Basing our decision, then, on the express language of the statute of Utah; and, having in mind the rule that the law of a sister state is presumed to be the same as that of ours until the contrary appears, also following Smiley v. Watson, supra, we conclude that the note in suit here is non-negotiable under the law of Utah."

Speaking of the construction of the Negotiable Instruments Act, the Supreme Court said:

"It is generally held that it is the duty of the courts in construing this law to have in mind the purpose of securing uniformity in the law of commercial paper. [Citing cases.] As the view of the supreme court of Utah on this rule of interpretation is of special interest, we quote from the case of Felt v. Bush, supra, as follows: 'This question, therefore, it seems to us, has passed beyond the domain of judicial discussion. As we understand it, the negotiable instruments law was intended to give legislative sanction to the majority rule, to which reference has been made, and was conceived by its authors and adopted by the different state legislatures for the express purpose of harmonizing the conflicting decisions which had been rendered on the subject of negotiable instruments and

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8 (1919) 180 Cal. 1, 179 Pac. 160.
10 180 Cal. at pp. 3-4.
the rights of those interested therein whose rights were acquired before maturity. As we view it, therefore, it is our plain duty to follow the numerous decisions that have directly passed upon the negotiable instruments law, and have construed it in accordance with the majority rule. The question is one of business expediency, and not of logic or equity as applied to an individual case. [Citing cases.]

Referring to the note in suit, the court said:

"... There seems no reason for supposing that in this attempt to secure uniform legislation and decision it was intended to change a well-settled rule of the law merchant, by which in nearly every state such a note was negotiable. Construed in the light of such rule, and under the plain language of the statute, the note is clearly negotiable."

"... Our attention is called to certain decisions by the courts of California upon the subject of the negotiability of promissory notes. [Citing cases and referring to rule of California cases that stipulations accelerating maturity destroy negotiability.] ... The decisions of the courts of this state based upon its various code provisions concerning negotiable instruments, and particularly upon sections 3088 and 3093 of the Civil Code, since repealed and replaced by the uniform negotiable instrument act, obviously can be of no assistance in ascertaining the law of Utah under the uniform act."

In this connection it should be noted that the title of the Act as adopted in California states that it is "to make the law of negotiable instruments in the State of California uniform with the law of other states."

The decision in Bank v. Smith, supra, and the rule of construction there adopted, accord with the authorities elsewhere.

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11 180 Cal. at p. 6.
12 Negotiable Instruments Act, Cal. Stats. 1917, p. 1531. It is interesting to observe in connection with the case of Utah State National Bank v. Smith that the decision is broader than the language of the Negotiable Instruments Act itself. "It is worth noting that § 2(3) of the Negotiable Instruments Law validates installment instruments accelerated by default of interest, but does not specifically mention such provisions in non-installment instruments. Yet the Supreme Court of California [in Utah State National Bank v. Smith] has taken advantage of the Act to hold an instrument with such a provision negotiable, and has declared its intention to disregard decisions under the California Code which took a hostile attitude toward acceleration provisions in general." Z. Chafee, Jr., "Progress of the Law—Bills and Notes," 33 Harvard Law Review, 255, 260.
The early cases in New York followed the prior decisions of that state regardless of considerations of uniformity, but those cases have been overruled, and New York has now departed from her previous decisions that an antecedent debt does not constitute value. In Wisconsin the supreme court has overturned two of its earlier decisions, holding that stipulations accelerating maturity make a note non-negotiable. In Massachusetts and Ohio the courts have disregarded their prior decisions to the effect that placing of his name on the back of a note by a third person constitutes a contract of suretyship and not one of indorsement, and in Utah, where it had previously been held that stipulations for attorney fees destroyed negotiability, that rule has been abandoned.

The purpose of the Negotiable Instruments Act and the true rule of construction are well stated in Union Trust Company v. McGinty, where the Massachusetts court said:

"It is a matter of common knowledge that the Negotiable Instruments Act was drafted for the purpose of codifying the law upon the subject of negotiable instruments and making it uniform throughout the country through the adoption by the legislatures of the several states and by the Congress of the United States. The design was to obliterate state lines as to the law governing instrumentalities so vital to the conduct of interstate commerce as promissory notes and bills of exchange, to remove the confusion or uncertainty which might arise from conflict of statutes or judicial decisions amongst the several states, and to make plain, certain and general the controlling rules of law. Diversity was to be moulded into uniformity. This act in substance has been adopted by many states. . . . It ought to be interpreted in such a way as to give effect to the beneficent design of the legislature in passing an act for the promotion of harmony upon an important branch of the law. . . . Care should be taken to adhere as closely as possible to the obvious meaning of the act, without resort to that which had heretofore been the law of this commonwealth, unless necessary to dissolve


14 Broderick v. McGrath, supra, n. 13.
15 Thorp v. Mindeman, supra, n. 13.
16 Union Trust Co. v. McGinty, supra, n. 13; Rockfield v. Bank, supra, n. 13.
obscurity or doubt, especially in instances where there was a difference in the law in the different states."

From what has been said, it may have been gathered that in dealing with questions under the new Act, California decisions on matters that arose prior to July 27, 1917, should be read with some caution; and it should be observed that this is so, even though the former provisions of the Civil Code were practically the same as those of the Negotiable Instruments Act, as is illustrated by the opinions of the District Court of Appeal and Supreme Court in Bank v. Smith, supra. The superseded section of the Civil Code, under which it had been held in this state that stipulations accelerating maturity destroyed negotiability, was as follows:

"Section 3088. A negotiable instrument must be payable in money only and without any condition not certain of fulfillment."

The provisions of the Negotiable Instruments Act under which the contrary was held by the supreme court in the Utah Bank case are as follows:

"Section 3082. An instrument to be negotiable must conform to the following requirements:

"(2) Must contain an unconditional promise or order to pay a sum certain in money;

"(3) Must be payable on demand, or at a fixed or determinable future time."

"Section 3085. An instrument is payable at a determinable future time, within the meaning of this act, which is expressed to be payable—

"(1) At a fixed period after date or sight; or

"(2) On or before a fixed or determinable future time specified therein; or

"(3) On or at a fixed period after the occurrence of a specified event, which is certain to happen, though the time of happening be uncertain.

"An instrument payable upon a contingency is not negotiable, and the happening of the event does not cure the defect."

The break with the earlier California cases involved in bringing the law into conformity with views that have hitherto generally prevailed may perhaps be better appreciated after a glance at the history of the subject and comparison of California cases on the
negotiability of corporate bonds decided in 1914 and 1918 with a leading case on the same subject in the United States Supreme Court decided in 1863 and a leading English case decided in 1875.

The history of the law merchant has been divided into four periods. Prior to the seventeenth century, the law merchant was administered in special courts composed in part of “grave and discreet merchants.” The law administered by these courts was international in character and not part of the common law of England. The second period began with Coke’s accession to the King’s Bench in 1606 and lasted until 1756, when Lord Mansfield became Chief Justice. During this period the special courts died out and the law merchant was administered by the courts of common law but as custom and not as law. In other words, points of mercantile law were specially pleaded and went to the jury as matters of fact. The law merchant did not take juristic form until the time of Lord Mansfield. For his legal principles Lord Mansfield went for guidance to the Roman, Italian and Dutch writers and he took the customs of trade from his celebrated special juries, composed of merchants.

The draftsman of the English Bill of Exchange Act in writing of his preparation for drafting the act said:

“I read through the whole of the decisions, beginning with the first reported case in 1603. But the cases on the subject were comparatively few and unimportant until the time of Lord Mansfield. The general principles of the law were then settled, and subsequent decisions, though very numerous, have been for the most part illustrations of, or deductions from, the general propositions then laid down. On some points there was a curious dearth of authority. As regards such points I had recourse to American decisions, and to inquiry as to the usages among bankers and merchants.”

Referring to the law merchant in England since the time of Lord Mansfield, the United States Circuit Court of Appeals for the Eighth Circuit, speaking through Judge Amidon, said in Cudahy Packing Company v. State National Bank:

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20 Mercer Co. v. Hackett, supra, n. 3.
21 Goodwin v. Robarts (1875) L. R. 10 Ex. 337.
22 Scrutton, Elements of Mercantile Law, Chap. I.
24 (1904) 134 Fed. 538, 543.
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"In no branch of the law has the sound judgment of the English Courts shown itself more conspicuously than in the treatment of this subject. Whenever a new instrument varying in some of its features from the ordinary promissory note or bill of exchange has been presented for admission to the class of commercial paper, those courts have called for their guidance men from the actual business world best qualified to speak on the subject. If, from their evidence, it has appeared that the instrument in question was by the general custom and practice of the business world treated as a negotiable instrument, the court has given effect to that usage and adjudged the instrument to be subject to the same law as other negotiable paper. This was true not only in the early and formative periods of the commercial law, coming down to the age of Lord Mansfield, but has been followed with the same freedom from time to time down to the current year."

And the learned judge added:

"Those courts have never forsaken the business world to pursue a definition."

Turning now to the California cases we find them holding corporate bonds non-negotiable, although for years such instruments had been treated as negotiable by business men and bankers and had been so recognized by the courts in other jurisdictions. The reasoning of our Supreme Court in these cases is indicated in the following excerpts:

"It is the contention of appellants that the bonds, being supported by a mortgage containing conditions not certain of fulfillment and notice of the mortgage and its conditions appearing upon the bonds and coupons themselves, the bonds are not and cannot be negotiable instruments. In other words, appellants rely upon the rule announced in Meyer v. Weber, 133 Cal. 685 (65 Pac. 1110), and emphasized in later decisions, notably National Hardware Co. v. Sherwood, 165 Cal. 5 (130 Pac. 881), that a note secured by a mortgage on land, both being executed at the same time as part of one transaction, is not negotiable in law, even if negotiable in form, where the purchaser takes it with knowledge of the existence of the mortgage. It is the belief of counsel for appellants that bonds come under the same rule. Both promissory notes and bonds are listed by the code as among the six classes of negotiable instruments (Civ. Code, sec. 3095), yet a promissory note loses its negotiability when conditions not certain of fulfillment are introduced into it (Civ. Code, sec. 3088). There is no essential difference between the two kinds of instruments and we see no escape from the logic of the position of appellants that a bond, like a note, if dependent upon a mortgage, is subject to all equitable defenses against a holder with notice."
The bonds sued upon are payable not upon the general credit of the maker (Civ. Code, sec. 3088), but out of a specific fund."

"It may be that some of the reasons which led to the exception of negotiable instruments from the general rule that a seller can give no better title than he has himself would apply with equal force to instruments payable to bearer, but not negotiable in form. But this is not sufficient excuse or reason for including such instruments within the exception. The exception has been established from time immemorial and it has hitherto been confined to negotiable instruments, money and currency. It is to be presumed that this is generally understood that the owners of such property guard the same with greater care for that reason, a care which the owners of other property need not exercise. It would be unjust and inadvisable as a matter of policy to extend the exception by a judicial decision. And besides it would be judicial legislation, a thing forbidden to the courts. Moreover, in this state, the same cause would logically extend the exception to all personal property."

Contrast the point of view in the above excerpts with what the United States Supreme Court said in 1863 regarding the negotiability of municipal bonds:

"This species of bonds is a modern invention, intended to pass by manual delivery, and to have the qualities of negotiable paper; and their value depends mainly upon this character. Being issued by States and corporations they are necessarily under seal. But there is nothing immoral or contrary to good policy in making them negotiable, if the necessities of commerce require that they should be so. A mere technical dogma of the courts or the common law cannot prohibit the commercial world from inventing or using any species of security not known in the last century. Usages of trade and commerce are acknowledged by courts as part of the common law, although they may have been unknown to Bracton or Blackstone. And this malleability, to suit the necessities and usages of the mercantile and commercial world, is one of the most valuable characteristics of the common law. When a corporation covenants to pay to bearer and gives a bond with negotiable qualities, and by this means obtains funds for the accomplishment of the useful enterprises of the day, it cannot be allowed to evade the payment by parading some obsolete judicial decision that a bond, for some technical reason, cannot be made payable to bearer."

Observe also in this connection the judgment of the Court

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27 Mercer Co. v. Hackett, supra, n. 3.
of Exchequer Chamber in the leading case of Goodwin v. Robarts. That case involved the question whether a particular form of debenture script was negotiable, it being alleged that by the custom of merchants it had been so for the preceding twenty years. In opposition it was argued that no addition could be made to the law merchant by so recent a usage. The court said:

"Having given the fullest consideration to this argument, we are of the opinion that it cannot prevail. It is founded on the view that the Law Merchant is fixed and stereotyped, and incapable of being enlarged so as to meet the wants and requirements of trade in the varying circumstances of commerce. It is true that Law Merchant is sometimes spoken of as a fixed body of law forming part of the law, and, as it were, coeval with it, but as a matter of legal history this view is altogether incorrect . . . The Law Merchant is of comparatively recent origin; it is neither more or less than the usages of merchants and traders in the different departments of trade ratified by the decisions of the Courts of Law, which, upon such usages being proven before them, have adopted them as settled law with a view to the interests of trade and public convenience, the Court proceeding herein on the well-known principle of law that, with respect to transactions in the different departments of trade, Courts of Law; in giving effect to the contracts and dealings of the parties, will assume that the latter have dealt with one another on the footing of any custom or usage prevailing in that particular department."

It may perhaps be said that the provisions of our Civil Code left no course open to our courts but the one taken by them. However that may be, it cannot be insisted too strongly that if the new Act is to accomplish its purpose of making "the law of negotiable instruments in the state of California uniform with the law of other states," it must be construed on different lines than were the superseded sections of the Civil Code. That such will be the case is indicated by the opinion of the Supreme Court in the Utah Bank case. Sufficient warrant for this may be found in the necessity of securing uniformity of decision in the several states, already adverted to. And this does not involve doing violence to recognized legal principles. Thus, in dealing with the code provisions on presumptions,29 judicial notice30 and

28 Supra, n. 21.
29 People v. Stokes (1866) 71 Cal. 263, 266, 12 Pac. 71; Title Ins. & Trust Co. v. California Dev. Co. (1914) 168 Cal. 397, 401, 143 Pac. 723.
servitudes, the courts have not regarded the statutory enumerations as exclusive. And not without interest in this connection is the following from Katz v. Walkinshaw:

"The true doctrine is, that the common law by its own principles adapts itself to varying conditions, and modifies its own rules so as to serve the ends of justice under the different circumstances, a principle adopted into our code by section 3510 of the Civil Code: 'When the reason of a rule ceases, so should the rule itself.' . . . In Beardsley v. Hartford, 50 Conn. 542, the court says: 'It is a well-settled rule that the law varies with the varying reasons on which it is founded. This is expressed by the maxim: "Cessante ratione, cessat ipsa lex." This means that no law can survive the reasons on which is founded. It needs no statute to change it; it abrogates itself. If the reasons on which a law rests are overborne by opposing reasons, which, in the progress of society, gain controlling force, the old law, though still good as an abstract principle, and good in its application to some circumstances, must cease to apply or to be a controlling principle to the new circumstances."

California lawyers are aware that codification does not usually achieve the marvels claimed by Jeremy Bentham in 1817 for his "Book of Laws," when he wrote in a pamphlet distributed in this country: "Accept my services; no man of tolerably liberal education but shall, if he pleases, know more—and without effort—much more, than at the end of the longest course of the intensest effort it is possible for the ablest lawyer to know at present." But lawyers will find in the text of the Negotiable Instruments Act a fairly ready answer to the great majority of questions arising under it. Relative to the construction of the Act, attention should be called to two general observations made in 1902 by Mr. Charles L. McKeehan, in reviewing the Ames-Brewster controversy. Mr. McKeehan said:

"In the first place, no one can judge the new act fairly who does not realize that the Commissioners were attempting to codify the law. Their aim was not to reform the law of negotiable paper. It was to state accurately and concisely the existing law. Of course, here and there it was necessary to choose between two or more conflicting views. Very frequently a section changes the law in a small minority of states which had departed from the almost uniform current of

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33 Quoted in Brannan’s Negotiable Instruments Law (3d ed.) p. 475.
authority. Occasionally, though very rarely and only when there seemed to be no room for a difference of opinion, the law was deliberately changed. But the main, and almost the sole purpose of the framers of the Negotiable Instruments Law was to reproduce, as exactly as possible, that which the great weight of authority had declared to be the law.

"Second, in interpreting some sections of the act, the language used must be given not a hyper-literal meaning, but a reasonable legal meaning, derived, to some extent, from a knowledge of the cases on which the sections are based. . . . Indeed, Judge Brewster said to the American Bar Association, in discussing the new act in 1898, 'Care has been taken to preserve, as far as possible, the use of words which have had repeated construction by the courts, and have become recognized terms in the law merchant'."

This brings me to the brief consideration of several problems presented by the new Act.

As already stated, prior to the adoption of the Act, the California courts were alone in holding that merely by reason of being secured by a mortgage a note was necessarily non-negotiable. Relative to the negotiability of such paper, there has been a divergence of judicial opinion as to the test of negotiability. The better view appears to be that even though the mortgage contains provisions which if incorporated in the note would destroy its negotiability, nevertheless if the note does not expressly adopt the terms of the mortgage, the mortgage, though referred to in the note, is but ancillary to it and does not effect its negotiability. 84

Has the rule that a note secured by a mortgage is necessarily non-negotiable been superseded in California? The reason on which that rule was rested in the leading case of Meyer v. Weber, 85 and the cases following it, is that by reason of section 726 of the Code of Civil Procedure, the amount of payment is rendered uncertain. Section 726, which was not repealed by the adoption of the Negotiable Instruments Act, is as follows.

"There can be but one action for the recovery of any debt or the enforcement of any right secured by mortgage upon real property or personal property which must be in accordance with the provisions of this chapter."

That is to say, as the court pointed out in Meyer v. Weber, supra,

84 Thorp v. Mindeman, supra, n. 13; Frost v. Fisher (1899) 13 Colo. App. 322, 58 Pac. 872; Des Moines Savings Bank v. Arthur (1913) 163 Iowa 205, 143 N. W. 556; Bright v. Offield (1914) 81 Wash. 442, 143 Pac. 159.

85 Supra, n. 5.
"by a suit to foreclose and a sale of the mortgaged premises and ascertainment of the deficiency if there be any."

In view of the earlier decision that a stipulation for attorney fees rendered the amount due on a note uncertain, it was logical enough to hold in Meyer v. Weber, supra, that taking mortgage security did likewise. But now that the law of California is that collateral stipulations designed to make unconditional payment more secure do not destroy negotiability, as evidenced by provisions of the Act, and cases in other jurisdictions relative to costs of collection, exchange, waiver of exemptions, of notice and diligence in presentation and of the statute of limitations, power to confess judgment after maturity, additional interest after maturity, option of holder to extend time of payment and stipulations accelerating maturity, how can it be said that taking mortgage security renders the amount due uncertain?

The prevailing view as to requirements for certainty, which is now the law in California, is that such requirements have nothing whatever to do with matters of remedy.

In Hastings v. Thompson, the Minnesota court said:

"The reason and purpose of the rule that the sum to be paid must be certain is that the parties to the instrument may know the amount necessary to discharge it without investigating facts not within the general knowledge of every one and which may be subject to more or less uncertainty, or more or less under the influence or control of one or the other of the parties to the instrument."

Commenting with approval upon the above quotation, the United States Circuit Court of Appeals in Cudahy Packing Company v. Bank, supra, said:

"The rule requiring certainty in commercial paper was a rule of commerce before it was a rule of law. It requires commercial, not mathematical, certainty. An uncertainty which does not impair functions of negotiable instruments in the judgment of business men ought not to be regarded by the courts."

Of interest in this connection is Croft v. Bunster et al., where in referring to the negotiability of a mortgage given as security for a negotiable note, the court said in part:

"The mortgage, in such a case, would pass as an incident to the note, and might be enforced by the holder, in spite of

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37 134 Fed. 538 at 542.
38 (1859) 9 Wis. 457, 463, 464.
any existing equities between the mortgagor and mortgagee.

... The doctrine that an assignee can enforce the mortgage for no more than is justly and actually due, between the mortgagor and the mortgagee, had its origin at the time when the practice of giving mortgages as collateral security for the paper was wholly unknown; and was made to rest upon the ground that such would be the rule adopted in a suit at law, upon the covenant or bond to which the mortgage was collateral; and the assignee should stand no better in equity than at law. . . . The reason of the rule ceasing in the case of negotiable securities, transferred before maturity, and without notice, the rule also ceases. The debt is the principal thing, the mortgage the incident; the transfer of the debt carries with it the mortgage. It is the debt which gives character to the mortgage, and fixes the rights and remedies of the parties under it, and not the mortgage which determines the nature of the debt." 39

Both on principle, and in order to secure uniformity, it is submitted that the California doctrine relative to notes secured by mortgages should be abandoned.

The negotiability of a note secured by a trust deed has not thus far been presented to our Supreme Court. In 1913 the question was before the District Court of Appeal for the Second District, but that court declined to pass upon it as the point had not been argued by counsel. The court said: 40

"Counsel in arguing the case have assumed that the law applicable to a note secured by a mortgage is likewise applicable where the security given is by deed of trust. While the distinction between the two instruments is obvious, since in reducing the security the provisions of section 726 of the Code of Civil Procedure, with reference to procedure, have no application to the deed of trust, our view renders it unnecessary to enter upon the discussion of a subject not presented either by brief or oral argument."

In a case in the Superior Court, Judge (now Presiding Justice) Finlayson, in holding a note secured by deed of trust to be negotiable, said: 41

"The first question to be considered is whether the mere fact of a trust deed, regardless of its terms or provisions, will

41 Frances Investment Co. v. Stoddard, San Francisco Recorder, April 26 and 28, 1919 (Superior Court, Los Angeles County, No. B51875).
destroy the negotiability of the promissory note. . . . Here
the instrument was not a mortgage, but a trust deed. It is
ture that our supreme court, in the case of Powell v. Patison,
100 Cal. 236, held that a personal judgment on a debt secured
by trust deed cannot be had prior to the exhaustion of the
security, but the decision in that case, or the foundation for
the decision of that case, has been shaken by what is said by
the supreme court of this state, sitting en banc, in the later
case of Herbert Kraft Co. v. Bryan, 140 Cal., pp. 80 and 81,
so much so that I feel at liberty to follow my own reasoning,
which leads irresistibly to the conclusion that the mere fact that
a trust deed upon real estate was given does not prevent the
payee named in the note from bringing an action upon the note,
if it choose, without any attempt to exhaust the security, as was
pointed out by the supreme court, sitting en banc in the Her-
bert Kraft Co. case. That course can be pursued in a case
where personal property security is given, and there is no
reason why the same rule should not apply where the security
is real estate.”

In December, 1920, the District Court of Appeal for the First
District, in passing upon the negotiability of an instrument made
in California on March 15, 1918 (after the adoption of the Nego-
tiable Instruments Act), citing a case in the Supreme Court
decided in 1915 (before the adoption of the Act), holding a
note secured by a mortgage to be non-negotiable, declared:42

“For the purpose of securing payment of the same, she
made and executed a deed of trust to a certain title insurance
trust company. The note was therefore non-negotiable.”

Neither the fact of the adoption of the Negotiable Instruments
Act or the rule of decision under it were referred to by the
court. The authority of the case is obviously open to question.

A curious situation is presented in California relative to the
negotiability of corporate bonds. Following the decision in the
Kohn case, the Legislature in 1915 passed an act amending section
3088 of the Civil Code and made bearer bonds negotiable.43 That
amendment has now been repealed by the Negotiable Instruments
Act, the draftsmanship of which in this regard is somewhat
unfortunate. The English Bills of Exchange Act was carefully
confined to bills, notes and checks, as it was thought that the
remainder of the law of negotiable instruments was not suffi-

42 Quinn v. Rike et al. (1920) 33 Cal App. Dec. 709, 194 Pac. 761.
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siently well worked out to be ready for codification. But the American act declares: 44

"An instrument to be negotiable must conform to the following requirements" [enumerating five requirements, of which the second is:] "Must contain an unconditional promise or order to pay a sum certain in money."

Mr. Machen in his "Modern Law of Corporations" says: 45

"The Negotiable Instruments Law may have a disturbing effect upon the negotiability of some corporation bonds and debentures. . . .

"It is submitted that the courts of those states in which the Negotiable Instruments Law has been adopted should struggle to reach the same conclusion [as that reached by the English Courts]. The Act, if construed otherwise, would abrogate the noblest characteristic of the common law, its adaptability to new commercial conditions, and substitute a rule of Chinese stagnation. Being in derogation of the common law, the Act should be construed strictly. So, Senator Daniel is of opinion that statutory tests of negotiability should not be construed to apply to coupon bonds. Nevertheless, the sweeping language of the Negotiable Instruments Law is hard to avoid."

The highest courts in New York and Massachusetts have held in cases arising under the Act that corporate bonds are negotiable, and the same thing has been held in New Jersey concerning municipal bonds. 46 There appear to have been no cases to the contrary.

The tendency of codification is to make a Procrustean bed of the law, but this is guarded against in the Negotiable Instruments Act by the declaration that "in any case not provided for in this title, the rules of law and equity, including the law merchant, shall govern." 47 This section does not, however, control positive rules laid down in the Act and it is not to be expected that the Act will not from time to time require amendment. In two articles published in the Harvard Law Review in 1913, Mr. Joseph D. Brannan lists and discusses "Some Necessary Amendments of the Negotiable Instruments Law." 48 Among other things, these proposed amendments relate to whether the payee can be bona fide

45 2 Machen, Modern Law of Corporations, § 1740A.
purchaser, liability of accommodation maker where endorsement is had after maturity, effect of transfer by holder having knowledge of fraud and re-transfer to himself by bona fide purchaser, commencement of running of statute of limitations on bank notes and certificates of deposit, presentation of demand paper, presentation of instruments falling due on Saturday.

It is a truism that the decisions of the courts to a large extent but reflect the intelligence and industry of counsel. If the Negotiable Instruments Act is to meet the needs of business and bring the law of this state in conformity with the law elsewhere, it will depend largely upon the bar.

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