X-4880

FEDERAL RESERVE BOARD

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

June 21, 1927.

SUBJECT: Decision of the Supreme Court of Texas as to negotiability of trade acceptances.

Dear Sir:

There is enclosed herewith for your information a copy of an opinion recently rendered by the Supreme Court of Texas in the case of Lane Co. v. Crum, in which it was held that a trade acceptance is rendered non-negotiable by a statement contained thereon as follows: "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer, maturity being in conformity with the original terms of purchase". There are also enclosed for your further information on this subject copies of certain correspondence which the Board has had in this connection and a copy of a memorandum of the Board's General Counsel with regard to this question.

A similar decision has also been rendered by the Supreme Court of Florida with regard to trade acceptances bearing an endorsement of this kind.

These decisions raise serious doubt as to the negotiability of acceptances containing statements of this kind in all jurisdictions where the courts of last resort have not yet held such acceptances to be negotiable. The Federal Reserve Board considers that it is advisable to change the standard form of trade acceptance now in use by eliminating therefrom the clause giving rise to this doubt and by inserting in lieu thereof a provision to read as follows: "The transaction which gives rise to this instrument is the purchase of goods by the acceptor from the drawer."

Very truly yours,

D. R. Crissinger,
Governor.

Enclosures: To Governors & Chairmen of all F. R. Banks.

(COPY)

X-4880-a

April 28, 1927. 434

To Federal Reserve Board

From Mr. Wyatt - General Counsel

SUBJECT: Negotiability of Trade Acceptances containing statement that, "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer."

The attached correspondence relates to an opinion recently rendered by the Supreme Court of Texas in the case of Lane Company v. Crum, wherein the Court held a trade acceptance is rendered non-negotiable by the appearance thereon of the following clause:

> "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer, maturity being in conformity with the original terms of purchase."

No Federal reserve bank was a party to this suit, but the decision is of importance to all Federal reserve banks because they frequently discount or purchase trade acceptances containing similar statements. It is also of importance to the Federal Reserve Board, because the Board has heretofore ruled that such acceptances are negotiable; and, relying upon such ruling, the American Acceptance Council has prepared and furnished to its members standard forms of trade acceptances containing a similar clause.

I have delayed reporting on this matter because Mr. Stroud advised me that a motion for a re-hearing had been filed in the above entitled case; but I was advised yesterday that such motion was denied.

It appears from the attached memorandum forwarded to me by the General Counsel of the American Bankers Association that the Supreme Court of Florida has also held such acceptances to be non-negotiable.

OPINION

With all due respect to the Supreme Courts of Texas and Florida, I believe that their decisions on this question are wrong. They are contrary to a number of decisions in other States and, in my opinion, are contrary to that section of the Negotiable Instruments Act which provides in substance that an instrument is negotiable even though coupled with "a statement of the transaction which gives rise to the instrument."

I believe it is unlikely that these decisions will be followed by many of the other State Courts; but they render such acceptances non-negotiable in the States of Texas and Florida and raise serious doubts as to the negotiability of such acceptances in all States where the Courts of last resort have not yet held them to be negotiable.

It is advisable, therefore, to change the standard form of trade acceptance so as to eliminate this doubt. In my opinion, this could be accomplished by changing the standard clause to read as follows:

> "The transaction giving rise to this instrument is a purchase of goods by the acceptor from the drawer."

RECOMMENDATIONS.

It is respectfully recommended that:

1. Copies of the attached opinion, the attached correspondence and this memorandum be sent to all Federal reserve banks for their information as soon as possible; and

2. That the attached opinion of the Supreme Court of Texas be published in the Federal Reserve Bulletin with a statement suggesting that, in view of the doubts raised by these decisions, it is advisable to change the wording of the standard clause of trade acceptances as suggested above.

DISCUSSION.

Section 3 of the uniform Negotiable Instruments Act, which has been adopted in all of the States, reads in part as follows:

> "An unqualified order or promise to pay is unconditional within the meaning of this Act, though coupled with:
>
> * * * * * * * * * * * * * *
>
> "2. A statement of the transaction which gives rise to the instrument."

This means, in effect, that an instrument which is otherwise negotiable is not rendered non-negotiable by the appearance thereon of a statement of the transaction which gives rise to the instrument.

Relying upon this provision of the Negotiable Instruments Act, the Board provided in its Regulation P, issued under date of July 15, 1915, that:

> "A trade acceptance must bear on its face, or be accompanied by, evidence in form satisfactory to the Federal Reserve Bank, that it was drawn by the seller of the goods on the purchaser of such goods. Such evidence may consist of a certificate on or accompanying the acceptance, to the following effect. 'The obligation of the acceptor of this bill arises out of the purchase of goods from the drawer.' Such certificate may be accepted by the Federal Reserve Bank as sufficient evidence; provided, however, that the Federal Reserve Bank, in its discretion, may inquire into the exact nature of the transaction underlying the acceptance."

Subsequently, there was published on page 142 of the Federal Reserve Bulletin for February, 1919, an opinion of the Board's Counsel holding that a trade acceptance is negotiable although it contains a statement that, "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer as per invoices, a record of which is given in the subjoined statement."

It appears that, relying upon these rulings, the American Acceptance Council has prepared and distributed to its members a standard form of trade acceptance containing the following statement:

> "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer."

It is acceptances of this general character which have been held to be non-negotiable by the Supreme Courts of Texas and Florida.

With all due respect to the Supreme Court of Texas, I am of the opinion that its decision in the case of Lane Company v. Crum is wrong. The clear intent of the clause quoted was merely to state the transaction out of which the instrument arose, as permitted under the above quoted provision of the Negotiable Instruments Act; but the Court ruled that:

> "The obligation of the acceptor, according to the terms of said clause, arises not from the instruments themselves, but from a collateral transaction. For an instrument to be negotiable, the obligation of the maker must arise exclusively from the instrument."

Except in the case of an accommodation maker or endorser, I hardly see how the obligation of a party to any negotiable instrument could arise out of the instrument itself. Negotiable instruments are merely promises or orders to pay certain sums of money arising out of obligations resulting from business transactions and, except in the case of an accommodation maker or endorser, the obligation cannot possibly arise from the instrument itself. On the contrary, the instrument is merely evidence of a pre-existing obligation, which, in order to be negotiable, is stripped of all details of the contract or other transaction out of which it arose except a bare unconditional promise or order to pay to bearer, or to a certain person or order, a sum certain in money on demand or at a specified time. The fact that such an instrument contains on its face the statement that the obligation evidenced by the instrument arises out of some other transaction does not, in my opinion, have the effect of importing into the instrument itself the terms of the transaction out of which it arose, and the above quoted provision of the Negotiable Instruments Act is clearly intended to provide expressly that it shall not have such effect.

The Supreme Court of Texas, however, first reached the conclusion that such an instrument was non-negotiable and then endeavored to support its conclusion by arguing that the above quoted clause had the effect of making the holder of the instrument subject to all equities in favor of the acceptor resulting from the transaction out of which the instrument arose. This reasoning, however, merely "begs the question". A bona fide holder for value would not be subjected to any equities existing in favor of the acceptor, unless the instrument is non-negotiable, and the Negotiable Instruments Act provides that an instrument is not rendered non-negotiable by the appearance thereon of a statement of the transaction which gave rise to the instrument.

The Court apparently considered the above clause as more than a statement of the transaction which gave rise to the instrument, because it used the words "obligation of the acceptor."

Although I believe the decision of the Supreme Court of Texas to be wrong, it renders such instruments non-negotiable in the State of Texas and apparently the same rule has been established in Florida by a decision of the Florida Supreme Court. While it appears from the memorandum submitted by the General Counsel of the American Bankers' Association that such acceptances have been held to be negotiable in a number of other States, the Texas and Florida decisions at least raise a doubt as to the negotiability of such instruments in all States in which such instruments have not yet been held to be negotiable. It is highly desirable, that this doubt be eliminated, therefore, and I am of the opinion the best way to eliminate it is to adopt the suggestions made by Judge Paton that the clause contained in the standard form of trade acceptances be changed to read as follows:

> "The transaction which gives rise to this instrument is the purchase of goods by the acceptor from the drawer."

This would conform more closely to the language of the Negotiable Instruments Act and would eliminate the troublesome word "obligation".

In view of the importance of this decision to all the Federal reserve banks, I feel that it should be communicated promptly to them, together with copies of this memorandum and of the attached correspondence. I note that the Federal Reserve Bank of Dallas has placed this subject on the program for discussion at the Governors' Conference, and the information contained in this file would be helpful in connection with that discussion.

In view of the fact that the Board has heretofore published statements to the effect that trade acceptances containing the statement that "the obligation of the acceptor hereof arises out of the purchase of goods from the drawer" are negotiable, I believe it would be advisable to publish in the Federal Reserve Bulletin the opinion of the Texas Supreme Court and at the same time to suggest that the standard clause used in trade acceptances be changed to read as suggested above. This would prevent the public from being mislead by the statement heretofore published by the Board and would suggest a means of minimizing or eliminating altogether the harm which has been done by the decisions rendered by the courts of Texas and Florida. The only apparent disadvantage of publishing this decision in the Federal Reserve Bulletin is that it might provoke further attacks upon the negotiability of trade acceptances now outstanding which contain this clause. I believe, however, that it is only fair to advise the member banks of the doubts as to the negotiability of such acceptances and to suggest a new clause which would eliminate such doubts.

Respectfully,

(Signed) Walter Wyatt,
General Counsel.

COPY

FEDERAL RESERVE BANK
OF DALLAS

X-4880-b

March 29, 1927

Federal Reserve Board,
Washington, D. C.

Gentlemen:

Our Counsel, Messrs. Locke, Locke, Stroud & Randolph, has called our attention to a recent decision of the Supreme Court of this state in the case of Lane Co. vs. Crum et al, the language of which it would seem to us would have a very far-reaching effect. The court held that the following language in a trade acceptance, to-wit:

> "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer, maturity being in conformity with the original terms of purchase,"

renders the same non-negotiable.

The language used by the court in rendering this decision is as follows:

> "For an instrument to be negotiable, the obligation of the maker must arise exclusively from the instrument. No obligation arising from a collateral transaction can be imported into the terms of the instrument without destroying the negotiability of the instrument."

Although a motion for re-hearing is now being prepared this is law in Texas at the present time. The judgment of the Supreme Court is so at variance with the expressed opinion of some of the best legal talent of the country that I feel sure that the Board will be interested in having the action of the Texas Supreme Court called to its attention.

Yours very truly,

(Signed) Lynn P. Talley,
Governor

COPY

X-4880-c

April 28, 1927

Mr. Robert H. Bean, Executive Secretary,
American Acceptance Council,
120 Broadway,
New York City.

My dear Mr. Bean:

I received your letter of April 21st referring to a memorandum prepared by Judge Paton, General Counsel to the American Bankers Association, with reference to the negotiability of trade acceptances containing the statement that "the obligation of the acceptor hereof arises out of the purchase of goods from the drawer."

I should have replied more promptly to your letter but I have been waiting to see whether the Supreme Court of Texas would grant a re-hearing in the case of Lane Company v. Crum, wherein it held such acceptances to be non-negotiable. I am now advised that the Supreme Court of Texas denied a re-hearing in that case.

I agree with Judge Paton that the holding of the Supreme Court of Texas appears to be wrong and that it is out of line with the decisions of other States; but it certainly establishes the law in the State of Texas and at least raises doubts as to the negotiability of such acceptances in other States where the Courts have not already held such acceptances to be negotiable. In view of these facts, I am of the opinion that it would be very unwise for the American Acceptance Council to distribute any further forms of trade acceptances bearing this clause. I think it would be wise to adopt Judge Paton's suggestion and change the clause to read:

> "The transaction which gives rise to this instrument is the purchase of goods by the acceptor from the drawer."

In view of the provisions of section 3 of the uniform Negotiable Instruments Law, I believe that acceptances bearing this clause would be held to be negotiable even in Texas andFlorida.

I am taking the matter up with the Federal Reserve Board and the Board may decide to publish a new ruling suggesting the adoption of the form proposed by Judge Paton.

With all best wishes, I am

Cordially yours,

Walter Wyatt,
General Counsel.

COPY

X-4880-d

AMERICAN ACCEPTANCE COUNCIL
120 BROADWAY
NEW YORK

April 21, 1927

Hon. Walter Wyatt, General Counsel,
Federal Reserve Board,
Washington.

My Dear Mr. Wyatt:

Judge Paton, General Counsel of the American Bankers Association, has sent me a copy of a memo prepared in his office on the subject of the negotiability of Trade Acceptances which contain the clause which has been in use for the past several years, this question having been raised by a recent decision of the Supreme Court of Texas. Judge Paton has also sent me a copy of his letter to you suggesting a change in the wording of the clause under consideration so that it will completely conform to the provision of the Negotiable Instrument Act.

This is quite an important matter as we are continuing the sale and distribution of a considerable quantity of Standard Trade Acceptance forms that bear the disputed clause. If there is to be a change I am inclined to think that we should withhold further distribution and advise inquirers that a revised wording of the Trade Acceptance is under consideration.

I would appreciate very much you letting me know whether in your opinion the action of the Supreme Courts of Texas and Florida declaring that the present clause destroys the negotiability of the instrument warrants a change in the form for use in other states. I am in doubt whether the Council should give any publicity to the recent decision at this time and on this point I would like your opinion.

With kind regards, I am

Very sincerely yours,

(Signed) Robert H. Bean
Executive Secretary.

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X-4880-c

April 28, 1927

Mr. Thomas B. Paton, General Counsel,
American Bankers' Association,
110 East 42nd Street,
New York City.

Dear Judge Paton:

I have received and read with much interest your letter of April 12th and the enclosed memorandum with reference to the recent decision of the Supreme Court of Texas holding that a trade acceptance is rendered non-negotiable by the appearance of the following clause on the face thereof:

> "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer, maturity being in conformity with the original terms of purchase."

I should have replied more promptly to your letter, but I was advised that there was pending in the Supreme Court of Texas a petition for a rehearing in the case of Lane Company v. Crum and I was waiting to see whether such re-hearing would be granted. I am now advised that the court denied a re-hearing.

I agree with you that the decision of the Supreme Courts of Texas and Florida appear to be inconsistent with the provisions of the Negotiable Instruments Law and with the holdings in other States. They have the effect, however, of rendering such instruments non-negotiable in the States of Florida and Texas and these decisions at least raise a doubt as to the negotiability of such instruments in other States where the Courts have not yet specifically held such instruments to be negotiable. In view of this fact, I think it would be very wise to adopt your suggestion and change the standard clause on trade acceptances to read as follows:

> "The transaction giving rise to this instrument is the purchase of goods by the acceptor from the drawer."

Such a statement would, I believe fully serve the purposes to be served by the clause now in use and would follow so closely the language of the Negotiable Instruments Act that I believe such acceptances bearing this clause would be held to be negotiable even in the States of Texas and Florida.

I am taking the liberty of submitting your valuable suggestion to the Federal Reserve Board with the recommendation that it be adopted. Inasmuch as the Board has not yet acted upon this matter, I should appreciate it if you would kindly consider this letter as purely personal and confidential. It expresses merely my own views and not those of the Federal Reserve Board.

With all best wishes, I am,

Cordially yours,

Walter Wyatt,
General Counsel.

COPY

THOMAS B. PATON
110 East 42nd Street
New York.

X-4880-f

April 12, 1927.

Hon. Walter Wyatt, General Counsel,
Federal Reserve Board,
Washington, D. C.

Dear Mr. Wyatt:-

The Supreme Court of Texas has recently held, following the decision of the Supreme Court of Florida, a year or so ago, that the standard clause in the trade acceptance which has been prescribed, I believe, under authority of the Federal Reserve Board, namely,

> "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer"

destroys the negotiability of the instrument. I am enclosing a statement prepared in this office which explains the situation more fully.

The theory of the Texas court is that the quoted clause must be construed as meaning that the obligation of the acceptor does not arise from the instrument itself by reason of the terms of the acceptance or by reason of accepting the acceptance, but arises out of a collateral transaction, namely, the fact that the acceptor has purchased goods from the drawer and that it is necessary for the purchaser, in order to know what such obligation is, to look into the transaction itself. In other words, the purchaser is put on inquiry as to the terms and conditions of the transaction.

Of course, the phrase "obligation of the acceptor" is intended to mean the instrument as an accepted obligation, or the acceptance itself, and it seems to me a misinterpretation of its clear meaning to hold that the obligation of the acceptor arises out of his making of the acceptance rather than out of the transaction which gives rise to the instrument. It might just as well be held where A makes his note "for goods sold" that the note arises out of itself and not out of the sale of the goods.

Nevertheless, the fact remains that the Supreme Courts of two states have now held that the standard clause is not a statement of the transaction which gives rise to the instrument under the Negotiable Instruments Act but couples the trade acceptance with the transaction of sale of goods to the acceptor so as to make the obligation depend upon the terms and conditions of such transaction.

In view of this, it might be well to consider the question of

reframing the standard clause of trade acceptance somewhat along the following lines:

> "The transaction which gives rise to this instrument is the purchase of goods by the acceptor from the drawer."

This would strictly conform to the provision of the Negotiable Instruments Act that the negotiability is not affected by a statement of the transaction which gives rise to the instrument.

I am taking the liberty of sending a copy of this letter and enclosure to Mr. Robert H. Bean, Executive Secretary, American Acceptance Council, 120 Broadway, N. Y. City, for his information.

Very truly yours,

(Signed) Thomas B. Paton.

COPY

X-4380-g

Legal memorandum from Office of General Counsel of American Bankers Association.

File No. 1808 (168).
Prepared by: D. W.

Trade acceptance--Negotiability--Texas Decision--Suggested change in form of trade acceptance to render instrument negotiable even in Texas and Florida--

On March 2, 1927 the supreme court of Texas held a trade acceptance nonnegotiable. This decision followed an opinion of section A of the Commission of Appeals of Texas, Lane Company v. Crum, not yet reported. The trade acceptance contained the following phrase: (first clause) "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer, (second clause) maturity being in conformity with the original terms of purchase." The opinion is quoted below so far as it relates to the negotiability of the trade acceptance. (The underlining is used to bring out such wording of the court as is most important and striking.)

> "We agree with the conclusion reached by Associate Justice Stanford in his dissenting opinion as to the legal effect of the clause just quoted. In our opinion the clause has effect to render the trade acceptances non-negotiable under the law merchant as well as under the Negotiable Instruments Act. The obligation of the acceptor, according to the terms of said clause, arises not from the instruments themselves, but from a collateral transaction. For an instrument to be negotiable, the obligation of the maker must arise exclusively from the instrument. No obligation arising from a collateral transaction can be imported into the terms of the instrument without destroying the negotiability of the instrument. 8 Corpus Juris, pp. 113-114. A negotiable instrument has been termed 'a courier without luggage,' whose countenance is its passport. This apt metaphor does not fit these trade acceptances, for the reason they are ladened with the equipment of a wayfarer who does not travel under safe conduct. By their express terms, these instruments bear burdens whose nature must be sought for beyond the four corners of the instruments themselves. The clause in question is more than a mere 'statement of the transaction which gives rise to the instrument,' as permitted by paragraph 2, section 3 of Article 5932 of the Revised Statutes. So far from being a mere descriptive reference to the transaction which gave rise to the instrument, the clause, in definite terms, points to that transaction as the source of the acceptor's obligation to pay the amount named in the instrument. The legal effect of the clause is to render the paper subject to all the rights and equities of the parties to the collateral transaction from which the obligation of the acceptor arises. Parker vs American Exchange Bank, 27 S. W. 1072, 8 C.J. 124."

The opinion of Justice Stanford to which reference is made is found in 284 S. W. 980, at page 982. This opinion so far as it deals with the negotiability of the trade acceptance is as follows: (As in the above, quotations of the most striking phrases are underlined.)

"There are two matters that stand out very prominently by rea-

son of the above indorsement, to wit: That 'the obligation of the acceptor arises,'not by reason of the terms of the acceptance, nor by reason of the accepting of said acceptance, but out of the fact that acceptor has purchased goods from the dealer. Then, in order for Mrs. Crum to know what the obligation of the acceptor was, she would necessarily have to look beyond the acceptance, she would have to examine the supposed contract of purchase, and when she did this she would learn there was no purchase of said goods, but only a 'special agency agreement.' Again, said acceptances on their face appear to fall due in 30, 90 and 120 days, but said clause above referred to recites: 'Maturity being in conformity with the original terms of purchase.' If the original terms of purchase had provided that said acceptances matured in 6, 9, and 12 months after date, then would not such provision of the contract have been controlling? And if this be true, before Mrs. Crum could know definitely when said acceptance matured, would she not be required to examine the original terms of said supposed purchase? And when she did this, she would have learned there was no purchase of said goods, but only a 'special agency agreement,' entered into, by the termsof which, in effect, said goods were so left at the place of business of the Lane Company and the Cascade Products Company agreed to put on a special campaign and sell said goods itself, and, if it failed to sell said goods in 60 days, to take them back, etc. In fact, it is thought, under the terms of the contract, the obligation of the acceptor, as well as the maturity of all said acceptances, was dependent upon a sale of said goods by the Cascade Company or by the joint efforts of the Cascade Company and the Lane Company, and that Mrs. Crum was chargeable with notice of the provisions of said supposed contract of purchase as they affected the obligation of the acceptor, and also the maturity of said acceptances, and this being true, said acceptances were not negotiable, and that the trial court was correct in so holding and admitting appellee's evidence of fraud, etc."

It is possible to construe the phrase "maturity being in conformity with the original terms of purchase" as the particular provision that renders the instrument nonnegotiable. So far as this phrase is concerned it would seem that there could be a reasonable difference of opinion as to the effect on negotiability. While the opinion of the Commission of Appeals does not segregate its treatment of the first clause from that of the second clause such segregation is made by Justice Stanford. Consequently, with the decision that the second clause renders the instrument nonnegotiable this office has no particular quarrel, especially in view of the fact that this clause is not embodied in the recommended form for trade acceptance. However, this office is vitally concerned with the question whether the first phrase, "The obligation of the acceptor hereof arises out of a purchase of goods from the drawer?" renders the instrument nonnegotiable. This matter is considered in detail in Paton's Digest, 1926, opinion 168 and the following. Opinion 168a in the second volume is a criticism of the decision of the Florida supreme court in Citizens' State Bank of Marianna v. Carmichael, 103 So.111, holding a trade acceptance nonnegotiable. In this Florida case the opinion is a short "per curiam" opinion which does not give any extended reasoning in support of the holding; in fact it is quite difficult to ascertain from the opinion exactly what the decision of the court is. This lack of clearness weakens the effect of the Florida decision as a precedent. In addition to the decisions cited in the Digest there have been several rendered subsequent to the publication of the Digest, some of which are digested below:

Alabama: Exchange National Bank v. Abbott Nursery Co.,--Ala.-- 110 So. 809. The trade acceptance on its face contained the following: "Part payment for 5,000 Vlag automatic grove heaters and contingent upon delivery prior to October 1st, 1923." The court considered the trade acceptance nonnegotiable but this may have been entirely due to the quoted provision.

California: Fagin v. Schilling, 250 Pac. (Cal. App.) 574. The opinion does not give the form of the trade acceptances involved but it is presumed that they were in the standard form and contained the first clause quoted in the Texas decision. The court stated "that the acceptances were subject to the same defenses as if they were nonnegotiable" because the holder was not a bona fide purchaser.

Kansas: Howard v. Reiter, 243 Pac. 278; rehearing denied 244 Pac. 4. The Kansas supreme court definitely committed itself to the proposition that a trade acceptance is a negotiable instrument. It stated in support of such conclusion:

> "There is nothing new in this case, and it is controlled by the recent decisions involving similar instruments executed by other victims of the same derelict oil company. Bank v. Fowler, 113 Kan. 440, 215 P. 290; National Bank v. Greathouse, 114 Kan. 903, 220 P. 1053; State Bank v. Harford Bros., 116 Kan. 262, 226 P. 750; State Bank v. Grennan, 116 Kan. 442, 227 P. 530; Bray v. Wetzel, 118 Kan 283, 234 P. 965."

New Jersey: Asbury Park Electric Supply Co. v. McGill, 133 Atl. (Sup.) 181. The trade acceptance is quoted in the opinion which shows that it is in the regular form with the standard clause: "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer." The court seems to assume that the instrument was negotiable since it quoted Sec. 14 of the Negotiable Instruments Act, which is confined in its application to negotiable instruments. It also stated that the plaintiff was not a holder in due course. Such a statement implies that the instrument was negotiable for if it were nonnegotiable it would be immaterial whether the holder was a holder in due course or not.

North Carolina: First National Bank of Columbus v. Rochamora, 136 S. E. 259. While the form of the trade acceptance is not given in the opinion nevertheless it is assumed as above, that such acceptance was in the standard form. The court said: "The 'bill of exchange' or 'trade acceptance' was a negotiable instrument. This is conceded on the record. Sherrill v. Trust Co., 176 N. C. 591, 97 S. E. 471."

Oklahoma: American Trust Company v. Walker, 246 Pac. 833. The form of the trade acceptance is quoted in the opinion which shows that the standard form was used. The court stated that there was no evidence "that the plaintiff was not the holder of the notes (trade acceptances), in due course, for value and before maturity, and without notice of any claim of fraud." This phraseology is material only if the instrument be considered negotiable; consequently the use of the above wording shows that the court considered the instrument negotiable.

Rhode Island: Salem Trading & Finance Co. v. Peterson, 136 Atl. 445.

The form of the trade acceptance is not given but, as above, the presumption is that the standard form was employed. The court assumed that the trade acceptance was negotiable and left to the jury the question whether the owner was a holder in due course. If the instrument were a nonnegotiable one, to leave such question to the jury would have been erroneous.

The above list of digested decisions may not be exclusive. It, however, shows the opinion of the courts outside of Texas and Florida to the effect that trade acceptances in the standard form are negotiable.

It is well known that federal reserve banks discount trade acceptances. This is expressly authorized by Regulation A of the Federal Reserve Board, series of 1924. See particularly paragraph 1009 on page 859 of Paton's Digest. Furthermore federal reserve banks are authorized to purchase in the open market trade acceptances. Regulation B, series of 1924, quoted on page 861 of Paton's Digest. The standard form of trade acceptance has been approved by the Federal Reserve Board. Mathewson's "Acceptances, Trade and Banker's, "p. 21. The original Regulation P of the Federal Reserve Board as quoted on page 42 of Mathewson's book reads in part as follows:

> "Such evidence", that the trade acceptance is drawn by the seller on the purchaser of goods, "may consist of a certificate on or accompanying the acceptance to the following effect: 'The obligation of the acceptor of this bill arises out of a purchase of goods from the drawer.'"

(In passing it may be well to quote the following sentence from page 15 of this book: "A trade acceptance is a negotiable acknowledgment of the receipt of goods." This statement the author quotes with approval from the president of a large national bank.) The statements immediately above are of particular value if it is the invariable custom of federal reserve banks not to rediscount nonnegotiable paper. Such custom would seem to be inevitable for it would be decidedly improper for a federal reserve bank to take paper which would be subject to defenses which the purchaser of goods might have against the seller. That such is the custom of federal reserve banks is made absolutely certain by a ruling of the Federal Reserve Board given in the May, 1923 Federal Reserve Bulletin, p. 559. Certain extracts from this ruling follow:

> "Although negotiability is not required in specific terms by the Federal reserve act or by the board's regulations as a condition of the eligibility of notes, drafts, or bills of exchange for rediscount, it has always been contemplated by the board as one of the primary requisites of eligibility. .....The definition of a draft or bill of exchange contained in the board's Regulation A is substantially the same as the definition of abill of exchange set forth in the negotiable instruments law, thus indicating clearly that these instruments also must be negotiable in order to be eligible for rediscount.
>
> "All nonnegotiable notes, drafts, and bills of exchange, therefore, are ineligible for rediscount at Federal reserve banks."

It appears from the above that neither the Federal Reserve Board nor the federal reserve banks had prior to the decisions in Florida and Texas any doubt as

to the negotiability of a trade acceptance in the standard form. This means that the standard form was so interpreted in commercial circles as not to render the instrument nonnegotiable. It would certainly seem that the courts should put into effect this practically universal commercial interpretation of the form of the trade acceptance.

We come now to the merits of the Florida and the Texas decisions. We have already considered the Florida decision and as above noted this is criticized in Paton's Digest, opinion 168a. However, the Texas decision needs more extended treatment since the court gives reasons for its conclusions. The court states in substance that the form, "The obligation of the acceptor hereof arises out of a purchase of goods from the drawer," makes the instrument nonnegotiable since if the obligation arises from a collateral transaction that collateral transaction must be resorted to in order to ascertain the exact obligation. In the light of the Texas decision it is seen that the statement, that the obligation of the acceptor arises out of the purchase of goods, is subject to certain technical objections. It is true that the obligation of the acceptor as acceptor arises from his acceptance. Only indirectly does it arise from the purchase of goods. The obligation arising from the purchase of goods is normally a nonnegotiable obligation. An obligation arising from an acceptance is usually negotiable. The distinction between negotiable instruments and nonnegotiable instruments is very marked. The former are not subject to defenses between the original parties while the latter are. Notwithstanding the fact that the phrase used in the standard form is subject to technical objection nevertheless, as above stated, it seems that the courts should take the real meaning of the phrase and construe the instrument accordingly. It is undoubtedly true that the parties to trade acceptances from their very inception have considered that such instruments were not subject to any collateral transactions. In other words, such parties considered that the face of the instrument itself embodied the whole obligation of the acceptor irrespective of any collateral transactions between the parties. This is the test of negotiability so far as the phrase in question is concerned.

Although the Texas and Florida decisions may be erroneous (and this office considers them such) nevertheless such decisions do actually exist and if the courts in two states have so held it is not beyond the realm of possibility that the courts in some other states may follow these decisions as precedents. Under these decisions of Texas and Florida trade acceptances are nonnegotiable. (This is on the assumption that it is not the second clause in the Texas form which alone renders the instrument nonnegotiable.) Trade acceptances accepted in Texas and Florida undoubtedly circulate to a large extent throughout the other states; consequently the question is not merely a local one for the two jurisdictions mentioned.

Suggested amendment to standard form of trade acceptance.

The above discussion leads to the suggestion that it may be possible so to alter the wording of the standard form of trade acceptance that the courts of Texas and Florida as well of other jurisdictions will be compelled to hold a trade acceptance negotiable. In other words, the question is presented whether it is possible to make the case for negotiability so clear that no court can go so far wrong as to hold them nonnegotiable. Sec. 3 of the Negotiable Instruments Act reads as follows:

"An unqualified order or promise to pay is unconditional, within the meaning of this act, though coupled with:- ....(2.) A statement of the transaction which gives rise to the instrument."

It should be noted that the standard form of trade acceptance states that the obligation of the acceptor arises out of the purchase of goods while the Negotiable Instruments Act makes reference to the "Instrument" which arises out of the transaction. There is a distinction of course between an obligation and an instrument. The very words of the Negotiable Instruments Act may be incorporated in a trade acceptance by the use of the following phrase:

"The transaction giving rise to this instrument is a purchase of goods by the acceptor from the drawer."

I do not see how the above suggested form could be so misinterpreted by any court that it would hold the instrument nonnegotiable. Consequently this form is recommended as a substitute for the present form used. Other forms might be suggested. These, however, to a lesser extent embody the very wording of the Negotiable Instruments Act, and consequently would seem to be less desirable. One of these, more concise than that above quoted, is as follows:

"This instrument arises out of a purchase of goods by the acceptor from the drawer."

It should be noted that both these forms follow the Negotiable Instruments Act in making an instrument rather than an obligation arise from the transaction.

COPY X-4840

NO. 910 - 4764
COMMISSION OF APPEALS
SECTION A.

THE LANE COMPANY,	*	
	*	
	*	FROM McLENNAN COUNTY,
PLAINTIFF IN ERROR,	*	
	*	
VS	*	
	*	TENTH DISTRICT.
MRS. B. V. CRUM, ET AL,	*	
	*	
DEFENDANTS IN ERROR.	*	

On June 24, 1924, W. E. Williams, under the trade name of Cascade Products Company entered into a contract in writing with The Lane Company, with reference to the delivery by the Cascade Company to The Lane Company of a certain number of washing machines. The contract is set out in full in the majority opinion of the Court of Civil Appeals. It is unnecessary to a decision here, that we determine whether such contract constitutes a sale contract or merely an agency agreement. In September, 1924, the number of machines called for in the contract were delivered by the Cascade Company to The Lane Company, who declined to accept them but held them subject to the order of the Cascade Company.

At the time the contract above mentioned was made, and as a part of the transaction, The Lane Company accepted three trade acceptances or drafts drawn by the Cascade Company, each for the sum of $378.00, and payable respectively sixty, ninety and one hundred and twenty days after date. The form of these instruments is such as to make them negotiable instruments, unless the clause appearing in each of them, which is hereinafter stated, renders them non-negotiable in-

struments.

On October 29, 1924, The Lane Company brought this suit against W. E. Williams and Mrs. B. V. Crum to cancel these three trade acceptances on the ground that the washing machines were not as represented, and the machines were tendered to the defendants. Mrs. Crum answered by a cross-action seeking to recover on the trade acceptances, alleging that she was an innocent holder thereof in due course of trade, for value, before maturity. The cause was tried before a jury and resulted in a judgment being rendered cancelling the three trade acceptances and awarding to Mrs. Crum the washing machines. On appeal, this judgment was reversed by the Court of Civil Appeals, and judgment rendered by that court for Mrs. Crum on the trade acceptances, (284 S.W. 980)- Associate Justice Stanford dissenting.

The contention of The Lane Company is that the following clause of the trade acceptances renders same non-negotiable and therefore subject to the rights and equities of said company growing out of its said contract with the Cascade Company, to wit:

> "The obligation of the acceptor hereof arises out of the purchase of goods from the drawer, maturity being in conformity with the original terms of purchase."

We agree with the conclusion reached by Associate Justice Stanford in his dissenting opinion as to the legal effect of the clause just quoted. In our opinion the clause has effect to render the trade acceptances non-negotiable under the law merchant as well as under the Negotiable Instruments Act. The obligation of the acceptor, according to the terms of said clause, arises not from the instruments themselves,

but from a collateral transaction. For an instrument to be negotiable, the obligation of the maker must arise exclusively from the instrument. No obligation arising from a collateral transaction can be imported into the terms of the instrument without destroying the negotiability of the instrument. 8 Corpus Juris, pp. 113-114. A negotiable instrument has been termed "a courier without luggage," whose countenance is its passport. This apt metaphor does not fit these trade acceptances, for the reason they are ladened with the equipment of a wayfarer who does not travel under safe conduct. By their express terms, these instruments bear burdens whose nature must be sought for beyond the four corners of the instruments themselves. The clause in question is more than a mere "statement of the transaction which gives rise to the instrument," as permitted by paragraph 2, section 3 of Article 5932 of the Revised Statutes. So far from being a mere descriptive reference to the transaction which gave rise to the instrument, the clause, in definite terms, points to that transaction as the source of the acceptor's obligation to pay the amount named in the instrument. The legal effect of the clause is to render the paper subject to all the rights and equities of the parties to the collateral transaction from which the obligation of the acceptor arises. Parker vs American Exchange Bank, 27 S. W. 1072, 8 C. J. 124.

We recommend that the judgment of the Court of Civil Appeals reversing the judgment of the trial court and rendering judgment for

defendant in error, be reversed and that the judgment of the trial court be affirmed.

HARVEY,

Presiding Judge.

Judgment of the Court of Civil Appeals reversed, and that of the District Court affirmed, as recommended by the Commission of Appeals.

C. M. CURETON,
Chief Justice.

March 2, 1927.

FEDERAL RESERVE BOARD

456

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

X-4881

June 21, 1927.

SUBJECT: Assessment for general expenses of Federal Reserve Board, July 1 to December 31, 1927.

Dear Sir:

Confirming telegraphic advice of this date, there is enclosed herewith copy of a resolution adopted by the Federal Reserve Board at a meeting held on June 21, 1927, levying an assessment upon the several Federal reserve banks of an amount equal to one hundred three thousandths of one per cent (.00103) of the total paid-in capital stock and surplus of such banks as at close of business June 30, 1927, to defray the estimated general expenses of the Federal Reserve Board from July 1 to December 31, 1927.

Kindly deposit one-half of the amount of your assessment in the General Account, Treasurer, U. S., on your books July 1, 1927, and one-half September 1, 1927, in each instance issuing a C/D for credit of "Salaries and Expenses, Federal Reserve Board, Special Fund", assessment for general expenses, and sending a duplicate C/D to the Federal Reserve Board. Also please furnish a statement of your capital and surplus used as a basis for the assessment.

Very truly yours,

Enclosure.

Fiscal Agent.

(Sent to Chairman of each Federal reserve bank).

X-4881-a

RESOLUTION LEVYING ASSESSMENT

Whereas, under Section 10 of the Act approved December 23, 1913, and known as the Federal Reserve Act, the Federal Reserve Board is empowered to levy semi-annually upon the Federal reserve banks in proportion to their capital stock and surplus an assessment sufficient to pay its estimated expenses, including the salaries of its members, assistants, attorneys, experts and employees for the half-year succeeding the levying of such assessment, together with any deficit carried forward from the preceding half-year; and

Whereas, it appears from estimates submitted and considered that it is necessary that a fund equal to one hundred three thousandths of one per cent (.00103) of the total paid-in capital stock and surplus of the Federal reserve banks be created for the purpose hereinbefore described, exclusive of the cost of engraving and printing of Federal Reserve notes; Now, therefore,

BE IT RESOLVED, That pursuant to the authority vested in it by law, the Federal Reserve Board hereby levies an assessment upon the several Federal reserve banks of an amount equal to one hundred three thousandths of one per cent (.00103) of the total paid-in capital and surplus of such banks as of June 30, 1927, and the Fiscal Agent of the Board is hereby authorized to collect from said banks such assessment and execute, in the name of the Board, receipts for payments made. Such assessments will be collected in two installments of one-half each; the first installment to be paid on July 1, 1927, and the second half on September 1, 1927.

X-4882

FEDERAL RESERVE BOARD
STATEMENT FOR THE PRESS

For immediate release. June 22, 1927.

CONDITION OF THE ACCEPTANCE MARKET
May 19, 1927 to June 15, 1927

The supply of bills in the New York acceptance market was steady and in good volume during the four weeks ending June 15, although slightly less than during preceding weeks. The bulk of bills bought by dealers was based on cotton, silk, coffee and sugar. There was a distinct decline in demand early in the period on account of a falling off in orders for foreign account, and rates on 6 months bills were increased by some dealers but exceptionally heavy foreign buying of 90-day bills occurred toward the middle of June. Dealers' portfolios were thus reduced to moderate proportions with small offerings to the Federal reserve bank. An inadequate supply of short bills was reported from Boston and Chicago, with a surplus of 90-day bills during the first three weeks of the period.

Market rates remained unchanged, except for an advance in 6 months bills on June 8, and stood as follows at the beginning and end of the period:

Acceptance rates in the New York market

Maturity	May 19 Bid	May 19 Asked	June 15 Bid	June 15 Asked
30 days	3 5/8	3 1/2	3 5/8	3 1/2
60 "	3 3/4	3 5/8	3 3/4	3 5/8
90 "	3 3/4	3 5/8	3 3/4	3 5/8
120 "	3 7/8	3 3/4	3 7/8	3 3/4
180 "	3 7/8 - 4	3 3/4 - 3 7/8	4	3 7/8

X-4883

FEDERAL RESERVE BOARD

WASHINGTON

459

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

June 23, 1927.

SUBJECT: Code word designating
San Antonio Branch.

Dear Sir:

The Board has been advised by the Federal Reserve Bank of Dallas that its San Antonio Branch will be opened for business on Tuesday, July 5, 1927.

Accordingly, the code word "DREDGING" has been designated to indicate the San Antonio Branch of the Federal Reserve Bank of Dallas, which word should be inserted on page 76 of the Federal Reserve Telegraph Code.

Very truly yours,

E. M. McClelland,
Assistant Secretary.

TO GOVERNORS OF ALL F.R.BANKS.

FEDERAL RESERVE BOARD

460

WASHINGTON

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

X-4885

June 23, 1927.

SUBJECT: Report of the Pension Committee.

Dear Sir:

The Pension Committee submitted to the Governors' Conference held here last May a report recommending among other things that there be appropriated an additional $10,000 for the expenses of the Committee which, with the balance remaining from the original appropriation, the Committee believes will be sufficient to permit the new actuarial work recommended by it and to pay such other necessary expenses as will be incurred within one year.

The Board approves of the Federal reserve banks making the additional appropriation recommended by the Committee and has requested the Federal Reserve Bank of New York to call upon the other Federal reserve banks for their pro rata share thereof.

Very truly yours,

D. R. Crissinger,
Governor.

TO ALL GOVERNORS.

FEDERAL RESERVE BOARD

WASHINGTON

X-4886

ADDRESS OFFICIAL CORRESPONDENCE TO
THE FEDERAL RESERVE BOARD

June 23, 1927.

SUBJECT: Report of the Standing Committee on Collections.

Dear Sir:

The Federal Reserve Board has considered and approved of the action of the Governors' Conference in referring the report of the Standing Committee on Collections to all Federal reserve banks for study and comment upon the suggestions contained therein prior to the next Governors' Conference.

Very truly yours,

D. R. Crissinger,
Governor.

TO GOVERNORS OF ALL F. R. BANKS.