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Negotiability of Highway Improvement Bonds

William F. Elliott

Indianapolis Bar Association

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NEGOTIABILITY OF HIGHWAY IMPROVEMENT BONDS

Municipal bonds are usually negotiable in the fullest sense of the term. But street improvement bonds and other highway bonds are ordinarily made payable only out of a particular fund to be collected by special assessments or taxation on property within a taxing district deemed to be specifically benefited. They are not strictly municipal bonds and do not constitute an indebtedness of the city or county,¹ when payable only out of such specific fund, even though the statute authorizing them to be issued designates them as "county bonds" or "bonds of the county," or the like, and although they may be commonly referred to as municipal bonds and may, perhaps, be regarded as being a particular species or kind of municipal bond.²

It is held by the Supreme Court of Washington in a case recently reported, that municipal improvements bonds payable only out of a special assessment in a local improvement district are not negotiable under the Uniform Negotiable Instrument Act as instruments negotiable under the law merchant so as to cut off defenses against bona fide purchasers that might have been set up as between the original parties.³ The statute in question provides that an instrument to be negotiable must contain among other things, an unconditional promise or order to pay a sum certain in money, and that an unqualified order or promise to pay is unconditional though coupled with an indication of a particular fund out of which reimbursement is to be made, "but an order or promise to pay only out of a particular fund is not unconditional." Our Negotiable Instrument Act contains the same provisions,⁴ and this is in substance the rule of the law merchant.

¹ *Quill v. City of Indianapolis*, 124 Ind. 392, and cases there cited; *Town of Windfall City v. First National Bank*, 172 Ind. 679, and cases there cited; *Board of Commissioners of Jackson County v. Branaman*, 169 Ind. 80, and cases there cited; *Smith v. Board of Commissioners of Hamilton County*, 173 Ind. 364; *Brown v. Guthrie*, 185 Ind. 668; *Hull v. Board of Commissioners of La Porte County*, 195 Ind. 150; *Brown v. Board*, 70 Fed. 369; *Washington County v. Williams*, 111 Fed. 801; *City of Bainbridge v. Jester*, 157 Ga. 505, 121 S. E. 798, 33 A. L. R. 1406, 1415, and other cases there cited in note. See also *Elliott Roads and Streets*, (3rd Ed.), 478, 658, 659.

² *Forrey v. Board of Commissioners of Madison County*, 189 Ind. 257; *Thorlton v. Guirl Drainage Co.*, 184 Ind. 637, 641, 642.

³ *Manker v. American Savings Bank & Trust Co.*, 131 Wash. 430, 230, Pac. 406, 42 A. L. R. 1021.

⁴ 3 Burns' Annotated Ind. Stat. 1926, Secs. 11360, 11361, 11362.

When, therefore, such bonds are payable only out of a particular fund raised or to be raised by special assessment on the property benefited, and, as held in the cases already cited, are not obligations constituting or evidencing an indebtedness of the municipality, they are not negotiable instruments under such a statute or the law merchant. This is well settled. They are usually made payable to bearer and are negotiable in the sense of being transferable by assignment or delivery so as to best legal title in transferee and give him right to sue in his own name, but they do not have all the qualities and incidents of negotiable commercial paper under the law merchant or the Negotiable Instrument Act. Reason and authority concur in this conclusion.⁵

In the Washington case the bonds had been stolen from the owner and thereafter purchased by a bank in due course of business, and it was held that such owner and not the bank was entitled to the money collected by the city for their payment.

The Supreme Court of Indiana also has held that gravel road bonds issued under the Indiana statute, although in form bonds of the county, create no indebtedness of the county and are not negotiable paper, and that a purchaser or holder thereof is bound to take notice of the statute under which they were issued and to see to it that there were or would be assessments which he could cause to be collected.⁶

But it is provided in the Indiana Act of April 15, 1905, that all street improvement bonds issued thereunder "shall be negotiable as inland bills of exchange and be free from all defenses by any property owner or property owners."⁷ So, as to park bonds, it is provided that they shall be negotiable as inland bills of exchange.⁸ And it is also provided that "flood control bonds" issued under the Act of 1915 as amended in 1920, by cities of the third or fourth class "shall have all the qualities of negotiable paper under the law merchant."⁹

Although some of the statutes referred to were passed and in force before our Negotiable Instrument Act, yet as they are specified and relate to particular kinds of instruments, there is

⁵ *Washington County v. Williams*, 111 Fed. 801; *Northern Trust Co. v. Wilmette*, 220 Ill. 417, 77 N. E. 169, 5 Ann. Cas. 193; *Kirsch v. Brown*, 153 Ind. 257, and other cases cited in note in 42 A. L. R. 1027, *et seq.* See also *State v. Hawes*, 112 Ind. 323; *Cleveland R. Co. v. Edward C. Jones Co.*, 20 Ind. App. 97; *Stanton v. Glover*, 155 U. S. 513, 15 Sup. Ct. 186.

⁶ *Kirsch v. Brown*, 153 Ind. 247, 257.

⁷ 3 Burn's Ann. Ind. Stat. 1926, Sec. 10454. See also as to certificates issued to contractor, Sec. 10442 and Sec. 10571.

⁸ 3 Burn's Ann. Ind. Stat. 1926, Secs. 10642, 10683.

⁹ 3 Burn's Ann. Ind. Stat. 1926, Sec. 10821. But see Sec. 10776.

little, if any, doubt that they control as to such bonds. And it has been expressly held in Kentucky that street improvement bonds payable to bearer, issued under a statute containing similar provisions are negotiable instruments.¹⁰

So, when bonds are the general and unrestricted obligations of the municipality or corporate body issuing them, and are not payable solely out of a particular fund, they are not rendered non-negotiable, although a particular fund is designated or provided for their payment.¹¹

There seem to be some Indiana statutes that do not provide that such bonds as those here under consideration, payable only out of a particular fund, shall be negotiable. This appears to be true of some, or all, of the statutes authorizing so-called county bonds for construction or improvement of highways and making them payable solely out of a particular fund, and where such is the case they are not negotiable within the law merchant or Negotiable Instrument Act; but they are carefully guarded by statutory provisions, and if the statute is followed or the property owners are estopped there is practically no danger of loss so far as the validity or ultimate payment of the bonds to the party entitled thereto is concerned.¹²

WILLIAM F. ELLIOTT.

Of the Indianapolis Bar.

¹⁰ *Citizens Trust Co. v. Hays*, 167 Ky. 560, 180 S. W. 811.

¹¹ *Cleveland County v. Citizens National Bank*, 157 N. Car. 191, 72 S. E. 996. See also *Fidelity Trust Co. v. Palmer*, 22 Wash. 473, 61 Pac. 158, 79 Ann. St. 953; *Marcus v. Ofner*, 103 Wash. 478, 175 Pac. 31, note in 33 A. L. R. 1422, and first part of section 3 of Negotiable Instruments Act, 3 Burns' Ann. Ind. Stat. 1926, Sec. 11362.

¹² For instance, Sec. 8422 of 2 Burns' Ann. Ind. Stat. 1926 provides that gravel road bonds issued thereunder shall be payable out of assessments on the property benefited and not otherwise, and contains no provision making them negotiable, but the assessments are made liens on such property and the bonds can be issued only on written request of such property owners and their written agreement that they will not make any objection to any illegality or irregularity in the proceedings up to and including the letting of the contract and the issuing of such bonds, and that they will pay such assessments, with interest, as the same become due. Similar provisions also exist as to street improvement bonds. All this, however, does not protect a bona fide holder of a stolen bond that is not negotiable as commercial paper.