Indiana Law Journal

Volume 5 | Issue 7 Article 6

4-1930

# Bills and Notes-Negotiability-Essential Allegations in Answer to Fraud and Failure of Considerations

BILLS AND NOTES—NEGOTIABILITY—ESSENTIAL ALLEGATIONS IN ANSWER TO FRAUD AND FAILURE OF CONSIDERATION—Action on a promissory note. The defendant's answer admitted execution of the note and that the payee endorsed and delivered it to the plaintiff before maturity and for value.

The note contained the following statement: "This note covers deferred installments of a conditional sale contract made this day between the payee and the maker thereof." The answer alleged facts showing failure of consideration and fraud in the inducement. A demurrer to the answer was sustained and the defendant, refusing to plead over, judgment was rendered on the pleadings for the plaintiff. The defendant prosecuted this appeal contending the above statement rendered the note non-negotiable and that the court for that reason erred in sustaining the demurrer to the answer. *Held*: Judgment affirmed. (1) Provision that note covered deferred installments under conditional sale contract did not render it non-negotiable. (2) Answer failing to allege that the plaintiff, the due course holder, had knowledge that the burner for which the note was given was of no value, or that the plaintiff had knowledge of alleged fraudulent representations was demurrable. *Berry v. Brandt C. Downey Co. et al.* Appellate Court of Indiana, July 6, 1929, 167 N. E. 136.

Section 3 of the Negotiable Instrument Act (Sec. 11362, Burns' Ann. State.) provides that an unqualified promise to pay is unconditional within the meaning of the act, though coupled with "a statement of the transaction which gives rise to the instrument." In determining whether a reference in a note to an extraneous writing is "a statement of the transaction which gives rise to the instrument" or whether the reference subjects the note itself to the terms of the extraneous agreement, the court is confined to the examination of the note itself and cannot look to the provisions of the extraneous writing for assistance; it is the negotiability of the note and not of the extraneous writing which is being determined. The following statements were held not to destroy the negotiability of an otherwise negotiable instrument: "As per contract," *Waterbury-Wallace Co. v. Ivey*, 99 Misc. Rep. 260, 163 N. Y. S. 719; *Strand Amusement Co. v. Fox*, 205 Ala. 183, 87 Sou. 332, 14 A. L. R. 1121; "This note is given in accordance with a land contract of even date," *Doyle v. Considine*, 195 Ill. App. 311; "For payment under contract of even date," *Slaughter v. Bank of Bisbee*, 17 Ariz. 484, 154 Pac. 1040; "As per terms of contract," *National Bank of Newbury v. Wentworth*, 218 Mass. 30, 105 N. E. 626. In the latter case the court intimated that if the words had been "subject to the contract," the note would have been made non-negotiable. In *Hereth et al. v. Meyer*, 33 Ind. 511, decided before the adoption of the Negotiable Instruments Act, the phrase "this given for patent right," was held not to destroy the negotiability of the note. In the recent case of *Dorbecker v. Downey Co. et al.*, (1928) Ind. App., 163 N. E. 535, the note contained the identical statement involved in the instant case. In concluding that the note in question was negotiable the court said: "The said note and the said sale contract were each complete in and of themselves. There was no interdependence, and the fact that the note, by way of recitation, mentioned the sales contract, did not make said sales contract a part thereof."

Granting that the note was not rendered non-negotiable by the reference to the contract, the sustaining of the demurrer to the answer is clearly correct so far as the question of failure of consideration is concerned. "Where want of consideration is pleaded by the maker of a promissory note as a defense to the suit of an indorsee of such note, the burden is upon the defendant to prove such defense by a fair preponder-

ance of the evidence bearing on that question." *Bright Nat'l Bank of Flora v. Hartman et al.*, (Ind. App.) 109 N. E. 846, 849. Failure of consideration is no defense as against a holder in due course, and "The burden of proof that he is a holder in due course, is not put on the plaintiff, by proof of total or partial failure of consideration or want of consideration. The terms of Sec. 55, which define defective titles, do not include want or failure of consideration." *Wheat v. Goss*, 193 Ind. 558, 141 N. E. 311; *Farmers Trust Co. v. Sprowl*, 72 Ind. App. 564, 126 N. E. 81; Sections 55 and 59, Negotiable Instruments Act (1926 Burns' Ann. Stat., Secs. 11414 and 11418.)

The correctness of the conclusion that an answer alleging fraud, without alleging knowledge by the holder of the fraud is subject to demurrer is not so obvious. In *Millikan v. Security Co.*, (Ind. App.) 118 N. E. 568, the court said: ". . . Both paragraphs are bad for failure to allege that appellee (holder) had notice of these infirmities"; in accord: *Parker v. Hickman*, (Ind. App.) 111 N. E. 649. In *Lapp v. Merchants Nat'l Bank of Indianapolis*, (Ind. App.) 124 N. E. 707, the court drew a distinction between an answer failing to allege notice to the plaintiff when such an answer was given to a complaint in which the plaintiff has not set out that he was a holder in due course, and the case in which such an answer as the one in the principal case is given to a complaint which does not affirmatively allege that the plaintiff is a holder in due course. In the former case the court points out that it is necessary to allege notice; in the latter it is not necessary. The opinion in the principal case does not state whether the complaint alleged that the plaintiff was a holder in due course. The first clause of Sec. 59 of the Negotiable Instruments Act (Sec. 11418, Burns' Ann. Stat.) declares that "Every holder is deemed prima facie to be a holder in due course . . ." It would seem to follow that an allegation in the complaint of a holder that he is a due course holder would be merely surplusage and that the distinction made in the Lapp case is artificial and illogical. Indiana has consistently, both before and after the adoption of the Negotiable Instruments Act, held that "Where the evidence establishes that the title of the parties negotiating the instrument was defective, the holder claiming to be a purchaser in good faith for value and without notice must make this claim good by the greater weight of evidence." (Brannan's Negotiable Instrument Law, p. 531, citing the Indiana case of *Bright Nat'l Bank v. Hartman, supra; First National Bank v. Rupert*, 178 Ind. 669, 100 N. E. 5; *Shirk v. Neible*, 156 Ind. 66, 59 N. E. 281; *Ray v. Baker*, 165 Ind. 74, 74 N. E. 619, I Ind. L. Jour. 49. Since the adoption of the Negotiable Instruments Law the Indiana decisions have interpreted Section 59 (11418 Burns' Ann. Stat.) to mean that when fraud is shown that the holder has the burden of proving that "he or some person under whom he claims acquiring a title in due course" by a preponderance of the evidence. In *Shirk v. Neible, supra*, the court says "that if the holder of paper negotiable by the law merchant and to which the maker has exhibited a valid defense for fraud, relies upon the fact that he is a bona fide holder thereof, for value, the burden is upon him to *aver* and *prove* that he obtained such paper before maturity without notice of the defense of the maker and that he paid a valuable consideration therefor." *In Ray v. Baker et al., supra*, the de-

fendant answered fraud, and the plaintiffs' reply was a general denial. The Supreme Court said that "no question as to plaintiff's being a good-faith purchaser can be raised under the issues. If the appellant were a good-faith purchaser, before maturity, of commercial paper, the burden was on him affirmatively to *plead* and to prove the same on the trial." It would seem a logical inference from the above statements that an answer alleging fraud is not vulnerable to demurrer since under the Indiana rule the burden of proving due course holding, which includes as one element lack of knowledge of the fraud, is on the plaintiff holder, when the defendant has established the evidence of the fraud. It would seem to follow that the burden of allegation is satisfied by an answer which alleges fraud; for if the defendant in his answer must allege both the fact of fraud and the fact of the plaintiff holder's knowledge of the fraud, he is required to allege a fact which he is not required to prove. T. R. D.