Banks and Banking—Negotiable Instruments—Notes—Security—County Treasurer.

A bank which held the notes of various persons deposited such notes with the county treasurer as collateral security for county money on deposit with such bank. Thereafter and without the knowledge or consent of the county treasurer the bank renewed certain of these notes and deposited the renewal notes as collateral security for other obligations owed by the bank. The bank also collected money on some of these notes.

Held: (1.) That the original note in the hands of the county treasurer is still a valid and subsisting obligation and can be enforced by the county against the maker of the note. (2.) That the county cannot establish a trust relationship between itself and the bank so as to entitle the former to claim the money in the hands of the receiver of the bank as a trust fund.

W. M. Millis, Esq., July 6, 1925.
County Treasurer,
Columbus, Montana.

My dear Mr. Millis:

Your letter of June 17th submits the following statement of facts:

> Stillwater county had on deposit with the Stockmen's National Bank of Columbus at the time the latter closed its doors, about $60,000. It held collateral in the form of notes deposited with it by the bank in the sum of $60,000. While this collateral was in the possession of the county treasurer, and without notice to the treasurer or authorization by him, the bank made renewals of certain of these notes without calling in the original note, and

deposited the renewal note with other parties as collateral on debts owed by the bank to such parties. You desire an opinion upon the following questions:

"1. Is the original note in the hands of the treasurer or the renewal the valid exisiting obligation?

"2. If the bank collected any of the notes held by the treasurer without notifying the treasurer or calling in the notes and the proceeds are in the funds of the bank as part of its general funds or assets does that constitute a trust fund and therefore a preferred claim, and if so, what is the procedure in the case of a national bank?"

As to your first question, it is my opinion that as between the county and the maker of the note the original note is still a valid and subsisting obligation and can be enforced by the county against the maker of the note. I base this opinion upon the assumption that the note was transferred to the county before maturity as security for the obligation of the bank. If such is the case, the general agreement of authority is that the county is a holder in due course and for value. Being such holder the county is not bound by any defense which might have been asserted as between the original maker of the note and the payee thereof.

Joyce, in his work entitled: "Defenses to Commercial Paper," section 376, states the law as follows:

"A party receiving negotiable paper as collateral security is entitled to be protected as a bona fide holder to the same extent as one who becomes an absolute owner and may sue in his own name as the real party in interest."

The same rule was announced by the supreme court of Montana in Yellowstone National Bank of Billings vs. Gagnon, 19 Mont. 402, 48 Pac. 762.

"If a negotiable note has been endorsed and transferred bona fide before its maturity as collateral security for a demand short of its nominal value, payment afterwards by the maker to the payee cannot be given in evidence in an action thereon against the maker by the endorsee to reduce the amount of the judgment to the sum that is actually due to him." (Joyce, supra, section 483, citing Gowen vs. Wentworth, 17 Me. 66.)

In Daniels, on Negotiable Instruments, the author discusses the conflict of opinion among the decisions of the courts upon the foregoing question but states his conclusion as follows:

"Section 831a. It is generally conceded that the conflict of authority disclosed in the preceding question of the text has been settled in those states which have adopted the statute (referring to the uniform negotiable instruments act) so that it is the rule in those states in view of the several provisions of the statute that one who takes a note merely as collateral security for a pre-existing debt is regarded as a holder for value."

As to your second question, I am inclined to doubt whether you can, under the existing facts, establish a trust as against the money collected by the bank. The difficulty of so doing occurs by reason of the fact that the bank did not as you phrase it "collect any of the notes." Had the bank gotten possession of the original note and surrendered it to the payee without the consent of the county then I think you could probably establish a trust relationship and impress the money received by the bank with a resulting trust ex maleficio. However, the bank did not collect the note. It collected some money from certain individuals who paid the same to the bank in settlement of a note which the bank did not own and which it had no power to accept money in payment of. The county never authorized nor requested the bank to make the collection nor did it ever surrender the note. Under these circumstances I do not believe that the county can establish a trust relationship between it and the bank so as to entitle the former to claim the moneys, if any, in the hands of the receiver as trust funds.

Very truly yours,

L. A. FOOT,

Attorney General.