

# The Rights of a Holder in Due Course of a Negotiable Document of Title to Goods

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## I. INTRODUCTION

The concept of negotiability is deeply rooted in the development of trade and commerce. It ultimately strikes at the very heart of practically all business transactions since ancient times up to the present. For both a pragmatic and

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orderly purpose, the systems of commerce not only in the local setting but in a multitude of societies as well, have embraced the application of negotiability. In our area of jurisdiction, the Negotiable Instruments Law<sup>1</sup> has been the bedrock of this application. In the same light, credit transactions have played as much a part in business as these negotiable instruments, and it is here where rights and obligations of the holders of either the negotiable instrument or of documents of title to goods arise. The Warehouse Receipts Law<sup>2</sup> governs these transactions on goods, while the Code of Commerce<sup>3</sup> and the Civil Code<sup>4</sup> also apply. The abovementioned laws, in line with the purpose that negotiability provides, create particular rights to the holders of these instruments or documents of title.

Negotiable Instruments under the Negotiable Instruments Law, which took effect in the Philippines on 2 June 1911,<sup>5</sup> contain a promise or order to pay a sum certain in money while negotiable documents of title to goods<sup>6</sup> under the Civil Code which took effect on 30 June 1950, contain an undertaking to deliver to the bearer or to the order of any person named therein the goods referred to therein.

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1. The Negotiable Instruments Law [NEGOTIABLE INSTRUMENTS LAW], Act No. 2031 (1911).
  2. The Warehouse Receipts Law [WAREHOUSE RECEIPTS LAW], Act No. 2137 (1912).
  3. Code of Commerce [CODE OF COMMERCE], Title 3, §1, Part 6 (chapter on Bill of Lading) (The Code of Commerce was adopted from the Spanish Code of Commerce of 1885, which was modified by the *Comision de Codificacio de las Provincias de Ultramar* which later on resulted in our Code extended to the Philippines by royal decree (issued on 6 August 1888) of Queen Cristina of Spain, and took effect in the Philippines on 1 December 1888.).
  4. An Act to Ordain and Institute the Civil Code of the Philippines [CIVIL CODE] Republic Act No. 386 (1950).
  5. AGUEDO F. AGBAYANI, COMMENTARIES AND JURISPRUDENCE ON THE COMMERCIAL LAWS OF THE PHILIPPINES 100 (1992 ed.) [hereinafter AGBAYANI, COMMERCIAL LAWS].
  6. CIVIL CODE, art. 1636. In the preceding articles in this Title governing the sale of goods, unless the context or subject matter otherwise requires:  
    'Document of Title to Goods' includes any bill of lading, dock warrant, 'quedan,' or warehouse receipt or order for the delivery of goods, or any other document used in the ordinary course of business in the sale or transfer of goods, as proof of the possession or control of the goods, or authorizing or purporting to authorize the possessor of the document to transfer or receive, either by indorsement or by delivery, goods represented by such document.

Having been created for the same purpose, the negotiability envisioned by law affects all forms of business transactions, whether in the form of a substitute for money, as that contemplated by negotiable instruments, or as a substitute for goods, as that referred to by documents to title of goods. In order to encourage trade and commerce, coupled with convenience and uniformity, negotiability has taken commercial law to greater heights. Instead of carrying the actual money or goods, representations of which are handily made available to individuals through the use of negotiable instruments and negotiable documents of title.

The controversy springs from the interpretation of the law which pertains to two different subject matters. It is quite clear that they are substitutes to different objects, the nature of which differs as well, but what may be of ultimate relevance is the purpose they purport to serve. A negotiable instrument serves as a substitute for money while a negotiable document of title serves as a substitute for goods. The negotiable instrument and the negotiable document of title both serve the same function: to facilitate the sale of goods and the convenient conduct of trade and commerce.

This Article will examine the rights of a holder in due course of documents of title to goods under the Civil Code, the Warehouse Receipt Law and the Code of Commerce. It will be based on the applicable provisions of Philippine Law, commercial necessity, convenience, equity and historical developments in the more advanced legal system in the United States. A holder in due course of a negotiable document of title to goods in the Philippines, in the same respect, takes the negotiable document of title to goods free from all personal defenses available against the original owner or prior party similar to that of a holder in due course of a negotiable instrument, under Section 527 the Negotiable Instruments Law.

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7. NEGOTIABLE INSTRUMENTS LAW, § 52:

What constitutes a holder in due course. A holder in due course is a holder who has taken the instrument under the following conditions:

- (a) That it is complete and regular upon its face;
- (b) That he became the holder of it before it was overdue, and without notice that it had been previously dishonored, if such was the fact;
- (c) That he took it in good faith and for value;
- (d) And that at the time it was negotiated to him he had no notice of any infirmity in the instrument or defect in the title of the person negotiating it.

II. NEGOTIABILITY<sup>8</sup>A. *Assignment vis-à-vis Negotiability*

*Negotiability* always pertains to commercial transactions both in business and legal parlance. But there exists a danger of confusing it with some closely associated terms that would entail some clarification.

*Assignment* is a term often confused with negotiation which is actually dissimilar in nature and legal significance. The law of assignments is the logical starting point for the study of the law of commercial papers. The law on assignment furnishes a convenient basis for making comparison of the unique characteristics of negotiability, which explains why negotiable commercial paper – our primary concern – plays such an important part in the world of commerce.<sup>9</sup> While a negotiable instrument may be either negotiated or assigned, a non-negotiable instrument can only be assigned or transferred, not negotiated. The other valuable distinctions worth noting are:

1. Negotiation refers only to negotiable instruments, while assignment refers generally to an ordinary contract;
2. In negotiation, the transferee is a holder, while in assignment, the transferee is an assignee;
3. A holder in due course is subject only to real defenses, while an assignee is subject to both real and personal defenses;
4. A holder in due course may acquire a better title than that of a prior party, while generally an assignee merely steps into the shoes of an assignor;
5. A general indorser warrants the insolvency of prior parties, while an assignor does not warrant the insolvency of prior parties unless expressly stipulated or the insolvency is known to him;
6. An indorser is not liable unless there be presentment and notice of dishonor, while an assignor is liable even without notice of dishonor; and
7. Negotiation is governed by the Negotiable Instruments Law, while assignment is governed by Articles 1624 to 1635 of the Civil Code.<sup>10</sup>

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8. The term *negotiability* is loosely interchangeable with *negotiation* as both pertain to the same subject matter.

9. CHARLES M. WEBER, *COMMERCIAL PAPER IN A NUTSHELL* 10 (2nd ed. 1975) [hereinafter WEBER].

10. HECTOR S. DE LEON, *THE LAW OF NEGOTIABLE INSTRUMENTS WITH DOCUMENTS OF TITLE* 104 (2004 ed.) [hereinafter DE LEON, *THE LAW OF NEGOTIABLE INSTRUMENTS*].

From the enumeration above, it is evident that the transferability of an instrument that is not negotiable is governed by the law on assignments.<sup>11</sup> An understanding of the distinctions gives one a picture of how negotiation operates, not only compared to *assignment per se*, but in general, as governed by the applicable law. While transfer is present in both, the ability to take the place of money and be treated as its equivalent makes negotiation a viable trade route in commercial transactions. Assignment applies to all kinds of contracts, whether negotiable or non-negotiable, compared to the exacting nature of negotiation in its most technical legal sense, meant only for negotiable instruments and negotiable documents of title to goods.

### B. *The Two Kinds of Negotiable Instruments*

There are two kinds of negotiable instruments -- the Promissory Note and the Bill of Exchange. The promissory note being an unconditional promise in writing made by one person to another, signed by the maker, engaging to pay on demand, or at a fixed or determinable future time, a sum certain in money to order or bearer.<sup>12</sup> The bill of exchange is an unconditional order in writing addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to order or bearer.<sup>13</sup>

Simply put, a promise to pay a sum in money is a promissory note, while an order made by one person to another to pay money to a third person is demonstrative of a bill of exchange. Special variations of both kinds also exist, bank checks, considered as a special kind of bill of exchange, is the most commonly used among them. Both come to life under the context of Section 1<sup>14</sup> of the Negotiable Instruments Law which gives the formal requirements of negotiable instruments. First of all, the instrument must be

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11. WEBER, *supra* note 9.

12. NEGOTIABLE INSTRUMENTS LAW, § 184.

13. *Id.* § 126.

14. *Id.* § 1 provides:

Form of negotiable instruments. -- An instrument to be negotiable must conform to the following requirements:

- (a) It must be in writing and signed by the maker or drawer;
- (b) Must contain an unconditional promise or order to pay a sum certain in money;
- (c) Must be payable on demand or at a fixed or determinable future time;
- (d) Must be payable to order or to bearer; and
- (e) Where the instrument is addressed to a drawee, he must be named or otherwise indicated therein with reasonable certainty.

in writing. Secondly, it must be signed by the maker or drawer. Third is that the instrument must contain an unconditional promise or order to pay in a sum certain in money, payable at a fixed or determinable future time or on demand. And lastly, that the instrument must be payable to order or to bearer, the drawee therein, being named or otherwise indicated in bills or checks with reasonable certainty.

The law requires a strict compliance with this particular provision, such that non-observance of one of those enumerated requisites, would make the instrument non-negotiable or one transferable only by assignment. The law is quite clear cut on this point, consequently making it easy to distinguish what types of instruments are negotiable just by looking at its face and not beyond whatever is presented thereat. So long as it meets the requirements, the instrument is negotiable.

Two features salient to negotiable instruments are: first, its *negotiability* as earlier defined, and the other key attribute being the *accumulation of secondary contracts*, as they transfer from one hand to another. The biggest benefit in this vein is that where more hands are drawn in the transfer, the better for the holder as he can proceed against the maker and all other transferors, as primary and secondary contracts are created each time.

### C. Negotiable Documents of Title to Goods

Documents of title to goods include any bill of lading, dock warrant, *quedan*, or warehouse receipt or order for the delivery of goods or any other document used in the ordinary course of business in the sale or transfer of goods, as proof of possession or control of goods, or authorizing or purporting authorize the possessor of the document to transfer or receive, either by endorsement or delivery, goods represented by such document.<sup>15</sup> As noted by an authority on the subject:

[i]n trying to have a good grasp of documents of title, it is imperative to know its nature and functions after having examined those which describe negotiable instruments. Documents of title refer to goods and not to money. They all have this in common: that they are receipts of a bailee, or orders upon a bailee. A different name is given in popular speech to the document when it is issued by a carrier and when it is issued by a warehouseman, but in substance, the nature of the document is the same in both cases.<sup>16</sup>

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15. CIVIL CODE, art. 1636 [1].

16. DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10, at 319 (citing 2 WILLISTON ON SALES 505).

Described above are the more popular documents of title to goods, namely the bill of lading and the warehouse receipt. The former is an instrument in writing, that the carrier or his agent signs, and which describes the freight so as to identify it, stating the name of the consignor, the terms of the contract for carriage, and agreeing or directing that the freight be delivered to the order or assigns of a specified person at a specified place.<sup>17</sup> It also signifies as a written evidence of a contract for the carriage of goods and the delivery as well, sent by sea for certain freight. Equally, this applies to similar receipt and undertaking given by a carrier of the goods by land. The law on Sales in fact, as can be observed from the New Civil Code, includes *bill of lading* under *documents of title to goods*.<sup>18</sup> A warehouse receipt on the other hand is a contract or receipt for the goods deposited with a warehouseman containing the latter's undertaking to hold and deliver the said goods to a specified person, to his order, or to bearer. The *quedan* is a variation of a warehouse receipt that refers to sugar received by the warehouseman.<sup>19</sup>

The two-fold character of the bill of lading is exemplary of its character as it works both as a receipt and as a contract. It functions as a receipt for the goods being shipped, as it recites the date, and place of shipment, the description of the goods as to quantity, weight, dimensions, identification marks and condition, quality and value. And as to the transport and delivery according to the stipulations therein, it serves as a contract, naming the parties and the obligations assumed by the parties.<sup>20</sup> But in cases of a charter of an entire vessel, the bill of lading is in fact and in legal contemplation merely a receipt and a document of title, not a contract, for the contract is the charter party.<sup>21</sup> In this regard we see the bill of lading being denominated as in fact a document of title to goods. In modern times, as supported by jurisprudence, bills of lading comprehend all forms of transportation including freight tickets or bus receipts, whether by sea or land.<sup>22</sup>

The main contention of this Article, that negotiation of a negotiable document of title has substantially the same legal signification of negotiation

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17. BLACK'S LAW DICTIONARY 168 (6d ed. 1998).

18. 3 TEODORICO C. MARTIN, COMMENTARIES AND JURISPRUDENCE ON THE PHILIPPINE COMMERCIAL LAWS 91 (1989 rev. ed.) [hereinafter, MARTIN].

19. DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10, at 320.

20. Phoenix Assurance Co. Ltd v. United States Lines, 22 SCRA 675 (1968).

21. Home Insurance Co. v. American Steamship Agencies, Inc., 23 SCRA 24 (1968).

22. Interprovincial Autobus Co. v. Collector of Internal Revenue, 98 Phil. 290 (1956).

of a negotiable instrument, finds support in the Civil Code definition of a negotiable bill of lading as against a non-negotiable bill of lading; to wit:

Article 1507. A document of title in which it is stated that the goods referred to therein will be delivered to the bearer, or to the order of any person named in *such document is a negotiable document of title* [emphasis supplied].<sup>23</sup>

And since the New Civil Code provides that in all matters not regulated therein, the rights and obligations of common carriers shall be governed by the Code of Commerce and special laws, being interlinked with the said duties and obligations, the bills of lading shall be primarily regulated by the New Civil Code.<sup>24</sup> This is where it becomes patent and logical that a connection can be drawn between the two seemingly distinct subject matters, where their negotiability puts them in the same light. Being a symbol of the goods covered and serving as evidence of transfer of title and possession, a document of title also serves as a binding contract between the parties.<sup>25</sup> The critical juncture that must be considered though is when the rights of third parties are involved, where real and personal defenses can be invoked.

#### *D. Varying Views and the Development of Negotiability*

Negotiability has been further defined as that quality or attribute of a bill or note whereby it may pass from one person to another similar to money, so as to give the holder in due course the right to hold the instrument and collect the sum payable for himself free from any defect in the title of any prior parties or defenses available to them among themselves.<sup>26</sup> Rightfully so, the definition caters to the transferability of an instrument, and the rights that attach therewith, but only point out to those which take the place of money. But negotiability is an attribute that is not particular to money substitutes alone, as will be illustrated below.

Three methods of transfer have been contemplated by one notable commentator; first is by assignment, second is by operation of law, and lastly, by negotiation.<sup>27</sup> Negotiation accordingly may either be by indorsement completed by delivery or by mere delivery. The usual way of negotiation when the instrument is payable to order, is by indorsement of the holder

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23. A bill of lading in which it is stated that the goods referred to therein will be delivered to a specified person named in such bill is a non-negotiable bill of lading. *See also* CIVIL CODE, art. 1511.

24. MARTIN, *supra* note 18, at 93.

25. DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10, at 319.

26. *Id.* at 3.

27. AGBAYANI, COMMERCIAL LAWS, *supra* note 5, at 253.

completed by delivery, but where it is payable to bearer, mere delivery is adequate. Apart from the usual way of indorsement and delivery, the writer admits of other possible means of negotiation.<sup>28</sup> Further the same commentator proposes a view wherein negotiation is not confined to transfer after the delivery to the payee.<sup>29</sup> In this regard, the delivery constitutes the payee the holder thereof, and since negotiation is defined under the first sentence of Section 30<sup>30</sup> as being such transfer of an instrument as to constitute the transferee the holder thereof, such delivery to the payee is negotiation.<sup>31</sup> The same commentator classifies documents of title into two classes, namely the negotiable and the non-negotiable, further subdividing the negotiable type into two. The first is where by the terms of the document, the goods covered are to be delivered to bearer, and the second one is where the goods covered are to be delivered to the order of a specified person. The commentator then concludes that a negotiable document of title is not a negotiable instrument; therefore the provisions of the Negotiable Instruments Act are not applicable thereto. For this writer, negotiability of a document of title merely indicates that in the passage of documents of title through channels of commerce, the law regards the property which they describe as following them and gives their regular transfer by indorsement, the effect of manual delivery of things specified in them.<sup>32</sup>

Another side expresses the view that negotiable documents of title are *Quasi-negotiable* instruments. This means that they may possess some of the attributes of negotiability, but they are not negotiable instruments under the Negotiable Instruments Law, or even the Uniform Commercial Code of the United States. The reason behind this is that such documents of title do not fit neatly into the requirements of the Negotiable Instruments Law, particularly regarding negotiability, though usage and subsequent statutory enactment have accorded them attributes of negotiability. This view further holds that the distinction between the documents of title to goods and negotiable instruments is basically one of form and function. A negotiable

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28. *Id.* at 254.

29. *Id.* at 255 (citing Brannan 591, 7<sup>th</sup> ed.).

30. NEGOTIABLE INSTRUMENTS LAW, § 30. This provisions provides:

What constitutes negotiation – An instrument is negotiated when it is transferred from one person to another in such manner as to constitute the transferee the holder thereof. If payable to bearer, it is negotiated by delivery; if payable to order, it is negotiated by the indorsement of the holder completed by delivery.

31. AGBAYANI, COMMERCIAL LAWS, *supra* note 5, at 255.

32. *Id.* at 504.

instrument depends upon the draftsmanship for its negotiability, while the important thing about a document of title is the fact that the holder is entitled to the delivery of specific goods. Though the view admits that one basic attribute of negotiability -- the possibility of the purchasers acquiring some greater rights than those of his transferor -- is common to all of these instruments. Lastly, these *quasi-negotiable* instruments are in close proximity to negotiable instruments.<sup>33</sup>

Another viewpoint, which is accepted as the prevailing principle, indicates that to be negotiable, an instrument must possess certain requisites,<sup>34</sup> and even if just one requisite is missing, it is not negotiable. The requisites being: it must be in writing and signed by the maker or drawer; it must contain a promise or order which must be unconditional specifying a sum certain; must be payable on demand or determinable future time; must be payable to order or bearer; and where the instrument is addressed to a drawee, he must be named or otherwise indicated. If the instrument is negotiable, it becomes transferable by the process of negotiation and is attended by many important legal consequences.<sup>35</sup> Although non-negotiable instruments are relevant in the discussion of commercial paper, negotiable instruments remain of primary concern in the study of negotiation.<sup>36</sup>

The views presented herein are currently of wide acceptance in the field of commercial law. There seems to be a strict construction in terms of satisfying the requisites provided by law, before being qualified as negotiable. Much of the legal writers have leaned towards a stringent interpretation, but have not completely taken away the attribute of negotiability of the documents of title to goods, as can be gleaned from above. This slight window of admission, not only by one author, gives this proposal some ground to stand on, considering the constantly evolving systems of commerce that would require fine-tuning when need and equity arises.

### III. THE LAWS APPLICABLE TO NEGOTIABLE DOCUMENTS OF TITLE TO GOODS AND THE DEFENSES AVAILABLE

The nature and character of negotiable instruments and negotiable documents to title of goods are comparable in respect to the rationale behind both, *vis-à-vis* commercial transactions. But apparently, what they may share

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33. GEORGE C. THOMPSON AND GERALD P. BRADY, *NEGOTIABLE INSTRUMENTS AND SALES* 24-25 (1964) [hereinafter THOMPSON AND BRADY].

34. The requisites referred to here are those found in § 1 of the Negotiable Instruments Law.

35. WEBER, *supra* note 9, at 43.

36. *Id.* at 72.

in pedigree, start to diverge when the special laws applicable to each begin to operate. Looking at the particular laws will be illuminating in being able to distinguish one from the other.

The laws governing negotiable documents of title to goods are the following:<sup>37</sup> the Civil Code, particularly Articles 1507 to 1520 and the second paragraphs of both Article 1532 and 1535, as well as the entire Article 1749; specifically those governing negotiable documents of titles to goods under the Law on Sales; the Warehouse Receipt Law, which principally governs warehouse receipts; and the provisions on Bill of Lading under the Code of Commerce on commercial contracts for transportation and maritime commerce together with the Carriage of Goods by Sea Act.<sup>38</sup>

Legal provisions on negotiation of a negotiable document of title to goods can only be found in the Civil Code and the Warehouse Receipt Law. While the Code of Commerce also gives ample attention to the Bill of Lading, the Carriage of Goods by Sea Act on the other hand, was intended as a means to attain uniformity in the ocean bills of lading, but do not contain provisions on the negotiation of the Bill of Lading. However, they may apply therewith when allowed by lawful circumstances, for instance, when a charter party is involved, the bill of lading is treated as a document of title to goods, instead of a contract, which the charter party fulfills. In such a case, the Carriage of Goods by Sea Act and the Code of Commerce give way to the Civil Code, since the latter is primordially the governing law applicable to common carriers.

The Warehouse Receipts Law covers all warehouses, whether public or private, bonded or not. And it is also applicable to warehousemen engaged in the business of receiving commodities for storage.<sup>39</sup> However, when the receipts are not issued by the warehouseman, the Civil Code will apply. The primary purpose of the law has been held to be the following:

1. To regulate the status, rights and liabilities of the parties in a warehousing contract;
2. To protect those who, in good faith and for value, acquire negotiable warehouse receipts by negotiation;
3. To render the title to, and right of possession of property stored in warehouses, more easily convertible;

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37. DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10, at 320.

38. Carriage of Goods by Sea Act [CARRIAGE OF GOODS BY SEA ACT] Public Act No. 521, 74th US Congress, Commonwealth Act No. 65.

39. *People v. Goco* 35 O.G. 2618. See also *Phil. Tobacco Flue Curing and Redrying Corp. v. Pablo*, 66 SCRA 136 (1975).

4. To facilitate the use of warehouse receipts as documents of title; and
5. In order to accomplish these, to place a much greater responsibility on the warehouseman.<sup>40</sup>

There is really no specific definition of a warehouse receipt in the Warehouse Receipts Law.<sup>41</sup> Some definitions point to it as a written acknowledgment by a warehouseman that he has received and holds certain goods therein described, in store for the person to whom it is issued.<sup>42</sup> Another classification is that it is a simple written contract between the owner of the goods and the warehouseman, to pay the compensation for that service.<sup>43</sup> Only a warehouseman may issue warehouse receipts. Hence, receipts not issued by a warehouse man are not warehouse receipts although in the form of a warehouse receipt. Nonetheless, nothing prohibits the warehouseman from authorizing an agent or officer to validly issue a warehouse receipt.<sup>44</sup>

Apart from being a substitute of the property itself, the warehouse receipts show some semblance to a negotiable instrument in its very function and utility, and are even declared to be possessing negotiability by the Warehouse Receipts Law.<sup>45</sup>

An examination of Art 1512<sup>46</sup> of the Civil Code and the Section 40<sup>47</sup> of the Warehouse Receipt Law, would show that a Negotiable document of

40. DE LEON, COMMENTS AND CASES, *supra* note 25, at 169 (citing 93 C.J.S. 400).
41. See WAREHOUSE RECEIPTS LAW (the absence of a definition has left its determination to judicial interpretation and the commentaries of publicists).
42. *Vannet v. Reilly-Herz Automobile Co.*, 173 N.W. 466 (N.D. 1919).
43. *Hale v. Milwaukee Dock Co.*, 23 Wins. 276, 67 C.J. 463 (1878).
44. *National Bank v. Producers' Warehouse Association*, 42 Phil 609 (1922).
45. It is not a negotiable instrument within the meaning of the Negotiable Instruments Law, in the sense that a bill of exchange or promissory note is negotiable, even though the warehouse receipt act declares it negotiable. See also 11 Am. Jur. 2d 35 (citing WEBER, *supra* note 9, at 342).
46. NEW CIVIL CODE, art. 1512, which provides that
  - Art. 1512. A negotiable document of title may be negotiated:
    - (a) By the owner thereof; or
    - (b) By any person to whom the possession or custody of the document has been entrusted by the owner if, by the terms of the document the bailee issuing the document undertakes to deliver the goods to the order of the person to whom the possession or custody of the document has been entrusted, or if at the time of such entrusting the document is in such form that it may be negotiated by delivery.

title maybe negotiated by the owner thereof or by any person to whom the possession or custody of the document has been entrusted by the owner. Similarly, both under Article 1513<sup>48</sup> of the Civil Code and Section 41<sup>49</sup> of the Warehouse Receipt Law, the holder in due course acquires only such title to the goods as the person negotiating the document to him had ability to convey to a purchaser in good faith or for value.

The most relevant provisions that must not be overlooked are the first part of Article 1518<sup>50</sup> of the Civil Code and Section 47<sup>51</sup> of the Warehouse

47. WAREHOUSE RECEIPTS LAW, § 40 which provides

Sec. 40. *Who may negotiate a receipt* - A negotiable receipt may be negotiated:

- (a) By the owner thereof, or
- (b) By any person to whom the possession or custody of the receipt has been entrusted by the owner, if by the terms of the receipt, the warehouseman undertakes to deliver the goods to the order of the person to whom the possession or custody of the receipt has been entrusted, or if, at the time of such entrusting, the receipt is in such form that it may be negotiated by delivery.

48. CIVIL CODE, art. 1513 which provides

Art. 1513. A person to whom a negotiable document of title has been duly negotiated acquires thereby:

- (a) Such title to the goods as the person negotiating the document to him had or had ability to convey to a purchaser in good faith for value and also such title to the goods as the person to whose order the goods were to be delivered by the terms of the document had or had ability to convey to a purchaser in good faith for value; and
- (b) The direct obligation of the bailee issuing the document to hold possession of the goods for him according to the terms of the document as fully as if such bailee had contracted directly with him.

49. WAREHOUSE RECEIPTS LAW, § 41 which provides that:

Sec. 41. *Rights of person to whom a receipt has been negotiated* - A person to whom a negotiable receipt has been duly negotiated acquires thereby:

- (a) Such title to the goods as the person negotiating the receipt to him had or had ability to convey to a purchaser in good faith for value, and also such title to the goods as the depositor or person to whose order the goods were to be delivered by the terms of the receipt had or had ability to convey to a purchaser in good faith for value, and
- (b) The direct obligation of the warehouseman to hold possession of the goods for him according to the terms of the receipt as fully as if the warehouseman had contracted directly with him.

50. NEW CIVIL CODE, art. 1518 (The validity of the negotiation of a negotiable document of title is not impaired by the fact that the negotiation was a breach

Receipt Law, where the negotiation is held valid in the hands of a holder for value and in good faith and is *not impaired by the fact that such negotiation was a breach of duty on the part of the person making the negotiation or by the fact that the owner of the receipt was induced by fraud, mistake, or duress to entrust the possession or custody of the receipt to such person.*

More importantly, Article 1518 of the Civil Code has expanded the protection of a holder of a negotiable document of title to goods in good faith and for value by insulating the validity of negotiation of the document of title to him from defenses arising from the fact that the owner of the document was deprived of the possession of the same by loss, theft... accident or conversion.

It must be noted, however, that the protection of a holder in due course of a negotiable document of title against defenses of prior parties is limited only to loss, theft or conversion of the document itself, as distinguished from loss or theft of the goods. It is explained by an authority on the subject:

Clearly, under Section 40 and 47 of the Warehouse Receipts Law, the negotiation is invalidated by the fact that the owner of the document was deprived of its possession by loss or theft. It should be noted however that Article 1518 speaks of theft of the document itself, and not the goods covered by such document. In the latter case, it needs no argument to show that even a bona fide holder of a document issued over such goods cannot acquire title.<sup>52</sup>

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of duty on the part of the person making the negotiation, or by the fact that the owner of the document was deprived of the possession of the same, by loss, theft, fraud, accident, mistake, duress, or conversion, if the person to whom the document was negotiated or a person to whom the document was subsequently paid value thereof in good faith without notice of the breach of duty, or loss, theft, fraud, accident, mistake, duress, or conversion).

51. WAREHOUSE RECEIPTS LAW, § 47 (When negotiation not impaired by fraud, mistake or duress – The validity of the negotiation of a receipt is not impaired by the fact that such negotiation was a breach of duty on the part of the person making the negotiation or by the fact that the owner of the receipt was induced by fraud, mistake, or duress to entrust the possession or custody of the receipt to such person, if the person to whom the receipt was subsequently negotiated paid value therefore, without notice of the breach of duty or fraud, mistake, or duress.).
52. DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10, at 332; *see* JOSE C. CAMPOS JR. AND MARIA CLARA LOPEZ-CAMPOS, NOTES AND SELECTED CASES IN NEGOTIABLE INSTRUMENTS LAW 620 (3d ed. 1971).

#### IV. HOLDER IN GOOD FAITH FOR VALUE OF A NEGOTIABLE DOCUMENT OF TITLE TO GOODS AS A HOLDER IN DUE COURSE

Under the present state of the law in the Philippines, a question arises as to whether or not a holder in good faith and for value of a negotiable document of title to goods is entitled to the benefits and protection of a holder in due course of a negotiable instrument under Section 52 of the Negotiable Instruments Law. It is submitted that the answer is in the affirmative, in the sense that he is not subject to personal defenses of prior parties arising from loss, theft, fraud, accident, mistake, duress, or conversion of the document, for the following reasons:

First, the provision of Article 1518 of the Civil Code placing the holder in due course of a negotiable document of title in the same level as a holder in due course under Section 52 of the Negotiable Instrument law must prevail over articles 1512 and 1513 of the same Civil Code and Sections 41 and 47 of the Warehouse Receipt Law because Article 1518 represents a later and therefore prevailing legislative intent of the framers of the Civil Code. The intent of the lawmakers in this regard should be given due weight by making the later provision, article 1518, a qualification of the earlier provisions (Articles 1512 and 1513).

The Civil Code, although it may be considered a general law, is intended to specifically apply also to a warehouse receipt on negotiation because Section 40 of the Warehouse Receipt Law has been incorporated, reproduced and codified in what is now article 1512 of the Civil Code on negotiation of documents of titles to goods. The Civil Code specifically provides coverage of its provisions on negotiation to document of title which contains an undertaking of a carrier, warehouseman or other bailee to deliver the goods to bearer, to specified person or order.<sup>53</sup>

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53. CIVIL CODE, art. 1510 (If a document of title which contains an undertaking by a carrier, warehouseman or other bailee to deliver the goods to bearer, to a specified person or order or to the order of a specified person or which contains words of like import, has placed upon it the words "not negotiable," "non-negotiable" or the like, such document may nevertheless be negotiated by the holder and is a negotiable document of title within the meaning of this Title. But nothing in this Title contained shall be construed as limiting or defining the effect upon the obligations of the carrier, warehouseman, or other bailee issuing a document of title or placing thereon the words "not negotiable," "non-negotiable," or the like.).

The Civil Code also does not limit or prohibit its applicability to warehouse receipts under Article 18.<sup>54</sup> Instead, it specifically provides that any deficiency in the Code of Commerce or a special law shall be supplied by the provisions of the Civil Code. Thus, the provisions on loss, theft and conversion under Article 1518 of the Civil Code have supplementary application to negotiation of a negotiable warehouse receipt.

Second, a negotiable document of title to goods is as valuable as a negotiable instrument in trade and commerce because it likewise facilitates the sale and delivery of goods with ease and convenience to all the parties. The function of negotiability to facilitate trade and commerce in a convenient way is the same in both the negotiable instruments and the negotiable documents of title. If a holder in due course of a negotiable document of title to goods would be subjected to the personal defenses of prior parties, its function to facilitate sale and delivery of the goods would in fact be impaired and will not be as attractive and as convenient as when the holder is vested with the same rights of a holder in due course of a negotiable instrument free from personal defenses of prior parties.

A third reason would pertain to the intention of the Code Commission that drafted the Civil Code which was to adopt the prevailing law and practice in the United States by incorporating the amendments to the Uniform Sale Act<sup>55</sup> vesting in the holder in due course of a negotiable document of title to goods the benefits and protection of a holder in due course under Section 52 of the Negotiable Instruments Law through the adoption of Section 38 of the Uniform Sale Act into the present Article 1518 of the Civil Code. This is of immense significance, bearing in mind that the provisions of the Civil Code on documents of title are reproduced practically verbatim from the Uniform Sales Act, which is in fact, substantially enforced in numerous jurisdictions in the United States.<sup>56</sup>

Fourth, as now codified in the Uniform Commercial Code in the United States, rights acquired by a holder of a negotiable document of title in good faith and for value are not impaired even through the negotiation or any prior negotiation constituted a breach of duty or even though any person has been deprived of possession of the document by misrepresentation, fraud, accident, mistake, duress, loss, theft or conversion,

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54. WAREHOUSE RECEIPTS LAW, § 18 ("In matters which are governed by the Code of Commerce and special laws their deficiencies shall be supplied by the provisions of this Code.").

55. The Uniform Sales Act of 1906 (1906).

56. DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10, at 320.

or even though a previous sale or other transfer of the goods or document has been made to a third person.<sup>57</sup>

And lastly, Article 1518 must be harmonized with Articles 1512 and 1513 which both seem to convey that the right of a transferee in good faith for value of a document of title is only that of an assignee under the law on contract who cannot have a better right to the document than what the assignor had the ability to convey. Article 1518 is clear that the holder in good faith and for value takes the document free from defenses of prior parties arising from the fact that the owner of the document was deprived of the possession of the same by loss, theft, fraud, accident, mistake, duress or conversion. These laws, falling under the same title, cannot be taken to contradict each other, and harmonization would be just and equitable to whomever would choose to avail of them, concurrent to the interpretation given to the Uniform Commercial Code.<sup>58</sup>

#### V. CONCLUSION

Observing the prevailing principles and jurisprudence, it can be induced that one of the more compelling reasons why documents of title were taken out of the ambit of the Negotiable Instruments Law is because it does not fall squarely under the requisites provided for in Section 1, all else being virtually the same. No law in this regard prohibits its application, and in fact some provisions are very similar, if not identical. This has led some writers not to discount its negotiable character completely. After keen observation, though some writers prefer a strict construction of the law, there are others who have made the admission of its proximity to negotiable instruments even labeling them as *quasi-negotiable*, or one of *limited negotiability*, in any case, not stripping it of its negotiable character completely.

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57. Uniform Commercial Code [UCC] § 7-502 [2].

58. Construction of the Uniform Commercial Code to Promote its Purposes and Policies: Applicability of Supplemental Principles of Law § 1-103.

(a) The Uniform Commercial Code must be liberally construed and applied to promote its underlying purposes and policies, which are: (1) to simplify, clarify, and modernize the law governing commercial transactions; (2) to permit the continued expansion of commercial practices through custom, usage, and *agreement* of the parties; and (3) to make uniform the law among the various jurisdictions.

(b) Unless displaced by the particular provisions of the Uniform Commercial Code, the principles of law and equity, including the law merchant and the law relative to capacity to *contract*, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, and other validating or invalidating cause supplement its provisions

Concurrently, where the meaning is doubtful, the courts have adopted the policy of resolving in favor of the negotiability of the instrument. The purpose is to encourage the free circulation of the negotiable papers because of the admittedly indispensable function that they perform in commercial business transactions in any given country and the world at large.<sup>59</sup>

The view of the authors is that negotiable instruments and the negotiable documents of title to goods have the same functions. The negotiable instrument serves as a substitute for money under its feature of negotiability which allows it to pass freely from hand to hand in commercial markets and to take the place of money in commercial transactions. Similarly, a negotiable document of title to goods serves as a substitute for the goods and its negotiable characteristic allows the goods referred to therein to be sold transferred and delivered through negotiation of the document of title to the goods.

The negotiability of a document of title has the same concept and significance as that of a negotiable instrument. A holder of a negotiable document of title to goods in good faith and for value without any notice of the defect in title of his transferor acquires a better title to the goods than what the transferor had,<sup>60</sup> even if the holder took the negotiable document from a thief, as long as the original bailor-depositor of the goods was the owner thereof or had apparent authority from the owner to deposit or deliver the goods to the bailor-warehouseman.<sup>61</sup>

Ultimately, a fair interpretation of the law would entail going back to its very purpose. We should go back to the very root of why and how the idea of a commercial paper evolved:

The policy of the law in the commercial context is aimed at achieving seven goals: uniformity, conformity to common expectations, individual autonomy, individual and group responsibility, equality through reversible situations, facility of commerce, and justice.<sup>62</sup>

Given several views and the critical purpose of negotiability, a harmonious construction towards more equitable rights for holders of documents of title to goods deserves prime consideration.

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59. DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10, at 5.

60. DE LEON, COMMENTS AND CASES, *supra* note 25.

61. See CIVIL CODE, art. 1513. and DE LEON, THE LAW OF NEGOTIABLE INSTRUMENTS, *supra* note 10.

62. THOMPSON AND BRADY, *supra* note 33.