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THE THEORY OF FIELD WAREHOUSING

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The pledging of personal property by giving exclusive possession of that property to the pledgee either by actual or constructive delivery, has since earliest times been recognized as a safe and convenient method of securing a debt.[1] In the majority of cases in which the validity of a pledge has been questioned in a court, the inquiry has always been directed to the factual question of whether or not the possession of the pledged article has changed from the control of the pledgor to that of the pledgee.[2] If sufficient change of possession has been proved, the pledge is valid.[3]

It has always been a difficult problem to find a security device acceptable to both the banker and merchant when the latter wishes to obtain a substantial loan and give as security heavy and miscellaneous articles of a shifting stock of goods. A chattel mortgage covering the whole stock is a possible solution but is usually avoided by those in a position to loan money because of the difficulty of proper description, the restrictions imposed by the required accounting provisions and the statutory necessity of recording.[4] This type of personal property cannot be readily pledged in the usual manner because the cost and inconvenience of changing possession is prohibitive. The courts have, however, held valid pledges of this type of property when the pledgee leased from the pledgor a portion of his plant or warehouse into which was put the property to be pledged, the pledgee maintaining exclusive and absolute possession by placing an agent in charge of the leased premises.[5] A further requirement necessary is that signs be posted or the pledged goods marked in such a manner that the pledgee's interest clearly appears to third parties.

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[1]Casey v. Cavaroc, 96 U. S. 467, 24 L. Ed. 779 (1877).

[2]Ackerson v. Babcock, 132 Wash. 435, 232 Pac. 335 (1925).

[3]Lippman v. Ross, 130 Wash. 319, 226 Pac. 1017 (1924).

[4]Kerr, *Chattel Mortgages on Shifting Stocks of Goods in Washington* (1936) 11 WASH. L. REV. 199.

[5]Kentucky Furnace Co., as trustee, v. Nat'l Bank of Paducah, 75 S. W. 848 (1903) (pig iron); American Pig Iron Storage Warrant Co. v. German, 28 So. 603 (pig iron); Ward v. First Nat'l Bank of Ironton, 202 Fed. 609 (C. C. A. 6, 1913) (lumber); Proctor v. Shotwell, 79 S. W. 728 (Mo. 1904) (grain); Lippman v. Ross, 130 Wash. 319, 226 Pac. 1017 (1924) (merchandise); Manufacturers & Traders Bank v. Gilman, 7 F. (2d) 94 (C. C. A. 1) (engine parts). Cases in which the court has held the attempted pledge invalid because of insufficient change of possession: Geilfuss v. Corrigan, 70 N. W. 306 (Wis. 1897) (pig iron); Sequeira v. Collins, 95 Pac. 876 (Calif. 1908) (bricks); In re Spanish-American Cork Products Co., 2 F. (2d) 203 (C. C. A. 4, 1924) (cork); In re Pittman, 275 Fed. 681 (N. Car. 1921) (store fixtures); In re Millbourne Mills Co., 172 Fed. 177 (C. C. A. 3, 1909) (wheat, flour).

A moment's thought on the mechanics of this manner of obtaining security, together with the realization that in nine cases out of ten the pledgee is a bank, will force upon the reader the fact that this type of pledge is awkward and cumbersome to the pledgee and unsuited to the business requirements of the pledgor. In order to make effective this type of pledge the pledgee must constantly to be on the alert to guard against any disregard for the rules set up to insure a legal change of possession, and if he takes many pledges of this type he must add to his staff of employees a sufficient number of trusted men to act as his agent in possession on the premises of the pledgor. This transaction is not wholly satisfactory to the pledgor because in order to sell all or part of the pledged property and thus reduce his debt, permission must be obtained from the pledgee and often the resulting delay causes the pledgor's customer to go elsewhere.

The system of "field storage warehousing" has been developed to provide a simple but safe means whereby the owner, manufacturer, producer or extractor can obtain credit on goods which cannot be readily moved or mortgaged. Field storage warehousing is fundamentally the same transaction as the pledge discussed above, except that now a bona fide warehouse company takes the place of the pledgee's agent and the pledgee has constructive possession of the goods by virtue of a warehouse receipt instead of actual possession as in an ordinary pledge.

Warehouse companies specializing in "field storage warehousing" have developed this security device to such a degree of perfection that the holder of these receipts can rest assured that his loan is legally protected by the field warehouse receipts issued and deposited with him.[6]

The field warehouse is established on the premises of the customer usually through the rental of space from that customer by an independent warehouseman. This warehouse space is put under lock and key, with a custodian in charge who is paid by and responsible to the warehouseman. Adequate signs are posted informing the public that the warehouse company now occupies the premises. Into this warehouse the customer places the com-

[6]Philadelphia Warehouse Co. v. Winchester, 156 Fed. 600 (Dela. 1907): "The system of 'field storage' under which the warehouse company largely, if not wholly, conducts its business, has much to commend it, if care be taken not to mislead the public. It is both convenient and economical. It is promotive of the welfare of manufacturing and commercial industries. It avoids all necessity for unreasonably moving from place to place heavy and bulky material. Sound industrial policy requiries that when conducted with reasonable safeguards for the public, it should be encouraged, and not discountenanced." Equitable Trust Co. v. A. C. White Lbr. Co., 41 F. (2d) 60 (Idaho 1930); In re Taylor Log & Lumber Co., 41 F. (2d) 249 (Wash. 1925).

modities upon which he wishes to raise money, thus establishing an effective bailment. Warehouse receipts are issued by the warehouse company for the goods stored, and these in turn are then used as collateral just as are warehouse receipts issued by other public warehouse companies.[7]

Assuming that the warehouse receipts are in proper form,[8] that they have been effectively negotiated,[9] and that they have been issued by a bona fide warehouse company; that is, one storing goods for profit,[10] and not by a subsidiary warehouse company; that is, one owned by and doing business only for the borrower,[11] then the one question of importance which must be considered in determining the validity of these receipts is whether or not there has been sufficient change of possession from the owner of the goods to the warehouse company to constitute a bailment. The same change of possession is necessary as that which must be present in order to create a valid pledge, and the same rules for determining whether or not there has been a sufficient change of possession apply.

The Supreme Court of the United States has in two leading cases[12] recognized the validity of field storage warehousing and has by these two cases shown what will and what will not be considered a sufficient change of possession to validate this type of warehouse receipt.[13]

In the *Wilson* case[14] a wholesale leather dealer, prior to bankruptcy, walled off part of his basement and leased it at a nominal rental to a warehouse company. He there stored part of his stock so that it was not visible to third parties entering his store. The warehouse company alone had access to this basement storeroom. On the outside door of the storeroom the warehouse company posted signs to the effect that it occupied the premises and had

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[7]*A Better Look at Field Warehousing* by Arthur Van Vlissingen, Jr., in Vol. 20, No. 14, p. 14, THE BURROUGHS CLEARING HOUSE.

[8]REM. REV. STAT. §§ 3588-89 (Uniform Warehouse Receipts Act).

[9]REM. REV. STAT. §§ 3623-26 (Uniform Warehouse Receipts Act).

[10]REM. REV. STAT. § 3644 (Uniform Warehouse Receipts Act).

[11]Citizens Nat'l Bank v. Willing, 109 Wash. 464, 186 Pac. 1072.

[12]Union Trust Co. v. Wilson, 198 U. S. 530, 49 L. Ed. 1154; 25 Sup. Ct. 766 (1905); Security Warehousing Co. v. Hand, 206 U. S. 415, 51 L. Ed. 1117; 27 Sup. Ct. 720 (1907).

[13]Pattison v. Dale, 196 Fed. 5 (C. C. A. 6, 1912): "The cases of (citing *Wilson* case and *Hand* case) furnish illustration of what conditions will, and what will not, be regarded as sufficient to exclude the owner from control of goods capable of delivery, which he owns and desires to pledge. In both cases, the place of storage was part of the structure of the pledgor. In the first case, the facts justified the conclusion that a change of possession was wrought; but the facts of the second case induced the court to characterize the scheme as a 'mere pretense, a sham'."

[14]Union Trust Co. v. Wilson, 198 U. S. 530, 49 L. Ed. 1154, 25 Sup. Ct. 766 (1905).

possession of the goods within. The warehouse company charged the dealer storage and issued to him certificates or receipts for the goods. The dealer pledged these receipts at the bank as collateral. The dealer's trustee in bankruptcy claimed the warehouse receipts were invalid because the warehouse company had not obtained sufficient possession of the goods. The court held that the warehouse receipts were valid and their hypothecation with the bank constituted a lawful pledge of the leather they represented.

The following quotation from the opinion gives the court's answer to the attack of creditors:

> "It is true that the evident motive of Flanders was to get his goods represented by a document for convenience of pledging rather than to get them stored, and the method and amount of compensation show it. But that was a lawful motive and did not invalidate his acts if otherwise sufficient. He could get the goods by producing the receipt and paying the charges, of course, but there is no hint that the company did not insist upon its control. It is suggested that the goods gave credit to the owner. But, in answer to this, it is enough to say that the goods were not visible to any one entering the shop. They could be surmised only by going to the basement, where signs gave notice of the company's possession and probably could be seen only if the company unlocked the doors."

In the *Hand* case[15] it was claimed that the same situation was present as in the *Wilson* case, but the court held the receipts invalid, first, because of a Wisconsin statute providing that no warehouse receipts were valid except those issued by a public warehouse openly held out as such and subject to use by all persons on equal terms and, secondly, because there had not been a sufficient change of possession of the goods. The evidence here showed that the warehouse company's agents on the premises of the bankrupt were in fact the employees of the bankrupt who cared for and shipped out its goods. The evidence also disclosed that, not only were no signs posted telling the public that the goods were in a warehouse, but the stored goods were visible to the public through the fence which surrounded them. The court, speaking through Justice Peckham, concluded by saying:

> "There was really no delivery, and no change of possession, continuous or otherwise. The alleged change was a mere pretense, a sham."

The limitations in field warehousing and the test of the validity of field warehouse receipts are to be found in these two cases. It will be unnecessary to extend the length of this paper by a detailed

[15]Security Warehousing Co. v. Hand, 206 U. S. 415, 51 L. Ed. 1117, 27 Sup. Ct. 720 (1907).

discussion of the many factual situations to which this test has been applied in the reported cases. Reference is made in the notes[16] to the principal cases in which the validity of field warehouse receipts was questioned. In all of them the question of change of possession proved controlling.

Because of their local interest attention is called to four cases arising in this state. In the case of *In re Taylor Log and Lumber Co.*[17] the lumber company, in order to raise needed cash, set up a field warehouse in its lumber yard. In subsequent bankruptcy proceedings, the warehouse company and the bank which held warehouse receipts as security sought to establish the validity of the warehousing. The warehouse company asserted that at the time of the bankruptcy it was in possession of the lumber and was therefore entitled to a lien for its storage charges. The bank, as pledgee of the warehouse receipts, claimed title to the lumber described by them. The court held that the warehouse company was not entitled to its lien because it had voluntarily surrendered possession of the lumber. The court, however, held that the bank had a good lien because at the time the warehouse receipts were issued the warehouse company did have possession and because the bankrupt had not been clothed with ostensible ownership of the lumber.

The evidence showed that the warehouse company leased at nominal rental the lumber yard of the bankrupt and placed signs six by ten inches at the entrance of the yard stating that it was a storage yard of the warehouse company. Similar signs were placed in front of the piles of warehoused lumber. By the terms of the lease the bankrupt was not excluded from the yard. The lease was recorded. And although the evidence showed that the warehoused lumber was inventoried and marked with paint, it also showed that non-warehoused lumber was interspersed with ware-

[16]In the following cases the warehouse receipts were held invalid because there was insufficient change of possession: Geilfuss v. Corrigan, 70 N. W. 306 (Wis. 1897) (pig iron); Tradesmen's Nat'l Bank v. Jagode, 40 Atl. 1018 (Pa. 1898) (wool); In re Millbourne Mills Co., 172 Fed. 177 (C. C. A. 3, 1909) (wheat, flour); Citizen's Nat'l Bank v. Willing, 109 Wash. 464, 186 Pac. 1072 (lumber); In re Rodgers, 125 Fed. 169 (C. C. A. 7, 1903) (seeds); American Can Co. v. Erie Preserving Co., 171 Fed. 548 (1909) affirmed 183 Fed. 96 (canned goods); MacDonald v. Aetna Indemnity Co., 97 Atl. 332 (Conn. 1916) (grain); Peoples Bank of Buffalo v. Aetna Indemnity Co., 98 Atl. 353 (Conn. 1916) (lumber). In the following cases warehouse receipts were held valid because there was sufficient change of possession: Love v. Export Storage Co., 143 Fed. 1 (C. C. A. 6, 1906) (lumber); Bush v. Export Storage Co., 136 Fed. 918 (1904) (railroad cars); Philadelphia Warehouse Co. v. Winchester, 156 Fed. 600 (Del. 1907) (steel); Equitable Trust Co. v. A. C. White Lbr. Co., 41 F. (2d) 60 (Idaho 1930) (lumber); In re Taylor Log & Lbr. Co., 41 F. (2d) 249 (Wash. 1925) (lumber). See McGaffey Canning Co. v. Bank of America, 284 Pac. 977, 294 Pac. 45 (canned goods) for a well considered case reviewing all the authorities.

[17]In re Taylor Log & Lbr Co., 41 F. (2d) 249 (Wash. 1925).

housed lumber and at times non-warehoused lumber was piled on warehoused lumber. Testimony by the superintendent of the bankrupt disclosed that the bankrupt often filled orders from the warehoused lumber without the permission of the warehouse company and shipped it out of the yard. The warehouse company employed no permanent custodian to take charge of the yard but sent one of their representatives to make periodic inspections.

In view of these facts, the court's holding that the warehouse receipts were good and therefore entitled the bank to possession of the lumber described in them might be considered a departure from the rule that a warehouseman must maintain exclusive and continuous possession in order to validate outstanding warehouse receipts. The court, however, limited the lien of the bank to only that lumber which could be identified:

> "* * * The storage receipts being negotiable in form, duly indorsed and delivered for value, to the bank, without notice of any fact impeaching the title evidenced by them, vested the bank with a lien prior to any right of the trustee to such of the lumber in the original placarded piles as can, by a fair preponderance of the evidence, be identified."

This decision shows that field warehouse receipts will not be invalid in toto if the warehouseman relaxes his possession but will be upheld as to those goods in storage which have been sufficiently marked to notify third parties of the warehouse company's interest.[18] The court no doubt felt the notices and markings warned third parties just as effectively as if the warehouse company had exerted complete dominion and control.

Although the Supreme Court of the State of Washington has never had the question of the validity of field storage warehouse receipts directly before it, we do have three warehouse cases which would indicate that the problem, when presented, will be decided by the application of the test set for in the *Wilson* and *Hand* cases.

In 1895 our court decided in the case of *Steaubli v. Blaine Nat'l Bank*[19] that the owner of goods cannot be his own warehouseman. A bank loaned the proprietor of a shingle mill the sum of $200.00. As security it took an instrument in the following form:

"INTERNATIONAL MILL CO., MANUFACTURERS
OF CEDAR SHINGLES,
J. B. Chown, Proprietor.

Blaine, Wash., Nov. 18, 1891.

"Received from J. B. Chown 150,000 shingles valued at

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[18]67 C. J. 490, § 74.

[19]Steaubli v. Blaine Nat'l Bank, 11 Wash. 426, 39 Pac. 814.

> $240, subject to the order of T. G. Steaubli, now in dry house at mill.
>
> C. H. McKnight,
> Warehouseman."

McKnight was the manager of the mill and the warehouse was a part of the premises of the mill. The court held that this was not a warehouse receipt, saying:

> "The only thing in the least tending to give it that character was the addition of the word 'warehouseman' to the signature of McKnight, and this was entirely insufficient for that purpose in view of the fact shown by the plaintiff's own testimony, to the effect that the shingles were held by the mill company under substantially the same conditions as the product of mills of the kind is generally held."

In the case of *Citizens Bank v. Willing*,[20] the court held invalid warehouse receipts issued by a subsidiary warehouse company. In this case there was a warehouse company in name but the court found it was not engaged in the business of storing goods for profit.

> "This presents the question whether the Fidalgo Warehouse Company was a 'warehouseman' within the contemplation of the uniform warehouse receipts act. Section 1 of this act provides that 'warehouse receipts may be issued by any warehouseman, and must be issued in manner and form as provided by this act.' In § 3369-58, 'warehouseman' is defined to mean 'a person lawfully engaged in the business of storing goods for profit'. In this case the Fidalgo Warehouse Company had no separate building of its own; it did not store goods for the public generally or at all; it only stored the product of the Red Cedar Company in a room or shed upon the premises of that company. It was simply a device by which the bank was furnished negotiable warehouse receipts as collateral security for the loans which it had made to the Red Cedar Company. The evidence fails to show that the warehouse company was storing goods for profit, and therefore it would not come within the statutory definition."

There can be no question but that bona fide warehouse companies specializing in "field storage warehousing" are storing goods for profit because that is their sole means of revenue.[21]

In *Laube v. Seattle National Bank*, Frank Waterhouse & Co. prior to bankruptcy borrowed money from the bank and pledged as collateral ten warehouse receipts representing ten Vulcan trucks.

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[20]Citizens Nat'l Bank v. Willing, 109 Wash. 464, 186 Pac. 1072.

[21]Note 7 *supra*. In re Taylor Log & Lbr. Co., 41 F. (2d) 249 (Wash. 1925); Laube v. Seattle Nat'l Bank, 130 Wash. 550, 228 Pac. 594.

These warehouse receipts were issued by the Arlington Dock Company. Some evidence was introduced to show that the dock company was a subsidiary warehouse company of the bankrupt but the court did not so find and held it to be a bona fide warehouse company storing goods for profit. The trucks were not stored in the dock company's warehouse but were stored some distance away at the plant of the Vulcan Company and separated by that company from the rest of its property. The dock company had free access to the trucks. It was agreed between the dock company and the bankrupt that the trucks should remain with the Vulcan Company; and it was agreed between the dock company and the Vulcan Company that the physical possession of the Vulcan Company would be as agent for the dock company. The bank took possession of these trucks under its warehouse receipts and the trustee sued to recover them, arguing that the warehouse concern cannot lawfully issue warehouse receipts unless it has physically stored the property in its own warehouse. The court held for the bank, saying the trustee did not state the law correctly. The court adopted the rule that the property may be in the possession of a third party as agent for the warehouse company, citing as authority *Love v. The Export Storage Company,*[22] and the *Wilson* case[23]. The following language of the court sets forth its holding on this question:

> "* * * The argument seems to be that a warehouse concern cannot lawfully issue warehouse receipts evidencing storage of property with it unless it has physically stored the property in its own warehouse. This, we think, is not unqualifiedly the law. If a warehouse concern has acquried the possession of the goods to the extent that the owner is excluded therefrom, it seems to us that neither the owner nor those claiming under him, even though the latter represent his creditors in insolvency or bankruptcy proceedings, can rightfully claim that the warehouse receipt was illegally issued merely because the goods were left in the custody of a third person by the warehouse concern as its agent. This record, it seems to us, renders it quite plain that the Waterhouse company surrendered all physical control over these trucks, with no right to assume possession of any of them, except upon return of the warehouse receipt or receipts therefor properly endorsed, such being the express terms of the receipts."

The actual situation of a field warehouse, together with the question of whether or not there had been sufficient change of possession from the owner to the warehouse company, was not involved in the *Laube* case because the trucks were not at any

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[22]Love v. Export Storage Co., 143 Fed. 1 (C. C. A. 6, 1906).

[23]Union Trust Co. v. Wilson, 198 U. S. 530, 49 L. Ed. 1154, 25 Sup. Ct. 766 (1905).

time on the premises of the bankrupt and therefore no false credit could be given the bankrupt by this transaction. However, the court did hold that a warehouse receipt to be valid need not represent goods actually within the physical walls of a warehouse building but would be valid if held for the warehouse company by an agent. If they will recognize as part of a warehouse a building owned by a third party some distance from the warehouse, would they not recognize a warehouse on the premises of the owner of the stored goods, provided the necessary change of possession is effected? The writer submits the answer is yes, and it seems more true when the reader remembers that our court relied on two leading cases on field warehousing to support its holding.

Conclusion

Warehouse receipts issued by a bona fide warehouse company engaging in field warehousing are valid when in the hands of third parties both as against creditors and trustees in bankruptcy, provided there has been sufficient change of possession to negative any ostensible ownership on the part of the debtor or bankrupt.

The courts of the State of Washington should follow the rules laid down in the *Wilson* and *Hand* cases when required to pass upon the validity of field warehouse receipts.