8-21 Bank’s Right to Pay: Bank’s right to pay → bank’s right to debit the customer’s account after paying.

Class

- **Problem 21.1:**
  o A. A bank may charge a customer’s account for an item even though it results in an overdraft. Customer ordered bank to pay by writing the check. In creating an overdraft situation, it’s not the bank creating the risk.
    ▪ A check is not properly payable when (bank won’t get paid
    o Forged drawer’s signature
    o Forged endorsement
    o Proper post-date notice by the customer, and the bank pays
    o Proper stop payment order logged.
  o B. Customer not liable if the customer never signed the item nor benefit from the item. Here, didn’t draw or sign. A spouse benefits any time their spouse receives a benefit. Comment 2
    ▪ No clear answer: even if can’t come to a definitive answer, but know what issue the answer hinges on. Here, definition of “benefit” when other spouse gets direct benefit. Court would decide it.

- **21.2:** §4-401(c): allows checks to pay postdated checks unless customer gave effective notice and identified the checks.
  o Jasmine could have sent the bank numbers once she knew of them.
  o Does technology allows the bank to identify the checks with certainty.
  o §4-403(b): Jasmine’s written notice effective if identified check with reasonable certainty. Issue is whether check id’d with reasonable certainty.

- **21.3:** Check paid contrary to timely stop-payment order due to clerical error.
  o 4-401(a): Not properly payable. Stop-payment right of customer observed properly.
  o 4-407(2): Bank may step into Carol’s shoes and may assert any rights check depositer may have against the check writer. Subrogation rights here.
    ▪ To determine whether bank’s subrogation claims effective, look at whether the cooking equip’t. what it had promised. If there was a difference, then bank’s mistake hurt him.
    ▪ If goods are worth something but not full price, then bank will get partial subrogation rights.
  o If court requires bank to recredit account,
    ▪ Bank inherits customer’s right against the party cashing the check. Bank inherits the customer’s claim.
    o Could not keep goods if successful suit: would be unjustly enriched by getting free cooking equipment.

- Article 4 explicitly made for banks and checking. Supercedes Art. 3, even though there may be some inconsistencies.

- **3-310:** Personal checks always uncertified.
  o Suspension of contractual rights to the same extent that they would be discharged. Lasts until dishonor or payment of the instrument
    ▪ Dishonor. 3-310b3: Carol’s (check casher’s) rights revived.
      o May sue receiver of the check on capacity of drawer of the check.

Book Notes

- Two broad classes of transactions
  o Sale transactions: seller receives payment at the time of the transaction
  o Credit transaction: lender agrees to accept deferred repayment of a financial obligation.
- Non-cash payment systems: check, credit/debit card, wire transfers, letters of credit.
- Payment systems must respond to the likelihood of mistake and wrongdoing and determine what to do about any losses that occur.
- Federal rules preempt the agreements of the parties and any inconsistent provisions of state law.
- Most rules for the checking system are in UCC Art. 4, but some in Art. 3.
- It is proper for the bank to charge a customer’s account for any “item that is properly payable. §4-401(a), where properly payable means “if the customer has authorized the payment.” (Comment 1).
  o As long as the payee properly transfers the check to an intermediary (ex. personal bank), the intermediary becomes a “person entitled to enforce” the check and is entitled to payment of the check. §3-301.
  o §4-401: If check stolen, improper for bank to pay.
When an account is overdrafted (check pays more than account balance), payor bank can charge the account but may also dishonor the check/refuse to pay it. §4-401(a)

McGuire v. Bank One: Check w. current date given with verbal instructions to receiver not to cash for 2-3 days, which were ignored. Bank honored check, even though checking account “grossly insufficient” and sent overdraft notice the next day. Banks must exercise ordinary care under §4-103, even though authorized to charge properly payable check against a customer’s account under §4-401. Payment of a properly payable item creating an overdraft is an action approved by §4-401(a). Banks need not attempt to contact the drafter to show ordinary care. Paying a check creating an unusually large overdraft is properly payable, since the applicable statute places no limit on the size of the overdraft or the bank’s reason for payment.

- Banks may pay items (checks) in any order.
- A customer’s decision to pay does not become final at the time the customer issues the check. Art. 4 allows customer to “stop” payment if customer sends a timely and effective notice, removing payor bank’s right to charge the customer’s account for the item.
  - Limits
    - Prompt action required. §4-403: effective only if received at a time and in a manner affording the bank a reasonable opportunity to act.
    - Stop-payment order valid only for six months. §4-403(b)
- To prevent payee from obtaining double payment by collecting both on the check and on the underlying obligation/transaction, §3-310(b) suspends the payee’s right to pursue the customer on the underlying transaction when the payee accepts the customer’s check. This suspension ends if the check is dishonored.
- Checks not properly payable: bank must recredit the customer’s account with the fund improperly paid out, along with consequential damages where the charge to the account leads the bank to dishonor other checks.
  - Customer did not write the check
  - Payment made after a forged endorsement
  - Bank failed to comply with valid order to stop payment.
  - NOTE: limited by §4-407: Bank can assert payee’s rights against the drawer as a defense to bank’s obligation to recredit the account.
8 22 Bank must pay checks
- 22.1 Bank pays check after 7 mo.
  o §4-404: Bank not obliged to pay check, other than certified check, older than 6 months.
  o Bank had a right to pay? Yes. §4-404 says bank MAY charge as long as they act in good faith.
    §3-103: Common standards of fair dealing: commercial standards don’t require bank to examine instrument unless failure to do so violates bank’s prescribed procedures and procedures don’t vary unreasonably.
    Good faith beyond honesty in fact is standard commercial dealings. Similar to exercise ordinary care.
  o No clear answer
- 22.2: Regulation CC and Funds availability
  §229 Terminology: Regulation CC §229
  - Non-local check is “any check drawn on a bank located outside the check-processing region of the bank at which the check is deposited
  - Customer wishes to use funds indirectly (writing checks against them)
  - Customer wishes to use funds directly (withdrawing cash).
  NOTE: Large Deposits>$5,000: §229.13b: First $5K subject to normal rules. Remainder released under §4-215 when the bank knew the check has cleared/the bank knows the transaction would be final.
    - Low risk items: Cashier’s checks, US govt. checks: Full amt. due next biz day.
  229.10c1 CHECK TO SEE IF DEPOSITED CORRECTLY, WATCH OUT FOR “AND.”
  o Cash withdrawals from local checks
    - The bank must make $100 available on the first business day after the banking day of deposit
    - Must make an additional $400 available the second business day
    - Must make remainder available on third day
  o Cash withdrawals from non-local checks
    - Must make $100 available on the first business day after the banking day on which the funds are deposited.
    - Must make additional $400 available on the fifth business day
    - Must make remainder available on the sixth business day.
  o Noncash withdrawals from local checks
    - The bank must make $100 available on the first business day after the banking day on which the funds are deposited.
    - The rest must be available for withdrawal no later than the second business day
  o Noncash withdrawals from nonlocal checks
    - The bank has to make $100 available on the first business day after the banking day on which the funds are deposited.
    - The rest must be made available for withdrawal no later than the fifth business day after the . . .
  - A. Cash withdrawal of non-local check for $7,000 deposited Mar 1: $100 on Tuesday, Mar. 2. Day 5: $400 Fifth business day, §229.2(g), would be Monday, Mar. 8. $4500 on Tuesday, Mar. 9. The remaining $2000 released under §4-215 when the bank knew the check has cleared/the bank knows the transaction would be final.
    - Large amounts over $5,000: §229.13(b): Once a check is over $5,000, the first $5,000 subject to the normal rules. For the remainder,
      - If bank learned the check cleared on Mar. 3, could they hold out for the full time under Reg CC? Federal regulation would trump UCC since it is a state regulation.
        - Bank must make the account available not later than the time the bank knows the check cleared. Reg. CC sets an outer limit and allows state rules to make the check released sooner. If there’s a state law that gives more protection, the federal statute defers to the state law.
• Reasoning being that the bank no knows the check can go through and the bank is not at risk.
  o B. $1,000 cashiers check with teller, non-state check, 3rd party.
    ▪ No special treatment since Reg. CC G229.10c(iv): Account must be held by the payee of the check. Carl was a special endorsee, not the payee of the check.
  • Non-local, non cash items. Day 1, $100 mar.2, Day 5, $900 Mar. 8.
  o C. US Treasury Check: Low risk, so all $1000 Mar. 2. Funds must be made available the day after deposit with a check drawn by the US treasury into an account held by the depositor. §229.10c1i: Even when placed in a local ATM rather than deposited with a teller, get quick avail.
    ▪ Many items, only get quick availability when deposited with a teller.
  o D. $1,000 in non-local
    ▪ No, doesn’t qualify for exception. Even though drawn by state govt., depository bank in another state. §229.10c1iv: doesn’t meet requirements. $100 day 1. $900 day 5.

- 22.3: Damages for wrongful payment a $900 check.
  o Damages liable §4-402b: any damages, including consequential damages. $25 fee for the bounced check, likely the truck repossession and whatever damages resulting for the possession.
  o Was this a wrongful dishonor by FSB §4-402a: Look at whether the item was properly payable, unless overdraft agreement exists. This item was properly payable even though it would have created an overdraft because the only reason it would have created an overdraft would be FSB’s failure to honor a proper post-dated check notice. Bank liable for wrongful dishonor.

- 22.4: Bank determination of fund availability.
  o If bank had not noticed deposit: Dishonor would be rightful § 4-402: only have to pick one time to decide whether to pay. Comment 4 says the end of the day after receipt is a common time to choose.
  o Does bank’s knowledge and reexamination of bank’s decision change things?
    ▪ Look at whether bank’s rechecking counts as a subsequent examination made of the account to determine payment. Appears like it would.

Class notes
- Not wrongful to fail to credit the cash deposit the day it was received since Reg. CC allows for cash deposits to be made part of the account the next business day.
- UCC has DEFAULT rules regarding the bank/customer relationship.
  o Limits 4-103a: may be varied by agreement, but bank cannot disclaim lack of good faith or failure to exercise ordinary care.
- Federal law trumps the UCC due to the supremacy clause.
- Bank’s right to pay is a function of customer authorization, not of funds in customer’s account. (even overdraft provisions by banks causing the bank to pay the overdraft and then receive money from customer later.)
- Common law unjust enrichment theory: allows bank to collect from customer if the bank pays overdraft.
- Art. 4 allows for post-dating and stop-payments: if timely notice and customer complies with vague duty to describe the item with reasonable certainty.
  o Note that stop-payment order lapses every six months.
- Even when the bank honors an item not properly payable, the bank may use defensive subrogation to avoid recrediting the customer’s account.
  o If bank does recredit, then bank may recover from check’s payee. Offensive subrogation.
  o Subrogation rights based upon whether the payee’s check was good.
  o If no unjust enrichment, no subrogation rights for the bank.

Book Notes
- When funds available, bank has affirmative duty to pay debt.
  o Only obligation to drawer/customer.
- Account must have sufficient funds at time payor bank evaluates check. §4-042c
  o Only need to check once. Even if funds deposited later that day, the bank can still dishonor
Federal Reserve banks assist private banks in clearing and collecting checks.

“Regulation CC” provides a framework of deadlines to release funds.
  - Chart p 312, explan p.313
  - Banking days used rather than business days.

Special low-risk items whose entire amount of funds must be available after the first business day after the banking day on which the funds are deposited because low likelihood of non-payment
  - If 3rd party account, different rules. See p314.

Limits
  - New account
  - Checks >$5,000
  - Repeated overdrafts over 6 months
  - Reasonable belief check is uncollectable.

Banks want to maintain relationships with customers and good reputation, so often pay out earlier than required.

First National Bank v. Colonial Bank: “Check kiting” scheme, where large checks are overdrawn from bank accounts in two different banks and deposited in the other bank to give the appearance that money is being deposited. First National determined kiting system and returned the Colonial Bank Checks. Colonial Bank failed to return the First National Checks until the next day and ended up having to honor the checks and pay First National the interest of the account because the bank accommodated its customer to an extent far beyond its legal obligations.

Wrongful dishonor entitles customers to all of the damages proximately caused by the wrongful dishonor. Onerous since damages not capped at the amount of the check.

Possible problems: loss of business reputation with suppliers, individual’s arrest or prosecution for bounced check.

Maryott v First National Bank: Wronful dishonor proximate cause of Maryott’s damages is question of fact for jury. If the defendant’s conduct was a substantial factor in causing the plaintiff’s injury, it follows he will not be absolved from liability merely because other causes have contributed to the result. §404-2 does not define consequential damages that may be recovered, so look at state precedent. Bank’s illegal and irresponsible actions causing Maryott to be put out of business not outrageous conduct necessary to collect damages for intentional infliction of emotional distress.
  - Concurrence: legislature wanted all actual damages, including emotional distress, to be decided by jury.
8 23 Collection of Checks

- Banks will not be held liable for full amount of check unless improper dishonor.

23.1: Midnight Deadlines and Dishonor

- First Bank received check after stated time, had until midnight of next day. Sent check on Wednesday. New Haven Bank received the check Weds, returned it Thurs. afternoon: Met deadline. If was the same bank, deadline would have been midnight Wednesday.
- Branch of a bank is a separate bank for computing time in Art. 3&4. §4-107
  - Otherwise, would be an on-us item, meaning they would have to move a lot quicker in order to make the midnight deadline.
- Since across state lines, Reg. CC gives 4 days for the check to be returned. RegCC 220.30(a).
  - Check received and dishonored by the next business day. §4-301
- §4-302(a)(1): If item presented to and received by a payor bank: if retains item past midnight on the day received without changing the provisional settlement. Will become final on the midnight deadline: midnight of the banking day following the banking day on which the item is received.
  - May reverse and revoke the final settlement before this date
- Reg. CC: §229.30(a): May return using an expeditious manner
  - 2day/4day: local would be received two days after presented.
  - Forward collection rule: as long as use the same means of forwarding the check and use the same means as would a depositary bank, acceptable means of returning a check dishonored as a payor bank.
  - §229.33: if greater than $2500, must dishonor by the second biz day of receipt. Large item notice rule.
- Figure p351 on return obligations.
- If fail to meet the midnight deadline, would have to accept the check and pursue the drawer (their customer) to get the money. Strict liability.
- If fail to meet Reg. CC, only §229.38, only liable for actual loss caused. “No harm, no foul.”
- Payor bank subject to the midnight deadline rule.
- Depositary bank’s midnight deadline rule: Comes into play when the depositary bank has been dishonored.
  - Begins to run from the time the bank gets the item/learns of the dishonor. §4-104(a)(10): midnight of the banking day after the banking day when they learn.
  - Must revoke the provisional settlement by this time.
  - Responsible for any loss caused by the delay. §4-214(a).
- §4-107 ends up being dispositive.
- §4-215(a): Item finally paid
- Final payment usually made by the midnight deadline elapsing and default occurring, unless paying over the counter.
- Reg CC: Check sent by courier, so expeditious.
  - Don’t want to make the funds available: Funds availability rule, customer satisfaction concerns. §4-202(a)(1) concerns about liability too.

23.2: Bad check deposited, depositee trying to withdraw funds

- A: Depositee attempts to cash check for full account balance.
  - Should revoke provisional settlement (before final deadline and making final payment), notify Lassen
  - bank doesn’t need to give more than $100 for the check the following day
  - §4-301(b)
  - §4-214(c): charge of an on-us item like this is §4-301
- B: Permitted depositee to cash check when presented.
  - Would be final payment and would need to go after Carol.
    - §4-215(a)(1): paying item in cash would be final payment.
- Final payment means the bank has lost all rights against the depositor, so even if Lassen deposits money later, bank can’t touch. Must go after Carol
  - If gave the money, bank loses all charge-back rights.
- C: FSB didn’t put hold on funds and teller cashed bad check.
  - §4-301
  - If arguing that paying cash wasn’t final, can say was giving depositee funds as a depositary bank rather than the payor bank. Expedited funds availability: any depositary bank can do it w/o losing rights to revoke a credit given.
  - If a bank revokes credit when there isn’t enough money in the account
    - Could go after depositee. §4-301(b)
- 23.3: Check kiting scheme found, Colonial fails to dishonor checks by Weds or Thurs. Colonial lost case for delaying past Weds. On Thursday morning, can
  - Reg. CC 229.30(c)(1): Allows bank to extend its UCC deadline by one day if bank expedites delivery of returned item and chooses a method that will get it to the bank by midnight of the day following the deadline.
    - Can even get one day beyond the day if use a “highly expeditious” means of transportation. 2 banking days after the midnight deadline
    - Arrange for a messenger to get the check to FNB by Friday’s banking day. If so, Colonial would avoid default payment clause.
  - FNB may argue that Reg. CC exception was not intended to be institutionalized to allow banks to cover for late actions.

23.4: Ridiculously convoluted fact pattern.
- Need to know if TownBank met its notice and requirements since it relates to their ability to dishonor the check. Sufficient funds depends on whether the check is good.
  - Question of whether FSB acted properly comes down to whether FSB was in its rights to charge back the check that had been rejected from Ball.
  - What defines the rights of a bank to charge back:
    - Comes down to whether the payor/drawee bank will make final payment on the check they put through on collection or properly dishonor it (which would lead to acceptance of the check after the midnight deadline). Either proper dishonor or made final payment.
      - If payor bank made final payment, then you as a depository bank would remove your ability to charge back the account.
      - Means provisional deposit becomes final. Kimberly Trust, §4-214a, §4-215d
- If failure to revoke provisional payment, then all provisional payments become final.
- Definitions
  - Charge back: Depositary bank may do a charge back of the provisional credit.
  - Dishonor: payor bank will not accept check presented to it.
- TownBank: Midnight deadline of Article 4: missed the deadline: received on Monday, postmarked it Wednesday for mail. UCC requirement turns on when payor bank sent the item. 1-201b36: deposited in mail. 4-301b2: Item returned when sent or delivered.
  - Know SHOULD have received it on Weds, but can’t be sure.
  - Don’t know if sent on Monday or a day earlier.
  - If confident the check was received/presented on Wednesday
- FSB acted properly in dishonoring $2000 check.
  - Since missed midnight deadline, payor bank made final payment. Once payor bank made final payment, depositary bank must consider the provisional settlement final. Charge back by depositary bank would have been IMPROPER. If charge back improper, than also the dishonor of the $2000 check.
  - Damages under UCC: actual damages.
    - Can get funds. 4-215d
    - Needs to have $2000 check honored
- Can FSB recover from TownBank (payor bank)?
  - 4-302a: Recover for amount of item, but not wrongful dishonor damages.
  - Reg CC: 229.33a: 2500 check, so must get notice by second business day.
    - FSB got notice, relied on its notice to its detriment since the notice turned out to be inaccurate.
    - Reg CC warranty requirements. 220.33b? Warrants will be returned in a timely manner.
  - Reg. CC return deadline: 229.30a1: Due Tuesday, was received Wednesday morning. So, midnight deadline rule violated
    - Damages under Reg. CC not liable for damages for amount of the item.

- Bank like FSB had no way to know the payor bank was going to miss its midnight deadline. When get electronic notice: if charge back customer’s account, leave themselves open to consequential damages for wrongful dishonor, ones that FSB cannot recover from the payor bank.
  - If don’t charge back and instead allow funds availability for the check, then taking risk that Carol will spend the funds and that the funds withdrawn will be recoverable by FSB.
  - FSB is the depository bank: even though can do a charge back, still have to go after customer to get the money back.

- Middle ground for bank facing the dilemma: Expedited Funds Availability Act: Don’t do a formal charge back on the account. Instead, only make the funds available to the extent required by law.
  - 229.13b: reasonable cause to believe the check may be uncollectible, the regular funds availability schedule does not apply.
  - If electronic notice but not return of check, would be reasonable cause. Wait until get check back and see, or at least further investigate into whether midnight deadline attained.

23.5:
- May have met midnight deadline: received Wednesday, so had to send by midnight of Thursday. If deposited on Thursday evening, would be postmarked on Friday.
- If made midnight deadline, FSB within rights to dishonor $2000 check since within their rights to charge back.
- Right to dishonor check function of right to charge back, function of whether the payor bank met midnight deadline
  - If TownBank dishonored by midnight deadline but violated Reg CC midnight deadline obligations.
  - Reg CC obligations to give notice for a large check dishonor.
  - Failure to meet these requirements does not impact propriety or effectiveness of the dishonor.
    - Damages in general of failure of Reg CC obligation: Damages resulting from violation, capped at the amount of the item.
    - Payor bank still properly dishonored.
    - Anyone hurt by TownBank’s failure.

4-214: Collecting bank may withdraw provisional settlement. “if by its midnight deadline or within a longer reasonable time after it learns the facts it returns the item or sends notification… If the return or notice is delayed beyond the bank’s midnight deadline or a longer reasonable time after it learns the facts, the bank may revoke the settlement, charge back the credit… but it is liable for any loss resulting from the delay.”

23.6:
- UCC states the person/entity that must take responsibility for encoding failures, as summarized below
  4-209(a): person encoding liable for faulty check.
  229.34(c)(3): any bank presenting check warrants it to be correct if customer encodes.
Encoding warranty made to any subsequent collecting bank. Here, breach of warranty. Hunt bank liable to Country Bank for 4-209b. Penalties significant and not limited to amount of item. Here, loss trivial since honest mistake and no thievery. If deliberate, Hunt would be liable, even if it hadn’t originated the mistake.

229.34c3: warranty by ANY bank subsequently handling the check.

- Damages under Reg CC 229.34c: amount no greater than consideration received by bank.

- When approach a warranty, ask
  - Who makes warranty
  - Who does it run to
  - What promised
  - What are consequences/damages for violation of warranty.

Book Notes

- Legal right to force the payor bank to pay the check & obtaining payment
- Payee has no rights against the payor bank.
- Payee cannot force the bank to pay even if the account does have sufficient funds: §3-408: the check does not of itself operate as an assignment of funds available for its payment, and the drawee is not liable on the instrument until the drawee accepts it.
- Outdoor Technologies v. Allfirst Financial, Inc.: Bank won’t cash check, drawer filed for bankruptcy before check could be paid, payee out of luck.
  - Art 3 governs negotiable instrument, Art. 4 bank deposits and collections.
- If a payee is concerned that the payor bank will decline to pay, it can protect itself by:
  - Refusing to accept an ordinary check. There are special checks that offer an assurance that the payor bank will pay the check when presented.
  - Require the drawer to obtain the payor bank’s agreement to pay before accepting the check: Pre-accepted or “certified check.” §2-409(d), §3-104(g, h)
- Payee can go directly to the payor bank and obtain payment itself
  - Cash check §4-301(a), §4-315(a)(2). Note if the account does not contain sufficient funds to cover the check, the payor bank normally would refuse to cash the check.
  - If both have an account at the same bank, payor bank gives depositor credit for the item on the day it receives the item. “On-us” item. §2-104(a)(10). Payor has until midnight of the next day to decide whether to honor the check. If no decision by then, must honor.
  - or can obtain payment indirectly by transferring the check to an intermediary (like a bank), and receive funds from the intermediary in return for the check.
  - When a customer deposits a check into its account, an agency relationship is created between the customer and bank, making the bank a “collecting bank” under §4-105(5).
    - Bank gives a “provisional settlement” credit to the customer’s account for the amount of the check while it attempts to obtain payment. Provisional because the depositary bank may charge-back the amount
    - Banks exchange checks through the Federal Reserve process, or through multilateral clearinghouses, bilateral correspondents, and direct-send arrangements.
      - FR process: Federal Reserve accounts debited or credited, then the check forwarded to the payor banks, “presenting” the checks for payment §3-501(a)
      - More expensive than other systems and provides slower availability.
    - Kimberly A Allen Trust v. FirstBank of Lakewood: §4-124(a) defines collecting bank’s right of charge-back or refund. Under §4-215(a)(3) final settlement occurs when an item is deemed finally paid as a result of the payor bank’s failure to revoke a provisional settlement by a particular deadline.
Returning a check/dishonoring it may be done by notifying the other parties of its decision to dishonor the check by returning it by depositing it in the mail. §4-201(a)

Bilateral arrangements for direct-send and correspondent clearing made between large metropolitan banks also include smaller banks in the area which the larger banks will act as a transfer connection to.

- Regulation CC & the check-return process: adds an accelerated return deadline (dishonoring payor bank must send the check so that it will be received no later than 4pm 2 biz days later for a local and 4 biz days later for nonlocal check; midnight of banking day after the banking day on which payor bank receives the check extended to defer return until next day if payor bank selects an expeditious mode of return resulting in faster return than the UCC deadline), a notice-of nonpayment deadline (§229.33: dishonoring a check $2500+ must get notice of its determination to the depositary bank by 4pm on the second business day after the banking day on which the payor bank received the check., and alters UCC §4-301(a) midnight deadline for return.
  - Failure to meet the midnight deadline makes the payor bank accountable for the item under UCC§4-302. payment becomes final under UCC §4-215, and depositary bank loses any right of charge-back under UCC §4-214. Failure to meet Reg. CC’s deadline, under §229.38 less severe.

- Return obligations p351

- NBT v FNCB: Returning a check by the midnight deadline with an incorrectly coded magnetic strip did not cause the payor bank to become strictly accountable for the check where the depositary bank did not receive any damage from the error. Regulation CC states damages from noncompliance with Reg CC means a bank may be liable for the amount of the loss incurred, up to the amount of the check, less the amount of loss incurred even if defendant bank had exercised ordinary care.

- UCC §4-301(a): If the bank wants to dishonor a check, must return on the midnight of the banking day following the banking date of receipt.
- Reg CC 229.30(a): expeditious manner of return.
- $2500+: Reg 229.33: Notice of dishonor be received by 4 pm on the second biz day following the banking day of presentment.
- Depository bank has own midnight deadline to revoke temporary settlement
  - When learn of dishonor, has until next banking day to return item or send notice to customer.
  - Failure to meet this deadline only permitted if there is delay. Payor bank must pay damage.
- When payor and collecting bank the same
  - If pays immediate cash over the counter, this is final payment in its capacity as payor bank. Bank accountable for the item and has no recourse against the customer paid. Has recourse against customer whose account is overdrawn. “On-us.”
  - If deposited into account, bank has until midnight deadline to make decision about check.
  - If expedited availability of funds: bank’s capacity of depositary bank. Not a final payment. Discretionary decision, bank may charge back before midnight deadline if finds out no funds.
- If the payor bank dishonors by the midnight deadline, the depositary bank has the right to charge back. If payor misses, the depositary bank cannot charge back
- If Payor bank misses deadline, it cannot charge back. Strict deadline
- If Payor bank fails to fulfill its Reg. CC requirements or notice requirements for large items (2500+), bank is only liable for the damage it caused.
- Depository bank misses its midnight deadline for charging back the customer’s account, the depositary bank is only liable for any loss caused by the delay.
- Distinguish between charge back rights and requirement under Reg.
  - Charge back: function of whether the payor bank made final payment.
- Depository bank’s obligation to make funds available is a function of the EFAA timetables
  - If don’t have notice of the check’s clearance, depositary bank may still be within its rights to refuse to make funds available for the check which is in fact has already cleared the payor bank.
  - By withholding, may be seen as an improper chargeback. However, timing question: bank hasn’t charged back the credit, just hasn’t made it available since EFAA didn’t immediately require funds to be made available.
  - EFAA didn’t mean to make depositor wait longer than set out by the UCC.
Fraud

24.1: bank honors forged check, payor bank holding the loss right now.
- Was Bulstrode Bank required to recredit the account?
  o Since forged check/endorsement, the check was not properly payable in §4-401, so had to recredit account.
  o Conversion liability: payor bank not the proper plaintiff in a conversion case: payee of the check or another obligee who took the check as partial payment.
  o Contract liability: Can recover from 3-415: obligation of endorser.
    ▪ Any time a check is paid, lose your ability to sue anyone earlier in the chain for endorser liability. Not triggered unless the instrument is dishonored.
  o Warranty liability: 4-208: breach of presentment liability
- Warranty breached was presentment warranty:
  o Proper plaintiff is the drawee bank.
  o Defendants: Persons obtaining payment. 4-208(a)(i), and the previous transferor of the draft.
  o Earlier parties make presentment warranties. Only responsible for the instrument at the time you handled it. Not responsible for a guarantee against future forgeries. Make guarantee as to the state of the instrument at the time you handled it.
  o Breachers of the presentment warranty for all those after
- 4-208a1 breached: Not persons able to enforce the draft.
- Could payor bank recover against any other party for 4-207 breach of transfer warranty.
  o Under breach of transfer warranty, could recover from person granting the check.
  o 4-207a: transferee and subsequent accepting bank.
  o Drawee bank not a transferring nor collecting bank.
- Payor bank never able to use transfer warranty, only presentment warranty.
  o If recover for presentment warranty. Wessex can’t file for breach of presentment warranty, but can sue for breach of transfer warranty from depositor.
    ▪ Only need one to win
- Chargeback
  o Not relevant here since only work as a theory of recovery if you represent the payor bank

24.2: if forged indorsement noticed and check dishonored
- Conversion liability won’t work because conversion requires that the converting bank pay the check; 3-420(a) depositary not proper plaintiff.
- 3-415(a): obligation owed to the person entitled to enforce the instrument
- Even though dishonor, can’t recover
- Presentment warranty: No good since transferred rather than presented.
- Breach of transfer warranty: 4-207a1&2 are the relevant sections: proper plaintiff and defendant plus breach of the warranties.
  o Are damages present?
    ▪ If Wessex bank, when get notice of dishonor, charge back/reverse provisional credit and get no damages. Gets rid of warranty issues.
  o With transfer warranty, more defendants if money out the door and can’t find customer. Charge back right wouldn’t be worth much.
- If earlier parties, may be able to recover against them.

24.3 Forged drawer signature on stolen check. DB ➔ Thief ➔ DL ➔ CB ➔ BB ➔ WB
- Bulstrode Bank holding loss right now.
- Not conversion since Bulstrode not owner of the instrument, since that is the payee / person to pay the instrument
- Contract liability: 3-415a: dishonor and Bulstrode entitled to pursue since no forged endorsement. Forgery of a necessary endorsement prevents subsequent parties from pursuing. If forgery of a drawee signature, may pursue.
- Chetam’s signature w/o recourse. While 3-415a indicates could recover from Chetam, Chetam has disclaimed their endorser liability, which is effective. 3-415
- Warranty liability: presentment or transfer liability. Sue Chetam for breach of transfer warranty.
  - Bulstrode eligible plaintiff, Chetam eligible plaintiff. But, not all signatures authentic nor
    authorized.
  - Warranty disclaimer attempt: Doesn’t work because 3-416, 4-207: warranties cannot be
    disclaimed with respect to checks.
  - Damages: By using charge back, Bulstrode should need to rely on transfer warranties
    Bulstrode v Forger: breach of transfer warranty if can show damages, but forger here the issuer rather
    than an earlier transferor, so forger as transferor would not be eligible defendant.
  - Common law fraud would work 1-103

24.4: Same facts, but Wessex bank takes money from account, the recredits under 4-401.
- Not conversion since payer bank not owner of item
- Not endorser liability since check not dishonored
- Warranty liability no
- Presentment liability since payor bank that is suing
  - No, price says only forgery of drawer’s signature not enough to allow reversal of final payment.
  - Payor banks are supposed to know what customer’s signature looks like/ in best position to note
    forgery.
  - Forgery of a drawer’s signature doesn’t break the change of title. Only forger of indorsment
    signature
- Chargeback won’t work: not payor bank. Must dishonor in a timely way.
- Payor bank has rights against forger
  - Not conversion since not the owner
  - Endorser: no, since forger issuer, not endorser.
  - Drawer’s liability under 3-414: forger’s signature treated as if it was the forger’s rather than the
    party that they forged. If bank followed instruction, charge them
  - Warranty liability: no. Forger an issuer, so makes no warranties. Not presenter or transferor.
  - No chargeback rights
  - Can use 3-418: allows bank paying in good faith to recover from the person for whose benefit
    the payment was made.
  - Can use common law theories of fraud and restitution.

24.5: Person with signed, blank check in wallet has it stolen, filled out and presented.
- Bank may pay unless knew it was stolen. Incomplete instrument
  - 4-401d2: a bank making a good faith payment may credit the account of the customer unless the
    bank has notice.
  - 3-407c indicates payor bank paying a fraudulently altered instrument may enforce rights with
    respect to the instrument.
    - Alteration includes filling in a blank check as well as changing what was there.
    - 3-407, comment 2: intended even though instrument stolen from issuer.
    - Customer best able to prevent theft of checks. Negligence issues.
- If FSB wanted to recover from someone else to try to put the loss on someone other than their customer.
  - If recredit account, would FSB get rights to go against presenting bank?
    - Conversion? No. FSB isn’t owner of the instrument
    - Endorser liability: No. FSB paid check, so no liability for endorser.
    - Warranty liability
      - Presentment warranty if anything. 4-208a: was there a breach of presentment warranty
        by bank in this case. 4-208a2, draft hasn’t been altered.
      - 4-208b: damage formula for breach of warranty: May recover breach of presentment
        warranty for full amount of the damage (here $1000), less the amount the drawee
        received. If drawee recredited the customer’s account, would be zero. However, entitled
to receive $1000. Total damages against presenter bank will be zero. Damages set up so a nice payor bank will not be able to credit the customer’s account and sue a third party.

- §3-407(c) Payor bank paying a fraudulently altered instrument or a person w/o notice of alteration may enforce rights to the instrument according to its terms as completed for the case of an incomplete instrument.
- §4-401d: Could just charge the customer’s account.

24.6 altered instrument or a person w/o notice of alteration may enforce rights to the instrument according to its original terms. Only pay $1000. §4-401d: Could just charge the customer’s account for the intended amount

- Bank wants to know if it can recover the extra $9,000. 3-407c(i) and 4-401 state payor bank can enforce check for the original thousand dollars.
- No endorser liability. Look at warranty theory. Here, presentment warranty. Breach since the draft was altered, and the warranty says the draft was unaltered. Here, damages would be the $9,000. (10,000-1000 amount enabled to receive). So, payor bank able to put loss to earlier party who dealt with instrument before alteration.
- 3-418: Covers payment of draft that had a valid stop payment on it, or signature of drawer was authorized.
  - Limited tool for payor bank.

24.7 telemarketer check forged.

- Does payor bank need to recredit account?
  - If assume didn’t give authorization for check (will be a hotly contested issue), the payor bank would have to recredit account since check not properly payable under 3-401a
- Payor bank have recourse against depositary bank? Yes. Includes warranty unique to the remotely created items. Presentor states the person has made out the check to the presentor for the amount authorized
  - 3-417a4: If unaccepted draft presented to drawee for payment and drawee pays, person obtaining payment and previous transferors of the draft WARRANT any remotely-created consumer item, the person on whose account the item is drawn authorized the issuance of the item in the amount for which the item is drawn.
  - 4-207a6, 4-208a4
  - First party to deal with the wrongdoer gets stuck with burden. Idea is to have bank monitor actions of customer. Checks different than standard checks.

Book Notes

Forgery

- Payor bank cannot enforce indorser liability. It only obtains the instrument by paying for it. §3-415.
- Types of cases
  - Forged endorsement, payor bank pays check.
  - Forged endorsement, payor bank dishonors check.
  - Forged endorsement, payor bank pays check.
  - Forged endorsement, payor bank dishonors check.
- Checklist of bases for liability in these cases.
- 4 theories on which the non-wrongdoer left holding the bag can make themselves whole: Loss should lie with the wrongdoer. If can’t find them, then the first party to deal with the wrongdoer.
  - Conversion liability
  - Liability in contract: liability on the instrument (pursuant to the signature as issuer, endorser, etc.)
  - Warranty liability
  - (only for bank collection cases) Use chargeback rights under Art. 4. Self-help, so don’t have to sue anyone.
- Payor bank responsible for a forged drawer’s signature.
  - Presentment 4-208, 4-317
  - Court meant that the payment warranties were not breached.
- Loss should end up with the wrongdoer or the first party to deal with the wrongdoer for forged checks
- Price v Neil: loss lies with forger or the payor bank if the forger can’t be found when forged signature.

Forged endorsement, bank pays the check
- Bank must recredit account under §4-401.
- Payor bank can recover for breach of presentment warranty from any of the previous transferors or from the party presenting the check. Contrary to presentment warranty, these were not persons entitled to enforce the check.
  - No breach of presentment warranty if handled check before forged endorsement placed on the check.
  - Once there’s a forgery of a signature of the payee, the chain of title is broken and no one may be entitled to enforce the document.
  - Forgery of the drawer’s signature, will not break the chain of title.
- Payor bank: Whoever recovers from, likely the presenting bank, that party may recover from earlier parties for breach of transfer warranties due to the forged endorsement.

Payor bank does not pay the check and dishonors it
- Depositary bank gets the check back from the payor bank that dishonored it. Depositary bank exercises chargeback right under 4-214a.
  - No damages under the breach of transfer warranty.
  - May use breach of transfer warranty against whoever transferred the check to them. Allows push back of check to forger or first entity forger interacted with.

Forged drawer, bank properly dishonors.
Payor bank dishonors. Chargeback right used. Customer could put problem back on bank thru a breach of transfer theory, unless customer was the original payee of the check. First movement and last movement of the check are not transfers. First an issue, last a presentment. Therefore, the customer doesn’t get transfer warranties.
- Can sue on drawer’s contract.
- If forge someone else’s name, check treated as if forger signed own name, allowing enforcement against the forger. May sue as the drawer of the check on drawer contract.

Forged drawer, payor bank pays the check.
- Payor bank must recredit account. §4-401. Check with forged drawer’s signature is not a properly drawn check.
- No breach of a presentment warranty for a forged signature unless the other transferor knew of the forged signature. If knew, then breach of presentment, only the person who know can be hurt.
  - Price v Neil.
- Payor bank can come up with several theories, including fraud, 3-418 payment by mistake, quasi-contract theory under 3-414 contract of drawer, 3-403a?: treat forged check as if singed own name.
- Drawer of the check doesn’t make warranties since issuer of the check.

3-407(c) Payor bank paying a fraudulently
Transfer warranty.
Special Rules re Risk of Loss in Checking System

25.1: 3rd party forges indorsement on a lost check

- If say Cliff was not negligent, depositary bank loses in a forged endorsement case (assuming first party to deal with the forger). Once a forgery, no subsequent party can be a party authorized to enforce the instrument.
  o Chain of title is forever broken, so no warranty
  o Payor bank stuck with loss for forged drawer’s signature, since warrantor has no idea about the forged signature. Since wouldn’t know if the drawer’s signature is forged, payor bank would have to show a prior party had knowledge that the signature was forged in order to collect.
  o Cliff’s cause of action if not negligent: Payee of a stolen check.
    ▪ Payor bank not a refuge, since they don’t owe him anything.
    ▪ Claim of conversion. §3-420a, person taking the instrument who isn’t entitled to enforce the instrument.
    ▪ Sue payor bank for conversion and recover. Payor bank paid a party not entitled to enforce the instrument.
    ▪ If recover from payor bank on conversion theory, payor bank may claim of breach of presentment warranty. Early transferors would receive loss. Presentment warranties of payor bank passed back to first party dealing with the thief.

- If Cliff’s negligence substantially contributed to the forged signature:
  o Defendant is payor bank, depository bank: someone who bought instrument as a transferee
  o Intermediary banks between deposit get immunity under 3-420c
  o If bank exercises ordinary care, 3-406 states Cliff has no cause of action if negligence substantially contributes to making the unauthorized signature, precluded from conversion action against the bank. Forged endorsement, 3-420a, is lost, so no ability to recover on conversion action.
  o Can Cliff still recover against the drawer of the check. 3-310 states right to sue on underlying obligation until check is paid or dishonored. Once paid, the obligation goes away since can’t get paid twice. If check taken for obligation is dishonored, get the right to sue on the obligation.
  o Must be payee and deliveree of the instrument. 3-420: unless also receive delivery of the check, payee cannot sue.
  o 3-310b4: Cliff cannot collect on instrument. Even if not negligent, this section would prevent Cliff from needing to pay on the underlying obligation since the check may be in the hands of a lawful transferee and the payor shouldn’t be paid twice.
  o 3-309: Try to enforce instrument, but have to prove had instrument and provide adequate protection to the drawer so they do not have to pay twice. Indemnity bond standard.

- §3-110a: Look at intent of person signing as the issuer of the instrument. This intent stays even if the signor is not the intended person. So Cliff Janeway can claim that the money from the check may go to him.
- §3-420a: Conversion occurs when a person not entitled to enforce the instrument or a bank makes payment with respect to the instrument for a person not entitled to enforce the instrument or receive payment.
  o (ii): no action for conversion against acceptor of the instrument.
- §3-406: If negligently contributed to forgery through failure to exercise ordinary care, then cannot bring claim against bank cashing check (a) and loss may be allocated between precluded person and person asserting preclusion (b)
  o 3-103a9: Ordinary care: reasonable commercial standards. Comment 4: applies to people. Nothing intended to prevent a customer from proving procedures followed by bank are not reasonable.
25.2: Stolen checks

- A: Employee, no check-writing authority, writes check and forges signature, indorses, deposits, and withdraws.
  - If employer not negligent, §4-401a: A forged drawer’s signature or forged indorsement is not properly payable, so could go after bank for honoring the check. *Price v Neil:* payor bank stuck with loss if Gussie not negligent
  - If employer negligent, failure to exercise ordinary care would not require bank to recredit the account. §3-406a prevents ability to assert forgery and the check not properly payable.
    - Ex. leaving around a rubber stamp. 3-406 comment 1.
- §4-401a, Comment 1: A forged drawer’s signature or forged indorsement is not properly payable, so could go after bank for honoring the check. Bank may not require stop-payment order.
  - However, §3-406 indicates employer MIGHT be liable for not exercising ordinary care in safeguarding the check forms. (case 1) Triable fact.
  - §4-406 indicates employer should keep a close eye on the statement of accounts the bank gives to the business. (c) requires reasonable promptness in examining statement to determine whether any payment was not authorized.
  - §3-405 doesn’t occur since forger did not forge self as payee.
  - Important that employee doesn’t have authority to write checks
  - §3-404 doesn’t apply since no impostor (Gussie not pretending to be anyone else).

- B: Check issued to imposter. Forged indorsement
  - Classic forged endorsement case
  - Employer demand credit under properly payable rule, payor bank demands money under transfer warranty rule, passing it back.
  - 3-404a: Makes impostor’s signature enforceable: signature of payee by any person is enforceable by anyone acting in good faith. Employer would be stuck with the loss because the check becomes properly payable. Negligence by the party getting duped by the impostor, since that person in best position to prevent impostor from collecting.
  - §3-404 since impostor. (b) Since fictitious person, (1): whoever is in possession of the instrument is its holder. Bank goes after intended payee, intended payee goes after employer, who had best opportunity to determine there was a scam. (guy should call to make sure authorized agent legit, call and stop payment on check if tricked)

- C: Impersonator (same as above) passes on check to another
  - If employer negligent, substantially contributing to unauthorized drawer’s signature:
    - Can employer demand payor bank recredit account on a “not properly payable” theory:
      - 3-404b1: Person actually intended to be paid has interest in the instrument: Anyone’s signature as payee effective for fictitious person, so employer liable
      - 3-406a: Can’t assert forged drawer’s signature. Employer liable.
      - Forger’s intent becomes the relevant intent for payee. Employer stuck with loss.
  - If employer not negligent, then payor bank must credit account for forged drawer’s signature. Payor bank may pass the loss back on the presentment of warranty theory.
    - Forged endorsement:
      - 3-404b(i): Substantially effective for all purposes, so payor bank can’t assert forgery for breach of presentment warranty, so will hold the loss.
      - §3-404b(i) since impostor. (b) Since fictitious person, (1): whoever is in possession of the instrument is its holder. Bank goes after intended payee.
- **D: Impostor gets check, makes out to fictitious character**
  - If Spode not negligent, then 3-404 for forged endorsement.
  - If forged drawer’s signature, payor bank must recredit customer’s account since check not properly payable.
  - Payor bank will have presentment warranties, but can’t recover due to *Price v Nielson.*
    - Signature not treated as a fake for all effective purposes: to recover for presentment, have to show forgery that has been made ineffective due to the impostor rule of 3-404b(ii).
  - If employer negligent, which substantially contributed: 3-406 precludes any claim by employer.
    - 3-406a will not let him win on forged signature against bank for recredit. Forged endorsement will not work, 3-404b(ii) and b2: endorsement is effective, so Spode can’t use it as a reason to get the bank to recredit the account.

- **§3-404b(ii):**
  - Whoever has possession of instrument is holder,

- **E: Use of facsimile signature machine**
  - Don’t even need to enquire about negligence. Employee authorized to draft checks, so 3-402a indicates he has authority to draft checks and will be ok. Employer cannot complain 3-404b(i) and b2: drawer has no intent for drawee to have interest on check. Employer will be stuck with check unless can find the thief.
  - §3-402a: Person acting for Spode binds Spode by the signature. If unambiguous that check signed by Gussie rather than Spode, representative Gussie is liable on the instrument.
  - §3-404b(i) since impostor. (b) Since fictitious person, (1): whoever is in possession of the instrument is its holder. Bank goes after intended payee, intended payee goes after Spode, Spode may or may not be able to go after Gussie depending upon how check was filled out.

### NOTES
- Incomplete instruments completed by an unauthorized party: Payor bank has the right to pay the check and charge the customer’s account unless the payor bank has notice that the completion is unauthorized.
- **Payor bank limited to enforcing the check according to its original terms, not to the terms dictated by the third, fraudulent party.** Bank pays item as altered, can be made whole by using its presentment warranties to recover from any earlier party transferring the instrument after it was altered. **Account credited for the actual amount of the check.**
  - Transferors before the alteration are not insurers of the check, so do not need to worry about a subsequent change.

One party involved contributes to the making of an unauthorized signature.
- Previously, placed loss on the first party to interact with the wrongdoer. Exception when bank pays on a false signature, where put loss on payor bank, under *Price v Neil* since should know customer’s signature, although this is not sensical now.
- If one of the innocent parties was negligent in a way that contributed substantially to the loss, place the loss on that party rather than a non-negligent innocent party.

HSBC v F&M: do not need to fill a check out that covers all areas in order to satisfy “reasonable care” standard, sufficient that any alteration that was made was obvious.

- §3-406 only allows claim of negligence as a defense when the negligence leads to a forged signature.
- UCC depends on market forces to cause banks to develop cost-effective procedures for preventing loss. However, banks taking the initiative by adopting a new procedure departing from general banking may enhance likelihood the bank would be held liable for any losses that ensue.
- Forgery cases: must notify bank within one year after the bank’s statement covering the checks in question was made available to the payor. This length of time may be limited by agreement (one state said 60 days acceptable).
- **Bank-statement Rule:** customers can stop extended forgery schemes by the simple expedient of promptly reviewing their bank statements.
- **Stowell v Cloquet Co-op Credit Union**: Forger removed all credit statements from victim’s mail for a year while writing false checks. Account holder must exercise reasonable promptness in examining his or her account statements and notifying the bank of any forged checks. §4-406c. Duty of sending a statement ends when bank puts statement in the mail, so risk of nonreceipt falls on customer.

- **Employee Forgery**: When an employee forges employer’s indorsement on a check payable to the employer, either the general negligence rule or the bankstatement rule places such a loss on the employer. But when loss is caused by a responsible employee, §3-405 places loss on employer even if more general rules do not apply.
  - **Cable Cast Magazine v Premier Bank**: Employee cashed checks intended for employer in her account. When a depositary of money pays on a forged check, it is liable for the amount of the checks, but §3-405, applying to fraudulent indorsements by employees places risk of loss on the employer if the bank was not negligent in the transaction, since the employer is in a better position to avoid the loss by carefully choosing employees and supervising them. Depositing checks payable to the company in the employee’s account does not create bad faith on the part of the bank when employee claimed they are a representative, and had not reserved rights in the name. §3-103a7: reasonable care is reasonable commercial standards.
  - **Halifax Corp v Wachovia**: In case where customer was a high profile customer at bank due to the abnormal size of the checks, and bank knew depositor was company’s comptroller, §3-406 does not create an affirmative cause of action on behalf of the bank.
    - §3-404 & 5 may be utilized by a drawer against the depositary bank in a double forgery situation.

- **Impostors/Fictitious People**: 3-404a state loss should be allocated to the person that was victimized by the fraud, since others farther down the chain had no opportunity to prevent the loss.
  - **Meng v Maywood Proviso State Bank**: Where a named payee is a fictitious person, then the indorsement by any person in the name of the payee is effective as the indorsmeent of the payee. One named payeesufficient to receive money for the check.
    - 3-110d: identify the person to whom an instrument is payable: if payable to 2+ people alternatively, may be paid to any of them.
    - An enforceable contract arises when a cashier’s check is purchased and the contract calls for the issuing bank to pay instrument. Accompanied by implied contract that issuing bank promises to pay cashier’s check to the named payee only.