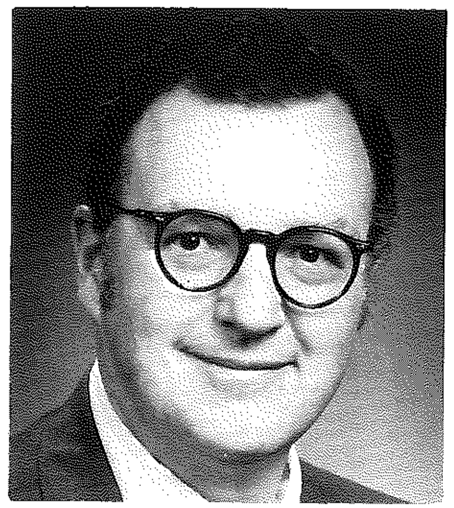
The New UCC Articles 3 and 4: Impact on Banking Operations

Alvin C. Harrell, *Oklahoma City University School of Law*
Frederick H. Miller

The New UCC Articles 3 and 4: Impact on Banking Operations

By Alvin C. Harrell and Fred H. Miller



Alvin C. Harrell is Professor of Law at Oklahoma City University School of Law, of Counsel to the Oklahoma City law firm of Pringle & Pringle, and President of Home Federal Savings and Loan Association of Oklahoma City. He is coauthor of several books, including THE LAW OF MODERN PAYMENT SYSTEMS AND NOTES (2d. ed. 1992) (with Professor Fred H. Miller). Professor Harrell is also Chair of the Publications Subcommittee of the Consumer Financial Services Committee of the Section of Business Law of the American Bar Association. He chairs an ABA UCC Committee Task Force on Oil and Gas Finance, and serves on the Governing Committee of the Conference on Consumer Finance Law.

Fred H. Miller is Professor of Law, Kenneth McAfee Centennial Professor, and George Lynn Cross Research Professor at the University of Oklahoma. He serves on the drafting committee of the National Conference of Commissioners on Uniform State Laws (NCCUSL) and American Law Institute (ALI) that prepared the new Articles 3 and 4 of the Uniform Commercial Code (UCC). He is coauthor of several books, including THE LAW OF MODERN PAYMENT SYSTEMS AND NOTES (2d. ed. 1992) (with Professor Alvin C. Harrell), and was recently elected Executive Director of the NCCUSL.

I. Introduction

A. Purpose and Scope

The first revision of Articles 3 and 4 of the Uniform Commercial Code ("UCC" or the "Code") since those Articles were promulgated in the 1950s occurred in July of 1990 when the National Conference of Commissioners on Uniform State Laws ("NCCUSL") and the American Law Institute ("ALI") approved the final draft of the revision of these UCC articles.[1] The purpose of this revision was to resolve ambiguities and deficiencies in the previous text, to make certain substantive changes in the law, and to update the Code to reflect modern technology and business practices.[2] While largely evolutionary, the changes are quite significant. It is expected that the revisions will have immediate effect, even in states that have not yet enacted them, as an authoritative statement of the law.[3]

The scope of Article 3 was expanded in certain important ways.[4] All fully negotiable instruments covered by the previous version remain within the scope of the new Article 3. In addition the definition of "negotiable instrument" at old section 3-104 was expanded to include any "unconditional promise or order to pay a fixed amount of money,"[5] specifically including adjustable interest rate instruments,[6] instruments containing the notice required by the FTC holder in due course rule[7] or similar state or federal law,[8] non-recourse notes,[9] and checks which are not payable to order or

1. Unless denoted otherwise, references to the UCC in this article are references to the 1990 Uniform Text. Generally, these are labeled the "Revised" sections; earlier versions are referred to as the "Old" sections.

2. Parts I-III of this article provide an overview of the 1990 UCC Article 3 and 4 revisions. Parts IV-X discuss many of these issues in greater detail.

3. *See, e.g.*, Goss v. Trinity Sav. Loan Ass'n, 813 P.2d 492 (Okla. 1991), as described *infra* at note 6. As of August 1, 1993 the following 29 states have adopted Revised Articles 3 and 4: Alaska, Arizona, Arkansas, California, Connecticut, Florida, Hawaii, Idaho, Illinois, Indiana, Kansas, Louisiana, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oklahoma, Oregon, Pennsyvania, Utah, Virginia, Washington, West Virginia, and Wyoming.

4. This expansion is not sufficient to change the result in cases like Ramirez v. Bureau of State Lottery, 463 N.W. 2d 245 (Mich. Ct. App. 1990), where a person sought to claim the benefits of an allegedly lost lottery ticket by using the Article 3 rules governing lost instruments. The court correctly concluded that a lottery ticket is not a negotiable instrument governed by Article 3. This case is discussed in the 1992 Annual Survey of the Uniform Commercial Code in *The Business Lawyer*, which noted that the *Ramirez* court missed an opportunity to explain that Lord Mansfield settled this issue over 200 years ago when he concluded that a lottery ticket is wholly unlike a negotiable instrument. *See* Robert G. Ballen, Joseph P. Savage, and Stephen C. Veltri, *Commerical Paper, Bank Deposits and Collections, and other Payment Systems*, 47 Bus. Law. 1551, 1558 (1992) [hereinafter "*1992 Annual Survey*"], citing Miller v. Race, 97 Eng. Rep. 398, 402 (1758). *See also* discussion *infra* at Part III.

5. Revised § 3-104(a). In Farha v. F.D.I.C., 963 F.2d 283 (10th Cir. 1992) the court took judicial notice of revised § 3-104(j) in concluding that a certificate of deposit is "essentially a promissory note." *Cf.* cases cited *infra* at note 63, discussing the nature of a certificate of deposit.

6. Revised § 3-112(b). In Goss v. Trinity Savings & Loan Association, 813 P.2d 492 (Okla. 1991), the Oklahoma Supreme Court held that a variable rate note was negotiable even under Old Article 3. For this, the court received praise in the 1992 Annual Survey of the Uniform Commerical Code in *The Business Lawyer*. *See* the *1992 Annual Survey*, *supra* note 4 (also noting that most cases are to the contrary). *See also*, Amberboy v. Societe de Banque Privee, 831 S.W. 2d 793 (Tex. 1992) (same as *Goss*); Carnegie Bank v. Shalleck, 606 A.2d 389 (N.J. 1992) (following *Goss* and applying the Article 4 revisions retroactively). *Cf.* Taylor v. Roeder, 360 S.W. 2d 191 (Va. 1987) and Doyle v. Trinity Sav. & Loan Ass'n, 940 F.2d 592 (10th Cir. 1991), *vacating* 869 F.2d 558 (10th Cir. 1989). *Doyle*, originally holding that variable rate notes are not negotiable, was vacated subsequent to the decision in *Goss*.

7. 16 C.F.R. § 433 (1990).

8. Revised § 3-106(d). Although the new Article 3 otherwise applies, there can be no holder in due course of such an instrument. *Id.* *See also* Revised § 3-104(d).

9. Revised § 3-106(b)(ii).

bearer.[10] The latter are not only subject to Article 3; they are treated as negotiable instruments even though they lack the traditional words of "negotiability."[11]

In effect the new Article 3 expands both the scope of Article 3 (to cover a range of previously nonnegotiable instruments such as checks not payable to order or bearer) and also the concept of negotiability (to include, for example, adjustable interest rate notes). For example as previously noted, an instrument is not rendered nonnegotiable (by reason of being conditional) merely because it is limited to payment from a specific fund;[12] as a result a non-recourse note can be negotiable.

A promise or order other than a check can be made nonnegotiable, however, by the addition of a "conspicuous statement . . . to the effect that the promise or order is not negotiable or is not an instrument governed by Article 3."[13] In addition the Official Comments to Revised section 3-104 specifically permit the parties to "contract into" Article 3 for instruments not otherwise covered.[14] The result is an expanded range of instruments subject to the rules governing negotiability and potentially creating a holder in due course, plus coverage of an expanded range of other instruments not subject to the holder in due course rules yet otherwise governed by Article 3.

For the first time there are specific definitions of "cashier's check" and "teller's check"; ordinary money orders are placed within the definition of "check."[15] Among other things this means that money orders will be treated as ordinary checks, and not as the equivalent of a cashier's check, for purposes of such things as stopping payment.[16] Revised Article 3 also clarifies the coverage of traveler's checks.[17]

II. Overview of Significant Changes -- Article 3

A. Limitation Periods

Revised section 3-118 provides a series of limitation periods for bringing actions under Article 3. For example, an action to enforce a term note must be brought within six years after the due date or the date of acceleration.[18] An action on a demand note must be brought within six years after demand; in the absence of demand, suit is barred if there has been no payment of principal or interest for a continuous period of ten years.[19] An action to enforce an unaccepted draft must be brought within six years after dishonor or within ten years after the date of the draft, whichever comes first.[20] An accepted draft is subject to a six year limitations period.[21]

An action to enforce a cashier's check, teller's check, certified check, or cashier's check must be brought within six years after demand for payment.[22] Certificates of deposit are subject to a similar six year bar.[23] Other actions under Article 3, including an action for breach of warranty or conversion, are governed by a three year limitation period.[24]

B. Breach of Fiduciary Duty

Revised 3-307 governs instruments payable to and taken from a corporate officer, trustee, or other fiduciary where that status is known.[25] If an instrument is payable to a corporation, trust, or fiduciary, the transferee will have notice of a breach of fiduciary duty if the instrument is taken in payment of or as security for a personal debt known to be such by the taker of the instrument from a corporate officer, trustee or other fiduciary or in a transaction otherwise known to benefit the fiduciary personally or if it is deposited to a nonfiduciary account (including, of course, a personal account of the corporate representative, trustee, or other fiduciary).[26]

The fact that an instrument is drawn by a corporation or a fiduciary acting as such does not give notice of any breach of duty, even if the instrument is made payable to the fiduciary in an individual capacity.[27] However if the instrument is drawn by the corporation or fiduciary to the transferee as payee, the transferee is on notice of a breach of fiduciary duty if it is taken in payment of or as security for a personal debt of the fiduciary known to be such by the taker or in a transaction known to benefit the fiduciary personally or is deposited to a nonfiduciary account. Therefore, for example, a bank accepting a check drawn on a corporate account and payable to the bank, for deposit to a personal account of a known corporate representative, takes with notice

10. Revised § 3-104(a), (c). Ordinary money orders fall within the definition of a "check" and are therefore subject to a stop payment order. *See* § 3-104(f), § 4-403, and *infra* note 365. Notes not payable to order or bearer remain nonnegotiable, and are entirely excluded from Revised Article 3. *Cf.* Old § 3-805, and *see* F. MILLER AND A. HARRELL, THE LAW OF MODERN PAYMENT SYSTEMS AND NOTES paras. 1.02[2] and 2.02[7][b] (2d Ed. 1992) [hereinafter Miller & Harrell).

11. *See* Revised § 3-104(c); Miller & Harrell, *supra* note 10.

12. Revised § 3-106(b)(ii); Miller & Harrell, *supra* note 10, para. 2.02[3][c].

13. *See* Revised § 3-104(d) and Comment 3. *See also* First Nat'l Bank of Nocona v. Duncan Sav. & Loan Ass'n, 656 F. Supp. 358 (W.D. Okla. 1987).

14. *See* Revised § 3-104, Comment 2; Miller & Harrell, *supra* note 10, para. 2.01[3][a]. Thus the parties to a separate guarantee, for example, may wish to consider whether they prefer the Article 3 rules on suretyship or the common law rules, and to the extent the Article 3 rules are preferred, contract for those rules even though the separate guarantee is not otherwise subject to Article 3.

15. *See* Revised § 3-104(f), (g), and (h), and Duggan v. State Bank of Antioch, 540 N.E. 2d 1111 (Ill. App. Ct. 1989), *appeal denied*, 545 N.E. 2d 108 (Ill. 1989). *Cf.* Unger v. NCNB Nat'l Bank, 540 So. 2d 246 (Fla. Dist. Ct. App. 1989). For further discussion *see infra* Parts VI.c and X.

16. This is particularly significant considering Revised § 3-411. *See also infra* Parts II. H. and X. (on cashier's checks); *infra* Parts III.D.5 and X.D. (on stop payment orders); Miller & Harrell, *supra* note 10, para. 6.03[7].

17. *See* Revised §§ 3-104(i) and 3-106(c) and Comment 2 to 3-106(c). *See also* Thomas C. Cook, Inc. v. Rowhanian, 700 S.W. 2d 672 (Tex. Ct. App. 1985); Xanthopoulos v. Thomas C. Cook, Inc., 629 F. Supp. 164 (S.D. N.Y. 1985); Miller & Harrell, *supra* note 10, para. 1.01[3][c].

18. Revised § 3-118(a). *See generally*, Miller & Harrell, *supra* note 10, para. 6.03[7]. *See also infra* Part VII.B.

19. Revised § 3-118(b). As noted in Comment 1 to § 3-118, the section does not state all rules with respect to limitations, such as the circumstances under which the statute may be tolled. *See also infra* Part III.D.2. *See, e.g.*, Karlton v. Jenkins, 587 A.2d 580 (Md. 1991) (limitations period tolled by letter from payee stating that he would not make demand for one year).

20. Revised § 3-118(c).

21. Revised § 3-118(f).

22. Revised § 3-118(d). Notice the absence of money orders from this list. They normally are treated as personal checks under Revised § 3-104.

23. Revised § 3-118(e). *See also infra* note 63.

24. Revised § 3-118(g). *Cf.* Revised § 4-111 (three year limitation period for actions under Article 4). *See* discussion *infra* text at Part III.D.2.

24. Revised § 3-118(g). *Cf.* Revised § 4-111 (three year limitation period for actions under Article 4). *See* discussion *infra* text at Part III.D.2.

Shupe & Yost v. Fallon Nat. Bank, 847 P.2d 720 (Nev. 1993), held that payment by a payor bank on a forged indorsement is conversion governed by the statute of limitations for a tort action (rejecting Citizens State Bank v. National Sur. Corp., 612 P.2d 70 (1980).). In Walker & Walker, Inc. v. Liberty National Bank and Trust Company, No. 75,600 (Sup. Ct. Okla. May 11, 1993), the Oklahoma Supreme Court held that a cause of action for payment of a forged check arises not when the check was processed and paid; but when the customer whose account was charged discovers the error and makes demand for payment. This case seems clearly incorrect, quite aside from the parties' failure to raise the § 4-406 issues. *See infra* Parts II.C. and IX.

25. *See* Revised § 3-307(a) and (b); Miller & Harrell, *supra* note 10, paras. 3-02[3][b][iii] and para. 3.03[2][2][iv]. *See also infra* Part IV.B, noting Revised § 3-110(c)(2)(i) and Old § 3-117(b) (identification of party entitled to payment).

26. Revised § 3-307(b)(2).

27. Revised § 3-307(b)(3). The Uniform Fiduciaries Act may also be helpful to a bank in these circumstances, so long as the item is paid in a manner consistent with the fiduciary's indorsement. *See, e.g.*, Lehigh Presbytery v. Merchants Bancorp., Inc., 600 A.2d 593 (Pa. 1991).

of a possible breach of fiduciary duty and cannot be a holder in due course.[28]

C. Payment on a Forged Indorsement

A payee of a check that has been paid on a forged indorsement (after the payee has lost possession of the instrument) has a cause of action against the depositary or payor bank for conversion.[29] A payee who did not receive possession has no right of action for conversion.[30] Nor does the maker, drawer, or acceptor have an action for conversion of an instrument paid on a forged indorsement.[31] A payee who has an action for conversion as noted above does not have a right of action against the drawer or maker on the underlying obligation.[32] Regarding the relationship between a customer and the payor bank that pays on a forged indorsement, *see infra* Part IX.

D. Personal Liability for Representative Capacity

The rules governing personal liability for a signature in a representative capacity were generally restated, but with two significant changes: Revised section 3-402(c) provides that a representative can always establish that there was no intent to create liability, except as against a holder in due course, and that an authorized signature of a representative on behalf of the principal on a check does not result in personal liability of the representative even if the representative capacity is not indicated.[33]

E. Lack of a Required Signature

If an instrument requires more than one signature to constitute the signature of an organization, and one of the required signatures is missing, the instrument is treated as if it was drawn with an unauthorized signature.[34]

F. Forgery by an Employee

Revised section 3-405 contains a new provision that makes employers responsible for forgeries of the employer's instruments by employees in certain circumstances. If an employer has entrusted the employee "with responsibility with respect to the instrument" as part of the employee's duties, then any forgery of an indorsement by the employee will be treated as an effective indorsement.[35] Most of the relevant terms in this provision (including "responsibility" with respect to the instrument) are defined at subsection 3-405(a).

However, if the bank (or other party) paying the instrument or taking it for deposit failed to use ordinary care and that failure substantially contributed to the loss, the bank is liable for the loss to the extent that the failure contributed to the loss.[36] For example, if a depositary bank allows the employee to deposit checks with forged indorsements in a "sham" corporate account established for this purpose, without requiring proper documentation for opening a corporate account, the bank's failure to exercise ordinary care may have contributed to the loss. *See also* Revised section 3-307 (notice of fiduciary duty), discussed *supra* at Part II.B.

G. Breach of Warranty; Restitution

The transfer warranties have been moved to Revised section 3-416; the presentment warranties are provided separately at Revised section 3-417. A new provision permits a person sued by the drawee for breach of warranty to assert a defense based on the drawer's inability to assert the forgery or alteration against the drawee because of a preclusion under Revised sections 3-406 or 4-406.[37]

Revised section 3-418 is clarified to provide that a drawee (called the "payor bank" in Article 4) who has made final payment may have a right to rescind the payment and recover in restitution.[38] This is a codification of the common law rule of restitution and represents the incorporation of that rule as a supplement to the final payment rules in Article 4. There is a somewhat similar but slightly more narrow supplement to the rule making a bank accountable for a failure to make final payment or dishonor before its midnight deadline, at Revised section 4-302(b).[39]

28. Revised § 3-307(b)(4). Comment 5 provides an example which is close to the facts of Eldon's Super Fresh Stores, Inc. v. Merrell Lynch, Pierce, Fenner & Smith, Inc., 207 N.W. 2d 282 (Minn. 1973). *See* Miller, *The Benefits of New UCC Articles 3 and 4*, 24 U.C.C. L.J. 99, 116-17 (1991). Citizens Fidelity Bank & Trust Co., 472 N.W. 2d 198 (Neb. 1991), applied the Ohio Uniform Fiduciaries Act to conclude that a depositary bank breached its duty of good faith when it allowed a corporate bookkeeper to deposit corporate checks payable to the bank into the bookkeeper's personal account. The court concluded that this was "commercially unjustifiable." *Citizen's Fidelity Bank* is noted in the *1992 Annual Survey, supra* note 4, at 1562-63 (noting that the case was decided under Old Article 3 but anticipated the 1990 revisions).

29. Revised § 3-420(a); Miller & Harrell, *supra* note 10, para. 7.03[3]; Shupe & Yost v. Fallon Nat. Bank, 847 P.2d 720 (Nev. 1993) (payment of item by payor bank on forged indorsement governed by tort statute of limitations). The cause of action accrues when action inconsistent with the owner's rights to the instrument is taken, regardless of when the loss is discovered. *See, e.g.*, Husker News Co. v. Mahaska State Bank, 460 N.W. 2d 476 (Iowa 1990), and other cases cited in the *1992 Annual Survey, supra* note 4, at 1569 nn. 138-39. A recent case to the contrary, Walker & Walker, Inc. v. Liberty National Bank and Trust Co., No. 75,600 (Sup. Ct. Okla., May 11, 1993) is clearly incorrect. *See also infra* Part IX.

30. Revised § 3-420(a), and Comment 1. *See also* Lund v. Chemical Bank, 760 F. Supp. 51 (S.D. N.Y. 1991), *aff'g* 665 F. Supp. 218 (S.D. N.Y. 1987), *rev'd on other grounds*, 870 F.2d 840 (2d Cir. 1989) (payee can sue in conversion for payment of a check on a forged indorsement only if the check was delivered to the payee); C.A.L., Inc. v. Worth, 813 S.W. 2d 12 (Mo. Ct. App. 1991) (remitter of cashier's check is not the owner of the instrument and hence cannot sue depositary bank in conversion for taking check on a forged indorsement); *1992 Annual Survey, supra* note 4, 1563-64.

31. Revised § 3-420(a).

32. *See* Revised § 3-310(b)(4) and Comment 4. *See also* Revised § 3-309.

33. *See* Revised § 3-402(c), and *infra* Part VI.A. This is a departure from prior law. *See, e.g.*, Jackson Chevrolet, Inc. v. Oxley, 564 P.2d 633 (Okla. 1977); Tom L. Holland, *Corporate Officers Beware - Your Signature on a Negotiable Instrument May be Hazardous to Your Economic Health*, 13 Indiana L. Rev. 893 (1980); F. MILLER & A. HARRELL, THE LAW OF MODERN PAYMENT SYSTEMS AND NOTES para. 5.03 (1985) [hereinafter "*Modern Payment Systems*, first edition"]. This rule does not apply to a promissory note. *See generally*, Miller & Harrell, *supra* note 10, para. 5.03[2], [3]; Greenberg, Rhein & Margaolis, Inc. v. Norris-Faye Horton Enters., 588 A.2d 185 (Conn. 1991); Central Ill. Public Serv. Corp. v. Molinarolo, 585 N.E.2d 199 (Ill. 1992).

34. Revised § 3-403(b); Miller & Harrell, *supra* note 10, para. 5.03[1]. *See also* Knight Communications, Inc. v. Boatman's Nat'l Bank, 805 S.W.2d 199 (Mo. Ct. App. 1991); American Ins. Co., v. Fidelity Bank & Trust Co., 583 A.2d 361 (N.J. Super. Ct. App. Dist. 1990); Smith, Barney, Harris Upham & Co. v. Citibank, 556 N.Y. S.2d 61 (N.Y. App. Div. 1990). These cases are collected in the *1992 Annual Survey, supra* note 4, at 1567 n. 123, which also reports that this was the law in Arkansas, Florida, Louisiana, Michigan, New Jersey, New York and Wisconsin, with cases to the contrary in the District of Columbia, Illinois, California and Maryland. *Id.*, citing cases collected in *Knight Communication*, 805 S.W.2d at 201. The rule should now be uniform in all states that have adopted Revised Article 3.

35. Revised § 3-405(b). This appears to be a variation or extension of the imposter and other preclusion rules at Old § 3-405. "Responsibility" is defined at Revised § 3-405(a)(3). "Employee" includes an independent contractor and its employeer. Revised § 3-405(a)(1). *See* Miller & Harrell, *supra* note 10, para. 4.02[2][a] and para. 7-03[3][c]; discussion *infra* at Part VI.A.

36. Revised § 3-405(b). This mirrors the other preclusion rules. *See* Revised §§ 3-404, 3-406, and 4-406. On the latter *see infra* Part VI.A. Ordinary care is determined under a new definition at Revised § 3-103(a)(7) that incorporates "observance of reasonable commercial standards."

37. *See* Revised § 3-417(c).

38. Revised § 3-418. This applies to payor banks, resolving an uncertainty under prior law. *See* Revised § 3-418, Comment 4; Revised § 4-301, Comment 7; *Modern Payment Systems*, first edition, *supra* note 33, at 221-222. *See* further dicussion of this issue and Revised § 4-215 *infra* at Part VIII.D. *See also* Miller & Harrell, *supra* note 10, para. 3.03[3][b], and para. 8.20[4].

39. The old rules on accountability suggested that once a payor bank became accountable for an item it lost any claim for restitution. *See* Old § 4-302, and *Modern Payment Systems*, first edition, *supra* note 33, at 221-222. However, the courts did not always agree, *see, e.g.*, Bank Leumi Trust Co. v. Bally's Park Place, 528 F. Supp. 349 (S.D. N.Y. 1981) (allowing recovery by the payor bank on restitutionary grounds where the item was presented with intend to defraud the bank). The Article 4 revisions adopt the latter view and permit rescission and restitution by a payor bank that otherwise would be accountable under Revised § 4-302(a). *See* Revised § 4-302(b); Miller & Harrell, *supra* note 10, para. 8.02[4]. This should permit a payor bank to defend itself (or proceed) against a check kiter or other holder who presents an item with knowledge that it is not drawn on sufficient funds. *See also* Revised § 3-418, Comment 4, and Revised § 4-301, Comment 7; *infra* Part VIII.

H. Dishonor of a Cashier's Check

A new provision at Revised section 3-411 seeks to resolve confusion over the ability of a payor bank to refuse payment of a cashier's check or similar instrument.[40] Unlike the drawer of a personal check or personal money order (signed by the customer or purchaser as drawer), the bank customer who procures the cashier's check (sometimes called the "remitter," apparently because he or she typically remits the instrument in payment of an obligation) does not sign as drawer and has no right to stop payment or to order the bank to do so,[41] and if the bank wrongfully refuses to pay a cashier's check or similar instrument (*e.g.*, on grounds of an asserted customer stop payment order), the bank may be liable for expenses, loss of interest and consequential damages. However, Revised section 3-411 precludes recovery of legal costs or consequential damages from the bank if the bank refuses payment because it has suspended payments, the bank itself has a defense it reasonably believed was good against the holder,[42] there was doubt as to the identity of the holder, or if payment is prohibited by law.[43] While this does not specifically permit a payor bank to refuse payment of its own cashier's checks, the effect is to allow the bank to refuse payment in any of these four circumstances without risk of liability for the cost of opposing counsel fees or consequential damages.[44]

Conversely, where a bank *wrongfully* refuses to pay a cashier's or certified check or wrongfully stops payment on a teller's check or refuses to pay one that is dishonored, the bank is liable for expenses and loss of interest.[45] In addition, if the bank *wrongfully* refuses to pay after receiving notice of the holder's particular circumstances giving rise to consequential damages, the bank may be liable for those consequential damages.[46]

The revisions confirm the *Malphrus* rule that a bank cannot (with a very narrow exception for theft) assert claims of a third party (*e.g.*, its customer) against the holder of the instrument.[47] The rules of Old section 3-306(d) precluding assertion of third party claims (now clarified and expanded at Revised section 3-305) still apply.[48] But Revised section 3-411 reduces the risk to a bank of asserting its own claims or defenses as a basis for dishonor, by offering a clear rule on this aspect of the situation.

Interestingly, the inclusion of personal money orders within the definition of an ordinary check (at Revised section 3-104(f)) rather than inclusion as a form of cashier's check (at section 3-411) means that such money orders are subject to customer stop payment orders and can be dishonored like an ordinary check.[49] This applies only to money orders signed by the purchaser as drawer; of course a bank money order or similar bank draft (drawn by the issuing bank) would be treated as a cashier's or teller's check.

I. Lost or Stolen Bank Checks

Another problem that was addressed in the revisions is illustrated by *Santos v. First National State Bank*,[50] where an (allegedly) unindorsed cashier's check was lost in the mail. When the issuing bank refused to reimburse the customer without a bond to protect it against double payment (in case the check had been indorsed in blank and came into the hands of a holder in due course), the customer sued. The court reached a practical result by ordering the bank to issue a certificate of deposit in the plaintiff's name for the amount of the missing cashier's check, at the highest prevailing rate of interest for such a deposit; the bank was allowed to hold the certificate (with the interest payable quarterly to the plaintiff) until the statute of limitations on the missing check had run. While this reflected a practical approach, it froze the plaintiff's funds and revealed the need for a better statutory solution. Revised section 3-312 provides this by permitting the remitter or other claimant to file a "declaration of loss" with the issuing bank; this requires the bank to refund the purchase price and to refuse payment of the check on or after the 90th day after issuance.[51] The right to file a "declaration of loss" is not a general right to stop payment on a cashier's check, though in the limited circumstances covered by Revised section 3-312 the result may be much the same.[52]

J. Alteration of a Certified Check

Another issue that was answered in the revisions relates to alteration of a previously certified check. Under Revised section 3-413, if an ordinary check is certified (or if a draft is "accepted") for a certain amount and is then altered to a higher amount and passed to a holder in due course, there is a two-pronged rule to allocate the resultant loss.[53]

If the certification (or acceptance) "states the amount certified" (or accepted), the obligation of the certifying bank (or acceptor) is limited to that amount. If, on the other hand, the certification (or acceptance) does not state an amount, and the amount is then raised and the instrument is negotiated to a holder in due course, the certifying bank (or acceptor) is liable for the amount of the instrument (as altered) at the time it is taken by the holder.[54]

40. This also covers teller's checks and certified checks. *See* Revised § 3-411(a), (b). It does not incude ordinary money orders, which are treated as personal checks. *See* Revised § 3-104(f).

41. *See e.g.*, Malphrus v. Home Savings Bank, 254 N.Y. S.2d 980 (Co. Ct. 1965); University Sav. Ass'n v. Intercontinental Consol. Companies, 751 S.W.2d 657 (Tex. App. Hous. 1. Dist. 1988); Hotel Riveira, Inc. v. First Nat'l Bank & Trust Co., 768 F.2d 1201 (10th Cir. 1985). Farmers & Merchants State Bank v. Western Bank 841 F.2d 1433 (9th Cir. 1987); TPO, Inc. FDIC, 487 F.2d 131 (3d. Cir. 1973); Bank One, Merrillville, N.A. v. Northern Trust Bank/DuPage, 775 F. Supp. 266 (N.D. Ill., 1991); First Financial L.S.L.A. v. First American Bank and Trust Co., 489 So. 2d 388 (5th Cir. 1986); Warren Finance v. Barnett Bank of Jacksonville, N.A., 552 So.2d 194 (Fla. 1989); *Modern Payment Systems*, first edition, *supra* note 33, at 247. *But see* Revised § 3-312, and discussion *infra*. *Cf.* Revised § 4-403; Miller & Harrell, *supra* note 10, para. 9.01[4][d]. In C.A.L., Inc. v. Worth, 813 S.W.2d 12 (Mo. Ct. App. 1991), the court concluded that the remitter could not sue the depositary bank in conversion for handling a cashier's check on a forged indorsement, because the remitter was not the owner of the check. *See also* discussion *infra* Part X; Comment 2 to Revised § 3-201.

42. This apparently is intended to reject the approach of cases like Hotel Riviera, Inc. v. First Nat'l Bank & Trust Co., 768 F.2d 1201 (10th Cir. 1985), and (to some extent) Yukon Nat'l Bank v. Modern Builders Supply, Inc., 686 P.2d 307 (Okla. Ct. App. 1984), which illustrate the unjustified tendency of some courts to deprive banks of legitimate defenses in such cases. In essence this adopts the view of better reasoned cases such as TPO, Inc. v. FDIC, 487 F.2d 131 (3d Cir. 1973); *see also Modern Payment Systems*, first edition, *supra* note 33, at 248-50; Miller & Harrell, *supra* note 10, para. 9-01[4][d]; *infra* Part X.

43. Revised § 3-411(c).

44. *See* Revised § 3-411 and the Official Comment.

45. Revised § 3-411(b). *See* Miller, *The Benefits of New UCC Articles 3 and 4*, 24 U.C.C. L.J. 99, 110 (1991).

46. *Id.*

47. *See* Revised § 3-305(a), (c), and (d); *Malphrus*, 254 N.Y. S.2d 980; and *supra* note 41. *See also infra* Part X.B, and cases collected *id.* at note 382.

48. *See, e.g.*, Revised § 3-305(a), (c), and (d). *See also* Revised § 3-602(b)(1)(ii).

49. *Cf.* Garden Check Cashing Service, Inc. v. First Nat'l City Bank, 25 A.D.2d 137, 267 (N.Y. S.2d 698 (1966), *aff'd on opinion below*, 223 N.E.2d 566 (1966). *See also infra* Part X.

50. 35 U.C.C. Rep. Serv. 518 (N.J. App. Div. 1982).

51. *See infra* Part X.C.; Miller & Harrell, *supra* note 10, para. 9.01[4][d][v].

52. *Cf.* the limited scope of Revised § 3-312 with § 4-403 (either version), permitting a customer to stop payment for any reason whatsoever.

53. *See* Revised § 3-413(b); Miller & Harrell, *supra* note 10. 4-04[2][b].

54. *Id.*

K. Suretyship and Accommodation Parties

The rules governing the rights and liabilities of accommodation parties are combined and clarified at Revised section 3-419.[55] Among other things, these rules specify that an instrument is enforceable against the accommodation party regardless of whether he or she received consideration.[56]

Companion revisions were made at Revised section 3-605, dealing with discharge of sureties for impairment of collateral and other action. These revisions provide for discharge of liability of the surety by an extension of the due date or other material modification of the obligation, or an impairment of collateral by the creditor without consent of the surety, notwithstanding a reservation of rights in the instrument.[57] However, in these circumstances there is no discharge, unless the creditor knew or had notice of the accommodation, there is no discharge if the surety has consented to the subject event or if the surety has signed a written waiver of discharge,[59] and any discharge is only to the extent of established loss.

III. Overview of Significant Changes -- Article 4

A. Definitions and Basic Concepts

1. Holder Status of Depositary Bank

Revised section 4-205 permits a depositary bank to be a holder (and therefore potentially a holder in due course) even though it takes without indorsement, if its customer (the depositor) was a holder of the item at the time of deposit.[60] These changes are particularly important in view of the potential for loss resulting from the required funds availability schedule under federal Regulation CC,[61] *e.g.*, the bank may have had to pay out uncollected funds under federal law and in such case holder in due course status may enhance the bank's ability to recover from the drawer or indorser. If the bank itself then negotiates the item, a payor bank should not return the item for lack of indorsement. There is a warranty under section 4-205(b) that later takers and payers may rely upon.

Also, in UCC Article 1, an addition to Revised section 1-207(2) provides that the rules on reservation of rights in an instrument (such as "paid under protest") do not apply to an accord and satisfaction.[62]

2. "Account"; "Item"; "Bank"

The definition of "account" at Revised section 4-104(a)(1) has been clarified to include any "deposit or credit" account, including a "demand, time, savings, passbook, share draft, or like account" other than a certificate of deposit.[63] The previous definition did not clearly include credit accounts and contained a shorter list of examples. Instruments written on home equity lines, for example, are now clearly within provisions of Article 4 governing "accounts."

The definition of "item" at Revised section 4-104(1)(h) was narrowed in one respect. The definition now excludes specifically "a payment order governed by Article 4A or a credit or debit card slip."[64] In another respect, however, its scope was clarified to include any "promise or order to pay money handled by a bank for collection or payment," in addition to "instruments."[65] Revised sections 4-104(b) and (c) contain an index to other relevant definitions in Revised Articles 3 and 4. Revised section 4-105(1) also contains a clarified definition of "bank," which now specifically includes savings banks, savings and loan associations, and credit unions. The term "depositary bank" means the first bank "to take" an item, even if it is also the payor bank, "unless the item is presented for immediate payment over the counter."[66]

3. Payable-Through Drafts

The provisions on "payable through" drafts at Revised section 4-106 have been completely rewritten. The new language provides that where an item is "payable through" a designated bank, that bank is a

55. *See also* Revised §§ 3-305(d) and 3-605.

56. Revised § 3-419(b). This should reduce the common, and nearly always spurious, arguments regarding consideration that are routinely made by sureties in these cases. *See, e.g.*, A. Harrell & J. Norton, *Fundamental Legal Considerations Respecting Accommodation Parties, Guarantors and Sureties*, 25 Bull. Sect. Bus. Law (Tex. Bar Assoc.) No. 4, at 1 (June 1988); Miller & Harrell, *supra* note 10, para. 6.03[5].

57. See Revised § 3-605(c), (d), (e). A reservation of rights, as opposed to a conditional modification, is no longer effective. Impairment of collateral provided by a third party will also discharge joint and several obligors under Revised § 3-605(f). Impairment of collateral is defined at Revised § 3-605(g). *See also* Miller & Harrell, *supra* note 10, para. 6.03[6][d].

58. *See* Revised § 3-605(h); Miller & Harrell, *supra* note 10, 5.02[1][b] and para. 6.03[6][d].

59. *See* Revised § 3-605(i) Miller & Harrell, *supra* note 10, para. 6.03[6][d][iii].

60. Revised § 4-205 reaffirms the rule of Bowling Green, Inc. v. State Street Bank and Trust Co., 425 F.2d 81 (1st Cir. 1970). *See also* Miller & Harrell, *supra* note 10, para. 8.01[1][a]; discussion *infra* at Part III.C.A, and Parts V.B. and C. Absent this rule, possession of an unindorsed instrument payable to the order of another is not sufficient for holder status. *See, e.g.*, F.D.I.C. v. McCrary, 977 F.2d 192 (5th Cir. 1992).

Note that instruments held by federal agencies (such as the Federal Deposit Insurance Corporation acting as receiver of a failed bank) are subject to federal common law rather than the UCC, and therefore those agencies may enjoy the equivalent of holder in due course status where private parties would not. *See, e.g.*, FDIC v. Byrne, 763 F. Supp. 727 (N.D. Tex. 1990), discussed in the *1992 Annual Survey, supra* note 4, at 1559. There are, however, limitations on the extent to which federal common law overrides state law defenses. *See, e.g.*, Patterson v. FDIC, 918 F.3d 540 (5th Cir. 1990) (homestead exemption); Sunbelt Savings, 918 F.2d 540 (5th Cir. 1991), *rev'd and remanded on other grounds sub. nom.* RTC v. Montross, 944 F.2d 227 (5th Cir. 1991); F.D.I.C. v. McCrary, 977 F.2d 192 (5th Cir. 1992). *Patterson* and *Montross* are also discussed in the *1992 Annual Survey, supra* note 4, at 1559-60. *See also* Scott Meacham, *Impact of Bank Insolvency on the Rights of Parties to Commercial Instruments, infra* this issue.

61. The required funds availability schedule in Regulation CC increases the likelihood that a depositary bank will be required to allow its customer to withdraw uncollected funds before receiving notice that an item deposited by the customer is being dishonored. This may leave the bank with an unsecured claim against its customer, plus possession of the dishonored check. The revisions discussed above make it likely that the bank will qualify as a holder in due course of the instrument. *See infra* Parts III.C.1 and VI.E.; Conni L. Allen, *New Rules Governing Collection and Payment of Checks in the Banking System; Impact of Regulation CC*, 47 Consumer Fin. L.Q. Rep. 129 (1993).

62. *See* Miller & Harrell, *supra* note 10, para. 7.01[3].

63. *Cf.* the definition of "deposit account" at UCC § 9-105(1)(e) (likewise excluding certificates of deposit) and the definition of "account" for purposes of Truth in Savings, 12 C.F.R. § 230.2(a) (including certificates of deposit). *See generally, Alvin C. Harrell, Security Interests in Deposit Accounts: A Unique Relationship Between the UCC and Other Law*, 23 U.C.C. L.J. 153 (1990); Stephen K. Huber & Alvin C. Harrell, *Truth in Savings: Disclosures to Depositors*, 47 Consumer Fin. L.Q. Rep. 181 (1993); Farha v. F.D.I.C., 963 F.2d 283 (10th Cir. 1992) (certificate of deposit is "essentially a promissory note"); Victory Nat'l Bank v. Oklahoma State Bank, 520 P.2d 675 (Okla. 1973) (CD is an investment security governed by UCC Article 8); Bank IV Topeka, N.A. v. Topeka Bank & Trust Co., 807 P.2d 686 (Kan. 1991) (non-transferable CD was not an instrument, but rather was a deposit account excluded from Article 9).

64. *See* Revised § 4-104(a)(9). This was designed to reverse cases applying Article 4 to credit card slips, which introduced Article 4 concepts such as stop payment orders into credit card transactions. *See, e.g.*, First United Bank v. Philmont Corp., 533 S.2d 449 (Miss. 1988); *In re* Twenty-Four Hour Nautilus Swim & Fitness Center, Inc., 81 Bankr. 71 (D. Colo. 1989). *See also* Broadway Nat'l Bank v. Barton-Russell Corp., 585 N.Y.S.2d 933 (Sup. Ct. 1992) (credit card is not a negotiable instrument).

65. Thus covering such things as savings withdrawal orders. *See* Shaw v. Union Bank & Trust Co., 640 P.2d 953 (1981), and discussion *infra* at note 225.

66. *See* Revised § 4-105(a). For a more detailed discussion of Article 4 definitions and concepts, *see* Miller & Harrell, *supra* note 10, para. 8.01[3]. The bank on which the item is drawn is called the "drawee" in Article 3, the "payor bank" in Article 4. *See infra* note 286 and Revised § 4-105(3).

collecting bank, and the bank must and can only make presentment and is not authorized to make payment on its own authority.[67] A "payable through" bank is not liable as a payor for missing the midnight deadline. In a change directed at some poorly reasoned cases,[68] new subsection 4-106(c) provides that "[i]f a draft names a nonbank drawee and it is unclear whether a bank named in the draft is a co-drawee or a collecting bank, the bank is a collecting bank."[69]

There are two alternative provisions governing items "payable at" a bank, designed to delineate the dividing line between payor and collecting banks.[70]

B. Automation of the Payments System

1. Check Truncation and Electronic Payments

The Article 4 revisions specifically recognize and authorize check truncation arrangements.[71] There is a new definition of "Electronic presentment agreement" and authority to have such an agreement to govern "retention, presentment, payment, dishonor, and other matters . . . ."[72]

2. The Process of Posting

The 1990 revisions delete the process of posting as a means of making final payment.[73] This revision effectively adopts the result in the *West Side Bank* case[74] by allowing the payor bank to dishonor the item after provisional credit has been given, at any time up to the midnight deadline.[75] The revision also eliminates the Old section 4-303(1)(d) provision listing the process of posting as a temporal point that will preclude effectuation of a stop payment order, legal process or notice, or setoff because the latter are not timely.[76] These are sometimes called "the four legals" because they are four events that preclude payment of an item if they occur before final payment of the item; it is therefore important to determine if there has been final payment prior to receipt of the stop order, process or notice or action in setoff, and the revisions eliminate the completion of the process of posting as a means of such final payment.[77]

The rationale for eliminating the process of posting test is to provide more certainty with regard to the crucial moment of final payment. It was also determined that the new rule is better suited to the realities of automated processing and check truncation. The considerable amount of litigation in this area, in which the courts and parties have been forced to focus on relatively subtle or obscure aspects of the process of posting, support this decision as an improvement in the law.[78]

3. Encoding warranties

Revised section 4-209 provides that any party who encodes information "on or with respect to an item after issue warrants to any subsequent collecting bank and to the payor . . . that the information is correctly encoded."[79] In effect this imposes a strict liability standard (with accompanying potential liability) on a depositary bank (or any other party) that encodes items.[80] In addition, in truncation arrangements the party who retains the item warrants to subsequent parties that the retention and electronic presentment are in conformity with the underlying agreement.[81]

4. Postdated checks

Under revised Article 4, banks are protected against liability for paying a postdated item before its payable date, unless the customer has given prior notice to the bank.[82] The notice is subject to the same kinds of requirements as a stop payment order.[83] If the customer gives the bank such a notice and the bank erroneously pays the item, the bank is liable for actual damages, including damages for resultant wrongful dishonor of other items.[84] This resolves uncertainties under prior law.[85]

The rationale for protecting the bank, by generally relieving the bank of liability for paying a postdated check, is to encourage automated processing by allowing the system to rely on MICR encoded information. This information does not include the check date, which is generally typed or hand written. Perhaps as technology progresses and automated processing systems develop the capability to read handwritten data (including the date of the item), it may be argued that this provides notice to the bank under Revised section 4-401(c) for purposes of triggering bank liability in these circumstances.

5. Dishonor of NSF items

Section 4-402(c) is a new provision that permits a payor bank to base its decision to dishonor a non-sufficient funds ("NSF") check based on the amount of the customer's account balance "at any time between

67. *See* Revised § 4-106(a). First National Bank v. Ford Motor Credit Co., 748 F. Supp. 1464 (D. Colo. 1990) (bank that treated unaccepted drafts as cash items, paying before drafts were accepted, could not collect from drawee when drawee refused to accept the drafts). This case was discussed with approval in the *1992 Annual Survey, supra* note 4, at 1561-62.

68. *See, e.g.*, Reynolds-Wilson Lumber Co. v. Peoples Nat'l Bank, 699 P.2d 146 (Okla. 1985).

69. Revised § 4-106(c). *See also* Miller & Harrell, *supra* note 10, para. 2.04[1], 8.03[1].

70. *See* Revised § 4-106(c). alternatives A and B.

71. *See* Revised § 4-110. *See also* Ballen & Homrighausen, *Revised Articles 3 and 4: Selected Topics*, 24 U.C.C. L.J. 3, 22-32 (1991); Miller, *The Benefits of New U.C.C. Articles 3 and 4*, 24 U.C.C. L.J. 99, 115-16 (1991); Miller & Harrell, *supra* note 10, para. 9.03[6].

72. Revised § 4-110(a).

73. Old § 4-109 is deleted; Revised § 4-110 is a modified version of Old § 4-108. *See also* Revised § 4-215, which is a modified version of the final payment rules at Old § 4-213, deleting entirely the Old § 4-213(1)(c) provision that recognized the completion of posting as a form of final payment.

74. *See, e.g.*, West Side Bank v. Marine Nat'l Exch. Bank, 155 N.W.2d 587 (Wisc. 1968); *Modern Payment Systems*, first edition, *supra* note 33, at 224-25; Miller & Harrell, *supra* note 10, para. 8.02[2][c].

75. Assuming final payment has not previously occurred under Revised § 4-215(a).

76. *See* Revised § 4-303(a) which now lists only acceptance, certification, payment in cash, and final settlement by other means as the only relevant events for these purposes. This mirrors the new final payment rules at Revised § 4-215.

As a result, payment can be reversed after the process of posting is complete, up to the midnight deadline, if a stop order is received or setoff is timely and properly made, unless final payment has otherwise been made. Note, however, that a right of setoff may be subject to prior claims of which the bank is aware, and the bank would be aware of any claim represented by a check previously presented to the bank. *See, e.g.*, Fast Food Systems, Inc. v. Ducotey, 837 P.2d 910 (Okla. 1992); Reston Hospital Center v. Querry, 18 U.C.C. Rep. Serv. 2d 831 (Va. 1992); John P. Roberts, *Banker's Right of Set-Off: Overview and Analysis*, 47 Consumer Fin. L.Q. Rep. 173 (1993).

77. *See* Revised § 4-303(a) and Comment 2. On the treatment of the "four legals" under prior law, *see Modern Payment Systems*, first edition, *supra* note 33, at para. 9.01[6]; Miller & Harrell, *supra* note 10, para. 9.01[7].

78. *See* Miller, *The Benefits of New U.C.C. Article 3 and 4*, 24 U.C.C. L.J. 99, 112-13 (1991).

79. Revised § 4-209(a). *See also* Miller & Harrell, *supra* note 10, para. 9.03[6].

80. *See* Revised § 4-209(a), (c); First Nat'l Bank v. Fidelity Bank, N.A., 724 F. Supp. 1168 (E.D. Pa. 1989) ($100,000 item encoded for $10,000); Azelea City Motels, Inc., v. First Alabama Bank, 551 So.2d 967 (Ala. 1989) ($100,000 item encoded for $10,000); SOS Oil Corp. v. Norstar Bank, 548 N.Y. S.2d 308 (N.Y. App. Div. 1989) ($255,000 item encoded for $25,000); and Port City State Bank v. American Nat'l Bank, 486 F.2d 196 (10th Cir. 1973) ($100 item encoded for $1,000).

81. *See* Revised § 4-209(b).

82. Revised § 4-401(c). *See also* Miller & Harrell, *supra* note 10, para. 9.01[2]; *infra* Part X.D.

83. Revised § 4-401(c). *See also infra* Part X.

84. *Id.* and Revised § 4-402; Miller & Harrell, *supra* note 10, para. 9.02[2].

85. *See, e.g.*, Siegal v. New England Merchants Nat'l Bank, 437 N.E.2d 218 (Mass. 1982).

the time the item is received by the payor bank and the time that the payor bank returns the item or gives notice [of dishonor] . . . ."[86] Furthermore, "no more than one such determination needs to be made."[87] In effect, this permits a payor bank to make a decision to dishonor an item based on the status of the account at the time the item is reviewed, and to proceed with implementation of the decision to dishonor the item even if a subsequent deposit is made and the insufficiency is cured before the item has been returned.[88] However, if the bank makes a redetermination as to the account balance it will be bound by this second determination.[89]

6. Bank Statements

Revised section 4-406 was significantly rewritten to specifically permit check retention (or truncation) by authorizing the payor bank to provide the customer with a statement containing stipulated information in lieu of returning the customer's canceled checks.[90] It also imposes certain retention or record-keeping requirements on payor banks that do not return the cancelled checks, for example, requiring that the bank retain the relevant information for a period of seven years and that it make the item (or a legible copy of the item) available to the customer within a reasonable time upon request.[91]

7. Computer Breakdown

New subsection 4-109(b) makes it clear that a delay caused by a failure of computer or other equipment is excusable and does not constitute a violation of the midnight deadline or other time limit prescribed by Article 4.[92] This applies to both payor and collecting banks.[93]

8. Sight Examination of Checks

Consistent with the other revisions noted above, Revised section 3-103(a)(7) defines "ordinary care" for a business (including a bank) as "observance of reasonable commercial standards, prevailing in the area in which the [business] is located. . . ." This definition also specifies that a bank taking an instrument "for processing for collection or payment by automated means" does not have to by sight examine every item "if the failure to examine does not violate the bank's prescribed procedures and the bank's procedures do not vary unreasonably from general banking usage. . . ." This should facilitate automatic processing and may have significant implications in terms of a bank's liability for payment of forged or altered items under Revised section 4-406, as discussed *infra* at Parts III.C.2 and VIII.

C. Other Check Processing Rules

1. Missing Indorsements

As noted *supra* at Part III.A.1, revised section 4-205 provides that a depositary bank qualifies as the holder of an item taken for deposit even if the depositor has not indorsed the item.[94] Under Old section 4-205 the depositary bank had *authority* to supply a missing indorsement to an item taken for deposit but some courts held that it was not a holder if it failed to do so.[95] Under the change it will be irrelevant whether the depositary bank actually supplies the missing indorsement.[96] Even without an indorsement the depositary bank warrants to subsequent collecting banks, the payor, and the drawer that the item was paid or credited to the customer.[97]

2. Ordinary Care

The new definition of ordinary care at Revised section 3-103(a)(7) makes clear that a payor bank which fails to sight examine every item presented will not be held negligent as a matter of law if it erroneously pays a forged or altered item, so long as it is observing reasonable commercial standards as recognized in that banking area.[98] This is designed to allow payor banks to utilize automatic processing systems so long as they do so within parameters commonly accepted as reasonable by other banks in the same market.[99]

Revised section 3-103(a)(7) should be read in conjunction with Revised section 4-406(e), which may partially excuse a customer from his or her duty to examine periodic bank statements and notify the bank of any forgeries or alterations if the bank has failed to exercise ordinary care and the failure substantially contributed to the loss.[100] Under Revised section 3-103(a)(7) customers normally will not be able to avoid liability by arguing that the bank's failure to personally examine each and every item presented (for purposes of discovering forgeries and alteration) constituted a *per se* lack of care which excuses the customer's negligence. Note, however, that this will not excuse the bank's failure to use ordinary care in other respects, and that the duty of ordinary care will now specifically include observance of "reasonable commercial standards."[101] In addition Revised section

86. Revised § 4-402(c); Miller & Harrell, *supra* note 10, para. 8.02[6]. *See also infra* Part VIII.

87. *Id.* If the bank makes a subsequent reevaluation for purposes of the decision to pay or dishonor, the bank is bound by the results of the later evaluation.

88. Revised § 4-402(c).

89. *Id.*

90. Revised § 4-406(a); Miller & Harrell, *supra* note 10, para. 9.03[4][b]. Unless there is an electronic funds transfer access feature, the bank is not required to provide an account statement. For example, passbook savings accounts typically do not involve account statements. But if the bank does not provide account statements, it loses the potential preclusion of a customer's right to assert forgeries and alterations under § 4-406. *See infra* Part III.D.1 and *infra* Part IX. The new disclosure requirements for account statements under Truth in Savings provide a significant incentive for eliminating monthly statements, but this must be balanced against the loss of a preclusion under UCC § 4-406, especially for transaction accounts that allow withdrawal by draft. *See generally* Stephen K. Huber & Alvin C. Harrell, *Truth in Savings: Disclosures to Depositors, supra* note 63.

91. Revised § 4-406(b).

92. *See* Revised § 4-109(b). This is a modified version of the Old § 4-108(2). *See also* Port City State Bank v. American National Bank, 486 F.2d 196 (10th Cir. 1973) (cited in Comment 2 to Revised § 4-109); Miller & Harrell, *supra* note 10, para. 8.02[7] and para. 8.03[3].

93. Revised § 4-109(b).

94. Revised § 4-205(1). *See* Bowling Green, Inc. v. State Street Bank & Trust Co., 425 F.2d 81 (1st Cir. 1970). This subsection is a completely revised version of Old § 4-205(1). *See also supra* Part III.A.1; *infra* Part V.B; Miller & Harrell, *supra* note 10, para. 8.01[1][a].

95. *See Modern Payment Systems,* first edition, *supra* note 33, at 91-92 and 215; Miller & Harrell, *supra* note 10, para. 3.01[1][b], para. 3.02[3][c], para. 8.01[1][a], and para. 8.04[3][g][4].

96. *Cf.* Marine Midland Bank v. Price, Miller, Evans & Flowers, 441 N.E.2d 1083 (N.Y. 1982). As noted *supra* at Part III.A.1, this may be crucial to the bank's holder in due course status and its ability to recover from those liable on the instrument.

97. *See* Revised § 4-205(2); Miller & Harrell, *supra* note 10, at 3-11 n. 35. *See also* further discussion *infra* at Part V.B.

98. *See* Revised § 3-103(a)(7); Rhode Insland Hosp. Trust Nat'l Bank v. Zapata Corp., 848 F.2d. 291 (1st Cir. 1988); *cf.* Medford Irrigation Dist. v. Western Bank, 676 P.2d 329 (Or. App. 1984). *See also* Revised § 4-406(e). However, this will not excuse the failure of the bank to use ordinary care in other respects. *See* Miller & Harrell, *supra* note 10, para. 9.03[4][c] and [5].

99. *See* Revised § 3-103(a)(7). Under either version of the Code, action in compliance with Federal Reserve Board regulations or Federal Reserve Bank operating letters will be deemed to constitute ordinary care. *See, e.g.,* Security Bank & Trust Co. v. Federal Nat. Bank and Trust Co., 554 P.2d 119 (Okla. App. 1976).

100. *See* Revised § 4-406(e). Such a failure may trigger allocation of the loss on the basis of comparative negligence. *Id.,* and *see* Miller & Harrell, *supra* note 10, para. 9.03[4][c] and [5]. *See also infra* Part IX.

101. *See* Revised § 3-103(a)(7). Again, this does not require sight examination of each item paid. *Id.*

4-406(e) excuses the customer from liability if the bank "did not pay the item in good faith." In conjunction with the new, tougher definition of "good faith" at Revised section 3-103(a)(4) (now including "reasonable commercial standards of fair dealing") this provides some additional ammunition to bank customers in those cases where the bank has paid a forged or altered item, despite the lack of a customer's ability to assert a need for sight examination of every check.[102] As noted *supra,* the latter rule was designed to facilitate use of efficient automated processing systems.

3. The Midnight Deadline

It should be noted that the Article 4 midnight deadline has survived both federal Regulation CC and the Article 4 revisions. Despite the addition of a plethora of new requirements, restrictions, and liabilities, the payor bank still becomes accountable for the amount of the item, under Revised section 4-302(a), if it does not pay, return or otherwise properly dishonor the item before its midnight deadline.[103] Similarly, collecting banks remain subject to their own version of the midnight deadline rule.[104] As noted, the "process of posting" has been eliminated as a factor in these cases.[105]

An important question under prior law was whether final payment by a payor bank under Old section 4-213 (now Revised section 4-215) precluded recovery by the payor bank on a restitutionary theory (otherwise permitted under section 3-418). Some cases held that the final payment rules of Article 4 superseded Old section 3-418 and precluded a restitutionary recovery.[106] The revisions reject this view and permit a restitutionary recovery by a bank that has made final payment.[107]

Another addition at Revised section 4-302(b) codifies a case law exception to the liability of the payor bank for violating the midnight deadline, where the claimant presented or transferred the instrument in an effort to defraud the bank. This would permit the payor bank to defend itself (or proceed) against a check kiter.

D. The Bank-Customer Relation

1. Customer's Duty to Examine the Bank Statement

Revised section 4-406 contains important revisions, for example introducing a comparative fault standard for allocation of losses due to forgery or alteration.[109] Revised section 4-406(e) provides that if the customer failed to meet its duty to examine its bank statements and notify the payor bank of any forgery or alteration within the stipulated time (now up to a maximum of 30 days) pursuant to subsection 4-406(d), and if the bank has failed to exercise ordinary care under Revised section 3-103(a)(7), and that failure substantially contributed to the loss, "the loss [will be] allocated between the customer . . . and the bank . . . according to the extent to which the failure of each to exercise ordinary care contributed to the loss."[110]

2. Limitation Periods

As noted above, under Revised section 4-406(d)(2), the maximum "reasonable period of time" for bank customers to examine their bank statements and notify the bank of any repeated forgery or alteration has been extended from 14 to 30 days. However, the basic duty is to discover "promptly" and report such irregularities, and acting within 30 days may not always meet this test.[111]

The one year statute of limitations for a customer to bring an action against a payor bank for payment on a forged drawer's signature or alteration is continued at Revised section 4-406(f). If the payor bank fails to assert this as a proper defense to liability, it thereby forfeits its right to recover for breach of warranty from prior parties under Revised sections 3-417 and 4-208.[112]

Note also that the warrantor has an independent and broader ability to assert a preclusion against the bank and its customer for violation of the customer's obligations under Revised section 4-406(d) and Revised sections 3-404 and 3-406, under Revised sections 3-417(c) and 4-208(c). The warrantor may assert the resultant preclusion directly against the bank and its customer in defense under Revised sections 3-417(c) and 4-208(c) to the extent of the customer's responsibility.

The three year preclusion for actions with respect to forged indorsements under Old section 4-406 was deleted, but there is a new three year general statute of limitations for actions under Article 4, at Revised section 4-111. This conforms to the new statute of limitations for actions under Article 3, at Revised section 3-118 (as discussed *supra* at

102. It is by no means clear that a bank must sight examine checks under Old Article 4, although some cases seem to suggest that. Other cases reached the same result by stretching the concept of good faith, since a bank that violates this duty essentially excuses any customer negligence. *See* Revised § 4-406(e) (no preclusion against customer if bank did not pay the item in good faith), also discussed *infra* at Part VIII and *supra* this paragraph. *Cf.* Commercial Cotton Co. v. United California Bank, 209 Cal. Rptr. 551 (1985) (bank violated duty of good faith by paying forged checks), with Price v. Wells Fargo Bank, 261 Cal. Rptr. 735 (Cal. App. 1 Dist. 1989), and Copesky v. Superior Court of San Diego County, No. D013448 (Cal. App. 4th Dist. Jan. 23, 1991) (rejecting Commercial Cotton as poorly reasoned). *Price* was discussed at Smith, *Update on California's Bad Faith Tort,* 44 Consumer Fin. L.Q. Rep. 54 (1990). In view of the confusion evidenced by these cases, it should be emphasized that Revised § 3-103(a)(7) and the payment of the checks without sight examination do not have anything to do with good faith. *See also* Miller & Harrell, *supra* note 10, para. 9.03[2], [4], [5]; *supra* Part IX; Peter G. Pierce III, *The Law's Excellent Banking Adventure -- Recent Developents in the Bank-Customer Relation, Trends in Lender Liability and the Impact of New Articles 3 and 4, infra* this issue [hereinafter Pierce].

103. *See* Revised §§ 4-104(a)(10), 4-215, 4-301, 4-302; Miller & Harrell, *supra* note 10, para. 8.02[2][d], [3]; *infra* Part VIII. Generally the midnight deadline is midnight of the banking day after the banking day in which the item is received. Revised § 4-104(a)(10). The scope of the banking day depends on the policy and operations of the bank. *See, e.g.,* Security Bank and Trust Co. v. Federal Nat. Bank & Trust Co., 554 P.2d 119 (Okla. App. 1976); Pracht v. Oklahoma State Bank, 592 P.2d 976 (Okla. 1979). Federal Reserve Board Regulations CC (Expedited Funds Availability) and DD (Truth in Savings) adopt a slightly different definition that excludes Saturdays, Sundays and legal holidays. *See* 12 C.F.R. § 229.2(f) and (g).

104. *See* Revised §§ 4-104(a)(1), 4-214. As before, the consequences of a failure to meet the midnight deadline are quite different for collecting and payor banks. *Cf.* Revised §§ 4-214 and 4-302. The former section approves the result in Appliance Buyers Credit Corp. v. Prospect National Bank, 708 F.2d 290 (7th Cir. 1983) (depositary bank liable only for actual damages caused by the delay). *See also* Miller & Harrell, *supra* note 10, para. 8.03.

105. *See* discussion *supra* Part III.B.2.

106. *See, e.g., Modern Payment Systems,* first edition, *supra* note 33, at 221-22; (noting uncertainty under prior law); Miller & Harrell, *supra* note 10, para. 8.02[3], [4] (explaining resolution under Revised Article 4).

107. *See* Revised § 4-215 and Comment 3, adopting the result in Nat'l Savings and Trust Co. v. Park Corp., 722 F.2d 1303 (6th Cir. 1983), *cert. denied,* 466 U.S. 939 (1984); Miller & Harrell, *supra* note 10, para. 8.02[3], [4].

108. Revised § 4-302(b). *See also* Revised § 3-418, Comment 4, and Revised § 4-301, Comment 7. Regarding § 4-302, *see* Revised § 4-302(b), and Bank Leumi Trust Co. v. Bally's Park Place, 528 F. Supp. 349 (S.D. N.Y. 1981); Miller & Harrell, *supra* note 10, para. 8.02. *See also supra* note 39, and *infra* Parts II.A. and IX.

110. Revised § 4-406(e). However, other customer preclusions may apply. *See, e.g.,* Revised § 3-404 (imposters and fictitious payees); Revised § 3-405 (responsibility for fraudulent indorsement by employee); Revised § 3-406 (negligent contribution to forgery or alteration). *Cf. Modern Payment Systems,* first edition, *supra* note 33, para. 7.02; Miller & Harrell, *supra* note 10, para. 7.03 and para. 9.03[2], [4], [5]. *See also infra* Part IX.

111. *See* Revised § 4-406(c); Flagship Bank v. Complete Interiors, Inc., 450 So.2d 337 (Fla. Dist. Ct. App. 1984); Miller & Harrell, *supra* note 10, para. 9.03[4][a]; *infra* Part IX.

112. *See* Revised § 4-406(f). *See also* Revised § 4-208 and discussion of warranties at Miller & Harrell, *supra* note 10, para. 6.03[7] and para. 7.02; *supra* Part II.F. and G.

Part II.A). This three year limitation period also would govern cases such as an action alleging violation of a restrictive indorsement, which under prior law might have been governed by the typically longer limitation periods under general contract law.[113]

3. Overdraft Liability of Joint Tenants

If one joint tenant writes a check that overdraws the account, and the bank pays the item, creating an overdraft, under Old Article 4 it is unclear whether the bank can recover the amount of the overdraft from the other joint tenant.[114] Revised section 4-401(b) clarifies this by providing that "[a] customer is not liable for the amount of an overdraft if the customer neither signed the item nor benefited from the proceeds of the item."[115]

4. Wrongful Dishonor

Revised section 4-402(2) unmistakably repudiates the "trader rule," a pre-Code concept allowing a presumption that a merchant customer suffered damages for loss of reputation by reason of wrongful dishonor.[116] Similarly, the Code clearly provides that there is no wrongful dishonor where the bank properly dishonors an item but gives notice of the wrong reason.[117] The second and third sentences of Revised section 4-402(b) and the Revised Comment 3 recognize the possibility of an action for wrongful dishonor being brought outside the UCC on some basis other than contract law, though the exact nature of such an action is not specified.[118]

5. Stop Payment Orders

Under Revised section 4-403(a) "any person authorized to draw on the account" may stop payment on any item drawn on that account. The 14 day and six month limitation periods for oral and written orders are reworded but essentially remain the same.[119] The revision added language clarifying that recoverable losses for violation of a valid stop payment order may include damages for dishonor of subsequent items under Revised section 4-402.[120]

A new Comment 1 to Revised section 4-403 states that the customer's stop payment order must provide sufficient information to allow the bank to identify the item with reasonable certainty using existing technology. Money orders are defined as checks at Revised section 3-104(f), clarifying that they are subject to a stop payment order by the purchaser. Compare *supra* Part II.H., regarding cashier's checks.

IV. Operational Issues Relating to the Enforceability of Instruments

A. Determining Who is Entitled to Payment: Ambiguous, Imposter, and Multiple Payees

Several new provisions in Revised Article 3 resolve practical issues that banking institutions must deal with on a regular basis. For example, Revised section 3-110(a) provides that "an instrument is payable to the person intended by the signer even if that person is identified in the instrument" by a different name.[122] Thus where a check is payable to "John Smith," and more than one person of that name seeks payment, the check is payable to the party intended by the drawer.[123] However, if the check is issued to someone else, posing as the intended payee (an "imposter payee"), the imposter's indorsement will be effective in favor of any party who, "in good faith, pays the instrument or takes it for value or for collection."[124] There is a similar rule for instruments payable to fictitious payees.[125]

If an instrument is payable to multiple payees in the alternative (*e.g.,* "John or Jane Smith"), it may be paid or negotiated or enforced if indorsed by either of such parties.[126] If an instrument is payable to multiple payees not in the alternative (*e.g.,* "John and Jane Smith"), it may be paid, negotiated, or enforced only if indorsed by all such parties.[127] If the instrument is ambiguous in this regard (*e.g.,* it is payable to "John and/or Jane Smith"), it is deemed to be payable to the named persons in the alternative.[128]

B. Determining Who is Entitled to Payment: Instruments Payable to Account Numbers, Organizations

If an instrument is payable only to an account number, it is payable to the person to whom that account is payable.[129] If it is payable to an account number and a person, it is payable to that person regardless of whether he or she owns the account.[130]

113. *See, e.g.,* Cairo Coop. Exch. v. First Nat'l Bank of Cunningham, 608 P.2d 1370 (Kan. Ct. App. 1980). *See also* discussion of the new Article 3 limitations periods, *supra* at Part II.A., and discussion *infra* at Part IX.

114. *See* Old § 4-401(1). *Cf.* Revised § 4-401(a).

115. The customer might agree to responsibility for the overdraft however. This codifies the rule of Cambridge Trust Co. v. Carney, 333 A.2d 444 (N.H. 1975). *See also* Miller & Harrell, *supra* note 10, para. 9.01[2].

116. *See, e.g.,* Miller & Harrell, *supra* note 10, para. 9.02[2].

117. *See* Revised § 4-402(a). The courts have not always recognized this fundamental point. *See, e.g.,* Johnson v. Grant Square Bk. & Tr. Co., 634 P.2d 1324 (Okla. Ct. App. 1981) (bank liable for wrongful dishonor when it returned item marked NSF in response to the customer's stop payment order). *Cf.* Algemene Bank Nederland, N.A. v. Federal Reserve Bank, No. 89 Civ. 4946 (SWK), 1991 U.S. Dist. LEXUS 470 (S.D. N.Y. Jan. 16, 1991) (bank liable for improper dishonor when it returned items stamped "REFER TO MAKER."). *See also 1992 Annual Survey, supra* note 4, at 1561.

118. The theory is that under § 1-103 there is no displacement by § 4-402 of a common law cause of action. The basis on which such action would proceed is not, however, specified. Miller & Harrell, *supra* note 10, para. 9.02[2][b].

119. Revised § 4-403(b). *See also* Miller & Harrell, *supra* note 10, para. 9.01[4]; *infra* Part X.D.

120. *See* Revised § 4-403(c).

121. This should be read to undermine cases like Parr v. Security Nat'l Bank, 680 P.2d 648 (Okla. Ct. App. 1984) ($.50 error in customer's stop payment order did not excuse bank's failure to stop payment, despite fact that bank's computer system required the exact amount), at least where the customer knows or has agreed that the stop order must contain the exact amount. The best solution is a clear disclosure and agreement between the parties. *See also* discussion *infra* at Part X.D.

122. Where more than one person signs, "the instrument is payable to any person intended by one or more of the signers." Revised § 3-110(a).

123. *See* Revised § 3-110, Comment 2.

124. Revised § 3-404(a); Old § 3-405 is similar. *See also* Miller & Harrell, *supra* note 10, para. 7.03[3][c]. In Newport Steel Corp. v. Thompson, 757 F. Supp. 1152 (D. Colo. 1990), checks normally were made payable to a manufacturer. One was instead made payable to the supplier who arranged the shipments. When the supplier deposited the check, it was alleged that this constituted conversion of the manufacturer's funds. The court disagreed, holding that since the check was made payable to the supplier it was the supplier's property. *Newport* is cited with approval in the *1992 Annual Survey, supra* note 4, 1564. *See also infra* Part VI.A.

125. *See* Revised § 3-404(b).

126. Revised § 3-110(d); Old § 3-116(a). Although this example describes two joint payees, the rule also applies if there are more than two such payees; the instrument may be negotiated or enforced by any one or more of them.

127. Revised § 3-110(d); Old § 3-116(b).

128. Revised § 3-110(d) and Comment 4. *Cf.* C.H. Sanders Constr. Co. v. Bankers Trust Co., 123 A.D.2d 251, 506 N.Y. S.2d 58 (N.Y. 1986). *See also* Miller & Harrell, *supra* note 10, at 2-55 n. 262.
This revision would have been very helpful in Van Lunen v. State Central Savings Bank, 751 F. Supp. 145 (S.D. Iowa 1990), where two payees were named on two separate lines, creating an ambiguity as to whether the instrument was payable to either or only to both payees. The court concluded they were joint payees; under Revised Article 3 an ambiguous instrument is to be treated as payable in the alternative. *Van Lunan* is noted in the *1992 Annual Survey, supra* note 4, at 1560.

129. Revised § 3-110(c)(1).

130. *Id. See also* Miller & Harrell, *supra* note 10, para. 2.02[7][b], para. 3.02[3][b][ii], and para. 6.03[6][b][ii].

If an instrument is payable to a trust or estate, or a person as trustee or other representative of a trust or estate, the instrument is payable to the trustee or representative (or a successor) regardless of whether the beneficiary or estate is named.[131] If an instrument is payable to a party as agent, it can be paid to the agent, or a successor, or the person represented.[132] If it is payable to a fund or organization that is not a legal entity, it may be paid to any authorized representative of the members of the fund or organization.[133] If payable to an office or person described as an office holder, it may be paid to the incumbent of the office or a successor.[134]

C. Other Rules Governing Interpretation, Liability, Payment, and Ambiguities

As before, where an instrument contains contradictory terms, "typewritten terms prevail over printed terms, handwritten terms prevail over printed terms, handwritten terms prevail over both, and words prevail over numbers."[135]

Two or more persons who sign an instrument in the same capacity as makers, drawers, acceptors, or indorsers are jointly and severally liable in that capacity. Such parties have a right of contribution against their co-obligors, in the event that one party discharges the debt owed by all.[136] In such a case the discharge of one co-obligor by the holder or owner of the instrument does not discharge the liability of that party to the other co-obligors by way of contribution.[138]

Between the parties to an instrument, liability on an instrument may be modified or discharged by a separate agreement entered into as a part of the same transaction.[139] However, such an agreement will constitute a "personal" defense that is not effective against a remote holder in due course.[140]

As noted *supra* at Part II.A., revised Article 3 contains a new statute of limitations barring the enforcement of most notes after six years; most checks cannot be enforced after three years.[141] Certificates of deposit cannot be enforced more than six years after demand for payment has been made.[142] An action to enforce such instruments must be commenced within these time periods or it is barred by law. The only section bearing on these issues in the Old Code is section 3-122, stating when a cause of action accrues. As a result, under the Old Code statutes of limitations outside Article 3 determined when an action was barred.[143] Whether Revised 3-118 may have retroactive application or, like the substantive rules of the Revised Code, only prospective application, is determined by other law.

Revised section 3-119 allows a party who is liable on an instrument to give notice of an action against that party to any third party who may also be liable (*e.g.,* a prior indorser). In turn, such third party may give similar notice to other persons who may be liable (*e.g.,* prior indorsers). If the notice states that (1) the person so notified may come in and assert a defense and (2) in the absence of such defense the person will be bound by the outcome as regards their liability, the person so notified will be bound by the results of that action.

V. Indorsements

A. Types of Indorsements

Four types of indorsements are recognized in the Revised Article 3: blank indorsements, special indorsements, anomalous indorsements, and restrictive indorsements.[144] A blank indorsement occurs when the indorser merely signs the indorser's name without adding any additional language; this will convert an "order" instrument (one payable to the order of a named payee or indorsee) into "bearer" paper subject to negotiation by transfer of possession alone.[145]

A special indorsement is one that makes the instrument payable to a particular party, thereby retaining the "order" character of the instrument and requiring a subsequent indorsement by the named party as a prerequisite to subsequent negotiation of the instrument.[146] An anomalous indorsement is one by a party outside the chain of title to the instrument; by one not a holder. The effect is to make such a party liable as an indorser and to create a presumption of accommodation status.[147]

A restrictive indorsement is not effective to restrict payment to a specified party, but may qualify or restrict payment to a specified class of transactions, for example by using words such as "for deposit," "for collection," or "pay any bank" (all designed to restrict subsequent negotiation to the banking system).[148] Any person other than a bank who purchases an instrument so restricted may be guilty of conversion,[149] and a depositary bank may be guilty of conversion if it pays the instrument in a manner inconsistent with the restrictive indorse-

131. Revised § 3-110(c)(2)(i). *Cf.* Old § 3-117(b). *See also supra* Part II.B. (notice of breach of fiduciary duty).

132. Revised § 3-110(c)(2)(ii). *Cf.* Old § 3-117(a).

133. Revised § 3-110(c)(2)(iii). *See* Miller & Harrell, *supra* note 10, at 2-56 n. 264.

134. Revised § 3-110(c)(2)(iv). *See* Miller & Harrell, *supra* note 10, at 2-56 n. 265.

135. Revised § 3-114; Old § 118(b), (c), and (c). On ambiguities generally, *see* Miller & Harrell, *supra* note 10, para. 2.04[1]. *Cf.* Galatia Community State Bank v. Kindy, 821 S.W.2d 765 (Ark. 1991) (check-writing machine amount controls over handwritten number).

136. Revised § 3-116(a); Old § 3-118(e). The instrument can otherwise provide, however. *See also supra* Part II. (personal liability for signature in a representative capacity); and *supra* Part III.D.3 (overdraft liability of joint tenants).

137. *See* Revised § 3-116(b); Ghitter v. Edge, 165 S.E.2d 598 (Ga. Ct. App. 1968); Miller & Harrell, *supra* note 10, para. 2.04[1]. An agreement can otherwise provide. *See also* § 3-419(e).

138. Revised § 3-116(c), and Comment 2. On discharge of liability, *see generally* Revised Article 3, Part 6; Miller & Harrell, *supra* note 10, para. 6.03[6][a].

139. This also may occur under an unrelated agreement if there is reliance on the agreement. Revised § 3-117; Old § 3-119; Miller & Harrell, *supra* note 10, para. 2.02[3][b][ii]. Any parol evidence rule applicable outside Article 3 is applicable to such an agreement.

140. Revised §§ 3-117, 3-305(a)(2), (b); Old § 3-119(1).

141. Revised § 3-118. *See also* Miller & Harrell, *supra* note 10, para. 6.03[7]; discussion *supra* Part II.A, and *supra* Part III.D.2.

142. Revised § 3-118(c).

143. *See, e.g.,* O'Neill v. Steppat, 270 N.W.2d 375 (S.D. 1978); Miller & Harrell, *supra* note 10, para. 7.01[1][a].

144. *See* Revised UCC §§ 3-204, 3-205, 3-206. "Indorsement" and "indorser" are defined at § 3-204. *See also* Miller & Harrell, *supra* note 10, para. 3.02[3], para. 4.06.

145. Revised § 3-205(b); Miller & Harrell, *supra* note 10, para. 3.02[3][c][i].

146. *See* Revised § 3-205(a); *see also* Revised §§ 3-103(a)(6), 3-104(a)(1) and (c), 3-201(b); Miller & Harrell, *supra* note 10, para. 3.02[3][c][ii].

147. *See* Revised § 3-205(d) and Comment 3, Revised § 3-419(c); Miller & Harrell, *supra* note 10, para. 3.02[3][b][iv], para. 5.01, para. 5.02.

148. *See* Revised § 3-206 and Comment 3, Revised § 4-201(b) and Comment 7; Miller & Harrell, *supra* note 10, para. 3.02[3][c][iii], para. 8.0-4[3][g]; Leghigh Presbytery v. Merchants Bancorp., Inc., 600 A.2d 593 (Pa. 1991).

149. *See* Revised § 3-206(c)(1) and Comment 3. On conversion *see* Revised § 3-420. *See also* Miller & Harrell, *supra* note 10, para. 3.02[3][c][iii][B]. Regulation CC also restricts transfer or negotiation of a check outside the banking system, once it has been indorsed by a collecting bank. *See infra* this Part.

ment.[150] However, a payor bank not the depositary bank and any intermediary bank "may disregard the indorsement and are not liable if the proceeds of the instrument are not received by the indorser or applied consistently with the indorsement."[151]

Moreover an indorsement that places a condition on subsequent transactions is not effective to prevent subsequent transfer or negotiation of the instrument and does not affect the right of the indorsee to enforce the instrument.[152] For example, an indorsement that limits payment to "A only" is not effective to preclude A from indorsing to another party or to prevent that later party from taking by negotiation.[153] Similarly, an indorsement conditioning payment upon compliance with a condition or contract is ineffective.[154]

Under Federal Reserve Regulation CC,[155] once a check has been indorsed by a bank, only a bank may be a holder of the item, until and unless the check is returned to the owner who deposited the check or initiated collection or has been specially indorsed by a bank to a nonbank party.[156] This is designed to provide the equivalent of a restrictive indorsement (limiting subsequent negotiation to the banking system) once a check has been indorsed by a bank without the need to clutter the back of the check with restrictive indorsement language.[157] Thus, once a check has been indorsed by a bank, it is unnecessary (and a violation of Regulation CC) for subsequent indorsements to contain restrictive language in order to restrict negotiation to the banking system.[158]

B. Missing Indorsements — Depositary Banks

As noted *supra* at Parts III.A.1 and III.C.1, old section 4-205 provided the depositary bank authority to supply missing customer indorsements on items taken for collection. Questions remained, however, as to whether such an indorsement would satisfy the requirement at Old section 3-202(1) and (2) for an indorsement "by or on behalf of the holder," so as to confer holder status on the bank (thereby laying the foundation for holder in due course status under section 3-302). There was also a question as to the effect of section 4-205 in cases where the bank could have supplied the missing indorsement but failed to do so. Under the Old Code at least one case held that section 4-205 superseded section 3-202 as to these issues, so that the bank could claim holder status despite the lack of an indorsement.[159]

Revised section 4-205 affirms this view, by allowing the depositary bank to be a holder of any item delivered to it for collection, if the customer delivering the item to the bank was a holder, whether or not the customer has indorsed the item. The revision specifically provides that this is sufficient to make the bank a holder, and thus it may qualify as a holder in due course, if the other requirements of section 3-302 are met.[160] There is no reason to deny the bank holder status or to force it to inspect each item for an indorsement, as this would only slow the bank collection process to no apparent purpose. As discussed *supra* at Part III.B, the Revised Code recognizes this, once again illustrating its intent to remove unneeded barriers to efficiency and automated processing.

C. Indorsements by Banks

As noted *supra* at Part V.A., Revised section 4-201(b) carries forward the time-honored rule that a restrictive indorsement such as "pay any bank" or the like precludes any party other than a bank from acquiring the rights of a holder, unless the item is returned to the customer who initiated collection or is specifically indorsed by a bank to a non-bank party.[161] The effect is to limit negotiation to the banking system once the item is so indorsed, subject to the stated exceptions.

As noted in Comment 7 to Revised section 4-201, Federal Reserve Regulation CC also governs bank indorsements.[162] Regulation CC section 229.3 provides standards for indorsement of items being processed for collection through the banking system.[163] Subsection 229.35(c) provides a rule somewhat similar to UCC section 4-201, except that under Regulation CC a bank's indorsement *per se* restricts subsequent negotiation to the banking system (subject to the same two exceptions), whether or not restrictive language such as "Pay any bank" or the like is added. Specifically, Regulation CC provides:

> (c) *Indorsement by a bank:* After a check has been indorsed by a bank, only a bank may acquire the rights of a holder . . . .[164]

The result is that a bank need not include restrictive indorsement language, such as "Pay any bank," in order to restrict subsequent negotiation to the banking system. Indeed, Appendix D to Regulation CC, setting forth specific indorsement standards, prohibits the use of such langauge in the indorsements of subsequent collecting banks.[165] The apparent purpose is to limit the content of collecting bank indorsements to essential information so as to make that information more readable.[166]

150. *See* Revised § 3-206(c)(2), (3) and Comment 3; Miller & Harrell, *supra* note 10, para. 3.02[3][c][iii][B], para. 8.04[3][g][4].
151. Revised § 3-206(c)(4) and Comment 3; Miller & Harrell, *supra* note 10, para. 3.02[3][c][iii][B].
152. Revised § 3-206(a), (b); Miller & Harrell, *supra* note 10, para. 3.02[3][c][iii][B[.
153. Revised § 3-206, Comment 2; Miller & Harrell, *supra* note 10, para. 3.02[3][c][iii][A].
154. *See supra* this discussion.
155. 12 C.F.R. Part 229.
156. 12 C.F.R. § 229.35(c); Miller & Harrell, *supra* note 10, para. 8.04[3][g][4].
157. *See* Federal Reserve Regulation CC Commentary § 229.35(c), and discussion *infra* Part V.C.
158. *Id.* One result is to simplify the indorsement trail on the back of a check. *See also infra* Part V.C.
159. Bowling Green, Inc. v. State Street Bank, 425 F.2d 81 (1st Cir. 1970). *See also Modern Payment Systems,* first edition, *supra* note 33, at 215 (noting cases to the contrary); Miller & Harrell, *supra* note 10, para. 8.01[1][a] (noting impact of the revision); *supra* Parts III.A.1 and III.C.1.
160. Revised § 4-205(1); *see supra* the preceding note.
161. *See* Revised § 4-201(b), and Comment 7; Old § 4-201(2), and Comment 7; Miller & Harrell, *supra* note 10, para. 3.02[3][c][iii], and para. 8.04[3][g][4]. *See also* discussion of Regulation CC, *infra* this Part.
162. Regulation CC, 12 C.F.R. Part 229, implements the federal Expedited Funds Availability Act, 12 U.S.C. §§ 4001-4010 (1991). *See generally* Miller & Harrell, *supra* note 10, para. 8.04; Conni L. Allen, *New Rules Governing Collection and Payment of Checks in the Banking System: Impact of Regulation CC,* 47 Consumer Fin. L.Q. Rep. 129 (1993).
163. This is part of Regulation CC, "Subpart C - Collection of Checks." The scope of Subpart C is limited to checks being collected through the banking system. *See* 12 C.F.R. § 229.1(b)(3).
164. 12 C.F.R. § 229.35(c); Miller & Harrell, *supra* noe 10, para. 8.04[3][g][1]; Allen, *supra* note 162.
165. *See* Regulation CC, Appendix D, Para. 2.
166. *See* Regulation CC Commentary § 229.35(c). *See also supra* Part V.A.

As to checks being collected through the banking system, then, Regulation CC preempts use of the traditional "Pay any bank" indorsement language by intermediary banks. However, as noted, Regulation CC applies only to checks being processed for collection or return by banks.[167] Therefore, restrictive indorsements such as "Pay any bank" or "for deposit only" are still permissible and may have utility for purposes of protecting holders of checks not yet being processed by a bank, as well as for non-check items being processed by banks.

VI. Secondary Liability of Indorsers and Drawers

A. Basis of Liability on the Instrument

Revised Article 3 carries forward the basic rule that a person is not liable on an instrument unless that person has signed it.[169] However, the converse of this is that a person who signs an instrument is liable on the instrument in the capacity in which the person signs.[169] This is important to a financial institution taking an item for deposit or collection, as the item may be returned unpaid by the payor, leaving the bank as holder of the item with need of recourse against the parties liable on it.[170] This liability, and the ability of the holder bank to pursue it, may depend on (1) the capacity in which each potentially liable party signed the instrument, (2) the statutory prerequisites to enforcing that liability, (3) any defenses or preclusions available, and (4) whether the institution has holder in due course status. Some exceptions and qualifications will be discussed below, then the first two factors will be analyzed *infra* this Part. The remaining factors will be discussed further *infra* at Parts VIII - IX.

There are five statutory exceptions to the rule at Revised section 3-401, providing that one is not liable unless that party has signed the instrument. In other words, these are instances where a signature by one person may be effective as the signature of another who did not sign the instrument:

1. A person is liable for any signature by an authorized agent;[171]
2. An unauthorized signature will become effective if ratified;[172]
3. Revised Article 3 provides a series of specific rules making unauthorized indorsements valid. For example, an employer may be held liable for an unauthorized indorsement by an employee;[173]
4. A person whose negligence has contributed to the making of a forgery or alteration may be precluded from asserting that forgery or alteration against a person who, in good faith, pays the instrument or takes it for value for collection;[174]
5. A bank customer who fails to examine his or her bank statements and to notify the bank of an improper (e.g. forged or altered) item may be precluded from asserting the impropriety against the bank.[175]

Under Old Article 3, these exceptions (to the extent recognized -- No. 3 above, for example, contains new provisions, although these are consistent with general principles embodied in prior law) had an all-or-nothing effect on liability; if the exception was triggered but the other party was negligent in a way that substantially contributed to the loss, the party whose liability was affected was not liable even though he or she had been substantially negligent.[176] Under Revised Articles 3 and 4 this allocation of loss may be qualified: If the holder seeking enforcement of the instrument failed to exercise ordinary care[177] and that failure substantially contributed to the loss, the loss instead may be allocated between the parties on the basis of the extent to which the failure of each party to exercise ordinary care contributed to the loss.[178]

167. 12 C.F.R. § 229.1(b)(3).
168. Revised § 3-401(a). The corollary is that a drawee bank is not liable on an instrument unless it has accepted it. It also is liable for final payment or undue delay. *See* Revised §§ 3-409, 4-215, 4-302; First Nat'l Bank of Nocona v. Duncan Sav. & Loan Ass'n, 656 F. Supp. 358 (W.D. Okla. 1987), *aff'd,* 957 F.2d 775 (10th Cir. 1992); Sabin Meyer Regional Sales Corp. v. Citizens Bank, 502 F. Supp. 557 (N.D. Ga. 1980); Miller & Harrell, *supra* note 10, para. 4.02. However, Agostino v. Monticello Greenhouses, Inc., 560 F. Supp. 557 (N.D. App. Div. 1990), allowed recovery for wrongful dishonor by a noncustomer, on common law grounds. *See also* Revised § 4-402, Comment 5. *Agostino* is noted in the *1992 Annual Survey, supra* note 4, at 1568.
169. Revised §§ 3-401(a), 3-409, 3-413, 3-414, 3-415, 3-419(b). "Signature" is defined broadly to include any mark or symbol executed or adopted with an intent to authenticate a writing. Revised § 3-4011(b), § 1-201(39). For the implications relating to a bank's liability on a cashier's check or other bank checks, *see infra* Parts IX and X.
170. Holder status is determined under Revised §§ 1-201, 3-104, 3-201 and 4-205. The holder may then qualify for the benefits of holder in due course status under §§ 3-302 and 3-305. *See also* Revised §§ 4-210, 4-211 (holder in due course status of collecting bank); Miller & Harrell, *supra* note 10, para. 3.03. As noted *supra,* the likelihood of this issue arising is somewhat increased as a result of Regulation CC. *See* Allen, *supra* note 162.
171. Revised §§ 3-401(b), 3-402; Miller & Harrell, *supra* note 10, para. 5.03[2], [3]; *supra* Part II.D; and Witten Productions, Inc. v. Republic Bank & Trust Co., 401 S.E.2d 388 (N.C. Ct. App. 1991) (forgeries by promoter constituted valid indorsements because promoter obtained checks as agent of payees).
172. *See* Revised § 3-403(a); Eutsler v. First Nat'l Bank, 639 P.2d 1245 (Okla. 1982) (customer ratified unauthorized signature by advising bank not to pursue remedies against forger); W.R. Grimshaw Co. v. First National Bank & Trust Co. of Tulsa, 563 P.2d 117 (Okla. 1977); Miller & Harrell, *supra* note 10, para. 4.02[2][b].
In Polles v. FDIC, 749 F. Supp. 136 (N.D. Miss. 1990), the bank claimed that a customer ratified an unauthorized indorsement by his former spouse because the customer waited two and a half years before notifying the bank. The court held that mere passage of time is not sufficient to constitute ratification. But in Union National Bank v. Daneshvar, 806 S.W.2d 567 (Ark. Ct. App. 1991), a bank customer notified the bank of a possible forgery of checks on her account, then declined to sign a forgery affidavit because she wasn't sure. Six weeks later she confirmed the forgery (by her husband) and signed the affidavit, but by then the forger had escaped. A jury verdict for the customer was caused on appeal and remanded for determination of the loss reversed the customer's comparative fault. *Polles* and *Union National* Bank are noted in the *1992 Annual Survey, supra* note 4, at 1564-66, which states that Professor Henry J. Bailey III believes that the latter case illustrates the new approach of Revised Article 3.
173. Revised § 3-406(b); Miller & Harrell, *supra* note 10, para. 7.03[3][c][ii]. *See also supra* Part II.F, and the rules governing imposter and fictitious payees at Revised § 3-404(a), (b). *See, e.g.,* Valley Ban v. Monarch Investment Co., 800 P.2d 634 (Idaho 1990) (imposter payee rule did not cover impersonation of agency under Old § 3-404; Revised § 3-404(a) is broader and would cover this situation). *See also supra* Part IV.A. Revised §§ 3-404(b) and 3-405(b) also cover the "padded payroll" cases, where a payroll check is improperly issued to a real or fictitious employee, or where a check is improperly issued to a real or fictitious supplier/creditor of a business. *See* Revised § 3-404, Comment 2 and Revised § 3-405, Comment 3; C.A.L.; Inc. v. Worth, 813 S.W. 2d 12 (Mo. Ct. App. 1991) (padded payroll involving forged indorsement of cashier's check); *Witten Productions, Inc.,* 401 S.E. 2d 388 (noted *supra* at note 171); discussion *supra* Part II.F; *infra* note 178.
The large number of recent cases involving alleged misappropriation of funds by trusted employees or agents suggests a major role for Revised § 3-405. *See, e.g., In re* Lou Levy & Sons Fashions, Inc., 988 F.2d 311 (2d Cir. 1993); J.W. Reynolds Lumber Co. v. Smackover State Bank, 836 S.W. 2d 853 (Ark. 1992); Oswald Machine & Equip., Inc. v. Yip, 13 Cal. Rptr. 2d 193 (1992), *rehearg. denied;* Fred Brunoli & Sons Inc. v. United Bank & Trust Co., 1991 WL 162187 (Conn. 1991); Acrometal Companies, Inc. v. First American Bank of Brainerd, 475 N.W.2d 487 (Minn. App. 1991); O'Mara Enters., Inc. v. Heritage Bank, N.A., 1992 WL 198078 (Ohio Ct. App. 1992); Lehigh Presbytery v. Merchants Bancorp. Inc., 600 A.2d 593 (Pa. 1991); O'Mara Enters., Inc. v. People's Bank of Weirton, 420 S.E. 2d 727 (W. Va. 1992); O'Petro Ambassador Financial Services, Inc. v. Indiana Nat'l. Bank, 591 N.E. 2d 1061 (Ind. App. 1992). While the results might or might not change, most if not all of these cases would involve an analysis under § 3-405(b) of Revised Article 4. The results in *Lou Levy & Sons* and *Witten Production* likely would be affected by application of the comparative negligence standard. *See also infra* notes 178-181 and accompanying text.
174. Revised § 3-406(a); Miller v. Harrell, *supra* note 10, para. 7.03[3][c][ii]. However, if the bank was also negligent it may be unable to assert this preclusion, under old Article 3. In Webb Carter Construction Co. v. Louisiana Central Bank, 922 F.2d 1197 (5th Cir. 1991) the bank was unable to assert the preclusion under old § 3-406 because the bank was negligent in cashing corporate checks for an employee not authorized to do so under the terms of the corporate resolution on file with the bank. In *In re* Lou Levy & Sons Fashions, Inc., 988 F.2d 311 (2d Cir. 1993), the depositary bank was barred from asserting a preclusion under Old §§ 3-404 or 3-406, despite the employer's alleged negligence in failing to detect the scheme, because the bank was assumed to be in the best position to prevent the fraud. As discussed *infra* this text, under Revised § 3-406 the loss in such a case would be proportioned on the basis of comparative negligence. *See infra* note 178 and accompanying text.
175. Revised § 4-406, discussed *infra* at Part IX.
176. *See, e.g.,* Old §§ 3-405 and 3-406. For example, in American Title Ins. v. Shawmut Bank, 812 F. Supp. 301 (D.R.I. 1993), the court held that the drawer's negligence was excused because the payor bank paid on a forged indorsement. The court held that the bank failed to exercise reasonable commercial standards because it did not have a forgery-detection procedure. *See also Lou Levy & Sons,* 988 F.2d 311, and discussion *supra* note 174.
177. Defined at Revised § 3-103(a)(7) to include observance of reasonable commercial standards. This does not necessarily require the bank to sight examine each item for forgery or alteration. *See supra* Parts III.B.8 and III.C.2; *infra* Parts IX and X.
178. This only applies to paragraphs three through five in the text above. *See* Revised §§ 3-405(b), 3-406(b), 4-406(e). For these circumstances, the revisions create a comparative negligence standard for the imposter or fictitious payee, and "padded payroll" types of cases noted *supra* at note 173; the ratification rules at Revised §§ 3-402 and 3-403 (paragraphs one and two in the text above) do not incorporate the comparative negligence concept. For an example of the impact of a comparative negligence standard, *see* Union National Bank v. Daneshvar, 803 S.W.2d 567 (Ark. Ct. App. 1991), noted in the *1992 Annual Survey, supra* note 4, at 1566.

A word more about the imposter and fictitious payee and padded payroll rules at Revised sections 3-404 and 3-405.[179] The imposter payee rule provides that a person issuing an instrument to an imposter payee[180] thereby authenticates the imposter's indorsement as against a person who in good faith pays the instrument or takes it for value or collection. While this does not create liability for anyone who would otherwise not be liable on the instrument, it precludes the issuer of the instrument from defending against liability on grounds of an unauthorized indorsement. In effect, the issuer who is duped by an imposter cannot shift the resulting loss to an innocent holder or payor of the instrument. There is a similar rule in Revised Article 3 covering instruments issued to fictitious payees or improperly issued to a real payee.[181]

Note that revised sections 3-404, 3-405, 3-406, and 4-406 are consistent in that all preclude a party, whose failure to exercise care (as defined therein) contributed to the loss, from asserting a forgery (or in some cases an alteration) against an innocent nonnegligent party who took or paid the instrument for value and in good faith.[182] In all four instances such a preclusion can be mitigated by a showing that the person who took or paid the instrument failed to exercise ordinary care in doing so, in which case, if that failure substantially contributed to the loss, liability will be apportioned on the basis of comparative negligence.[183]

In addition, a bank customer cannot recover for improper payment of an item where that payment discharged a lawful debt of the customer.[184] Finally, where a person signs an instrument only as an "accommodation"[185] to another party, that person is liable in the capacity in which the person signs, except that the person may have the benefit of certain "accommodation party" defenses that will affect that liability.[186]

B. Nature of Liability of Indorsers and Drawers

Drawers and indorsers are secondarily liable, in the sense that each engages to pay the instrument, but only if someone else does not.[187] Generally this and any other conditions, or prerequisites to liability, are similar for both drawers and indorsers, although the ramifications of the failure of a condition are quite different, as it is more difficult for a drawer to be discharged as a result of a failure of a condition than it is for an indorser to be discharged in the same circumstances.[188]

Generally there are three prerequisites or conditions necessary to enforce the liability of an indorser: (1) The instrument must be properly presented (to the maker or drawee/payor), (2) it must be dishonored (by nonpayment), and (3) the indorser must be given proper notice of the dishonor.[189] The drawer of a draft is obligated to pay the draft upon its proper presentment and dishonor.[190]

Dishonor is defined at Revised section 3-502 to require prior presentment and nonpayment (and, in the case of an item governed by Article 4, return by the payor bank within its midnight deadline and the rules governing payor bank accountability at Revised sections 4-301 and 4-302).[191] Additional conditions pertaining to the time of presentment for checks are provided at Revised sections 3-414(f) (for purposes of the liability of drawers) and 3-415(e) (for purposes of the liability of indorsers): an indorser is discharged from liability if the check is not presented for collection or payment within 30 days of the indorsement;[192] the drawer may be discharged if the check is not presented for collection or payment within 30 days of its date, but only if the drawee/payor bank suspends payments after that 30 day period and the drawer is deprived of funds to pay the check as a result.[193]

Similarly, in order to hold an indorser liable, notice of dishonor must be given within certain time limits as a prerequisite to the liability of the indorser and in some cases the drawer must be given notice of dishonor as well. A payor or collecting bank has a duty to give notice of dishonor within its midnight deadline (the payor bank must do so by returning the item itself, unless the item is unavailable for return due, *e.g.*, to a truncation agreement).[194] Other parties must give notice of dishonor within 30 days after receiving notice of the dishonor.[195] Presentment, dishonor, and notice of dishonor may be excused or waived,[196] but otherwise are prerequisites to the liability of indorsers and some drawers.[197] Failure to give notice of dishonor within the time specified will discharge liability.[198] The revisions make it easier for nonbank holders to preserve liability by increasing the time for presentment (from seven to 30 days) and the time for giving notice of dishonor (raised from three to 30 days), but as before the liability of the drawer generally will be discharged by a delay only if the drawee has suspended payments and this causes the loss.[199]

179. The imposter payee rule is largely carried over from Old § 3-405, though the scope is expanded to cover one posing as an agent of the payee. *See* Revised § 3-404, Comment 1; Miller & Harrell, *supra* note 10, para. 7.03[3][c][ii]. Revised §§ 3-404(b) and 3-405(b) also cover cases where a check is improperly issued to a person not entitled to receive it, perhaps as part of a scam intended to defraud the issuer, and then is passed to an innocent party. *See* Revised § 3-404, Comment 2, and Revised § 3-405, Comment 3. Such innocent party may qualify as a holder in due course, despite the imposter's indorsement. *See, e.g.*, Derrico v. Bungee Intern. Mfg. Co., 989 F.2d 247 (7th Cir. 1993). *See also supra* notes 173 and 178.

180. One posing as someone else, or in league with an imposter. *See* Revised § 3-404, Comment 2; *C.A.L.*, 813 S.W.2d 12 (padded payroll and conspiracy). *See also supra* notes 173 and 178.

181. Revised §§ 3-404(b) and 3-405(b).

182. "Good faith" and "value" are defined at revised § 3-103(a)(4) (" 'Good faith' means honesty in fact and the obsevance of reasonable commercial standards of fair dealing.") and § 3-303.

183. *See, e.g.*, Miller & Harrell, *supra* note 10, para. 9.03[4][c]; Union National Bank v. Daneshvar, 803 S.W.2d 567 (Ark. Ct. App. 1991) (comparative negligence illustrated under nonuniform Arkansas statute).

184. *See, e.g.*, Cooper v. Stockyards Bank, 644 P.2d 123 (Okla. App. 1981); Lehigh Presbytery v. Merchant Bancorp., Inc., 600 A.2d 593 (Pa. 1991); Ambassador Financial Services, Inc. v. Indiana Nat'l. Bank, 591 N.E. 2d 1061 (Ind. App. 1992); IXI Laboratories, Inc. v. First Bank, N.A., 483 N.W.2d 84, 17 UCC Rep. Serv. 2d 520 (Minn. App. 1992).

185. *See* Revised § 3-419(a). In effect this means the person is signing in order to benefit another party (*e.g.*, as surety or guarantor), without directly receiving the value or benefit given for the instrument.

186. *See* Revised §§ 3-419(c), 3-605, 3-305(d); Miller & Harrell, *supra* note 10, para. 5.02; *supra* Part II.K.

187. *See* Revised § 3-414, 3-415. This rule does not apply to the drawer of a cashier's check or other draft drawn on the drawer. Such a drawer is subject to primary liability, like the maker of a note. *See* Revised § 3-412. *See also* Revised §§ 3-312, 3-411, and discussion *infra* at Part X; Miller & Harrell, *supra* note 10, para. 9.01[4][d], [e]. If a personal check is certified by the drawee bank, the bank assumes the sole obligation to pay the instrument, and the drawer is discharged from liability. *See* Revised § 3-414(c) and *supra* Parts VI.C and X.

188. *See* Revised §§ 3-414, 3-415, 3-501, 3-502. *Cf.* Revised §§ 3-414(f), 3-415(e). *See* discussion *infra* this text; Miller & Harrell, *supra* note 10, para. 4.03 and para. 406.

189. *See* Revised §§ 3-415, 3-501, 3-502, 3-503, and discussion *infra* this text. Not all prerequisites apply in every case. The prerequisites of presentment and notice of dishonor may be excused under Revised § 3-504, or Old § 3-511. *See* Miller & Harrell, *supra* note 10, para. 4.06[2].

190. Revised § 3-414(b); Miller & Harrell, *supra* note 10, para. 4.03[2][a]. In some cases, notice of dishonor must also be given. *See* Revised § 3-503(a).

191. *See* Revised § 3-502(b). Proper presentment is defined at Revised § 3-501. *See*, Miller & Harrell, *supra* note 10, para. 4.03[2][a][i], para. 8.03, and para. 8.04[3][f].

192. Revised § 3-415(e). This time limit is expanded from seven days under Old § 3-503(2)(b), thus reducing the likelihood that indorsers will be discharged in most cases. *See* Miller & Harrell, *supra* note 10, para. 4.06[2][a].

193. *See* Revised § 3-414(f), Miller & Harrell, *supra* note 10, para. 4.03[2][d][i]. Despite the extension of the time limit from seven to 30 days for indorsers, it remains more likely that an indorser will be discharged than the drawer. For example, presentment more than 30 days after the indorsement, alone, may discharge the liability of the indorser, while the drawer will be discharged only if the payor bank suspends payments.

194. Revised §§ 3-503(c), 4-104(a)(10), 4-301. The depositary bank is a collecting bank unless it is also the payor bank. *See* Revised § 4-105(2), (3), (5). A failure to meet this requirement does not, however, preclude chargeback to the customer's account by a collecting bank under Article 4, though the bank may be liable for damages resulting from the delay. *See* Revised §§ 4-214, 4-202, 4-109, 4-103(e); Miller & Harrell, *supra* note 10, para. 4.06[2][a]. The liability of a drawee/payor bank in these circumstances is governed by Revised §§ 4-215, 4-301, and 4-302, and is somewhat more absolute though still subject to exceptions. *See* Miller & Harrell, *supra* note 10, para. 4.06[2][a].

195. Revised § 3-503(c). This is up from three days under Old § 3-508(2).

C. Impact on the Underlying Obligation

Revised section 3-310 replaces old section 3-802, generally preserving the old rule but providing greater specificity. As before, if a certified check, cashier's check, or teller's check[200] is taken for an obligation, the obligation is discharged as if paid in cash.[201] If an uncertified (*i.e.* personal) check is taken for an obligation, the obligation is "suspended" until the instrument is paid, certified, or dishonored.[202] If the check is paid or certified, this discharges liability for the underlying obligation to the extent of the amount of the check.[203]

If an uncertified check is taken for an obligation, and the check is dishonored,[204] then suspension of the obligation terminates and the person who took the check in payment (the obligee on the underlying obligation) may enforce either the obligation or the liabilities on the instrument,[205] if that obligee is both the person to whom the obligation is owed and the person entitled to enforce the instrument.[206] If the obligee is à depositary or intermediary bank, and it has met the conditions to invoke the liability of indorsers, it may proceed to collect from the indorsers pursuant to their liability on the instrument. Alternatively (again assuming the bank has retained possession of the instrument and is a holder or is otherwise entitled to enforce the instrument) the depositary or intermediary bank may seek recovery from the drawer as a result of the drawer's liability on the instrument, or may charge-back the item to its customer's account and, if this results in a deficit balance (commonly called an "overdraft"), that can be recovered from the customer. These matters will be discussed further *infra* at Part VIII.B.

D. Impact of Liability on The Instrument On Rights of Collecting Banks

As noted, in limited circumstances if a check has not been presented for payment or collection within 30 days after its date, the drawer may be discharged from liability.[207] If the instrument is not presented or collection initiated within 30 days of an indorsement, the indorser will be discharged.[208]

Any of these time periods may affect the ability of a collecting bank to collect an instrument that it cashes or takes for deposit or collection.[209] While a collecting bank normally will qualify as a holder in due course,[210] if the instrument is overdue or liability has been discharged by the lapse of time, this may preclude holder in due course status and impair the ability of the bank to collect the instrument.[211] However, this will not affect the ability of the collecting bank to charge back the dishonored item to the customer's account.[212]

E. Impact of Secondary Liability on the Instrument with Respect to the Underlying Obligation

There is some misleading wording in Revised Article 3 at section 3-310(b)(1). That section was taken from Old section 3-802(1)(b), which read in part: "discharge of the underlying obligor on the instrument also discharges him on the obligation."[213] Revised section 3-310(b)(1) was intended to carry that rule forward into the new Article 3, but the revision states only that "[p]ayment or certification of the check results in discharge of the obligation to the extent of the amount of the check."[214] The negative inference, apparently not intended by the drafters, is that discharge of liability on the instrument by means other than payment or certification does not discharge liability for the underlying obligation.

For example, suppose that a check is taken from an indorser for payment of an underlying obligation (*e.g.*, a bank loan). This could occur where a bank's borrower makes payment by indorsing to the bank a check drawn to the borrower/indorser by a third party. If (perhaps due to a clerical error or misplacing of the check) the bank does not present the check or commence collection for more than 30 days, the indorser will be discharged of liability on the instrument.[215] Under prior law this discharge of liability on the instrument would also discharge the borrower's liability for the un-

196. Revised § 3-504. *See* Miller & Harrell, *supra* note 10, para. 4.03[2][a][i] (liability of drawer) and para. 4.06[2][b] (liability of indorser).

197. Revised §§ 3-501, 3-502, 3-503(a). *See* Miller & Harrell, *supra* note 10, para. 4.06[1], [2].

198. *Cf.* Revised §§ 3-414(d), 3-415(c).

199. *See* Revised §§ 3-414(f), 3-415(c), (e); Miller & Harrell, *supra* note 10, para. 4.03[2][1][ii] and para. 4.03[2][d].

200. The revision thus treats teller's checks the same as cashier's checks and other, similar bank obligations. Generally they were treated the same as cashier's checks under prior law, but it was necessary for the cases to clarify this point. *See, e.g.*, Malphrus v. Home Sav. Bank, 254 N.Y. S.2d 980 (Co. Ct. 1965); Revised § 3-104(h) defines "Teller's check" as a draft drawn by a bank on another bank or payable at or through a bank, and Revised Article 3 generally treats teller's checks like cashier's checks as illustrated by Revised § 3-310. *But cf.* Revised §§ 3-312, 3-411, 3-412, 3-414, and *see* discussion *infra* Part X; Miller & Harrell, *supra* note 10, para. 9.01[4][d].

201. *See* Revised § 3-310(a); Old § 3-802(1)(a); Miller & Harrell, *supra* note 10, para. 7.01[1].

202. Revised § 3-310(b)(1); *cf.* Old § 3-802(1)(b). Miller & Harrell, *supra* note 10, para. 7.01[1][c].

203. Revised § 3-310(b) (1). Discharge of liability on the instrument by any other means also discharges the underlying obligation to the same extent, as under the Old Code, although the revision does not specifically say so. *See infra* Part VI. E.

204. Generally dishonor occurs if proper presentment is made and the instrument is not paid. *See* Revised §§ 3-501, 3-502; Miller & Harrell, *supra* note 10, para. 4.03[2][a] and 4.06[2][a].

205. *See generally* Revised § 3-414 and Miller & Harrell, *supra* note 10, para. 4.03 (liability of drawer); § 3-415 and Miller & Harrell, *supra* note 10, para. 4.06 (liability of indorsers).

206. Revised § 3-310(b)(3); Miller & Harrell, *supra* note 10, para. 7.01[1] and 7.03[3][a].

207. *See* Revised § 3-414(f), and discussion *supra* at Part VI.B. The drawer will be discharged only if the drawee has suspended payments. *Id.*; *see generally* Miller & Harrell, *supra* note 10, para. 4.06.

208. *See* Revised § 3-415(e) Miller & Harrell, *supra* note 10, para. 4.06.

209. Regulation CC may require the bank to allow customer withdrawals before the check is collected. If the check is returned unpaid and the bank is unable to collect from its customer the bank may seek recourse against those liable on the instrument.

210. *See* Revised §§ 4-205, 4-210, 4-211, and discussion *supra* at Parts III.A.1 and III.C.1.

211. *See* Revised §§ 3-302, 3-305; Miller & Harrell, *supra* note 10, para. 3.03.

212. *See* Revised § 4-214(1) and *supra* Part VI.B.

213. *See* Old § 3-802(1)(b), and Comment 2; Miller & Harrell, *supra* note 8, para. 7.01[1][b], [c].

214. Revised § 3-310(b)(1); Miller & Harrell, *supra*.

215. Revised § 3-415(e). The bank would still have recourse against the drawer unless the drawee has suspended payments. *See* Revised § 3-414(f); Miller & Harrell, *supra* note 10, para. 4.03.

derlying obligation.[216] Revised section 3-310 apparently was intended to provide the same result, but the plain language of Revised section 3-310(b)(1) indicates only that *payment* (or certification) of the instrument will discharge liability on the underlying obligation.[217] Revised section 3-310(b)(3) reinforces this by providing a rule like that of Old section 3-802 in the last sentence. Therefore, in the hypothetical fact scenario described above, the bank may be able to argue that, under the plain meaning of the Revised Article 3, discharge of an indorser under section 3-415(e) does not discharge the indorser's liability on the underlying obligation (in this hypothetical, the bank loan). But given no reason for a change, such a change[218] should not be found; other law through section 1-103 should provide a discharge.

VII. Payment & Dishonor

A. The Concept of "Properly Payable"

If a check is presented to the drawee/payor bank for immediate payment over the counter, the bank should first ascertain whether the item is properly payable. The bank will have authority to charge the check to its customer's account (the account of the drawer) only if the item is properly payable.[219] If the check is not properly payable, the bank cannot charge its customer's account, and will suffer any loss resulting from uncollectibility of the instrument that cannot be otherwise shifted (such as by warranty or preclusion).[220]

An item is properly payable "if it is authorized by the customer and is in accordance with any agreement between the customer and the bank."[221] While this definition recognizes that most of the rules in Articles 3 and 4 governing the concept of "properly payable" are subject to variation by agreement,[222] in most instances an item will have to conform to the requirements of Articles 3 and 4 in order to be properly payable.[223] Hence, before making payment the drawee/payor bank needs to be sure that the item being presented for payment has been properly executed, indorsed, and presented pursuant to the rules discussed in this article.[224] Conversely, refusal to pay an item that is properly payable under Revised section 4-401 may make the bank liable for wrongful dishonor under Revised section 4-402. This requires that bank staff be trained to identify properly payable items and to avoid wrongful dishonor of such items.[225]

A few examples will serve to illustrate the concepts of properly payable and wrongful dishonor. If the holder of a check, properly executed and indorsed, takes the check to the drawee/payor bank and requests that it be certified, the bank may refuse and this refusal will not constitute dishonor, because a refusal of certification is not defined as a dishonor,[226] and also because the Code explicitly so states.[227]

In contrast if such a check is presented for payment, and the drawee/payor bank refuses, this constitutes dishonor.[228] If the check was properly payable this will be wrongful dishonor, and the bank will be liable for resulting damages.[229] On the other hand, if the bank pays an item that is not properly payable, it cannot charge the customer's account for the amount of the item and therefore may suffer any resulting loss.[230]

In order to help the bank determine which items are properly payable, Article 3 permits the bank to require that the instrument be exhibited for inspection unless otherwise agreed,[231] and that the person making presentment provide "reasonable identification," sign a receipt, and (if full payment is made) surrender the instrument.[232] If the bank imposes these requirements and they are not met, the bank's refusal to pay does not constitute dishonor. Similarly, if the instrument lacks a necessary indorsement, or otherwise fails to comport with the agreement of the parties, the requirements of Articles 3 and 4, or other applicable law, refusal to pay will not constitute dishonor.[233]

B. UCC Time Limitations[234]

Time periods may or may not affect a payor bank's obligation to pay an instrument. As discussed *supra* at Part II.A, Revised section 3-118 provides a statute of limitations that requires commencement of

216. Old § 3-802(1)(b); Miller & Harrell, *supra* note 10, para. 7.01[1][b], [c].

217. Revised § 3-310(b)(1); Miller & Harrell, *supra* note 10.

218. *See* Comments to § 3-310 and Table of Disposition in Prefatory Note.

219. *See* Revised § 4-401(a) and Comment 1, citing Torrance National Bank v. Enesco Federal Credit Union, 285 P.2d 737 (Cal. App. 1955). If the item is properly payable the bank may charge the account even if it creates an overdraft. *Id.* Each account holder is not then liable for the overdraft, unless they either signed the check or benefited from it or contracted otherwise. Revised § 4-401(b). *See* Miller & Harrell, *supra* note 10, para. 9.01[1], [2]. *See also supra* Part VI.A. for some qualifications and exceptions.

220. *See generally*, the *1992 Annual Survey*, *supra* note 4, at 1564-1567 ("Shifting Losses to the Drawer"); discussion *supra* Part VI.A. and *infra* Part IX.

221. Revised § 4-401(a), and Comment 1. This generally confirms the contractual basis of the bank - customer relation, as one of debtor -creditor, absent some unusual circumstances. *See, e.g.,* W.R. Grimshaw Co. v. First National Bank & Trust Co. of Tulsa, 563 P.2d 117 (Okla. 1977); State Guaranty Bank of O'Keene v. Doerfler, 226 P.2d 1054 (Okla. 1924). However other law may apply to specific aspects of the relation. *See, e.g.,* Regulation CC, 12 C.F.R. Pt. 229 (Expedited Funds Availability); Regulation DD, 12 C.F.R. Pt. 230 (Truth in Savings). *See also* Miller & Harrell, *supra* note 10, para. 9.01[1]. The revisions confirm prior cases placing on the customer responsibility for items forged by unauthorized use of the customer's facsimile signature machine. *See, e.g.,* Revised § 3-404, Comment 2, Case No. 4, and Perini Corp. v. First Nat'l Bank of Habersham County, 553 F.2d 398 (5th Cir. 1977). The nature of the customer's contractual arrangements with other banks is irrelevant. Federal Insurance Co. v. NCNB Nat'l Bank of North Carolina, 958 F.2d 1544, 17 UCC Rep. Serv. 2d 597 (11th Cir. 1992). *See generally,* Pierce, *supra* note 102.

222. *See* UCC § 1-102(3); Revised § 4-103(a), and Comment 1; Miller & Harrell, *supra* note 10, para. 9.01[1], [2].

223. *See* Miller & Harrell, *supra* note 10, para. 9.01[1]. For example, if the name of the payee of a check has been altered the item is not properly payable. Biltmore Associates LTD v. Marine Midland Bank, N.A., 578 N.Y. S.2d 798, 17 UCC Rep. Serv. 2d 179 (N.Y. 1991).

224. Dishonor of a "stale" check is not wrongful dishonor even if it is otherwise properly payable. *See* Steenbergen v. First Fed. Sav. & Loan, 753 P.2d 1330 (Okla. 1987); *infra* Part VII.B.

225. For example, in Shaw v. Union Bank & Trust Co., 640 P.2d 953 (Okla. 1981), a savings withdrawal order was treated as an Article 4 "item" and the bank's refusal to honor the order constituted wrongful dishonor under § 4-402. The definition of "item" in Revised § 4-104(1)(9) confirms this result. *See supra* Part III.A.2.

226. *See* Revised §§ 3-501(a)(ii) and 3-502(b)(2); Miller & Harrell, *supra* note 10, para. 4.03[2][a][i].

227. *See* Revised § 3-409(d); Miller & Harrell, *supra* note 10, para. 4.04[1].

228. Revised § 3-501(a), § 3-502(b)(2). It should be noted that this requires presentment to the drawee/payor bank; a demand for payment on any other bank (*e.g.,* a depositary bank) will not constitute presentment. *Id.,* Revised § 4-105. *See supra* Part VI.B.

229. Revised § 4-402; Miller & Harrell, *supra* note 10, para. 9.01[1][2], para. 9.02[2][3]. The UCC limits this liability to the bank's customer. *See* § 4-402. However, in Agostino v. Monticello Greenhouses, Inc., 166 A.D. 2d 471, 560 N.Y. S.2d 690 (N.Y. App. Div. 1990), a noncustomer was allowed to recover for wrongful dishonor on common law grounds; section 1-103 was viewed as not precluding this.

230. Unless the bank can avail itself of the Code's loss - shifting rules. *See, e.g.,* Revised §§ 3-401 through 3-406, 4-208, 4-406, and 4-407; discussion *supra* at Part VI.A., and *infra* at Part VIII; Miller & Harrell, *supra* note 10; the *1992 Annual Survey, supra* note 6, at 1564-67 ("Shifting Losses to the Drawer"). The bank may also become liable for wrongful dishonor of other items when the account is depleted by the wrongful payment. *See* Revised § 4-402; Miller & Harrell, *supra* note 10, para. 9.02[2][3].

231. Revised § 4-110.

232. Revised § 3-501(b)(2). If the presentment is being made on behalf of another, reasonable evidence of authority may be required. *Id. See generally,* Miller & Harrell, *supra* note 10, para. 4.03[2][a][iii].

233. Revised § 3-501(b)(3); Miller & Harrell, *supra* note 10, para. 4.03[2][a][i] and [iii]. But note Revised § 4-205.

234. *See also infra* Part IX.F. (discussing one year limitation period at Revised § 4-406(f)).

an action to collect an unaccepted draft such as a check within three years after dishonor or within ten years of the date of the instrument, whichever comes first. After such time the claim is barred, but this does not mean the item ceases to be properly payable. The statute of limitations at section 3-118 merely bars assertion of a claim based on the instrument in court; it does not render the instrument void as an order to pay. Generally the limitation periods at Revised section 3-118 do not affect a payor bank's authority to pay the item or charge its customer's account. Similarly, Revised section 4-404 provides that a payor bank has no obligation to honor a check (other than a certified check) more than six months old, but this does not prevent a bank from paying such a check in good faith[235] or make such payment improper.[236]

Under Revised Article 3, for purposes of holding in due course, a check becomes "overdue" (or "stale") 90 days after its date.[237] This is up from 30 days under Old Article 3.[238] If a bank or other party takes such an instrument, it takes with notice that it is overdue, and cannot be a holder in due course.[239] Again, however, this does not prevent the instrument from being properly payable; while the resultant lack of holder in due course status may be fatal if a collecting bank seeks to collect a dishonored check by enforcing the liability of parties to the instrument, it does not prevent the drawee/payor bank from charging the check to the drawer's account as a properly payable item if that is done in good faith and in a manner not inconsistent with an agreement.

C. Wrongful Dishonor

Under Revised section 4-402(a) dishonor of a properly payable item is wrongful dishonor, and the bank may be held liable for actual damages caused to its customer as a result.[240] Absent an agreement to the contrary the bank may dishonor any item drawn on insufficient funds, even if it is otherwise properly payable. If an item is not properly payable there can be no wrongful dishonor, even if the bank stamps the wrong reason on the face of the check.[241]

The bank's liability for wrongful dishonor is limited to actual damages proved. As noted previously this rejects the old "trader" rule, holding banks liable for damages per se on grounds of a presumption that the customer's reputation was injured by the dishonor.[242] However, the actual damages suffered may include consequential damages, unless the parties have made an agreement to the contrary.[243]

Cases like *Shaw v. Union Bank & Trust Co.*[244] (holding that wrongful dishonor is a "tortious breach of a status-based duty of care") are essentially repudiated under the revisions. While Revised Article 4 does not specifically reject this line of reasoning, the very clear statutory remedies at section 4-402 should displace alternative theories pursuant to UCC sections 1-103 and 1-106(1). However, if punitive damages for the conduct constituting wrongful dishonor are available under other law, they are available here. But note that the trend of authority is to recognize that the nature of the bank-customer relation creates a debtor-creditor relationship governed by the agreement of the parties and statutory law, and to reject aberrational cases to the contrary absent truly egregious circumstances.[245]

Dishonor of a "stale" check is not wrongful dishonor,[246] even if it is otherwise properly payable.

VIII. Notice of Dishonor and the Midnight Deadline

A. Notice of Dishonor and Recourse on the Instrument -- Impact on Nonbank Holders

As a prelude to discussing the responsibilities of banks with regard to the dishonor and return of unpaid items under Article 4, it may be helpful to review the general requirements in Revised Article 3 for notice of dishonor, discussed *supra* at Part VI. In Article 3, notice of dishonor is primarily relevant to retaining the liability of indorsers on the instrument. Under Revised section 3-503 notice of dishonor must be given to prior indorsers by persons other than a bank within 30 days after that person has received notice of the dishonor.[247] Failure to do so will discharge the liability of the indorser,[248] unless notice is excused.[249]

As a consequence, if the owner of a deposited item (i.e., the depositary bank's customer) receives notice from the depositary bank that a deposited item has been dishonored by the drawee/payor bank, that customer must in turn give notice to any prior indorsers within 30 days or the liability of the affected indorser will be discharged.[250] It may be expected that, in the case of multiple, consecutive indorsements, each indorser will then give the required notice of dishonor to that indorser's prior indorser, thus preserving a chain of liability between indorsers leading ultimately to the payee and then the drawer. Collecting banks and others may give notice by any reasonable means, including oral, written or electronic communication.[251]

If, however, the immediately preceding indorser is insolvent or cannot be found, the holder of the instrument may give notice of

235. Revised § 4-404; Miller & Harrell, *supra* note 10, para. 9.01[4][b]. Payment of a stale check does not violate the bank's duty of good faith, even in the face of an expired stop payment order. *See* Hartford Accident & Indemnity Co. v. First Pa. Bank, N.A., 859 F.2d 295 (3d Cir. 1988). However, dishonor of a stale check is not wrongful dishonor. Steenbergen v. First Fed. Sav. & Loan, 753 P.2d 1330 (Okla. 1987). For cashier's checks, *see* Revised §§ 3-312, 3-411; Revised § 4-404 and Official Comment; Miller & Harrell, *supra* at note 10, para. 3.03[2][b]; *infra* Part X.

236. Revised § 3-103(a)(4) contains a new definition of good faith that incoporates both honesty in fact and the observance of reasonable commercial standards of fair dealing.

237. Revised § 3-304(a)(2); Miller & Harrell, *supra* note 10, para. 3.03[2][b][v].

238. *See* Old § 3-304(3)(c).

239. Revised § 3-302(a)(2)(iii); Miller & Harrell, *supra* note 10, para. 3.01[3], [4], para. 3.03[2][b][v], para. 3.04, para. 6.03.

240. Dishonor is defined at § 3-502. Under the Code, liability for wrongful dishonor is limited to the bank's customer. *See* § 4-402. However, Agostino v. Monticello Greenhouses, Inc., 166 A.D. 2d 471, 560 N.Y. S.2d 690 (N.Y. App. Div. 1990) allowed recovery by a noncustomer on common law grounds. *See also* Revised § 4-402, Comment 5.

241. This rejects the reasoning of Johnson v. Grant Square Bank & Trust Co., 634 P.2d 1324 (Okla. 1981). *But see infra* note 291.

242. *See, e.g.* Commercial National Bank v. Latham, 116 P.197 (Okla. 1911); Everett v. First National Bank of Geary, 109 P.2d 824 (Okla. 1941). The revisions reject this reasoning.

243. *See* Revised § 4-402(b). Only damages resulting from a lack of good faith or ordinary care are beyond modification by agreement, however.

244. 640 P.2d 953 (Okla. 1981). *Shaw* relied on pre-Code authority, concluding that it survived enactment of the UCC. 640 P.2d at 957-58. *See also* Smith v. Citizens State Bank, 732 P.2d 911 (Okla. 1986). This reasoning is dubious.

245. *See infra* Part IX.G; Pierce, *supra* note 102.

246. *See* Revised § 4-404, and Steenbergen v. First Fed. Sav. & Loan, 753 P.2d 1330 (Okla. 1987).

247. Revised § 3-502(c); Miller & Harrell, *supra* note 10, para. 4.06[2][a]. There are special rules for banks, as discussed *infra*. *See* Revised §§ 3-503(c)(i), 4-202, 4-214, 4-215, 4-301, 4-302; discussion *infra* at Part VIII.B, C, D; Miller & Harrell, *supra* note 10, para. 8.02 and para. 8.03.

248. Revised §§ 3-503(a), 3-415(c). *Cf.* the liability of drawers at Revised §§ 3-414(b), 3-414(d), 3-503(a), except under § 3-414(d). *See generally* Miller & Harrell, *supra* note 10, para. 4.03 and para. 4.06.

249. *See* Revised § 3-504; Miller & Harrell, *supra* note 10, para. 4.03[2][d][iii] and para. 4.06[2][b]; *supra* Part VI.

250. *See* Revised § 3-310, and discussion *supra* Parts VI.C and E.

251. Revised § 3-503(b). Return of an instrument that was delivered to a bank for collection constitutes notice. *Id.,* and Revised §§ 4-402(a)(2) and 4-214(a). Generally, however, a payor bank must return the item. *See* Revised § 4-301(a)(1); discussion *supra* Part III.B and *infra* at Parts VII.B, C, D; Miller & Harrell, *supra* note 10, para. 8.02.

dishonor to other prior indorsers and seek recourse directly against such parties based on their liability.[252] Indeed, the holder may seek to recover directly from any prior indorser who remains liable, so long as the 30 day notice of dishonor requirement is met.[253] While any reasonable means designed to inform prior parties will be sufficient,[254] the old provision specifically permitting notice by a mailing to the last known address was omitted from the revision.[255] Notice of dishonor may be excused, waived, or modified by agreement by the parties.[256]

B. Notice of Dishonor and the Midnight Deadline Under UCC Article 4 -- Collecting Banks

Each collecting bank is an agent or subagent of the owner of the item (*e.g.,* the depositor) and therefore owes a duty to follow the instructions of that party in handling and processing the item.[257] A collection agreement may therefore supersede many of the Article 4 rules on bank collections.[258] Absent such agreement, however, collecting banks handling checks are governed by Article 4, Part 2, and Federal Reserve Regulation CC.[259] This discussion focuses on the Article 4 issues.

The basic duty of every collecting bank is to exercise "ordinary care" in handling the item.[260] A collecting bank meets this duty if it processes and forwards the item before the bank's midnight deadline but it may act within a longer time as reasonable. Thus a collecting bank does not have a statutory duty to meet the midnight deadline as such; the midnight deadline is merely one means of meeting the duty of ordinary care.[262] Failure to give notice within the bank's midnight deadline may result in discharge of the liability of indorsers to such bank,[263] but will not affect the right of the collecting bank to charge back the item to the account of its customer or to collect any resulting overdraft from that customer.[264]

A collecting bank that misses its midnight deadline may still meet its duty of ordinary care by giving notice of dishonor at a later time, but the bank has the burden of establishing that the delay was reasonable.[265] The bank is not responsible for the mistake or misconduct of any other party in the collection process. The collecting bank may either return the item (as notice of dishonor) or send other notice of the fact of dishonor.[266] Certain types of delays are specifically excused at Revised section 4-109.[267] If the collecting bank fails to establish that a delay was reasonable or excused, and is found to have violated the bank's duty of ordinary care, the bank is liable for actual damages caused by the delay, up to the amount of the item.[268] Again, however, this will not affect the bank's right of chargeback against the customer's account.[269]

C. Notice of Dishonor and the Midnight Deadline -- Depositary Banks

A "depositary bank" is the first bank to take the item, "even if it is also the payor bank, unless the item is presented for immediate payment over the counter."[270] The depositary bank is also a collecting bank (unless it is the payor bank), and therefore is subject to the rights and duties discussed *supra* with regard to collecting banks.[271] In addition, a depositary bank is subject to certain duties relating to the relationship with its customer (the depositor or other owner of the item being collected through the banking system).[272]

Generally speaking, the depositary bank has the same obligation as other collecting banks to use ordinary care in handling the item on behalf of its owner.[273] As noted *supra,* a collecting bank discharges this duty if it acts within its midnight deadline, but the bank may act within a reasonably longer time.[274] This is further subject to various excuses for delay, generally based on factors beyond the control of the bank.[275] If the bank violates its duty of ordinary care (and has acted in good faith), its liability is limited to actual damages up to the amount of the item.[276] If the depositary bank is also the

252. Revised §§ 3-503(a), 3-414(d), 3-415(a); Miller & Harrell, *supra* note 10, para. 4.03 and para. 4.06. Of course, the drawer could also be sued. *See supra* Part VI.

253. Revised §§ 3-503(c), 3-415(e). This is a good reason to attempt giving notice to all prior indorsers within the 30 day period. *See* Miller & Harrell, *supra* note 10, para. 4.03[2][b], para. 4.06[2][a].

254. Revised § 3-503(b); Miller & Harrell, *supra* note 10, para. 4.03[2][b].

255. *See* Old § 3-508(4); Miller & Harrell, *supra* note 10, para. 4.03[2][b]. This method may still be used; the change results from the effort in Revised Article 3 to provide rules of broad application.

256. Revised § 3-504.

257. The depositor's ownership rights to the item and its proceeds are nonetheless subject to statutory rights of the collecting bank arising from any credit given the customer and withdrawn under § 4-210. *See* Revised §§ 4-201(a), 4-214; Miller & Harrell, *supra* note 10, para. 8.03[4].

258. Revised § 4-103(a); § 1-102(3); Miller & Harrell, *supra* note 10. para. 8.01[2], para. 9.04[3].

259. 12 C.F.R. Pt. 229. For discussion of Regulation CC, *see* Miller & Harrell, *supra* note 10, para. 8.04; and Conni L. Allen, *The New Rules Governing Collection and Payment of Checks in the Banking System: Impact of Regulation CC,* 47 Consumer Fin. L.Q. Rep. 129 (1993).

260. Revised § 4-202(a). "Ordinary care" is defined at Revised § 3-103(a)(7) to mean observance of reasonable commercial standards prevailing in the local area. This does not necessarily require sight examination of each item. *See supra* Part III.C.2.

261. Revised § 4-02(b); Miller & Harrell, *supra* note 10, para. 8.03[3].

262. *Cf.* Revised § 4-301 (midnight deadline for payor banks).

263. *See* Revised §§ 3-415(c), 3-503(a), (c); Miller & Harrell, *supra* note 10, para. 4.06[2][a]; *supra* Part VI.

264. Revised § 4-214; Miller & Harrell, *supra* note 10, para. 8.03. Similarly, failure to meet the bank's midnight deadline does not affect the bank's right to recover from the drawer of the item, assuming the bank has retained possession of the item. *See* Revised § 3-414.

265. Revised § 4-202(a)(2) and (b); Miller & Harrell, *supra* note 10, para. 8.03[3]. *See also* Revised § 4-214(a). Symonds v. Mercury Savings & Loan Association, 275 Cal. Rptr. 871, 13 U.C.C. Rep. Serv. 2d (Callaghan) 31 (Cal. Ct. App. 1990) involved a bank that allegedly failed to forward a check for a period of eight months. While properly declining to characterize the bank's obligation as quasi-fiduciary (*see infra* Part IX.G), the court discussed the level of conduct that would permit a bank customer to recover in tort for intentional infliction of emotional distress in this context. *See also* 1992 Annual Survey, *supra* note 4, at 1562; Pierce, *supra* note 102.

266. Revised § 4-202(a)(2). As noted *supra,* however, the bank's ability to recover from the drawer and other parties liable on the instrument may depend upon the bank's retention of possession of the item, in order to achieve holder status, suggesting a reason not to give notice by return of the item. *Cf.* Revised § 4-301(a)(1) (for payor banks). *See generally* Miller & Harrell, *supra* note 10, para. 3.03.

267. The revision added computer or other equipment failures to the list of excused delays. This change codifies Port City State Bank v. American Nat'l Bank, 486 F.2d 196 (10th Cir. 1973). *See* Revised § 4-109, Comment 3.

268. Revised §§ 4-103(e) and 4-214(a). Other damages may be appropriate if the bank was guilty of bad faith. *Id. See also* Miller & Harrell, *supra* note 10, para. 9.03[1], [2]; *infra* Part IX.G.; *Symonds,* 275 Cal. Rptr. 871 (noted *supra* note at 265).

269. *See* Revised § 4-214(a); discussion *supra* this Part; Bank of New York v. Asati, Inc., 585 N.Y. S.2d 411, 18 UCC Rep. Serv. 2d 535 (N.Y. App. 1992).

270. Revised § 4-105(2); Miller & Harrell, *supra* note 10, para. 8.01[3][c].

271. *See supra* Part VIII.B and Revised § 4-105(5) ("collecting bank means a bank handling an item for collection except the payor bank.").

272. *See, e.g.,* Revised § 4-201(a); Miller & Harrell, *supra* note 10, para. 9.03[1].

273. Revised §§ 4-201(a), 4-202(a); Miller & Harrell, *supra* note 10, para. 8.03.

274. Revised §§ 4-202(b), 4-214(a), (d); Miller & Harrell, *supra* note 10, para. 8.03[3].

275. Revised § 4-109(b); Miller & Harrell, *supra* note 10, para. 8.03[3].

276. Revised § 4-103(e); Miller & Harrell, *supra* note 10, para. 8.03[4]. However, as noted, the bank does not lose its right to charge back the item to the customer's account. Revised § 4-214(a); Bank of New York v. Asati, Inc., 585 N.Y. S.2d 411, 18 UCC Rep. Serv. 2d 535 (N.Y. App. 1992).

payor bank, it is subject to the rules governing payor banks, discussed *infra* at Part VIII. D.

As noted, the depositary bank is also subject to restrictions arising from its relation with the depositor. The depositary bank is an agent of its depositor (the owner of the item deposited[277]). But if the item is dishonored by the payor bank, returned unpaid to the depositary bank, and charged back to the depositor's account creating an overdraft,[278] the depositary bank will also be a creditor of the depositor and will be the holder of the item.[279] As such it may qualify as a holder in due course of the item, if the other requisites are met.[280] This may be important to the bank's ability to recover from parties liable on the instrument.

If chargeback of the dishonored item has created an overdraft, the depositary bank may seek to recover that overdraft by pursuing several different remedies, but in doing so it must meet the prerequisites appropriate to each. Generally the depositary bank may seek to recover (1) from its customer under other law including the depository contract, (2) from its customer under Revised sections 4-201 and 4-214, or (3) as holder of the item from those liable on the instrument. The last approach requires that the bank retain possession of the instrument in order to retain holder status and meet the conditions to liability for those liable on the instrument. As noted, Revised section 4-214(a) allows the bank to retain a dishonored item and to meet its duty of care by sending notice of the facts.[281]

Seeking recovery from prior parties on the basis of their liability on the instrument will require that timely notice of dishonor be given.[282] Failure to give notice of dishonor to indorsers within the bank's midnight deadline will discharge their liability on the instrument.[283] In contrast, timely notice of dishonor generally is not a prerequisite to the liability of the drawer.[284] Regulation CC and Revised Article 4 also require the depositary bank to give notice of dishonor to the depositor; however, failure to give notice will not preclude recovery of any overdraft from the depositor under Article 4 or the deposit contract, although the bank will be liable for any actual damages caused by its delay in giving notice.[285]

D. The Midnight Deadline -- Payor Banks

When an item is presented to the payor bank for payment,[286] the payor bank must either dishonor it[287] or make some form of settlement.[288] If the bank elects to settle for the item, it may do so by paying it in cash or by allowing final or provisional credit for the item.[289] If the payor fails to either dishonor or settle for the item within its midnight deadline, it will be "accountable" for the amount of the item.[290]

If the payor bank makes provisional settlement, that settlement may be revoked if the bank properly dishonors the item within its midnight deadline.[291] Alternatively, the payor bank may make payment under Revised section 4-215(a).[292] As noted, if the payor bank does not pay or properly dishonor the item within the midnight deadline, it becomes "accountable" for the amount of the item under Revised section 4-302(a).[293]

Settlement will constitute final payment, and hence will not be subject to revocation, if the payor bank does any of three things:[294]

1. pays the item in cash;[295]
2. makes irrevocable settlement for the item under statute, clearing-house rule, or agreement;[296] or

277. Revised § 4-201(a). Generally this agency status is also reflected in the depository contract.

278. Revised § 4-214 and Comment 3.

279. *See* Revised §§ 4-201(a), 4-401(a), (b), § 1-201(20). The customer's rights of ownership are subject to the bank's right to recoup such an overdraft. *See* Revised §§ 4-201(a) and 4-210. The depositary bank's holder status depends on its retention of the item. *see supra* Part VIII.B.

280. *See* Revised §§ 3-302, 3-305, 4-210, 4-211; Miller & Harrell, *supra* note 10, para. 3.03.

281. Revised § 4-214(a) and *supra* Parts VI. D. and VIII. B. Regulation CC is similar. *See* 12 C.F.R. § 229.33(d); Miller & Harrell, *supra* note 10, para. 8.03 and para. 8.04

282. *See* Revised § 3-414(d) (certain drawers); § 3-415(e) (indorsers); § 3-503(a) (both); Miller & Harrell, *supra* note 10, para. 4.03[2][b], para. 4.06[2][a]. As to drawers, *see* § 3-414(f). As to indorsers and presentment, *see* § 3-415(e).

283. Revised § 3-502(a), (c); § 3-415(c); Miller & Harrell, *supra* note 10, para. 4.06[2].

284. The drawer will not be discharged, except as to accepted drafts under Revised §§ 3-414(d), 3-503(a). *See also* Revised §§ 3-409, 3-413; Miller & Harrell, *supra* note 10 para. 4.03[2][b].

285. *See* 12 C.F.R. §§ 229.33(d), 229.38(c) and Commentary; Revised §§ 4-214(a), (d), and 4-103(e); Miller & Harrell, *supra* note 10, para. 8.04[3][d][3]; Connie L. Allen, *The New Rules Governing Collection and Payment of Checks in the Banking System: Impact of Regulation CC,* 47 Consumer Fin. L.Q. Rep. 129 (1993); Bank of New York v. Asati, Inc., 585 N.Y. S.2d 411, 535 (N.Y. App. 1992) (requirement to send notice is a duty of care, not a prerequisite to charge back under UCC).

286. The drawee bank under Article 3 becomes the payor bank under Article 4. *See* Revised § 3-501 for the elements of presentment. This analysis applies whether the instrument is presented for payment over the counter or through the banking system.

287. *See* Revised § 3-502; Miller & Harrell, *supra* note 10, para. 4.03[2][a], para. 4.06[2][a], para. 7.01[1][c], para. 8.02[6].

288. *See* Revised § 4-302(a). If a check is presented for immediate payment over the counter, the check will be deemed to be dishonored if it is not paid on the day of presentment. Revised § 3-502(b)(2). *See generally* Miller & Harrell, *supra* note 10, para. 8.02[1].

289. *See* Revised §§ 4-215 and 4-213 and the definition of settle at Revised § 4-104(a)(11); Miller & Harrell, *supra* note 10, para. 8.01[3][k].

290. *See* Revised § 4-302(a); Miller & Harrell, *supra* note 10, para. 8.02[1].

291. Revised § 4-302(a). Generally this requires return of the item unless it is unavailable for return. *See* Revised § 4-301(a)(1), (2). The "midnight deadline" is defined at Revised § 4-104(a)(10). *See also* Regulation CC, 12 C.F.R. § 229.30 ("Paying bank's responsibility for return of checks"); Miller & Harrell, *supra* note 10, para. 8.02, para. 8.03[3][a], [b].

In order to be able to revoke the settlement, the bank must take care to be sure the dishonor is proper as well as timely. In Pace Publications, Inc. v. Bank of New York, 585 N.Y. S.2d 8, 18 UCC Rep. Serv. 2d 252 (N.Y. App. 1992), the item was first marked "paid" during processing, but this was canceled and the item was returned before the midnight deadline. The bank was not accountable for the amount of the item. But in Algemene Bank Nederland, N.A. v. Federal Reserve Bank, No. 89 (Civ. 4946 (SWK), 1991 U.S. Dist. LEXIS 470 (S.D. N.Y. Jan 16, 1991) the payor bank returned the checks in timely fashion, marking "Refer to Maker" on the face of each check. The "Refer to Maker" notation is a time honored means of signifying that an item is being returned to the depostary bank. The checks were dishonored again by the payor but as a result of the re-presentment they were late being returned to the depositary bank. The court concluded that the notation "Refer to Maker" was ambiguous and that this might have caused the erroneous re-presentment by the Federal Reserve Bank, hence the payor bank's initial dishonor was improper and it was liable. *Algemene* is discussed in the *1992 Annual Survey, supra* note 4, at 1561. The language of Revised § 4-402(a) rejects cases like Johnson v. Grant Square Bank & Trust Co. 634 P.2d 1324 (Okla. App. 1981) (holding that dishonor was wrongful because the bank stamped the wrong reason on the face of the check), and seems inconsistent with *Algemene* as well.

292. *Cf.* Old § 4-213(1); Revised § 4-215(1). The revision deletes the process of posting as a means of making final payment, for reasons discussed *supra* at Part III.B.2. *See also* Miller & Harrell, *supra* note 10, para. 8.02[2].

293. This accountability is subject to exceptions at Revised § 4-302(b). Note that technically the conduct resulting in accountability is treated as a dishonor, if the check was presented other than for payment over the counter, under Revised § 3-502(b)(1). However, the bank becomes accountable to pay the item under § 4-302(a). *See also* Revised § 4-215(a)(3), and Comment 7; Miller & Harrell, *supra* note 10, para. 8.02[3]. Generally this is not affected by equitable or other considerations not provided for in Articles 3 and 4. *See, e.g.,* Schwegmann Bank & Trust v. Bank of Louisiana, 595 So.2d 1185 (La. App. 1992) (accountability of payor bank not affected by existence of check kiting scheme). *But see* Revised § 4-302(b), and discussion *infra.*

294. Revised § 4-215(a).

295. Revised § 4-215(a)(1).

296. Revised § 4-215(a)(2). Examples would be settlement by cashier's check if the check is paid after timely presentment or a settlement that is irrevocable under clearing house rules. *See* Revised § 4-213. *See also* Revised § 4-215(b) and Comment 8; Revised § 4-301, Comment 3; Revised § 4-302, Comment 2 and Revised § 4-213, Comments 2 and 3. Payor banks often seek to specifically reserve the right to revoke in the deposit contract, in addition to the statutory right in § 4-301, or in supplementation of it. *See* Miller & Harrell, *supra* note 10, para. 8.02[2][b].

3. fails to revoke the provisional settlement in the time and manner provided by statute, clearing house rule, or agreement.[297]

Once final payment has been made by a payor bank under Revised section 4-215 it cannot be revoked, but the bank may be able to recover the payment by asserting breach of warranty or on restitutionary grounds.[298]

Revised Article 4 thus recognizes a distinction between final payment under section 4-215(a), and accountability under section 4-302(a). For example, if the payor bank makes provisional settlement and that settlement becomes final payment under Revised section 4-215(a), it is a matter of final payment and not a matter of accountability under Revised section 4-302(a) because Revised section 4-302(a) makes the payor bank accountable only if the bank does not pay or dishonor the item within the midnight deadline; hence the bank does not become accountable under section 4-302 if it makes final payment under section 4-215.[299]

The Official Comment to Revised section 4-301 illustrates this distinction by using an example.[300] If a depositary bank presents an item to the payor bank with instructions to remit payment in the form of a teller's check, and the payor bank does so on the day of presentment, the payor bank has made provisional settlement,[301] and that settlement may be revoked if the payor bank dishonors the presented item by returning it within the midnight deadline.[302] If it fails to so dishonor the item it will be treated as finally paid under Revised section 4-215 *if* the teller's check that was given in payment is honored by its drawee.[303] But if the teller's check is dishonored, there has been no final payment,[304] and since the provisional settlement was not revoked[305] the result is that the payor bank will be accountable under Revised section 4-302(a).[306] Revised section 4-215 Comment 7 provides a similar example where provisional settlement is made pursuant to a clearing house agreement,[307] and failure to revoke the settlement is treated as final payment under Revised section 4-215(a)(3).

A cashier's check or a teller's check may be used as a means of settlement with the agreement of the parties, and such settlement occurs when the instrument is sent.[308] However, such settlement becomes final only when the instrument is paid if the recipient forwards the check for collection within its midnight deadline.[309] If the cashier's check or teller's check is not paid, there is no final payment under Revised section 4-215(a),[310] and failure to dishonor within the midnight deadline will make the bank accountable under Revised section 4-302(a).[311] However, if an item is presented for payment over the counter, and is settled for by cashier's check or teller's check, this constitutes final settlement under Revised section 4-215(a)(2).[312] Since this payment was never provisional, Revised section 4-215(b) does not apply.[313] Hence there is final payment under section 4-215(a) rather than accountability under section 4-302.[314] The difference is that remittance by cashier's check is a form of provisional settlement as to any item presented through a collecting bank (under Revised section 4-301(a)), but is a form of final payment where an item is presented for payment over the counter (also under section 4-301(a)).[315]

As a general proposition, final payment occurs under Revised sections 4-213 and 4-215(a) when the payor bank provides a settlement[316] to the party making presentment[317] and that settlement is or becomes final (*e.g.,* by payment or by failing to revoke that settlement before the midnight deadline).[318] In contrast, if the payor bank makes only provisional settlement and that settlement never becomes final, the payor bank may be accountable for the amount of the item under section 4-302(a).[319] The distinction between payment (section 4-215(a)) and accountability (section 4-301(a)) can be important, because in the former case parties on the instrument are discharged and payment has been completed and generally cannot be retrieved by the payor;[320] in the latter case parties on the instrument may not be discharged and in addition accountability is a legal liability of the payor that may be enforced by the claimant, although Revised section 4-302(b) provides a set of exceptions to the bank's accountability.[321]

297. Revised § 4-215(a)(3). This suggests that a failure to revoke settlement by dishonoring the item constitutes final payment. *Id.*, Comment 7. However, other provisions and comments indicate that payment under § 4-215 is distinguishable from accountability under § 4-302 for purposes of liability other than between the holder and the bank; that is, with respect to parties on the instrument. *See* Revised § 4-215, Comments 6 and 8; Revised § 4-301, Comment 3; Revised § 4-302, Comment 2; Revised § 3-502(b)(1); Miller & Harrell, *supra* note 10, para. 8.02[3]. In Gordon v. Planters & Merchants Bancshares, Inc., 18 UCC Rep. Serv. 2d 263, 832 S.W.2d 492, (Ark. 1992), the payor and depositary banks charged back an item at the drawer's request, after the payor bank's midnight deadline. Since the item was paid and the right of charge-back terminated at the payor bank's midnight deadline, this was improper and had to be reversed.

298. *See* Revised § 4-301, Comment 7; Revised § 3-418. *Cf.* Revised § 4-302(b). *See also* Miller & Harrell, *supra* note 10, para. 8.03[3], [4]. *But see* Chicago Title Ins. Co. v. California Canadian Bank, 2 Cal. Rptr. 2d 422 (Cal. Ct. App. 1991); Los Angeles Nat'l Bank v. Bank of Canton of California, 280 Cal. Rptr. 831 (Cal. Ct. App. 1991) (refusing to allow revocation of final payment on tort grounds); Citizen's Fidelity Bank & Trust Co. v. Southwest Bank & Trust Co., 472 N.W.2d 198 (Neb. 1991) (final payment could not be reversed even though depositary bank knew that the check might be counterfeit and called the payor bank to discuss payment without disclosing this knowledge). These three cases are noted in the *1992 Annual Survey, supra* note 4, at 1562-63, with inferential criticism of *Citizen's Fidelity Bank.*

299. Compare Revised § 4-302(a) and Comment 2.

300. Revised § 4-301 Comment 3 and Revised § 4-215 Comment 8.

301. *Id.* But query why the teller's check does not constitute an irrevocable obligation to pay and hence final payment under Revised § 4-215(a)(2)? *See* Revised §§ 3-414(b) and 3-411; Miller & Harrell, *supra* note 10, para. 4.03[1], [2], para. 8.03[5], para. 9.01[4][d]. The answer is that while the check represents an obligation that must be paid, the Code allows that settlement to not constitute payment if the teller's check is not paid. *See* Revised §§ 4-213(c), 4-215(b).

302. Revised § 4-301(a)(1) and Comment 3.

303. Revised § 4-301, Comment 3; § 4-215(a)(3).

304. Revised §§ 4-213(c) and 4-215(b); Revised § 4-301, Comment 3.

305. Revised § 4-301(a).

306. *Id.*, Comment 3. *See also* Revised § 4-215(b). This will be subject to Revised § 4-302(b). Revised § 4-215 Comment 8 will provide a similar example.

307. *See* Revised § 4-213 and Comment 2.

308. Revised § 4-213(a) and (a)(2)(i).

309. Revised § 4-213(c)(1); Miller & Harrell, *supra* note 10, para. 8.03[5], para. 8.04[3][c][4].

310. Revised § 4-215(b) and Comment 8.

311. Subject to Revised § 4-302(b); Miller & Harrell, *supra* note 10, para. 8.02[3].

312. *See* revised § 4-215, Comment 8; Miller & Harrell, *supra* note 10, para. 8.02[2][a], [b]. The reason is that § 4-301(a) does not make settlement provisional in an over the counter presentation and thus there is no right to revoke even if there is a defense under § 3-411; one needs provisional settlement by agreement in order to revoke. However, this is often provided for by contract.

313. Revised § 4-215, Comment 8.

314. *Id.* Of course, if the cashier's or teller's check is not paid the issuing bank may be liable as drawer. *See infra* Part X.

315. *Id. See also* Miller & Harrell, *supra* note 10, para. 8.02[2][a], n. 125.

316. *See* Revised § 4-104(a)(11); Miller & Harrell, *supra* note 10, para. 8.02[1].

317. *See* Revised § 3-501; Miller & Harrell, *supra* note 10, para. 8.02[1].

318. Revised §§ 4-301(a) and 4-215(a); Miller & Harrell, *supra* note 10, para. 8.02[1][c], para. 8.02[2].

319. This is subject to exceptions at Revised § 4-302(b). *See* Miller & Harrell, *supra* note 10, para. 8.02[3].

320. Revised §§ 3-602 and 3-418.

321. *Cf.* Revised §§ 3-418, 4-302(b), Comment 8 to Revised § 4-215; Miller & Harrell, *supra* note 10, para. 8.02[3], [4].

IX. The Bank — Customer Relation and Revised Section 4-406

A. Introduction

The legal relationship between the payor bank and its customer (the drawer of checks drawn on an account at the payor bank)[322] is derived from several sources, primarily UCC Article 4, Part 4, and the deposit contract.[323] This discussion will focus on the impact of Revised section 4-406 when a payor bank pays an item that is not properly payable because of a material alteration or unauthorized drawer's signature.

Generally the payor bank is authorized to charge the account of its customer only if the item is properly payable;[324] therefore, all other things being equal, a payor bank that pays an improper item cannot charge its customer's account or otherwise recover from its customer and may suffer any loss resulting from uncollectibility of the item.[325] However, this basic principle may be qualified by other rights and duties of the parties under Revised section 4-406, as discussed below and as discussed *supra* at Part VI.A.

B. Obligation of the Bank to Provide a Statement of Account

There is no requirement that a bank make periodic statements (showing account activity) available to its customers, and many accounts (*e.g.* passbook savings and certificate of deposit accounts) do not feature such statements. One result is that section 4-406 does not apply to such accounts, and the customer therefore has no specific duty to discover or report unauthorized signatures and alterations.[326]

If, on the other hand, a bank makes periodic statements of account (showing payment of items on the account) available to a customer, section 4-406 provides that the bank may either make available the items paid or provide a description sufficient to allow the customer "reasonably to identify the items paid."[327] This permits the bank either to return cancelled checks with the account statement or to provide a statement describing the items paid in lieu of physical return of the items.[328] In the latter event, Revised Article 4 provides a basic guideline by providing that it is sufficient to trigger the customer's duties for the bank to describe the items paid by item number, amount, and date of payment.[329] If the bank does not return paid items to the customer, it must either retain the items or (if the items are destroyed) "maintain the capacity to furnish legible copies" for a period of seven years.[330] Upon a request by the customer, the bank must provide within a "reasonable time" either the paid item or (if it has been destroyed or is not available) a "legible copy" of the item.[331]

C. Obligation of the Customer to Report Improper Items

If the bank makes available a statement of account as described above, "the customer must exercise reasonable promptness in examining the statement or the items to determine whether any payment was not authorized" because of an alteration or improper drawer's signature.[332] If the customer "should reasonably have discovered the unauthorized payment, the customer must promptly notify the bank of the relevant facts."[333] It should be noted that the customer's duty is to give "prompt" notice to the bank. This obligation is not extended by the subsequent 30 day notice provision at Revised section 4-406(d)(2); if the customer fails to give prompt notice and has no good reason for the delay, the customer will have breached this duty even if notice was given within 30 days.[334]

D. Customer Preclusion Under Revised Section 4-406(d)

Revised section 4-406(d) is one of the most important provisions governing the bank-customer relation. It recognizes a preclusion that may prevent the bank's customer from asserting that an item was not properly payable, thereby permitting the bank to charge the customer's account even

322. *See* Revised §§ 4-104(a), (5) and 4-215(3) for the definitions of "customer" and "payor banks." *See also* Miller & Harrell, *supra* note 10, para. 8.01[3][b], [d], and [g].

323. *See generally* Peter G. Pierce, III, *The Law's Excellent Banking Adventure - Recent Developments in the Bank-Customer Relation, Trends in Lender Liability, and the Impact of New Articles 3 and 4, infra* this symposium; Miller & Harrell, *supra* note 10, Ch. 9; Pierce & Harrell, *Financers as Fiduciaries: An Examination of Recent Trends in Lender Liability,* 42 Okla. L. Rev. 79 (1989); Harrell, *The Bank-Customer Relationship: Evolution of a Modern Form?,* 11 Okla. City U.L. Rev. 651 (1986); discussion *infra* Part IX.

324. Revised § 4-401; *see supra* Part VII.A. (properly payable) and Part VI.A (certain exceptions).

325. The bank may be able to recover from the party who received the payment. *See, e.g.,* Revised §§ 4-208, 4-302, 3-418. *See* also (as to an ability of the bank to charge its customer) Revised §§ 3-404, 3-405, and 3-406. However, typically the payor bank will not have recourse on the instrument for items paid on a forged drawer's signature under the time-honored doctrine of Price v. Neal, 3 Burr. 1354, 97 Eng. Rep. 871 (1762). *See also* Miller & Harrell, *supra* note 10, para. 7.02[3], para. 9.02[3]; B. CLARK, THE LAW OF BANK DEPOSITS, COLLECTIONS AND CREDIT CARDS para. 8.02[2] (1990). In addition the bank that makes an improper payment will be subrogated to the rights of the drawer against the payee (or other owner of the instrument), and the rights of the payee (or other owner of the instrument) against the drawer, under § 4-407. If the payee was entitled to receive payment, the drawer cannot recover from the bank for wrongful payment or otherwise force the bank to recredit the account. *See, e.g.,* IXI Laboratories Inc. v. First Bank, N.A., 483 N.W.2d 84, 17 UCC Rep. Serv. 2d 520 (Minn. App. 1992). *See also supra* Part VI.A.

326. *Cf.* Revised § 3-406, which applies a similar but broader preclusion rule to all negotiable instruments. However, savings passbooks and many certificates of deposit typically are not negotiable instruments and would not be subject to Article 3. *See* Revised §§ 3-102(a), 3-104. *Cf.* Victory Nat'l Bank v. Oklahoma State Bank, 520 P.2d 675 (Okla. 1973) (certificate of deposit is investment security governed by UCC Article 8); Farha v. F.D.I.C., 963 F.2d 283 (10th Cir. 1992) (certificate of deposit is "essentially a promissory note"); Bank IV Topeka, N.A. v. Topeka Banks & Trust Co., 807 P.2d 686 (Kan. App. 1991) (non-negotiable CD was deposit account, not an instrument); Skiles v. Security State Bank, 1992 WL333163 (Neb. 1992) (CD is not an instrument). On the other hand, the customer may be subject to an estoppel similar to the preclusion rule at § 3-406, on common law or equitable grounds. In J.W. Reynolds Lumber Co. v. Smackover State Bank, 836 S.W.2d 853 (Ark 1992), the court recognized a duty of the customer to review not only its bank statement but its duplicate deposit slips. Because the customer failed to review its deposit slips and this permitted a dishonest employee to embezzle funds, the customer was precluded from recovery against a depositary bank that violated restrictive indorsements. *See also* Revised §§ 3-403, 3-404, 3-405, and discussion *supra* at Part VI.A.

327. Revised § 4-406(a). If the customer relies on a dishonest agent to review the statement or otherwise entrusts review of the statement to a party who forges or alters items drawn on the account, so that the customer fails to identify the wrongdoing, the customer will be responsible for any resulting loss. *See, e.g.,* Westport Bank & Trust Co. v. Lodge, 325 A.2d 222 (Conn. 1973). Pre-Code cases to the contrary, like First Nat'l Bank of McAlester v. Mann, 410 P.2d 74 (Okla. 1965), are rejected by the UCC. *See also* discussion *supra* Part VI.A.

328. This revision is designed to facilitate truncation arrangements, where the physical handling of checks is "truncated" in order to permit more efficient processing by electronic means, and "safe keeping" arrangements, where the items are not returned to save handling and mailing costs. Revised Article 4 permits, but does not mandate, check truncation or safe keeping, leaving that decision to negotiation between the bank and its customers. *See, e.g.,* Miller & Harrell, *supra* note 10, para. 8.01[3][n], para. 8.04[3][f][3], and para. 9.03[6]. Some banks now are providing images of the checks and more can be expected to do so as customer demand for the service increases and the technology becomes more feasible.

329. Revised § 4-406(a).

330. Revised § 4-406(b).

331. *Id.*

332. Revised § 4-406(c). In general the customer's duty includes an obligation to make sure that the account statement is received by the proper party and to make inquires if that does not occur. For example, in Mesnick v. Hempstead Bank, 434 N.Y. S.2d 579 (Sup. Ct. 1980) the customer was preluded from asserting forgeries against the bank under § 4-406, even though the customer did not receive the statements because they were intercepted by the wrongdoers. And in American Insurance Co. v. Fidelity Bank & Trust Co., 583 A.2d 361 (N.J. Super. Ct. App. Div. 1990) a surety was precluded from asserting unauthorized payments against the bank even though the statements were sent to the co-owner of the account, on grounds that the surety should have done a better job of monitoring the account. But there are cases that reach a contrary result where the bank violated the instructions of its customer in mailing the statements to the wrongdoer. *See* Miller & Harrell, *supra* note 10, para. 9.03[4][a].

333. Revised § 4-406(c). As noted *supra* at note 326, J.W. Reynolds Lumber Co. v. Smackover State Bank, 836 S.W.2d 853 (Ark. 1992) recognized a customer duty to examine deposit slips as well as bank statements.

334. *See* Revised § 4-406(c), (d), (2), and Comment 3; Miller & Harrell, *supra* note 10, para. 9.03[4][a].

if the item has been altered or the drawer's signature is improper.[335] The customer may be precluded from such assertions in two circumstances as described at Revised section 4-406(d)(1) and (2).

Section 4-406(d)(2) is the more important of the two. It provides that if the bank paid an altered item or an item with an unauthorized drawer's signature that was included or described in a periodic statement of account, and the customer should have but did not discover and report the improper item within "a reasonable period of time, not exceeding 30 days," then the customer is precluded from asserting an impropriety by the same wrongdoer as to any other item paid by the bank after the end of that "reasonable period of time, not exceeding 30 days."[336] In effect, this recognizes the customer's obligation to discover and report improper items, and provides that if the customer fails to do so and that failure results in the payment of additional forged or altered items, the fault lies with the customer and the customer should bear the loss.[337] The 30 day period (up from 15 days in Old section 4-406(2)(b)) provides an outer limit for what constitutes a "reasonable time" to examine the statement and report any improper items. Obviously 30 days likely will be deemed a "reasonable time" for certain types of accounts (*e.g.,* a corporate account with hundreds of monthly transactions); in other cases (*e.g.,* a small consumer account with only a few dozen entries, or an account overdrawn when it clearly should not be) a reasonable time in which to act may well be less than 30 days.[338]

Whatever that "reasonable time" may turn out to be, section 4-406(d)(2) provides a preclusion only as to items paid after the end of it and before any notice from the customer. This preclusion operates without any need for the bank to make any other showing of loss. In contrast, section 4-406(d)(1) provides a preclusion as to items included or described in the account statement and paid *before* the customer has had a reasonable time to notify the bank, "if the bank also proves that it suffered a loss by reason of the [customer's] failure [to discover and report the forged or altered items]."[339] Thus section 4-406(d)(1) may preclude the customer from asserting a forgery or alteration as to the *first* improper item paid by the bank (as well as any additional such items included in the account statement), if the bank can prove that it "also suffered a loss" by reason of the customer's failure to "exercise reasonable promptness in examining the statement or the items" or to "promptly notify the bank of the relevant facts."[340] Thus if a customer fails to promptly notify the bank of forged or altered items, the customer may lose entirely the ability to require recredit of the account if for example, a recovery might have been had from the wrongdoer or some other fund.

"Reasonable promptness" likely will depend on the facts of the case; a delay of several weeks due to illness or perhaps even absence from town probably could be excused, while a similar delay due to sloppy bookkeeping practices likely would not.[341] It should be emphasized that the 30 day rule at section 4-406(d)(2) is a maximum period and does not provide a safe harbor for the customer under section 4-406(c) and (d)(1).[342]

The more difficult question may be how the bank can satisfy the requirement of establishing that it "suffered a loss by reason of the [customer's] failure" to meet obligations imposed under section 4-406(c).[343] Traditionally this has been taken as a reference to instances where the forger or other wrongdoer was able to escape apprehension because of the customer's unexcused delay in discovering or reporting the impropriety.[344] In such cases, to compensate for an unexcused delay that contributed to the loss (and as a means to encourage prompt action[345]), the customer is precluded from asserting the forgery or alteration as to the item paid by the bank and included in the statement of account.[346]

Under Revised subsections 4-406(c), (d)(1), and (d)(2), then, there are two specific time periods during which forged or altered items may potentially be paid and charged to the customer's account by reason of the preclusion rules. The first such period is that covered by the first statement to include the improper items. Any such item may be subject to a preclusion under section 4-406(d)(1). The second period is that time period following the end of a "reasonable period of time, not exceeding 30 days," during which the customer is required to examine the statement or items and to notify the bank of any forgery or alteration under section 4-406(d)(2). If the customer fails to comply with section 4-406(d)(2), the customer is precluded from asserting forgery or alteration by the same wrongdoer as to items subsequently paid. As to items paid during the "reasonable period of time, not to exceed 30 days," for the customer to examine the statement, no preclusion can exist except perhaps under section 4-406(d)(1).[347] This is illustrated by the following table:

Period covered by bank statement	Period from bank statement to a "reasonable time, not exceeding 30 days"	Period subsequent to end of "reasonable time, not exceeding 30 days"
Forged or altered items included in bank statement are subject to possible preclusion under section 4-406(d)(1)	Possible preclusion under section 4-406(d)(1); 3-406	Possible preclusion under section 4-406(d)(2)

335. Revised § 4-406(d); Revised §§ 4-401 to 4-403.

336. Revised § 4-406(d)(2).

337. *See* Revised § 4-406, Comment 3.

338. *See* Revised § 4-406, Comment 3; Miller & Harrell, *supra* note 10, para. 9.03[4][a], [b].

339. Revised § 4-406(d)(1).

340. *See* Revised § 4-406(c), (d), (1), Comment 3.

341. *See, e.g.,* Clark, *supra* note 325, para. 8.02[4][a]; Miller & Harrell, *supra* note 10, para. 9.03[4][a], [b].

342. *See* Revised § 4-406, Comment 2.

343. Revised § 4-406(d)(1).

344. *See* Clark, *supra* note 325, para. 8.02[4][a]; Miller & Harrell, *supra* note 10, para. 9.03[4][a], [b].

345. *See* Revised § 4-406, Comment 3.

346. Revised § 4-406(c), (d)(1).

347. Revised § 4-406(d)(1) and (2). Unless, of course, the general preclusion based on negligence at § 3-406 is applied.

E. Comparative Negligence

Revised Articles 3 and 4 introduce the concept of comparative negligence in the context of four possible "preclusion rules":[348] Section 3-404(d) (imposter and fictitious payees); section 3-405(b) (employer responsibility for fraudulent indorsement by an employee); section 3-406(b) (negligence contributing to forgery or alteration); and section 4-406(e) (customer's duty to discover and report forgeries and alterations). This discussion will focus on the latter provision as illustrative.

Revised section 4-406(e) applies only if the customer of a payor bank is precluded from asserting a forgery of the drawer's signature or an alteration against the bank under Revised section 4-406(d) (discussed *supra* at Part IX. D). In that event, the customer has the opportunity to prove that the bank failed to exercise ordinary care in paying the item and that this failure "substantially contributed to the loss."[349] If the customer succeeds in proving these elements, the loss will be allocated:

> between the customer precluded and the bank asserting the preclusion according to the extent to which the failure of the customer to comply with subsection (c) and the failure of the bank to exercise ordinary care contributed to the loss. If the customer proves that the bank did not pay the item in good faith, the preclusion [at subsection 4-406(d)] does not apply.[350]

This provision is designed to encourage settlements in cases where both parties have contributed to the loss, by discouraging a "roll of the dice" in court in the hope of shifting the entire loss to the other party under the "all or nothing" approach of Old Article 4.[351]

F. One Year Limitation Period

Revised section 4-406(f) carries forward the one year limitation on the customer's right to claim that items charged to the customer's account were improper due to forgery of the drawer's signature or alteration. The former three year period for discovering and reporting forged indorsements was deleted; Revised section 4-406 "imposes no duties on [the] drawer to look for unauthorized indorsements."[352] However, Revised section 4-111 provides a three year statute of limitations for the customer's right to seek recredit of the account due to payment of an improper item.[353] New language was added at the end of Revised section 4-406(f) (but in substance carries forward Old 4-406(5)) to provide that a payor bank may not ignore the section 4-406(d) preclusion in order to protect its customer by shifting the loss to others in a suit for breach of warranty under Revised section 4-208.[354]

G. Impact on *Commercial Cotton*

The revisions (implicitly, at least) deal with two troubling California cases, *Sun 'n Sand, Inc. v. United California Bank,*[355] and *Commercial Cotton Co. v. United California Bank.*[356] Both of these cases involved potential preclusion of a bank customer for failure to examine bank statements or to notify the bank that altered or forged items were being paid. In both cases the drawers failed to give notice to the payor bank within the one year time limit at Old section 4-406(4) (Revised section 4-406 (f)). In *Sun 'n Sand* the court held that payment of the checks by the bank constituted the tort of negligence, independent of Article 4,[357] and that this cause of action was not affected by the limitation period at Old section 4-406(4). *Commercial Cotton* was characterized by its court as a similar case, although the facts were different in important ways favorable to the bank.[358] In *Commercial Cotton* the same bank (the defendant in *Sun 'n Sand*) again asserted Old section 4-406(4) as a defense; this was characterized by the court as "stonewalling" and the bank was assessed punitive damages of $100,000 in addition to requiring repayment of the amount of the forged checks ($4,000).[359]

Commercial Cotton was subsequently repudiated by the same appellate district court that decided it,[360] and (along with *Sun 'n Sand*) generally has been relegated to the

348. These rules generally preclude a person whose negligence has contributed to a loss from asserting that loss against another party. As noted *infra,* however, these preclusion rules may be qualified on the basis of comparative negligence. *See also supra* Part VI.A.

349. Revised § 4-406(e). Ordinary care is defined at Revised § 3-103(a)(7). *See also* Miller & Harrell, *supra* note 10, para. 9.03[4][c].

350. Revised § 4-406(e). "Good faith" is newly defined at Revised § 3-103(a)(4) to include honestly in fact *and* the observance of reasonable commercial standards of fair dealing. *See also* Miller & Harrell, *supra* note 10, para. 3.03[2][b]. It is not the same as a failure to exercise ordinary care.

351. *See generally* Union National Bank v. Daneshvar, 803 S.W.2d 567 (Ark. Ct. App. 1991), for an example of the impact this may have on customer preclusion cases. *Cf. In re* Lou Levy & Sons Fashions, Inc., 988 F.2d 311 (2d Cir. 1993) (bank liable despite alleged negligence of perpetrator's employer); Witten Productions, Inc. v. Republic Bank & Trust Co., 401 S.E.2d 388 (N.C. Ct. App. 1991) (bank's questionable handling of items had no bearing on drawer's liability); American Title Ins. v. Shawmut Bank, 812 F. Supp. 301 (D.R.I. 1993) (payor bank held liable for paying on forged indorsement, despite drawer's negligence, because bank did not have forgery - detection procedure). *Witten Productions* and *Union National Bank* were discussed in the *1992 Annual Survey, supra* note 4, at 1565-67. *See also supra* notes 173-74.

352. Revised § 4-406, Comment 5. *See also* Miller & Harrell, *supra* note 10, para. 9.03[4][d]. *Cf. In re* Lou Levy & Sons Fashions. Inc., 988 F.2d 311 (2d Cir. 1993).

353. Revised § 4-406, Comment 5. This carries forward the period of the former three year rule although a statute of limitations operates differently than an absolute bar rule. *See also* discussion of limitation periods *supra* at Parts II.A. and III.D.2; Miller & Harrell, *supra* note 10, para. 6.03[7]; Walker & Walker, Inc. v. Liberty National Bank and Trust Co., No. 75,600 (S. Ct. Okla., May 11, 1993) (statute of limitations did not begin to run until customer discovered forgery and demand was made for payment. This decision seems clearly incorrect, quite aside from the § 4-406 issues).

354. The defendant in such an action may raise the § 4-406 preclusion as a defense. Revised § 4-406, Comment 5. *See also* Miller & Harrell, *supra* note 10, para. 7.02 and 9.03[4][d]. Revised § 3-417 is the same.

355. 582 P.2d 920 (Cal. 1978).

356. 209 Cal. Rptr. 551 (Ct. App. 1985). *See also* Miller & Harrell, *supra* note 10, para. 9.03; Pierce, *supra* note 323.

357. The court cited § 1-103, a clear mis-use of that section, since § 4-406 covers the issues involved and the court used § 1-103 to hold the pre-Code rules still viable; in fact § 4-406 displaces negligence in this context under Old or Revised Article 4.

358. In *Sun 'n Sand* the wrongdoer made the altered checks payable to the bank and deposited them in her account at the bank. Arguably this might have alerted the bank to the fraud. In *Commercial Cotton* there was no similar bank negligence to mitigate the customer's negligence.

359. Barkley Clark described this case as "disturbing in the extreme." *See* Clark, *supra* note 325, at para. 8.02[5]. Under Revised Article 4, which defines ordinary care differently than good faith, both definitions should exclude the bank's action, and the result should be different.

360. *See* Copesky v. Superior Court of San Diego County, 229 Cal. App. 3d 678, 280 Cal. Rptr. 338 (1991). *See also* Symonds v. Mercury Savings & Loan Association, 275 Cal. Rptr. 871, 13 U.C.C. Rep. Serv. 2d (Callaghan) 31 (Ca. Ct. App. 1990); Chicago Title Ins. Co. v. California Canadian Bank, 2 Cal. Rptr. 2d 422 (Cal. Ct. App. 1991); Los Angeles Nat'l Bank v. Bank of Canton of California, 280 Cal. Rptr. 2d 422 (Cal. Ct. App. 1991) (tort-contract distiction) (all noted in the *1992 Annual Survey, supra* note 4, at 1562; Pierce, *supra* note 323.

status of an aberration.[361] The Article 4 comparative negligence standard at Revised section 4-406(e) clearly rejects the all-or-nothing standard used by the *Sun 'n Sand* and *Commercial Cotton* courts to ignore the negligence of the customer and place the entire loss (plus, in *Commercial Cotton,* punitive damages) on the bank. Under the revision, if the customer is subject to a preclusion under Revised section 4-406(d), the most that can be done to the bank is to impose liability for negligence on a *comparative* basis, under Revised section 4-406(e). This direct and exclusive allocation formula, based on comparative negligence, precludes any alternative tort analysis under section 1-103. This should cut-off a customer's escape from the one-year statutory bar at Revised section 4-406(f) by means of section 1-103, so as to preclude the kind of analysis used in *Sun 'n Sand* and *Commercial Cotton.* Only if the bank failed to exercise good faith, as newly defined at Revised section 3-103(a)(4), would the preclusion rule of Revised section 4-406(d) be unavailable.[362]

X. Cashier's and Tellers's Checks, Money Orders; Traveler's Checks; Stop Payment Orders and Post-Dated Items

A. Cashier's Checks, Money Orders, Traveler's Checks, and Teller's Checks -- Introduction

For the first time, these specialized types of instruments are defined, in Revised Article 3:

1. "Cashier's check" means a draft with respect to which the drawer and drawee are the same bank or branches of the same bank.[363]
2. "Teller's check" means a draft drawn by a bank (i) on another bank, or (ii) payable at or through a bank.[364]
3. "Check" is defined as a demand draft drawn on a bank, including checks denominated "money order."[365]
4. "Travelers check" is also defined, essentially as an ordinary check denominated a "traveler's check" (or by a "substantially similar term"), requiring a countersignature as a prerequisite to payment.[366]

The obligation of the issuer of a cashier's check is described at Revised section 3-412 and is essentially the same as the obligation of the maker of a note:

> The issuer of a note or cashier's check or other draft drawn on the drawer is obliged to pay the instrument (i) according to its terms at the time it was issued . . . . [367]

This carries forward the effect of Old section 3-118(a) ("a draft drawn on the drawer is effective as a note."), in the sense that both the drawer of a cashier's check and the maker of a note have "primary" liability on the instrument (they and not a third party are expected to pay and the obligation to pay is not subject to statutory conditions or prerequisites).[368] But unlike Old section 3-118(a), Revised Article 3 otherwise treats a cashier's check as a check rather than a note.[369] Thus the instrument is treated as a check even though legally the drawer's liability is equivalent to that of the maker of a note.[370]

B. Consequences of a Bank's Refusal to Honor

Along with clarifying that an ordinary money order (signed by the purchaser as drawer) is like a personal check (and therefore is subject to a stop payment order[371]), probably the most important revisions in this area of law relate to dishonor of cashier's checks, teller's checks, and certified checks.[372] Revised section 3-411 specifies the consequences of a bank's refusal to honor a cashier's check, teller's check, or certified check.[373] Revised section 3-312 provides a procedure whereby a person can recover from the issuing bank for a lost, destroyed, or stolen cashier's check, teller's check, or certified check. These provisions significantly clarify and in some cases alter the rights and liabilities of the issuing bank.

Briefly, Revised section 3-411 governs the liability of the issuing bank for wrongful refusal to honor or pay such a check.[374] This issue arises whenever a bank refuses to pay such a check (typically because it believes it or its customer has a valid defense), and in

361. *See also* Price v. Wells Fargo Bank, 213 Cal. App. 3d 465, 261 Cal. Rptr. 735 (1989) (also rejecting *Commercial Cotton*); Peterson Dev. Co. v. Torrey Pines Bank, 233 Cal. App. 3d 103, 284 Cal. Rptr. 367 (1991) (bank-customer relation is ordinary debtor-creditor relation and is not fiduciary in nature); Richard Nat'l Bank & Trust v. Swenson, 816 P.2d 1045 (Mont. 1991) (same); Rodgers v. Tecumseh Bank, 756 P.2d 1223 (Okla. 1988) (same); Frontier Federal Federal Sav. & Loan Assn. v. Commercial Bank, N.A., 806 P.2d 1140 (Okla. 1990) (same); Walker & Walker, Inc. v. Liberty National Bank and Trust Co., No. 75,600 (S. Ct. Okla. May 11, 1993); Aspinall v. U.S., 984 F.2d 355 (10th Cir. 1993) (when funds are deposited in a bank account, title passes to bank and depositor retains only a chose in action against bank). *See also* Carolyn S. Smith, *Allis-Chalmers v. Lueck: The United State Supreme Court Rejects Tort Liability for Breach of Good Faith,* 43 Consumer Fin. L.Q. Rep. 258 (1989); Pierce, *supra* note 323.

In Symonds v. Mercury Savings & Loan Association, 275 Cal. Rptr. 871, 13 U.C.C. Rep. Serv. 2d (Callaghan) 31 (Cal. Ct. App. 1990), the court refused to characterize the bank-customer relation as "quasi-fiduciary," but discussed the level of bank misconduct that would permit the customer to recover in tort for intentional infliction of emotional distress. In *Symonds* a collecting bank had allegedly failed for a period of eight months to forward a check for collection. *Symonds* is cited in the *1992 Annual Survey, supra* note 4, at 1562, which also notes Chicago Title Ins. Co. v. California Canadian Bank, 2 Cal. Rptr. 2d 422 (Cal. Ct. App. 1991); and Los Angeles Nat'l Bank v. Bank of Canton of California, 280 Cal. Rptr. 831 (Cal. St. App. 1991), as "thoughtfully distinguish[ing] the aims of tort and commercial law. . . ."

362. *See* Revised § 4-406(e). Again, negligence is not a breach of honesty in fact or reasonable commercial standards of fair dealing.

363. Revised § 3-104(g). *See generally,* Miller & Harrell, *supra* note 10, para. 8.01[3][m].

364. Revised § 3-104(h). Sometimes these have been called "bank drafts."

365. Revised § 3-104(f). As a result a money order will be treated as an ordinary check, and will be subject to a stop payment order, unless it fits within the definition of a cashier's check. *See* Revised § 3-104, Comment 4.

366. Revised § 3-104(i) and Comment 4.

367. Revised § 3-412.

368. *Cf.* the "secondary" liability of indorsers and other drawers. Revised §§ 3-414, 3-415, 3-503(a). *See* discussion *supra* at Part VI; Miller & Harrell, *supra* note 10, para. 4.03 and para. 4.05.

369. Revised § 3-412, Comment 2.

370. Revised § 3-412. Therefore the bank issuing a cashier's, teller's or similar check may refuse or stop payment of the check. *See, e.g.,* First Nat'l Bank of Nocona v. Duncan Sav. & Loan Ass'n, 656 F. Supp. 358 (W.D. Okla. 1987), *aff'd,* 957 F.2d 775 (10th Cir. 1992). In such case, however, the bank may be liable under Revised §§ 3-305, 3-312, 3-411, and 3-412. *See* discussion *infra* this text.

371. Revised § 3-104(f), and Comment 4; Miller & Harrell, *supra* note 10, para. 8.01[3][m], para. 9.01[4][d]. A bank "money order" signed by a representative of the issuing bank as drawer would be treated as a cashier's check despite its label.

372. *See* Revised § 3-411; Miller & Harrell, *supra* note 10, para. 9.01[4][d][iv]. For a recent case decided under Old Article 4, *see* Hecker v. Ravenna Bank, 468 N.W. 2d 88 (Neb. 1991) (bank liable in conversion for asserting a set-off claim against the joint payees of a cashier's check, as a basis for dishonoring the check). *See also 1992 Annual Survey, supra* note 4, at 1564, noting that this decision is incorrect if the bank had a valid claim to assert as a set off.

373. *See* Revised § 3-312; Miller & Harrell, *supra* note 10, para. 9.01[4][d][v]. *See* also Revised § 3-309 which, however, merely carries forward Old § 3-804.

374. Revised § 3-411(b). This liability is on the instrument as drawer or acceptor.

the ensuing litigation the defenses to liability are rejected by the court or held ineffective against a holder in due course. Having wrongfully refused to pay the check, the bank is liable on the instrument, and also pursuant to Revised section 3-411.[375] That section provides that upon wrongful refusal to honor a cashier's check, or certified check, or if payment is stopped on a teller's check, the bank is liable for "expenses or loss of interest resulting from the nonpayment" (plus, of course the amount of the check).[376] The bank may also be liable for consequential damages, but only "if the obligated bank refuses to pay after receiving notice of [the] particular circumstances giving rise to the damages."[377] Moreover, the bank is not liable for expenses and consequential damages if it refused payment because it has suspended payments, has asserted a defense that it reasonably believed was valid against the person seeking payment, had reasonable doubt that the person seeking payment was entitled to enforce the instrument, or if payment was prohibited by law.[378]

As a result, the issuing bank can safely refuse to honor a cashier's check any time it has reasonable grounds to believe that it has a valid defense against the person seeking payment. If this judgment is reasonable, but in court is proven to be wrong, the bank will be liable only for the amount of the item.[379] However, normally the bank cannot assert claims of its customer (the remitter) against the holder as a defense to the bank's liability. Under Revised section 3-305(c) (or Old section 3-306(d), if the customer joins the lawsuit and personally asserts his or her claim, then it can be raised. However, even if the bank believes that its customer has a valid claim against the holder of the bank's check, there is every reason for the bank to pay unless the bank is sure the customer will litigate the issue if necessary.[380] In such litigation any meritorious defense available to the customer may be raised as a basis for the bank's refusal to pay the check.[381]

To this extent the issuer of a cashier's check is now like any other obligor on an instrument: able to raise its own defenses to liability, subject to the rules governing liability on the instrument. Like any other obligor, the issuing bank can assert only its own defenses, not the claims of third parties (such as the remitter, or purchaser of the instrument, or any other customer of the bank).[382] Similarly, if the person seeking payment is a holder in due course the bank, like any other obligor, can assert only the "real" defenses to liability.[383] This essentially codifies the better cases, such as *TPO, Inc. v. FDIC,*[384] which treat the issuing bank like any other obligor for purposes of determining liability on the instrument under Article 3.[385]

This approach rejects the rationale of several well-known but confused cases. One of the most notorious is *Hotel Riviera, Inc. v. First Nat'l Bank & Trust Co.,*[386] where the court held that the issuing bank could not refuse payment of a cashier's check even if it had a defense valid against the holder, because "cashier's checks have an aura of cash . . . [and] [w]hether that aura bears scrutiny in the law is irrelevant here."[387] Revised section 3-411 directly confronts the *Hotel Riviera* rationale. Similarly, the revisions reflect a retreat from cases like *Yukon Nat'l Bank v. Modern Builders Supply,*[388] which declined to allow the issuing bank to assert failure of consideration as a defense against the payee who had purchased the cashier's check with checks that later bounced. It should be emphasized again, however, that a holder in due course not directly subject to such defenses will be immune to personal defenses of the bank.[389]

C. Lost, Destroyed, or Stolen Cashier's Checks, Teller's Checks, and Certified Checks

Revised Article 3 provides two procedures allowing a claimant to receive reimbursement from the issuing bank for a lost, destroyed, or stolen bank check. One may involve posting a bond for the limitations period.[390] The other is Revised section 3-312. The latter section apparently resulted from cases like *Santos v. First Nat'l. State Bank,*[391] where the purchaser of a lost cashier's check sought reimbursement for the amount of the check and was met with a demand to post a bond for the statute of limitations period under the procedure at Old section 3-804.[392] Revised section 3-312 permits such a claimant to obtain reimbursement on or after the 90th day following the date of the check or of its acceptance, by submitting then or earlier an affidavit in the form of a "Declaration of loss" stating that the check was lost, destroyed, or stolen and that the claimant is the drawer, payee, or remitter entitled to payment.[393]

This does not give such party an unrestricted right to stop payment after 90 days.[394] The "Declaration of loss" must recite certain facts and can be used only

375. *Id.* In this instance the bank is *not* liable for wrongful dishonor under § 4-402, as that section governs the liability of the payor bank to its customer, the drawer of a dishonored item. In the case of a cashier's check, teller's check, or certified check the issuing bank is the drawer or (in the case of a certified check) has replaced the drawer as obligor. *See* Revised §§ 3-409, 3-412, and 3-310. Therefore the bank's exclusive liability is under those sections and § 3-411.

376. Revised § 3-411(b), and Comment 2.

377. Revised § 3-411(b). This essentially is the Hadley v. Baxendale test for consequentials. *See* Comment 2 to § 2-715.

378. Revised § 3-411(c), and Comment 3.

379. The bank will not be liable for the plaintiff's litigation expenses or consequential damages under Revised § 3-411(c). The bank will also be liable for interest, under Revised § 3-411(b), but presumably can cover that liability by earning interest on the amount in question during the litigation. Of course, there is some risk that the court will conclude that the bank's defense was not reasonable or that it should have known there was a holder in due course, depriving the bank of the protection afforded by Revised § 3-411(c) and subjecting the bank to liability for the plaintiff's costs and/or consequential damages, under Revised § 3-411(b).

380. Revised §§ 3-305(c) and 3-602(b)(1).

381. *See* Revised § 3-411(c)(iii). It should not be necessary to specify this, but was made so by cases like *Hotel Riviera,* discussed *supra* at notes 41 and 42, and *infra* this text at note 386.

382. *See* Revised §§ 3-305(c) and 3-602; Hecker v. Ravenna Bank, 468 N.W.2d 88 (Neb. 1991); Valley Bank v. Monarch Investment Co., 800 P.2d 634 (Idaho 1990); Malphrus v. Home Sav. Bank, 254 N.Y. S.2d 980 (Co. Ct. 1965); Miller & Harrell, *supra* note 10, at para. 9.01[4][d], [i], [ii]. There is a limited exception for theft, and for accommodation parties at Revised § 3-305(d). *See also supra* Part II.H.

383. *See* Revised § 3-305(a), (b); Miller & Harrell, *supra* note 10, at para. 3.03[3][a], para. 3.04[1][b].

384. 487 F.2d 131 (3d Dir. 1973); *see also* Miller & Harrell, *supra* note 10, at para. 9.01[4][d][iii].

385. In Revised Article 3 the basis for this liability is § 3-412 in the case of a cashier's check; Revised § 3-414 in the case of a teller's check.

386. 768 F.2d 1201 (10th Cir. 1985); *see also* Abilities, Inc. v. Citibank, N.A., 449 N.Y. S.2d 242 (N.Y. Sup. Ct. 1982).

387. *Riviera,* 768 F.2d at 1204 (citations omitted). This case is discussed in Miller & Harrell, *supra* note 10, para. 9.01[4][d][iii], n. 70.*See also supra* notes 41 and 42.

388. 686 P.2d 307 (Okla. App. 1984).

389. Revised § 3-305(b). Thus the utility of a cashier's check as means of payment to an innocent party in not impaired.

390. *See* Revised § 3-309.

391. 451 A.2d 401 (N.J. Super. 1982); *see also* Miller & Harrell, *supra* note 10, at para. 9.01[4][d][iii] n. 70, and para. 9.01[4][d][v].

392. Revised § 3-309. This was intended to protect the bank from double payment in the event the check was later presented for payment by a holder in due course.

393. Revised § 3-312(a)(2), (3), and (b). During the 90 days the check must be paid by the issuer even if the affidavit is filed. Revised §§ 3-312(b)(2) and 3-602. Most such checks are presented within 90 days.

394. *Cf.* Revised § 4-403 (customer's right to stop payment on an ordinary check); Miller & Harrell, *supra* note 10, para. 9.01[4][d][i].

where the check has been lost, destroyed, or stolen. Even after receipt of such a declaration, the issuing bank can pay the check during the first 90 days after its issue. But clearly Revised section 3-312 gives the payee or remitter of a cashier's or teller's check (and the drawer of a check certified by the drawee bank) a new right to receive reimbursement and prevent payment on and after the 90th day in certain circumstances.

Obviously there are some new risks in all of this, for both the issuing and depositary banks. The risk for the issuing bank is small but includes the possibility that a claimant may fraudulently present a declaration of loss and obtain reimbursement, knowing that the check is in the hands of a holder in due course who has delayed presentment of the check for some legitimate reason (perhaps due to an illness, being out of the country, etc.). Having reimbursed the claimant, the issuing bank may then have to pay again to the holder in due course to preserve its credibility,[395] being left with recourse against the fraudulent declarant (who presumably will have skipped with the money).

For the depositary bank, new risks will be created when a depositor deposits a cashier's check near the end of the 90 day period. The depositary bank may be required to provide next-day funds availability for the amount of the check, and to allow full withdrawal of those funds as a matter of right, under Regulation CC, which treats cashier's, certified, and teller's checks essentially like cash for funds availability purposes.[396] Yet the depositary bank may not be certain that the check will be presented to the issuing bank and paid before the end of the 90 day period provided at Revised Article 3 section 3-312(b)(1), thereby suggesting a risk that a "Declaration of loss" may intervene so as to prevent payment to the depositary bank, after it has released the funds.[397] There is no clear way to prevent this, as even a telephone call to confirm the absence of such a declaration will not preclude subsequent presentment of such a declaration to the issuing bank, prior to payment of the check. One possibility is to send a notice to the issuing bank, by facsimile transmission (FAX), to notify the issuing bank of the depositary bank's claim as a holder in due course and the imminent presentment of the check.[398] However, there is no guarantee that such a notice will be effective to assure payment or to protect the issuing bank where a proper "Declaration of loss" is received by the issuing bank and the check is presented on or after the 90th day.[399] This scenario also presents a quandary for the issuing bank, faced with notice of a possible holder in due course (the depositary bank) and a statutory duty to pay the claimant.[400] One possibility for the depositary bank is to hand-deliver the check (or otherwise expedite presentment) to the issuing bank so as to receive payment (or dishonor) before the depositary bank must pay the funds to its depositor, but obviously this will be impractical in many instances. Perhaps the most practical solution is to invoke the exception in Regulation CC section 229.13(e) concerning reasonable cause to doubt collectibility, using by analogy the federal comment discussing stale checks and post-dated checks.

D. Stop Payment Orders and Post-Dated Checks

The customer's unqualified right to stop payment of ordinary checks is retained at Revised section 4-403.[401] The revision provides that where more than one person is authorized to draw on the account, any such person may stop payment on any item drawn on that account (even if the item was drawn by a different customer) or may close the account.[402] If the account agreement requires both joint account holders to sign items drawn on the account, and one of the customers closes the account, the bank probably should make the proceeds check payable to both parties, not in the alternative,[403] so as to require the indorsement of both account holders.[404] If two signatures are required and the bank pays items on only one signature, it will be treated as an unauthorized item and will not be properly payable.[405]

As under Old Article 4, an oral stop payment order is effective for 14 days and then for six months if confirmed in writing within the 14 days. It may be renewed in writing for additional six month periods each if the renewal is made within the six month effective period.[406] The customer has the burden of proving the fact and amount of any loss resulting from the bank's failure to honor an effective stop payment order, but the damages may include damages for wrongful dishonor of subsequent items.[407]

As under Old Article 4, a stop payment order comes too late to prevent payment if the bank has (1) accepted or certified the item, (2) paid it in cash, (3) settled irrevocably, or (4) become accountable for the item

395. It is clear from the language of the comment to the statute that section 3-312 excuses the bank from liability to a holder in due course. There is no mention of this among the "real" defenses at Revised § 3-305(a)(1), but the provisions should be read *in pari materia*. Moreover, it can be argued that a holder who takes such a check knows the law and thus has notice of the bank's rights. Revised § 3-305(a)(2).

396. Regulation CC § 229.10(c)(1)(v), 12 C.F.R. § 229.10(c)(1)(v). *See also* Conni L. Allen, *The New Rules Governing Collection and Payment of Checks in the Banking System: Impact of Regulation CC*, 47 Consumer L. Q. Rep. 129 (1993).

397. *See* Revised § 3-312(a)(3), (b)(1).

398. *See* Appendix C to Regulation CC for a possible format for such a notice.

399. *See* Revised § 3-312(b)(3).

400. *See* Revised §§ 3-302, 3-305, 3-312(b)(1). Perhaps interpleader would work.

401. Friendly Nat'l Bank of Southwest Okla. City v. Farmers Ins. Group, 630 P.2d 318 (Okla. 1981) held that a draft conditioned upon "acceptance" was negotiable because the right to refuse to accept the draft was in essence merely the right to stop payment under § 4-403. However, unlike a refusal to accept, where the drawer stops payment the drawer remains liable on the instrument under Revised § 3-414. *See also* Revised §§ 3-106(c), 3-401(a), 3-408, 3-409, 3-413, and discussion *supra* at Part VI. *See also* First Nat'l Bank, Conway Springs, KS v. Jones, 839 P.2d 535 (Kan. App. 1992) (holder in due course could collect from drawer despite stop payment order); Commodity Traders, Inc. v. Finn, 487 N.W. 2d 297 (Neb. 1992) (same).

402. *See* Revised § 4-403(a); Miller & Harrell, *supra* note 10, para. 9.01[2].

403. "A and B," not "A or B." *See supra* Part IV. B.

404. *See* Revised § 3-110(d); Miller & Harrell, *supra* note 10, para. 2.02[7], para. 3.02[3][b][ii], and para. 6.03[6][b][ii]; discussion *supra* Part IV.

405. *See* Revised §§ 3-403(b), 4-401(a); Miller & Harrell, *supra* note 10, para. 3.03[3][b][ii]. As a result the payor bank may be unable to charge the customer's account. *See supra* Part VII.A. *But see* Revised §§ 3-406, 4-406 (customer whose negligence contributed to the loss precluded from asserting forgery). *See* discussion *supra* Parts VI.A. and IX. In addition the customer may not recover if the item paid discharges a valid debt of the customer. Cooper v. Stockyards Bank, 644 P.2d 123 (Okla. 1981).

406. Revised § 4-403(b). In addition the customer may not recover if the item paid discharges a valid debt of the customer. Cooper v. Stockyards Bank, 644 P.2d 123 (Okla. 1981).

407. Revised § 4-403(c). This may occur because failure to honor the stop payment order depletes the account. *See also* Revised § 4-402; Miller & Harrell, *supra* note 10, para. 9.02[2].

In Dunnigan v. First Bank, 585 A.2d 659 (Conn. 1991) the bank erroneously paid an item over a valid stop payment order, but the court held that there were no damages because the check paid a valid debt of the customer. The customer sought to stop payment on this check in order to recoup a loss suffered by the customer in an earlier transaction with the payee of the check. The court declined to recognize this as an element of the damages flowing from the wrongful payment, limiting the analysis to the specific debt paid by the check (clearly a valid debt). This case is noted in the *1992 Annual Survey, supra* note 4, at 1568, which credits Professor Patricia B. Fry with the observance that the bank's rights against its customer should have been subject to the customer's right of recoupment arising from the earlier transaction, under the Article 4 subrogation rules at Old § 4-407(b), Revised § 4-407(2)). *Cf.* IXI Laboritories, Inc. v. First Bank, N.A., 483 N.W. 2d 84, 17 UCC Rep. Serv. 2d 520 (Mn. App. 1992) (bank's subrogation to rights of drawer as against payee).

by reason of the midnight deadline.[408] Subject to these considerations, the bank may pay, accept, certify, or charge items to the customer's account in any order it chooses.[409] The customer's stop payment order must describe the item with "reasonable certainty."[410] Revised Article 4 (like its predecessor) does not define "reasonable certainty," thus leaving that issue to resolution by agreement or the courts. For example, *Parr v. Security Nat'l Bank*[411] held that a stop payment order was effective despite a 50 cent error in the amount, but the court distinguished *Poullier v. Nacua Motors, Inc.*,[412] where the bank advised the customer that the precise amount of the check was needed. In *Johnson v. Grant Square Bank & Trust Co.*,[413] a three cent error did not prevent the stop order from being effective; the court noted that the order correctly identified the payee, the date of the check, the check number, and the customer's account number.

Revised section 4-403 Official Comment 5 indicates that the customer must provide the information needed by the bank under the technology then existing to identify the item subject to the stop order, unless there is an agreement to the contrary. Thus it is arguable that the precise amount of the item may be essential where the bank's processing equipment identifies items on that basis. This is consistent with the general thrust of Revised Article 4, to accommodate automated processing systems. Of course, a bank may waive its right to precise identification of the item, as for example where the bank accepts a stop order knowing that the customer is unsure of the amount or other necessary information, and not explicitly qualifying that acceptance with a clear statement that it will not work if the amount (or other information) is not exact. Such issues should be resolved in the deposit contract or by giving notice to the customer in the form or orally that a stop order must include the precise amount of the check or other needed information if that is the case. Note also that for checks, Revised section 4-303(a)(5) allows the bank to establish "a cutoff hour no earlier than one hour after the opening of the next banking day . . . and no later than the close of that next banking day . . ." beyond which any stop payment order or similar notice will be ineffective until the following banking day. If no such cutoff hour is fixed by the bank, the cutoff will be the close of the next banking day after the banking day on which the bank received the check.[414] This cutoff hour allows the bank to refuse to honor a stop payment order or legal process that becomes effective before the time for final payment of the check under Revised section 4-215(a).

Revised Article 4 treats post-dated checks much like a check subject to a possible stop payment order. The bank is entitled to pay a post-dated check upon presentment, regardless of the date of the check, unless the customer has provided a notice to the bank similar to a stop payment order.[415] Under Old Articles 3 and 4, a post-dated check was sometimes held to be not properly payable, so that a bank paying such an item was unable to charge the customer's account.[416] Revised Article 4 changes this and permits payment of post-dated items at any time, unless the customer provides the requisite notice, describing the check with "reasonable certainty" to the bank and "at such time and in such manner as to afford the bank a reasonable opportunity to act on the notice before the check is paid." Like a stop payment order, an oral notice is effective for 14 days or for six months if confirmed in writing.[418] If the bank pays despite timely receipt of such notice, it will be liable for resulting damages including damages for wrongful dishonor of subsequent items due to depletion of the account.[419]

XI. Conclusion

Revised Articles 3 and 4 contain many benefits for banks, and for customers, including facilitation of bank operations and payment transactions, so that costs to customers can be held down. Overall, it is a good law that improves the law of payments and its legal environment and is being rapidly enacted by the states.

408. Revised § 4-303(a). *See also* Revised §§ 4-215(a), 4-301(a), 4-302(a); Miller & Harrell, *supra* note 10, para. 8.02[2]. Revised § 4-303(a)(5), because the cut off point of posting was dropped also allows the bank to set a cut off hour by its own action and, in the absence of doing so, sets one no later than close of business on the banking day after the banking day of receipt of the check.

409. Revised § 4-303(b). Section 4-405 authorizes a payor bank to continue paying checks for ten days after the death of the drawer, even with notice of the death. However, this does not excuse failure to comply with a stop payment order. *See, e.g.*, Lietzman v. Ruidoso State Bank, 827 P.2d 1294, 17 UCC Rep. Serv. 552 2d (N. Mex. 1992).

410. Revised § 4-403(a). Parr v. Security Nat. Bank, 680 P.2d 648 (Okla. App. 1984); *Pollier*, 439 N.Y. S.2d 85 (N.Y. Supp. 1981); Johnson v. Grant Square Bank & Trust Co., 634 P.2d 1324 (Okla. App. 1984). Comments to Revised § 4-403 indicate this must be with regard to the "technology then existing." Generally, Revised Articles 3 and 4 seek to facilitate technological advances. *See, e.g.*, §§ 4-110(c) (post-dated items), and 4-406(a) and (b) (statements of account and copies of items). Federal Reserve Regulation CC also encourages technological processing. *See also*, 12 C.F.R. §§ 229.30 (expeditious return of dishonored checks) and 229.36(c) (truncation of checks).

411. 680 P.2d (Okla. App. 1984).

412. 439 N.Y. S.2d 85 (N.Y. Sup. Ct. 1981).

413. 634 P.2d 1324 (Okla. App. 1981).

414. Revised § 4-303(a)(5).

415. *See* Revised § 4-401(c); Miller & Harrell, *supra* note 10, para. 9.01[2].

416. *See, e.g.*, Allied Color Corp. v. Manufacturers Hanover Trust Co., 484 F. Supp. 881 (S.D. N.Y. 1980); Siegel v. New England Merchants Nat'l Bank, 437 N.E. 2d 218 (Mass. 1982).

417. Revised § 4-401(c); *cf.* Revised § 4-403(a) (stop payment orders).

418. Revised §§ 4-401(c), 4-403(b).

419. Revised § 4-401(c); *cf.* Revised § 4-403(c). *See generally* Dunnigan v. First Bank, 585 A.2d 659 (Conn. 1991).