The Bank-Customer Relationship: Evolution of a Modern Form?

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THE BANK-CUSTOMER RELATIONSHIP: EVOLUTION OF A MODERN FORM?

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Traditionally, the relationship between a bank and its customer has been viewed as an essentially contractual relationship governed by common law contract and debtor-creditor law.¹ Although this has come to be supplemented by federal and state legislation and regulation,² in large part, these laws and regulations have left undisturbed the fundamental nature of the contractual relationship between a bank and its customer.³ Recently, however, observers have noted subtle but important shifts in the way courts, and juries, view the bank-customer relationship. These shifts have been noted with regard to both the bank lending⁴ and depository functions.⁵

The purpose of this article is to review selected examples of this phenomenon, and to analyze them in the context of modern case law in an effort to discern what patterns, if any, may be emerging from these developments. Specifically, the issue to be addressed is whether these cases represent only isolated developments, perhaps based on extreme or unusual facts, or whether they indicate a general trend and a significant new direction in the law governing the bank-customer relationship. In the case of the latter it will be important to isolate, identify and define the factors relevant to this new

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2. NORTON & WHITLEY, supra note 1, at §§ 1.07 & 11.02[2].


4. See, e.g., Flick, II & Replinsky, Liability of Banks To Their Borrowers: Pitfalls and Protections, 103 BANKING L.J. 220 (1986) [hereinafter Flick & Replinsky].


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direction so that banks and bank customers can be apprised of their new rights and liabilities under the law.⁶

The Djowharzadeh Case

Of seminal interest to any inquiry in Oklahoma concerning the bank-customer relationship is Djowharzadeh v. City National Bank and Trust.⁷ In this case, more than any other, an Oklahoma court outlined its view of the modern bank-customer relationship. As a result, this case must be considered first and as a reference point for analysis of other cases.

In Djowharzadeh, the wives of bank officials purchased a "bargain priced duplex" after learning of the bargain price from the loan application of a realtor who first spotted the deal. The realtor had disclosed the terms of the asking price as a part of the loan application, and felt that he had been wronged when that information was used by the wives of bank insiders to preempt his deal. Understandably, the court agreed. Undoubtedly there was something offensive and wrong about the misuse of confidential information disclosed in good faith as part of a loan application. But, as the court noted, this was a case of first impression in Oklahoma, and there was no prior law establishing or defining the existence of a confidential, fiduciary or other special relationship between a bank and its customer.⁸ Indeed, since no lending agreement had been or ever was consummated between the bank and the realtor, not even a bare contractual or debtor-creditor relationship existed between the parties. Technically, the realtor was not even a customer of the bank, and the bank itself was not directly involved in the usurpation of opportunity. What, then, distinguishes this case from any other in which one party learns of an opportunity from the other, and then wins the race to make the deal?

More specifically, what makes Djowharzadeh any different from the case where one party learns of a deal by eavesdropping on a conversation at a grocery store or restaurant?

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⁶ Of course the law is always evolving, and there is risk in attempting to describe what is doubtless a moving target. Nonetheless, intermediate efforts to do so are necessary for those attempting to function and adapt in a changing environment.
⁸ Id. at 618.
The answer must relate to the unique attributes of the banking business, interwoven as it is with the personal financial affairs of its customers and even those who seek to become customers. As the court described it:

The relationship created when a prospective borrower applies for a loan from a bank is a very special one. It has not yet ripened into a contract — because it has not yet crossed the threshold of formal agreement. Neither is it fiduciary [sic] — because it is by nature an arm’s length transaction. It does, however, impose special duties on each party which go beyond mere matters of courtesy.⁹

Essentially this derives from what the court viewed as the special status of banks in our society:

Banks exist and operate almost solely by using public funds and are invested with enormous public trust. Their financial power within the community amounts to a virtual monopoly in the field of money lending. The legislature has carefully defined their corporate charge within finite limits in direct proportion to their power.

One goal of this system is to assure that banks do not compete financially with their customers, but rather serve public financial needs fairly and evenly. Implicit in this policy of fair dealing and evenhandedness is a requirement that banks not use their favored position to the detriment of their customers, either directly or indirectly.¹⁰

Is this sound reasoning which recognizes a previously unarticulated but widely acceptable principle of law? Or is it largely hyperbolic,¹¹ a means of explaining a judicial decision

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⁹. Id. at 619.
¹⁰. Id.
¹¹. Consider, for example, the court’s concern that without this new judicial action

... banks would quickly become pervasive financial webs, serving only their owners, managers and friends by trapping all the best investments being innocently funneled by the public through their loan departments. Such a policy would soon destroy their public usefulness and benefit neither the public nor, ultimately, the banking industry.

Id. at 619. One might wonder how society managed to survive this long. Of course, the concerned loan applicant could always “tie-up” the property by obtaining a purchase agreement, contingent on financing, before disclosing the deal to anyone; indeed, this may be the only prudent approach, since banks are not the only potential “financial webs, serving only their owners, managers and friends...” Id.
based on unique facts and hence not otherwise supported by judicial precedent?

The only case cited in support of the decision was recognized by the court as “not squarely in point.”12 *Peterson v. Idaho First National Bank*13 dealt with a bank’s implied duty to maintain confidentiality of the bank’s records concerning its customers’ financial status. Since the basis of *Peterson* was founded on the contract between the bank and its customer,14 that case is clearly not persuasive in a dispute involving neither a customer nor a contract. Furthermore, that case dealt strictly with the customer’s right to privacy as to his bank records.15 This issue has been made subject to both state and federal regulation and legislation directed solely against disclosure to governmental agencies, with no inkling of an intention to restrict bank disclosure to private parties.16 There is also historical authority, though perhaps not indicative of current trends, holding that a bank’s records are solely the property of the bank and are not subject to any proprietary claim of the customer.17

It therefore appears that the *Djowharzadeh* decision is not well supported by the privacy-issue case cited by the court, nor by the privacy laws and cases in general. This does not, however, mean that there is no judicial authority supporting the decision. Perhaps the best example of support is *Pigg v. Robertson*,18 a case strikingly similar to *Djowharzadeh*. Mr. Pigg went to his bank to see the president, with whom he had done business for years, about a loan to purchase farmland. Mr. Pigg was told by a teller that the president was out of town, but that Mr. Pigg could talk to a

12. 646 P.2d at 619.
14. 646 P.2d at 619 (citing 10 Am. Jur. 2d Banks § 332 (1963)).
15. 83 Idaho at 588, 367 P.2d at 288-90.
18. 549 S.W. 2d 597 (Mo. Ct. App. 1977); *see also* Dawson, *supra* note 17, at 10-13.
Mr. Robertson. Mr. Pigg was ushered in to see Mr. Robertson in the office normally used by the president, and proceeded to tell Mr. Robertson about his "exceptional opportunity" to purchase a farm.\(^{19}\) Mr. Robertson was not an employee of the bank, but was an auditor working for an independent auditing firm. A short time after his conversation with Mr. Pigg, Mr. Robertson purchased the farm, and then resold it seven months later for almost twice the purchase price.\(^ {20}\)

Despite the obvious similarities, several significant factors distinguish the _Robertson_ case from _Djowharzadeh_. First and foremost, the defendant in _Robertson_ was the individual who usurped the opportunity; the bank was not a party to the lawsuit. Beyond this, Mr. Pigg was a longstanding customer of the bank, which seemingly could have made the bank liable as a result of the bank-customer relationship. The fact that the individual, not the bank, was found liable in these circumstances might seem to cast doubt on _Djowharzadeh_. _Robertson_ could be viewed as suggesting that only the usurper, and not the bank, should be held liable.

In _Djowharzadeh_ the bank was viewed as being a part of the usurpation. That court specifically found that the usurpation "resulted from deliberate conduct" of the bank for the benefit of the bank's "stockholders, officers and directors."\(^{21}\) Furthermore, the court in _Robertson_ made it clear that the existence of a previous banking relationship (making the loan applicant a "customer" of the bank) was not vital to its decision:

> The fact that plaintiff was a depositor in Marcus' bank is merely incidental, and significant in the present case only of the consideration that the borrower did not come uninvited to the lender. Of course, no man can obtrude either his trust or his secrets on another, to the extent of imposing upon that other any obligation in regard thereto, any more than he can render another his bailee in invitum. In that respect banks present a constant invitation to intending

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19. 549 S.W.2d at 598-99.
20. 1d at 599.
21. _Djowharzadeh_, 646 P.2d at 620. It is not clear how the bank stockholders, officers and directors would benefit from the transaction, except, of course, those persons individually involved.
borrowers, and thus subject themselves to whatever implication or obligation is to be drawn from that fact. In my opinion, however, the case would not be any different if the proposal were made to a private money lender, or even to an intimate friend, provided, always, that the application came to the lender at his invitation, express or implied, or with his equivalent consent.\textsuperscript{22}

Thus, the \textit{Robertson} and \textit{Djouharzadeh} courts each confirm the other in finding a special level of obligation imposed on banks because of their status as financial intermediaries serving the public. This obligation rises above the ordinary obligations imposed pursuant to a debtor-creditor or other contractual relationship and transcends the ordinary distinctions between tort and contract law.\textsuperscript{23} While similar duties can be imposed outside the banking context,\textsuperscript{24} the focus here is on the banking industry, a reflection of the unique status of banking institutions\textsuperscript{25} in our society:

\begin{quote}
This duty has existed traditionally and continues to exist, if not specifically in the law books, at least in the mind of the public in general and within the banking community in particular.

We take particular notice of banking practices and tradition which cultivates, encourages and even advertises the fact that banks can and should be trusted. Indeed, the words “trust,” “security” and “guaranty” are part of the name of many banks, including defendant Bank. The fact that no prior Oklahoma cases or statutes specifically define such a relationship is more of a tribute to past faithful performance of bankers than a proof that a special duty does not exist or need only be optionally observed.\textsuperscript{26}
\end{quote}

But what is the extent of this “special duty,” its basis, and its limits? The cases that help to answer this question will be

\begin{footnotes}
\footnotetext{22. 549 S.W.2d at 601 (quoting M.L. Stewart Co. v. Marcus, 124 Misc. 86, 207 N.Y.S. 685, 697 (1924)).}
\footnotetext{23. \textit{See}, e.g., Oklahoma Natural Gas Co. v. Pack, 186 Okla. 330, 97 P.2d 768 (1939), \textit{cited in Djouharzadeh}, 646 P.2d at 620 n.3.}
\footnotetext{24. 186 Okla. at 332-33, 97 P.2d at 770.}
\footnotetext{25. “Banking Institutions” in this context would logically include all of the regulated financial intermediaries, such as banks, savings and loan associations, and credit unions.}
\footnotetext{26. \textit{Djouharzadeh}, 646 P.2d at 620.}
\end{footnotes}
approached from three angles: those arising out of a bank's depository functions, those arising from the credit reporting function, and those arising from lending transactions.

The Depository Function

It might seem that cases involving bank deposits and collections would be fully covered by other specific law, for example the Uniform Commercial Code (U.C.C.),\textsuperscript{27} and indeed this is the case. But, unless specifically displaced, the U.C.C. is supplemented by other principles of law and equity,\textsuperscript{28} including a requirement of good faith\textsuperscript{29} and adherence to standards recognized by industry practice.\textsuperscript{30} This creates ample opportunities for the courts to expand the obligations of banks with regard to deposit transactions. The courts have utilized this opportunity accordingly, often using the special status of banks as society's financial intermediaries as a basis for formulating creative and even unique theories of bank liability.

In \textit{Shaw v. Union Bank and Trust},\textsuperscript{31} the bank improperly declined to allow a savings withdrawal by one joint tenant after the other joint tenant had died. While this might seem to be an ordinary breach of contract, based on the depository agreement, the court characterized the savings withdrawal slip as an "item" within the meaning of U.C.C. Article 4.\textsuperscript{32} Therefore, the savings withdrawal dispute was a "wrongful dishonor" under Article 4 and the bank was subject to a claim for consequential and punitive damages.\textsuperscript{33} While the court's reasoning is not above question,\textsuperscript{34} it may not be the most


\textsuperscript{28} U.C.C. § 1-103; \textit{Okla. Stat.} tit. 12A, § 1-103. See also Miller \& Harrell, \textit{supra} note 27, at 216-17.

\textsuperscript{29} U.C.C. § 1-203; \textit{Okla. Stat.} tit. 12A, § 1-203. Generally, however, outside Article 2 "good faith" means only honesty in fact and does not incorporate standards of commercial reasonableness. Cf. U.C.C. §§ 1-201(19) \& 2-103(1)(b).

\textsuperscript{30} U.C.C. § 1-205(2); \textit{Okla. Stat.} tit. 12A, § 1-205(2).

\textsuperscript{31} 640 P.2d 953.

\textsuperscript{32} Id. at 954-55; U.C.C. § 4-104; \textit{Okla. Stat.} tit. 12A, § 4-104.

\textsuperscript{33} 640 P.2d at 955-56 (citing \textit{Okla. Stat.} tit. 12A, § 4-402).

\textsuperscript{34} Miller \& Harrell, \textit{supra} note 27, at 257.
important aspect of the case. In his separate opinion in Shaw, Justice Opala focused on the nature of the relationship between a bank and society at large.\textsuperscript{35} A part of this opinion describes a special type of obligation imposed by law on banking institutions, not by reason of any particular contract or tort, but by reason of the "status" and "quasi-public character" of banking institutions:

A depositor's remedy against the bank for wrongful refusal to honor his order of payment is not just a breach of contract, express or implied, that the bank will pay to the depositor, or his order, any amount that does not exceed the balance on deposit. As institutions of "quasi public character" banks are engaged in a calling that places them under a common-law duty to exercise care in obeying their customers' mandates. The banker/depositor relationship embodies two distinct clusters of obligations. Its consensual origin gives rise to a contract, express or implied, which in turn creates a creditor/debtor bond. The law itself additionally affixes to it yet another attribute — that of status.\textsuperscript{36}

Again, this suggests obligations of a different nature and type from the ordinary common law duties, while leaving unanswered questions about the extent and limits of these special duties.

Other cases shed more specific light on the direction of this trend. One of the most important cases is Commercial Cotton Co. v. United California Bank,\textsuperscript{37} where a California court concluded that a "special relationship" exists between a bank and its depositors. As viewed by the California court, this special relationship apparently overrides the specific provisions of the U.C.C. and imposes a quasi-fiduciary duty on the bank in regard to its customers. In Commercial Cotton, a bank checking account customer lost some of his checks and one was subsequently forged, paid by the bank, and charged to the customer's account.\textsuperscript{38} The forged check was sent to the customer with his August or September, 1976 account statement, but he did not discover the forgery or report it to the

\textsuperscript{35} 640 P.2d at 957-58 (Opala, J., concurring in part and dissenting in part).
\textsuperscript{36} Id. at 957.
\textsuperscript{37} 163 Cal. App. 3d 511, 209 Cal. Rptr. 551, discussed in Kitada, supra note 5.
\textsuperscript{38} 163 Cal. App. 3d at 514, 209 Cal. Rptr. at 553.
bank until March, 1978. The bank declined to recredit the customer’s account for the amount of the forged check because it was notified of the forgery more than seven months after the end of the one year statute of limitations in California’s U.C.C. section 4406(4).\(^{39}\) The customer sued and the jury returned a verdict against the bank for the amount of the check ($4,000), plus $100,000 punitive damages. This verdict was affirmed on appeal.\(^{40}\)

The basis for the punitive damages award in *Commercial Cotton* was the fact that the bank’s refusal to recredit the account came eleven days after the California Supreme Court, in its decision in *Sun ‘N Sand, Inc. v. United California Bank*,\(^{41}\) held that the one year limitation period in Section 4406(4) does not apply when the claim against the bank is based on negligence. The court in *Commercial Cotton* held that the customer’s claim against the bank was founded in negligence, and therefore concluded that the bank’s reliance on the one year statute of limitations was “inexplicable” and amounted to bad faith, entitling the customer to recover punitive damages of $100,000.\(^{42}\)

It may seem extraordinary that a bank whose only fault was to rely on a statute of limitations in the U.C.C. could be held liable for $100,000 punitive damages as a result.\(^{43}\) But, strictly speaking, that is not the point, or the importance of

39. Id.

40. Id. at 518, 209 Cal. Rptr. at 556. An additional award of $20,000 in compensatory damages was reversed on appeal. Id.


42. *Commercial Cotton*, 163 Cal. App. 3d at 516, 209 Cal. Rptr. at 554. The court concluded that the customer’s “after-the-fact” conduct did not contribute to the bank’s negligence in making the $4,000 unauthorized payment. Id. Not only does this ignore the customer’s before-the-fact conduct, it overlooks one purpose of U.C.C. § 4-406(4), namely to require the customer to notify the bank within a reasonable time after the payment so that the bank will have an opportunity to pursue prior parties to the instrument and perhaps even the forger in an effort to recover the money paid. See, e.g., *Miller & Harrell supra* note 27, at 199-204.

43. An internal memorandum written by a staff attorney for the bank indicates that the bank considered arguing that in the computer age its failure to confirm each and every signature was a “reasonable commercial practice.” However, this defense was not pursued at trial and the bank “conceded it negligently paid the check.” 163 Cal. App. 3d at 513 n.1, 209 Cal. Rptr. at 553 n.1. Of course, in this view every payment of a forged check would constitute negligence, thereby excusing all negligence of the customer no matter how much it contributed to the loss. See *supra* note 42.
the case. Rather, the issue of focus is the nature of the bank-customer relationship, which the court found to be "special" and "quasi-fiduciary" in nature because it involves "vital public services affecting the public welfare:"

In the context of an insurance contract the Supreme Court emphasized the relationship between insurer and insured, characterized by elements of public interest, adhesion, and fiduciary responsibility created the necessary special relationship . . . .

Analogizing to the factors set out in Egan we agree with [Plaintiff's] contention that banking and insurance have much in common, both being highly regulated industries performing vital public services substantially affecting the public welfare. A depositor in a noninterest-bearing checking account, except for state or federal regulatory oversight, is totally dependent on the banking institution to which it entrusts deposited funds and depends on the bank's honesty and expertise to protect them. While banks do provide services for the depositor by way of monitoring deposits and withdrawals, they do so for the very commercial purpose of making money by using the deposited funds. The depositor allows the bank to use those funds in exchange for the convenience of not having to conduct transactions in cash and the concomitant security in having the bank safeguard them. The relationship of bank to depositor is at least quasi-fiduciary, and depositors reasonably expect a bank not to claim nonexistent legal defenses to avoid reimbursement when the bank negligently disburses the entrusted funds. Here, [the bank's] claimed defenses are spurious, and the jury found experienced legal counsel interposing them in an unjustifiable, stonewalling effort to prevent an innocent depositor from recovering money entrusted to and lost through the bank's own negligence, is a breach of the bank's covenant of good faith and fair dealing with its depositor."

As indicated by the language quoted above, the court in Commercial Cotton laid all blame for the loss on "the bank's own negligence," even though the forgery could be attributed at least partly to the customer's loss of his checks, his failure to report the loss to the bank and his failure to discover the forgery by examining his bank statements as required by U.C.C.

44. 163 Cal. App. 3d at 516, 209 Cal. Rptr. at 554 (citation omitted).
Moreover, the court made no mention of U.C.C. section 3-406, which precludes any party whose negligence contributes to a forgery from asserting that forgery against a drawee (the bank) which pays the instrument in good faith and in accordance with reasonable commercial standards. Instead, the court found that the bank’s defenses were “spurious” and interposed “in an unjustifiable, stone-walling” manner.

To the extent that Commercial Cotton finds negligence in the very act of paying a forged check and refusing to recredit the account on demand of the customer, it may suggest imposition of a standard of absolute or strict liability for bank payment of a forged check regardless of the customer’s negligence. Not only is this incongruous with modern commercial practice, involving the processing and payment of millions of checks daily (making it impossible for the bank to precisely scrutinize each check), it casts doubt on the viability of specific provisions of the U.C.C. in sections 3-406 and 4-406. Commercial Cotton also contradicts traditional efforts to place the liability on the party best able to avoid the loss. In practical terms, the case represents a threat of enormous punitive damages for any bank (at least in California) that dares to assert the U.C.C. statutory limitation period as a defense in a forgery case, and suggests that negligence of the bank in paying the item renders irrelevant any contributing negligence on the part of the customer. Moreover, the decision seems to be founded entirely on the “special relationship” with, and “quasi-fiduciary” duty of, the bank to its customer rather than on an analysis of fault or causation, thereby suggesting that neither the bank’s standard of care nor any other controllable factor could have affected the outcome. In effect, the result was based on the status of the parties’ relationship rather than the merits of the customary issues relating to forgery.

45. See Kitada, supra note 5, at 84.
47. 163 Cal. App. 3d at 516, 209 Cal. Rptr. at 554.
Although not immediately recognizable as such, a line of Oklahoma cases dealing with cashier's checks suggests a somewhat similar view.\footnote{48} Essentially, these cases hold that a bank cannot dishonor a cashier's check, even if the holder is not a holder in due course and the bank has a defense against payment of the instrument. This is currently a minority view\footnote{49} since most courts would allow a bank to refuse to make payment to a party against whom the bank has an assertable defense.\footnote{50} In Yukon National Bank v. Modern Building Supply, Inc.,\footnote{51} the bank issued cashier's checks to the payee as a result of a mistaken belief that the drawer had sufficient funds in its account to pay for the checks. When the mistake was discovered the bank notified the payee/holder that the cashier's checks would not be paid. The payee/holder nonetheless presented them for payment through a collecting bank. Upon dishonor the payee/holder sued. The Oklahoma Court of Appeals reasoned that a cashier's check issued by a bank should be treated just like cash and therefore required the bank to pay, even though the recipient of such payment had acquired the checks by mistake and without consideration.\footnote{52}

_Yukon National Bank_ represents the strictest possible view of liability on a cashier's check, in effect making the


\footnote{49. Note, A Banker's Right, supra note 48; but see University State Bank v. Allied Comroe Bank, 712 S.W.2d 183 (Tex. Ct. App. 1986).}

\footnote{50. See, e.g., Miller & Harrell, supra note 27 at 248-50. Even the majority view would allow dishonor only when the bank is the source of the defense and the holder is not in due course. This would not allow the bank to raise defenses assertable only by a third party, as where the remitter of the check asserts a claim or defense against the holder. See, e.g., Malphrus v. Home Sav. Bank, 44 Misc. 2d 705, 254 N.Y.S. 2d 980 (N.Y. Civ. Ct. 1965). However, where the bank has a defense arising out of its own transaction, and the holder has no special immunities as a holder in due course, most courts permit the bank to refuse payment. See, e.g., TPO Inc. v. FDIC, 487 F.2d 131 (3d Cir. 1973). The Oklahoma courts apparently do not recognize these distinctions. Texas may also have adopted the more strict Oklahoma view. See University State Bank, 712 S.W.2d 193.}

\footnote{51. 686 P.2d 307 (Okla. Ct. App. 1984).}

\footnote{52. Of course the bank could then charge the payee's account, create an overdraft, and seek to recover that amount in a separate action. See U.C.C. § 4-401. But this is not the consideration the bank bargained for.}
bank liable regardless of the merits of the bank’s claim or defense against the holder. This view was buttressed by the decision in *Hotel Riviera, Inc. v. First National Bank & Trust,*\(^{53}\) where a bank was required to pay a cashier’s check even though the holder lacked due course status and in fact had acquired the check in an illegal transaction. In *Riviera,* the cashier’s check had been obtained by fraud and then transferred to the Hotel Riviera in a transaction illegal under Nevada law. At trial, the bank argued successfully that this precluded holder in due course status and hence the holder was subject to all claims and defenses which could be asserted against the transferor.\(^ {54}\) Since the transferor obtained the check by fraud, this would enable the bank to assert fraud in the procurement as a defense to the demand for payment. This argument was rejected on appeal in a somewhat cursory opinion that essentially indicates that a bank should not be able to assert failure of consideration as a defense to its liability on a cashier’s check. In support of this unusual notion the court cited only the “peculiar nature” of a bank’s liability which gives “the aura of cash” to a cashier’s check. Furthermore, “[w]hether that aura bears scrutiny in the law” was deemed to be irrelevant.\(^ {55}\)

The foregoing cases represent examples where a bank, entirely because of its status as such, has been effectively denied the use of common law or statutory defenses that would have been available to other parties.\(^ {56}\) There appears to be no common law or statutory basis for such treatment, other than somewhat vague notions of “special” treatment for banking institutions as such.

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53. 768 F.2d 1201 (10th Cir. 1985).
55. 768 F.2d at 1204.
56. In *Commercial Cotton,* 163 Cal. App. 3d 511, 209 Cal. Rptr. 551, the bank was assessed punitive damages for asserting a U.C.C. statute of limitations as a defense; the bank customer’s negligence contributing to the loss was largely ignored. In *Yukon Nat’l Bank,* 686 P.2d 307 and *Riviera,* 768 F.2d 1201, banks were precluded from asserting common law defenses relating to mistake, fraud, and failure of consideration even though in one case the opposing party dealt directly with the bank and in the other took the check in an illegal transaction.
Less dramatic examples abound. In *Tonelli v. Chase Manhattan Bank*, three New York courts grappled with the same set of facts and applied grossly divergent theories of law. About the only similarity between the decisions is that in each case the court found the bank to be negligent in violating some special bank-oriented duty. In *Tonelli*, the bank issued a cashier's check in return for an unendorsed certified personal check payable to the same payee. In each instance the three New York courts concluded that this act was the significant factor which permitted an employee of the check's owner to defraud his employer. Indeed "[t]he central issue raised by this case is whether a drawee is negligent if it exchanges an unendorsed certified check for a cashier's check in the same amount made payable to the same payee." Scholars have pointed out the technical defects of the *Tonelli* decisions, and the danger of "a broad rule of law that it is per se negligent to make any payment or exchange of checks without indorsement." For our purposes, it is sufficient to note that the thrust of *Tonelli* would be to impose the adverse impact of this theory on banks, and to impose liability in such circumstances without regard to other factors which might have contributed to the loss. In effect, then, this represents but another example of "special" rules of law creating unique liability for bankers.

Of course, it has never been difficult to find cases which interpret existing laws in such a fashion as to be adverse to

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58. 86 Misc. 2d at 681, 386 N.Y.S. 2d at 724. Ironically, there is Oklahoma authority (decided in the context of different circumstances) holding that issuance of a cashier's check for an unendorsed personal check payable to the same payee does not alter the rights of the parties and does not subject the bank to liability. *See* Swan Air Conditioning Co. v. Crest Constr. Corp., 568 P.2d 1330 (Okla. Ct. App. 1977).

59. Lord, supra note 57, at 37 referring to 86 Misc. 2d at 683, 386 N.Y.S.2d at 725.

60. Id. at 36-47.

61. Id. at 47.

62. For example, in *Tonelli* the actual fraud occurred when the employee deposited the cashier's check in a dummy account at another financial institution, and later effectively withdrew most of the money. Yet, the New York court focused almost entirely on issuance of the cashier's check.
the interests of banks, and of themselves such cases normally might not evidence anything special. Taken together, however, these cases may constitute something more, and may in fact be evidence of a significant, even revolutionary, break with the past in regard to the bank-customer relationship. Reynolds-Wilson Lumber Co. v. Peoples National Bank may be another such case. In Reynolds-Wilson, a draft printed on an envelope in the customary form of a documentary draft was delivered along with a “collection letter” to Peoples National Bank. The draft was addressed as follows:

To Perdue & McCarthy Ctl. Co.

Peoples National Bank
Kingfisher, Oklahoma
Acct. #0001627

Pursuant to past practice, the bank treated this as a collection item, attempting to follow the written and telephoned instructions of the various parties, and giving oral notice of dishonor upon non-payment. If indeed the item was a collection item and the bank a collecting bank, this behavior was proper. Even if not proper, this behavior would subject the bank only to actual damages for any loss caused by the delay in giving written notice. A number of reasons were advanced by the bank as a basis for this view: previous dealings, the fact that the draft was drawn and signed by the payee, the use of a documentary draft form, the use of a “collection letter,” the use of telephone notice and instructions; in other words, the

63. 699 P.2d 146 (Okla. 1985).
65. 699 P.2d at 148.
66. Id. at 147-48. In more detailed discussion the court later concludes that the parties past practice was to treat these items like checks. Id. at 152 n.4.
bank argued that the draft was a collection item "payable through" the bank as a collecting bank.\textsuperscript{68}

Sweeping aside the bank's arguments, the court in \textit{Reynolds-Wilson} found that the bank was a payor bank and the draft was a "demand item." As a result, the bank was accountable for the amount of the draft under U.C.C. section 4-302.\textsuperscript{69} As to the bank's argument that addressing the draft "To Perdue & McCarthy Ctl. Co." at least created an ambiguity about the identity of the payor, justifying introduction of parol evidence as to the intent and understanding of the parties, the court concluded the bank and the cattle company were "co-drawers." "[T]he draft here involved was not ambiguous."\textsuperscript{70}

The issue may not have been as clear as the court indicated. For example, in \textit{Southern Cotton Oil Co. v. Merchants National Bank},\textsuperscript{71} the court was faced with a similar situation.\textsuperscript{72} That court noted that where the bank did not have authority to charge its customer's account for the draft, but instead was expected to notify the customer of each draft's arrival and act on instructions, the bank was acting only as a collection agent and not as a payor. As to the listing of the bank's name along with the customer's name on the face of the draft, the court said:

Where the names of both the customer and the bank were listed in the space for drawee, as in the present case, it was unclear whether the bank was the drawee. Surrounding circumstances must then be considered in resolving this ambiguity. Where the customer does not authorize the defendant bank to make payments out of its account on the plaintiff's order, there was no account out of which the plaintiff could draw funds. In the present controversy, it is clear that the Bank acted as a collecting bank, presenting the drafts to the

\begin{itemize}
\item \textsuperscript{68} 699 P.2d at 149-55. The court specifically found "a complete absence of any limiting language on the draft indicating it was to be paid 'through' or 'at' PNB." \textit{Id.} at 152. \textit{Cf.} U.C.C. § 3-120, \textit{cited in} 699 P.2d at 152 n.4.
\item \textsuperscript{69} 699 P.2d at 155.
\item \textsuperscript{70} \textit{Id.} at 150.
\item \textsuperscript{71} 670 F.2d 548 (5th Cir. 1982).
\item \textsuperscript{72} \textit{Reynolds-Wilson} represented an even stronger case for the bank since in \textit{Southern Cotton} the parties agreed that the draft was a demand item, while in \textit{Reynolds-Wilson} it had features of a documentary draft and collection item.
\end{itemize}
buyer for payment and forwarding the payment to the
seller's local bank only after receiving funds or authorization
from the buyer. 73

The Reynolds-Wilson court relied for its authority on Pecos
County Bank v. El Paso Livestock Auction Co. 74 In Pecos,
however, the draft on its face specifically directed the bank to
charge the account of the bank's customer. This is the
hallmark of a demand draft (a "check") being presented to a
payor bank for payment, as contrasted with a collection item
being sent to the bank for presentment to a separate payor. 75
As a result, Reynolds-Wilson appears to be more than just the
usual bank collection case; it suggests a judicial sentiment
that goes beyond the norm in imposing liability on a bank in
circumstances where the bank's duties and liabilities probably
were at least uncertain, and in this regard Reynolds-Wilson
seems to be only part of a larger pattern.

Several recent cases have dealt with the problem of bank
service charges. The best known of these, Perdue v. Crocker

73. 670 F.2d at 550 (citation omitted).
75. Cf. U.C.C. § 4-105(b) & (d). The Reynolds-Wilson court also cited New Ulm
relied on by the court in Pecos County Bank, 586 S.W.2d 183. New Ulm also is ap-
parently the source for the notion that the bank and its customer should be consid-
ered "joint payors." 558 S.W.2d at 25. New Ulm is particularly curious because that
case clearly dealt with a documentary draft, accompanied by a collection letter spec-
fically identifying the bank's customer (R. & R. Farms, Inc.) as the sole "payor." Id. at
24. Moreover, it was undisputed that the bank did not have the authority to pay the
draft, but only to present it for payment to its customer. The customer

appeared each day at the bank to examine the drafts which had been
presented . . . . He would customarily write a check for the amount of the
draft, and upon his payment, the bank would turn over the draft to him.
The bank would then apply the check against his account, and it would
send a cashier's check for the amount of the draft to the transferring bank.

Id. at 22. This is not the description of a payor bank. Cf. Farmers and Merchants
Ct. App. Div. 1968). Note that even the court described the sender as a "transferring
bank," which suggests that New Ulm was an intermediary collecting bank rather than
a payor. Cf. U.C.C. § 4-105(c). Yet, despite all evidence to the contrary, "all parties
concur that the bank acted [as a payor]." 558 S.W. 2d at 25. One could logically
conclude that the New Ulm case was wrongly decided on this issue.
National Bank, 76 imposed a duty of "good faith and fair dealing" 77 on the bank as a basis for questioning whether the bank's six dollar returned check charge was reasonable. 78 The duty of good faith and fair dealing was imposed because, in the court's view, the bank-customer relationship was created by a deposit contract that permitted one side (the bank) to set various service charge rates at its "will and discretion." 79 The court also viewed the deposit agreement as a "classic example" of an adhesion contract subject to special review by the court and unenforceable upon a finding of oppression or unconscionability. 80 While remanding for a factual determination, the Supreme Court of California made clear its sympathies:

In short, the bank structured a totally one-sided transaction. The absence of equality of bargaining power, open negotiation, full disclosure, and a contract which fairly sets out the rights and duties of each party demonstrates that the transaction lacks those checks and balances which would inhibit the charging of unconscionable fees. 81

77. Id. at 924, 702 P.2d at 510, 216 Cal. Rptr. at 352.
78. This court specifically held that state law was not preempted by federal law and banking regulations, despite pronouncements from the Office of the Comptroller of the Currency to the contrary. 38 Cal. 3d at 932-43, 702 P.2d at 516-23, 216 Cal. Rptr. at 358-66. See 12 C.F.R. § 7.8000, as amended, 49 Fed. Reg. 28,237 (1984).
79. 38 Cal.3d at 923, 702 P.2d at 510, 216 Cal. Rptr. at 352 quoting Automatic Vending Co. v. Wisdom, 182 Cal. App. 2d 354,357, 6 Cal. Rptr. 31, 33 (1960). Perdue held that such a contract is illusory citing California Lettuce Growers v. Union Sugar Co., 45 Cal.2d 474, 289 P.2d 785 (1955) for the proposition that such discretion does not render the contract illusory so long as it is required to be exercised "in good faith and in accordance with fair dealing."
80. 38 Cal.3d at 925, 702 P.2d at 511, 216 Cal. Rptr. at 353.
81. Id. at 928, 702 P.2d at 514, 216 Cal. Rptr. at 356. This rather curious view of contract law would, it seems, invalidate virtually every contract between individuals and businesses of any size, since this is about as good as a consumer contract gets. The terms of the deposit contract, including current service and returned check charges, typically are fully disclosed to the customer at the time the account is opened. The customer is under no compulsion, economic or otherwise, to open the account, having an almost incredible array of alternatives available. The court's language suggests to this author an almost medieval view, that contracts should not be enforced unless they are the result of haggling between two parties of nearly identical financial status, else inequality of "bargaining power" might taint the transaction. For a more reasoned view of this problem, see R. Posner, ECONOMIC ANALYSIS OF LAW 70-71, 84-86 (2d ed. 1977).
Several other cases have recently followed the lead of the California Supreme Court in *Perdue*. 82

As illustrated by *Jackson v. First National Bank*, 83 creative theories of bank liability are not solely the product of this decade. In that 1966 case, a church official forged checks on the church’s account. The forger was able to perpetrate the scheme because church officials failed to inspect the monthly bank statements as required by U.C.C. section 4-406, thereby failing to discover the forgeries and to notify the bank. The bank argued that the negligence of the church contributed to the loss and therefore the church should be precluded from asserting the forgery pursuant to U.C.C. sections 3-406 and 4-406. As in *Commercial Cotton*, 84 however, the court de-emphasized the customer’s negligence and focused exclusively on the bank’s negligent failure to monitor and ascertain the propriety of the customer’s checking transactions. The court was impressed by the fact that the checks were made payable to the forger personally and were endorsed by a nearby dog racing track.

What do these cases mean beyond illustrating bank liability pursuant to a miscellaneous collection of legal theories? At the very least, by their own terms, they represent the imposition of special duties on banking institutions, usually framed as a duty of “good faith” or “fair dealing” and typically imposed as the result of a perception of market power or public responsibility unique to financial institutions. 85 In some respects, these special duties resemble the concepts of


83. 55 Tenn. App. 545, 403 S.W.2d 109 (1966).

84. 163 Cal. App. 3d 511, 209 Cal. Rptr. 551.

85. Of course, some of the cases simply rest on a questionable application of existing law. *See, e.g.*, *Parr v. Security Nat’l Bank*, 640 P.2d 648 (Okla. Ct. App. 1984); *Friendly Nat’l Bank v. Farmers Ins. Group*, 630 P.2d 318 (Okla. 1981). It is difficult to categorize such cases in order to determine whether they are part of the new bank liability trend or merely represent dubious interpretations of the U.C.C. For example, in *Parr* the court emphasized the customer’s reliance on the bank’s failure to precisely identify the amount of the check subject to her stop payment order. This may be consistent with the “reliance” theory propounded in other bank liability cases as discussed *infra*. 
“merchant good faith,” unconscionability and exclusive dealings, as provided for in U.C.C. Article 2, although there appears to be no statutory basis for extending these concepts to purely financial transactions.86

Although the examples are not limited to recent cases, the volume of such cases seems to have increased in recent times. Also, the cases in this area are not limited to purely bank-customer transactions. Indeed, some of the more dramatic examples of special bank liability arise in the context of credit reports and other disclosures of customer information to third parties.

Credit Reporting and Other Disclosure of Financial Information

Information disclosure is a fairly routine activity for banks, but one which is nonetheless fraught with danger. One dramatic example is found in Maley v. East Side Bank,87 where the new owner of a small corporation used the credit record previously established by the former owners as a means of greatly expanding the corporate debt. The money was then funneled to the new owner (and president), ultimately leaving the corporation a bankrupt shell. When the corporate creditors discovered this, they sued the corporation’s bank because the bank had issued credit reports based on historical experience under the former owners and had allowed the new owner/president to endorse checks payable to the company for deposit to his own account.88 Although the bank had failed to obtain a new corporate resolution authorizing the new owner/president to sign and indorse company checks, there was no question that as president and sole owner of the corporation he had the right to do so. Nor was there any doubt that the bank had accurately reported its historical credit experience with the corporation. Furthermore, the bank had no contractual relationship with creditors of the corporation, and the

86. See U.C.C. §§ 2-103(1)(b) & 2-306(2). Cf. U.C.C. §§ 1-203 & 1-201(19); see also U.C.C. § 2-102. In addition, the banking law cases do not seem to follow the Code’s consistent deference to the agreement of the parties. See, e.g., U.C.C. §§ 1-102(3) & 2-301.
87. 361 F.2d 393 (7th Cir. 1966).
88. Id. at 396-98.
corporation probably should have been estopped by the participation of its president from asserting any breach of duty against the bank in bankruptcy.\textsuperscript{89} Nonetheless, the court found that the bank “committed a serious breach of its duty to its depositor . . . and to that corporation’s innocent creditors.”\textsuperscript{90} The exact nature of the duty was not made clear, nor was the basis for the bank’s liability to third party creditors with whom the bank had no other relationship.

Other cases have confirmed that this is more than just an isolated example, with other courts imposing liability on banks for a variety of miscues relating to information disclosure. A number of these cases have already been subject to commentary,\textsuperscript{91} including \textit{General Motors Acceptance Corp. v. Central National Bank}.\textsuperscript{92} In that case the bank reported to GMAC that the bank’s customer was current on its loans and was maintaining a “low five-figure balance.”\textsuperscript{93} In reality, the customer had maintained a five-figure balance on only one day of the period in question and the loan was current only because it had recently been renegotiated. The bank also indicated that there had been no recent overdrafts and no checks dishonored for insufficient funds, when in reality the bank’s records reflected a negative balance of $9,116 on that day and other sizeable negative balances on other days.\textsuperscript{94}

The \textit{General Motors Acceptance} case is more conventional than \textit{Maley},\textsuperscript{95} because in \textit{General Motors Acceptance} the bank’s liability was based on a misrepresentation of the customer’s financial status. In contrast, in \textit{Maley} the bank did not misrepresent the customer’s status. However, the creditors, having failed to discern the importance of the recent ownership change, then sought (successfully, it seems) to shift

\begin{itemize}
  \item \textsuperscript{89} \textit{Id.} at 401.
  \item \textsuperscript{90} \textit{Id.} at 402.
  \item \textsuperscript{91} \textit{See, e.g.,} Flick & Replansky, supra note 4, at 251-57; \textit{Current Decisions of Interest, Bank’s Misleading Disclosures to Customer’s Other Creditor Regarding Customer’s Financial Condition Held as Fraud, LII Leg. Bull. 144 (May, 1986)}.
  \item \textsuperscript{92} 773 F.2d 771 (7th Cir. 1985); \textit{see also} Flick & Replansky, supra note 4, at 251.
  \item \textsuperscript{93} 773 F.2d at 775.
  \item \textsuperscript{94} \textit{Id.}
  \item \textsuperscript{95} 361 F.2d 393.
\end{itemize}
their losses to a bank which had provided accurate credit information about the corporate account. Of course, in Maley there was the additional concern about the obsolete corporate resolution regarding corporate authority, but since there was no question that such authority existed, this alone probably does not justify the result. In this sense, then, Maley stands apart from General Motors Acceptance in imposing liability for accurate disclosure of account credit information.

Another case, however, demonstrates an approach consistent with Maley and may suggest a pattern indicative of an emerging theory of bank liability. In Central States Stamping Co. v. Terminal Equipment Co.,\textsuperscript{96} the bank incurred liability by disclosing information which was technically correct but which represented less than the bank’s total knowledge of the facts involved. In response to a telephone inquiry, the bank’s president had painted a positive picture of the bank’s customer, hedging only with the comment that the customer was undercapitalized.\textsuperscript{97} Relying on the bank president’s comments, the inquiring creditor extended a loan to the bank’s customer (most of which went to reduce the customer’s debt to the bank). Shortly thereafter the customer went bankrupt.\textsuperscript{98} The court concluded that the bank knew more than the president admitted in his telephone conversation with the creditor and had failed to disclose information about previous defaults and other financial problems of its customer. Knowing that the creditor was relying on the bank’s information, the bank was obligated to disclose all information which might be relevant to the inquiry.\textsuperscript{99} This suggests that a bank has a duty to go beyond disclosure of mere technical information, to reveal any other facts known to it which might bear on the creditor’s decision. This would help explain the Maley case, where the bank was faulted for disclosing only technical data and not the bank’s full knowledge, or even mere suspicions, concerning the customer’s behavior. This in turn is consistent with the notion that banks have some sort of “special” or

\textsuperscript{96} 727 F.2d 1405 (6th Cir. 1984); see also Flick & Replansky, supra note 4, at 251-52.
\textsuperscript{97} 727 F.2d at 1406.
\textsuperscript{98} Id. at 1407.
\textsuperscript{99} Id. at 1408-09.
"quasi-fiduciary" obligation to the public at large, which prohibits a bank from protecting its own interests by remaining silent at the expense of third parties. Indeed, some courts have even taken this so far as to require the bank to disclose information it discovers after the initial credit report has been given.\(^\text{100}\)

Obviously, these sorts of obligations create severe dangers for banks, since a misleading disclosure can lead to liability. For example, in Suburban Trust Co. v. Waller,\(^\text{101}\) the customer deposited a large sum of cash essentially equivalent to the amount recently stolen in a robbery. Suspicious that the cash might be the proceeds of the robbery, the bank notified the FBI. As a result, the customer was arrested and interrogated.\(^\text{102}\) When it turned out that the cash was the proceeds of a bona fide sale and was unrelated to the robbery, the customer sued the bank and was awarded damages for the bank’s breach of its duty of confidentiality.\(^\text{103}\) Therefore, a bank, or other institution, can also be held liable to the customer for release of credit information which is later proven to be false, even if the bank genuinely believed it to be correct at the time of disclosure. In Dun & Bradstreet, Inc. v. Greenmoss Builders, Inc.,\(^\text{104}\) the credit reporting agency was held liable for punitive damages for defamation as a result of furnishing an inaccurate credit report, despite a lack of any showing of malice or other wrongful intent.

These cases contrast, and perhaps conflict, with cases such as Maley\(^\text{105}\) and Central States Stamping,\(^\text{106}\) which at times seem to suggest that, in response to a credit inquiry, a bank has a duty to disclose mere suspicions or even volunteer a credit analysis of adverse factors relating to the financial condition and operations of bank customers. As a whole, these cases create a fine line for a bank to tread in furnishing credit information to others, balancing concern that full disclosure

\(^\text{100}\) See First Va. Bankshares v. Benson, 559 F.2d 1307 (5th Cir. 1977), cert. denied, 435 U.S. 952 (1978); see also Flick and Replansky, supra note 4, at 253.


\(^\text{102}\) Id. at 337-38, 408 A.2d at 760-61.

\(^\text{103}\) Id. at 349, 408 A.2d 766.

\(^\text{104}\) 105 S. Ct. 2939 (1985).

\(^\text{105}\) 361 F.2d 393.

\(^\text{106}\) 727 F.2d 1405.
of all known facts be given, against the danger of unneces-
sarily tainting the customer’s record with adverse data. What,
for example, should a bank do if its internal credit analysis
concludes that the customer is dangerously overextended and
not deserving of additional credit, yet the customer is and has
been in full compliance with all loan agreements? Does the
bank limit its credit reporting to the technical data indicating
an unblemished record, or is the bank obligated to reveal its
own conclusion (or suspicions) that the debtor is in financial
difficulty? If the bank fails to disclose all it knows, it may be
liable to creditors who extend credit as a result. Yet if the
bank gratuitously reveals its suspicion of impending trouble,
it may be liable to the customer.

A graphic example of this dilemma is found in Sanchez-
Corea v. Bank of America.107 A bank officer made unau-
thorized loans totaling $246,000 to the debtor, to help cover the
debtor’s overdrafts. When this was discovered, the bank im-
mEDIATELY demanded repayment and refused to advance addi-
tional credit.108 In the meantime, the debtor had arranged
other financing and an infusion of equity capital, all contin-
gent on reduction of the bank’s claim to $180,000 and the
granting of a $100,000 SBA loan. The bank refused to reduce
its claim and advised the SBA of the bank’s belief that the
debtor might be receiving stolen property. The debtor’s refi-
nancing was never completed and the debtor ultimately filed
bankruptcy.109 The debtor and the trustee in bankruptcy then
sued the bank for breach of contract, fraud, breach of implied
covenant of good faith and fair dealing, disparagement of
credit, interference with prospective economic advantage,
promissory estoppel, negligence, and intentional infliction of
emotional distress. The jury awarded $1 million general dam-
ages, $1 million punitive damages plus $100,000 damages for
emotional distress.110

In summary, some cases impose liability on banks for fail-
ure to monitor and disclose activities of bank customers, while
others impose liability for excessive or incorrect disclosure.

108. Id. at 897, 701 P.2d at 829, 215 Cal. Rptr. at 682.
109. Id.
110. Id. at 897-98, 701 P.2d at 830, 215 Cal. Rptr. at 683.
Moreover, the cases mandating increased disclosure sometimes seem to impose an affirmative duty on banks to seek out and protect parties who might be injured by the bank's customers. Forcing this new "watchdog" role on banks potentially represents a major expansion of the horizon of bank responsibilities and poses great risks for banks, which must now face an increasing danger of being caught in the middle of disputes between their customers and third parties.

In addition to *Sanchez-Corea* and the other cases already discussed,\(^{111}\) two recent cases seem to confirm the "watchdog" role that is emerging. *Metge v. Baehler*\(^ {112}\) suggests that where a bank has a close banking relationship with its customer, the bank has an affirmative duty to take action to prevent that customer from committing fraud against the public at large. This case arose in the context of a customer's securities offering and infers that in these circumstances a bank may be liable as an aider and abettor for violation of the securities laws if it allows an insolvent customer to sell securities to the public.\(^ {113}\)

*Merrill Lynch v. First National Bank*\(^ {114}\) also illustrates the movement toward a "watchdog" role for banks. In this case, the First National Bank became aware that checks deposited with it by a customer were being dishonored by the payor bank, and that this in turn would require dishonor of certain checks drawn by the customer on the bank and deposited to the account of Merrill Lynch. There was no allegation of failure to comply with applicable U.C.C. rules, but the bank did not act immediately to inform Merrill Lynch, as had been

\(^{111}\) Examples discussed previously include *General Motors Acceptance*, 773 F.2d 771; *Central States Stamping*, 727 F.2d 1405; *First Va. Bankshares*, 559 F.2d 1307; *Maley*, 361 F.2d 383; *Jackson*, 55 Tenn. App. 545, 403 S.W. 2d 109.


\(^{114}\) 774 F.2d 909 (8th Cir. 1985).
past practice. As it happened, the bank’s customer was engaged in a check “kiting” scheme, and as a result Merrill Lynch suffered substantial losses.

Merrill Lynch sued First National on several grounds, alleging negligence for failure to discover and alert others to the check kiting scheme, deceit and deviation from an established course of dealing. In its defense First National relied on the traditional view that a bank has no obligation to ferret out and disclose check kiting schemes of its customers. The court, however, distinguished the traditional cases on grounds that they involve dealings between banks “when both have equal opportunity to discover a check-kiting scheme, [and] they do not stand for the proposition that a bank may act unilaterally to shift the resulting loss onto a depositor . . . .” This is understandable to the extent it is based on the breach of a special arrangement arising out of an explicit course of dealing; but less so to the extent it is based on the theory that Merrill Lynch was not a bank.

Indeed, the court’s own description of Merrill Lynch’s status indicates a relationship with First National very much like that of a typical collecting bank relationship:

Merrill Lynch acted in a dual capacity. It had an account as a customer with FNB. It also behaved substantially as a bank in that it maintained . . . an account known as the Ready Assets Trust, through which customers could earn interest . . . [and] redeem these shares for cash through a “share redemption request,” which for most practical purposes had the same characteristics as an ordinary bank check.

The court stated that its decision to hold the bank liable was based on the bank’s course of dealing with Merrill Lynch.

115. Id. at 911.
116. Id. at 912.
117. Id., see, e.g., Mid-Cal Nat’l Bank v. Fed. Reserve Bank, 590 F.2d 761 (9th Cir. 1979); Citizens Nat’l Bank v. First Nat’l Bank, 347 So. 2d 964 (Miss. 1977), both cited in Merrill Lynch, 774 F.2d at 914. Mid-Cal Nat’l Bank, for example, held that absent a “special relationship” between the payor bank, the customer and the other bank, the payor bank has no duty to control its customer’s conduct or to discover or disclose its customer’s check kiting activities.
118. 774 F.2d at 914.
119. Id. at 911.
However, the opinion also focuses on the fact that First National suspected that a check kite might be in progress, and failed to seek out and notify Merrill Lynch of this suspicion.120 This, plus the court’s conclusion that previous practice constituted an enforceable course of conduct,121 suggests imposition of a higher standard than is evident from previous check kiting cases.122 It is reinforced by the court’s effort to distinguish the previous cases on grounds that Merrill Lynch was not a bank, when in fact Merrill Lynch was acting very much like a bank in offering its Ready Assets account.123 Again, this suggests a new “watchdog” role for banks, requiring scrutiny of customer activities and protection of other customers and the public from loss due to wrongdoing by customers of the bank. And again, such duties appear to be unique to banking institutions, suggesting that the traditional relationship between a bank, its customers and society may be in the process of changing to some special arrangement, based largely on the status of the bank as such and therefore no longer dependent on the merits of the parties’ rights according to traditional common law principles.

A number of the cases indicate that this “watchdog” role for banks may be limited to circumstances where there is some special aspect of the bank’s position which suggests that the bank should be held to a higher than normal standard in that case. The “course of dealing” in Merrill Lynch124 may be one example, the “special relationship” mentioned in Mid-Cal Nat’l Bank v. Federal Reserve Bank125 may be another. If this is correct, then the special duties imposed in these cases may not be generally applicable to banks at large unless a bank does something extra to assume such obligations. In that event it would be important for bank lawyers and employees to understand the point at which they cross over the line and subject the bank to special liabilities.

120. Id. at 914.
121. Id. at 915-16.
122. See supra note 117.
123. 774 F.2d at 911.
124. Id. at 914.
125. 590 F.2d at 763; see also Metge, 762 F.2d at 624-25.
Several cases illustrate the kinds of circumstances that can give rise to special bank responsibilities and liabilities. In *Klein v. First Edina Nat'l Bank*,\(^\text{126}\) the bank was relying on the bank's guidance in a transaction where the customer pledged stock as collateral for the loan of a third party. The court concluded that the bank breached an affirmative duty of disclosure by failing to explain the purpose of the loan to the customer, speculating that such disclosure might have changed the customer's mind about entering the transaction. In *Richfield Bank & Trust v. Sjogren*,\(^\text{127}\) the bank made a loan to its customer to buy goods from a seller known to the bank to be having financial difficulty. The court reasoned that the bank knew the seller probably could not deliver the goods, and had a duty to either disclose this to the buyer or not make the loan.

While the preceding two cases illustrate circumstances where the bank had special knowledge relevant to the transaction and failed to disclose it to interested parties, they do not go very far toward delineating the nature of the duty that mandates the disclosure. This uncertainty suggests an inquiry: Have banking institutions been turned into fiduciaries at large, accountable to the public and their customers as fiduciaries merely by reason of their status as banking institutions?

The Nature of the Bank-Customer Relationship and the Impact of Reliance

One possible interpretation of the trend is that banks have been made fiduciaries of their customers and perhaps even society at large, but such an interpretation would go far beyond what has been formally recognized by most courts. For example, in *Palmer v. Idaho Bank & Trust*,\(^\text{128}\) a customer claimed that the bank had a fiduciary duty to disclose that his bank account could be subject to an Internal Revenue Service

\(^{126}\) 293 Minn. 418, 196 N.W.2d 619 (1972), discussed in Miller & Harrell, *supra* note 27, at 262.

\(^{127}\) 309 Minn. 362, 244 N.W.2d 648 (1976) discussed in Miller & Harrell, *supra* note 27, at 262.

\(^{128}\) 100 Idaho 642, 603 P.2d 597 (1979), discussed in Miller & Harrell, *supra* note 27, at 263; see also B.C. Recreational Indus. v. First Nat'l Bank, 639 F.2d 828 (1st Cir. 1981).
(IRS) levy. The court held that the bank had no such duty. But, the Palmer case did not involve any element of reliance on the part of the customer (he had received four prior notices from the IRS), or anyone else. Indeed, virtually all of the cases discussed so far, where a bank has been held specially liable, also involve circumstances where there is some sort of reliance by the injured party on the expertise, knowledge or guidance of the bank.

Indeed, some cases specifically suggest that the key factor is not the nature of the relationship itself, fiduciary or otherwise, but rather the fact that the relationship induces reliance: "The relationship inducing reliance need not be a fiduciary one in a strict sense; the surrounding circumstances may reveal reliance even though the parties are not in a confidential relationship." 129 This suggests that the element giving rise to special bank liability is not the nature of the bank-customer relationship per se, but rather the effect of that relationship. An example of that effect is the fact that the nature and aura of banking institutions lead members of the public to repose confidence and reliance that such institutions will behave according to the highest ethical standards. When a party relies on such an assumption to his or her detriment, the court will look very closely at the bank's actions to determine if the bank took unfair advantage of its unique position. While the result may take on the appearance of something fiduciary in nature, it is probably more in the nature of a contractual obligation, akin to the notion of detrimental reliance as a substitute for consideration in contract cases. 130 This in turn is con-


130. The evolution of detrimental reliance as a substitute for consideration is one of the significant developments of contract law in the twentieth century, the beginnings can be traced to the nineteenth century. See, e.g., Ricketts v. Scothorn, 57 Neb. 51, 77 N.W. 365 (1898); Kirksey v. Kirksey, 8 Ala. 131 (1845). Detrimental reliance has been described as a form of promissory estoppel or waiver, and the basis has been described as follows:

It is not the intention of the party estopped but the natural effect upon the other party which gives vitality to an estoppel. It may be said here, as in the case of assent to a substituted contract, that it is the justifiable belief of the party relying on the so-called waiver which is the essential thing.
sistent with the traditional character of the bank-customer relationship as essentially contractual in nature.\textsuperscript{131} Such a view is also consistent with the traditional view that the bank normally does not owe a fiduciary duty to its customer,\textsuperscript{132} but that "if an institution assumes a special relationship of trust or confidence with a customer, it assumes a fiduciary duty to disclose material facts."\textsuperscript{133} A typical example would be the case where a customer relies on the bank to act as a financial advisor.\textsuperscript{134} And yet, it should be emphasized that a fiduciary relationship does not exist merely by reason of a long standing or close banking relationship with the customer.\textsuperscript{135} Indeed quite the opposite: The bank may incur special fiduciary-like obligations to persons with whom it has never done business,\textsuperscript{136} and yet have no such obligation to a


This doctrine was given added judicial emphasis after then Judge Cardozo's opinion in Allegheny College v. National Chautauqua County Bank, 246 N.Y. 369, 159 N.E. 173 (1927), which specifically adopted promissory estoppel as a form of consideration. It has also been subject to extensive commentary from a variety of perspectives. See, e.g., Childres & Garamella, The Law of Restitution and the Reliance Interest in Contract, 64 Nw. U. L. Rev. 433 (1969); Dawson, Restitution or Damages?, 20 Ohio St. L.J. 175 (1959); Fuller & Perdue, Jr., The Reliance Interest in Contract Damages 1 & 2, 46 Yale L.J. 52 & 373 (1936); Comment, Once More into the Breach: Promissory Estoppel and Traditional Damage Doctrine, 37 U. Chi. L. Rev. 559 (1970). Perhaps the best formal statement of the rule is the RESTATEMENT OF CONTRACTS, (SECOND) § 90(1) (1981):

Promise Reasonably Inducing Action or Forbearance.

A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

\textsuperscript{131} See NORTON & WHITLEY, supra note 1, at § 11.04[2].

\textsuperscript{132} See, e.g., Klein, 293 Minn. 418, 196 N.W.2d 619, cited in NORTON & WHITLEY, supra note 1, at § 11.04[3][d]; Klatt v. First State Bank, 220 N.W. 318 (Iowa 1928); see also B.C. Recreational Indus., 639 F.2d 828; Palmer, 100 Idaho 642, 603 P.2d 597.

\textsuperscript{133} NORTON & WHITLEY, supra note 1, at § 11.04[3][d].

\textsuperscript{134} See Stewart v. Phoenix Nat'l Bank, 64 P.2d 101 (Ariz. 1937), cited in NORTON & WHITLEY, supra note 1, at § 11.04[3][d].


\textsuperscript{136} See, e.g., Maley, 361 F.2d 393; Djowharzadeh, 646 P.2d 616; Robertson, 549 S.W.2d 597 discussed supra; see also Campbell v. Wells Fargo Bank, N.A., 781 F.2d 440 (5th Cir. 1986) (suggesting that non-customers may have standing to sue under the Bank Tying Act).
longstanding customer. The crucial element in all of these cases seems to be a notion similar to that of promissory estoppel: Has the bank acted in such a way as to induce the other party to rely on the bank's trust, advice or expertise to the detriment of that other party? If the answer is yes, the bank may be liable for any resultant damages, despite the absence, or existence, of a traditional bank-customer relationship. Of course, a longstanding or close banking relationship, while alone not enough to create a special or fiduciary-like duty, could indicate circumstances tending to induce the reliance necessary to trigger special bank obligations and liabilities.

This view would explain the many “course of conduct” cases that have appeared recently, imposing liability on banks for diverging from a course of conduct established by previous practice. Merrill Lynch, discussed supra, is a prime example. Other examples are a legion and only a few need be mentioned for illustrative purposes. In Postal Savings & Loan Association v. Freel, the mortgagee’s past practice of accepting late payments did not establish a course of conduct which constituted an implied waiver of the right to exercise an acceleration clause, because the written agreement between the parties was unequivocal and contained an anti-waiver clause. Significantly, the court held that the customer’s “contention that they reasonably relied on the [savings and loan association’s] past practice of overlooking defaults as an implied waiver of their obligation to pay the installments promptly must fail in light of the unambiguous and contrary provisions of the note.” The court’s emphasis on the lack of reasonable reliance reinforces the conclusion that reliance was the crucial element, and that such other matters as course of conduct or the bank-customer relationship are important primarily as they bear on the reasonableness of that reliance.

137. See, e.g., Klein, 293 Minn. 418, 196 N.W.2d 619, cited in Norton & Whitley, supra note 1, at § 11.04[3][d]; Klatt v. First State Bank, 206 Iowa 252, 220 N.W. 318 (1928); see also B.C. Recreational Indus., 639 F.2d 828; Palmer, 100 Idaho 642, 603 P.2d 597.
139. 774 F.2d 909.
141. Id. at 287, 698 P.2d at 384.
Compare with Postal Savings, another "course of conduct" case, National Livestock Credit Corp. v. Schultz.\textsuperscript{142} The creditor permitted sales of collateral in violation of the security agreement, and the court found that this established a course of conduct under U.C.C. section 2-208 and constituted consent to the sales under U.C.C. section 9-306.\textsuperscript{143} In this and other similar cases, courts have concluded that statements or behavior indicating that collateral could be sold free and clear can serve as a basis for reliance by other parties and therefore qualify as a waiver of the bank's rights.\textsuperscript{144} Also consider Vogel v. Carolina International, Inc.,\textsuperscript{145} where the creditor extended credit with knowledge of the debtor's difficulties and thereby established a course of conduct that tolerated the debtor's financial difficulties. The creditor also provided assurances of support to the debtor.\textsuperscript{146} When the creditor later altered this policy and repossessed collateral without notice, it was held to have previously waived its rights and to be liable for exemplary damages of $73,000, in addition to $18,743 actual damages and $16,040 damages for "outrageous conduct."\textsuperscript{147} Again, the customer's reliance on the bank and the bank's indications of support stand out as the crucial factors in the case.

In summary, the cases considered thus far may indicate that the crucial element in many of the bank liability cases has been circumstances which have induced the injured party to rely on the bank to his or her detriment. While the cases may speak of such things as fiduciary duty, course of conduct, the bank-customer relationship or "special" bank obligations, the common thread seems to be reliance. Upon analysis, the other factors, while relevant, seem to recede from center stage.

\textsuperscript{142} 653 P.2d 1243 (Okla. Ct. App. 1982).
\textsuperscript{143} Oddly, the court relied on the Article 2 course of performance provision at U.C.C. § 2-208, which should not be applicable unless one is a party to the sale, instead of the clearly applicable course of dealing provision at U.C.C. § 1-205.
\textsuperscript{144} See, e.g., Peoples Nat'l Bank & Trust v. Excel Corp., 236 Kan. 687, 695 P.2d 444 (1985), where a bank officer's oral statement at loan closing, to the effect that debtor was free to sell collateral if he would remit proceeds to the bank, permitted sale free of bank's security interest regardless of whether proceeds were applied to debt. Oral statements constituted waiver of security interest against purchaser by authorizing the sale under U.C.C. § 9-306(2).
\textsuperscript{146} Id. at 712-13.
\textsuperscript{147} Id. at 714-15.
as the primary foundation for the decisions and can be viewed as important only insofar as they bear on the reliance issue.

If this is correct, then banks and their counsel should be alert to any behavior which might be viewed as encouraging reliance by other parties. This in turn could compel a comprehensive re-evaluation of bank procedures and re-training of bank employees for purposes of re-emphasizing this consideration. Before recommending such a drastic step, however, the hypothesis must be tested in the context of that area of the law where the most important bank liability cases have arisen: Lender liability.

Lender Liability as an Adjunct of the Bank-Customer Relationship: The Role of Reliance

Few areas of the law have received so much recent publicity as the new line of cases holding lenders liable for a variety of perceived misdeeds against their customers, or even others.148 Some of the cases have become so well known as to have been described in detail in the popular business press.149 The significance of the trend and the importance of the cases have already been thoroughly analyzed in academic journals,150 so there is no need to attempt to do so in detail here. Rather, the purpose here is to examine a selection of the lender liability cases from the perspective of their impact on the bank-customer relationship as it appears to be developing in other areas of the law. Specifically, this is intended to serve as a comparison of the lender liability cases with the bank liability cases arising out of the depository and credit disclosure transactions previously discussed.

148. As to bank liability to non-customers, see, e.g., Campbell, 781 F.2d 440; Maley, 361 F.2d 393; Djowharzadeh, 646 P.2d 616; Robertson, 549 S.W.2d 597. Lender liability to customers has already been discussed in the context of the “course of conduct” cases. See, e.g., Vogel, 71 P.2d 708.


As noted throughout this article, many of the cases suggest that the courts are relying on the unique status\(^{151}\) of banking institutions to impose special duties and obligations on the financial industry. Although typically these duties and obligations are limited to banking institutions, and relate in some way to an expanded notion of the bank-customer relationship, the exact basis of the decisions is not always clear.\(^{152}\) As has been noted, considerations such as course of conduct,\(^{153}\) fiduciary duty,\(^{154}\) good faith and fair dealing\(^{155}\) have been cited as the reasons for bank liability. Yet, none of these theories explains the wide range of bank liability cases with vaguely similar characteristics, and none provides any specific basis for consistent guidance as to how banks should behave in a given situation.

The possible exception is the theory of reliance. In virtually all of the successful bank liability cases considered so far, some element of customer reliance seems to be significant even though the court frequently focuses its attention elsewhere or merely generalizes. True, the reliance is typically associated with, or a result of, the unique status of banking institutions.\(^{156}\) But, the distinguishing feature of the successful bank-liability cases seems to be the detrimental reliance that was induced by the bank’s behavior.\(^{157}\) For example, in Djowharzadeh,\(^{158}\) it was the loan applicant’s reliance on the bank’s implied duty to keep the application information confidential that formed the basis for the decision and in turn it was the bank’s status in the community which induced this reliance. In Robertson,\(^{159}\) the key factor was the plaintiff’s reliance on the apparent authority of the defendant to represent the bank. Shaw\(^{160}\) and Commercial Cotton\(^{161}\) may appear to

151. See, e.g., Flick & Replansky, supra note 4.
152. See Justice Opala’s separate opinion in Shaw, 640 P.2d at 957.
153. See, e.g., Riviera, 768 F.2d 1201.
154. See, e.g., Merrill Lynch, 774 F.2d 999.
155. See, e.g., Commercial Cotton, 163 Cal. App. 3d 511, 209 Cal. Rptr. 551; Palmer, 100 Idaho 642, 603 P.2d 597; see also supra text accompanying note 114.
156. See, e.g., Perdue, 38 Cal. 3d 913, 702 P.2d 503, 216 Cal. Rptr. 345; Djowharzadeh, 646 P.2d 616.
157. See Flick & Replansky, supra note 4.
158. 646 P.2d 616.
159. 549 S.W.2d 547.
160. 640 P.2d 953.
be ordinary cases of liability for breach of depository obligations pursuant to U.C.C. Article 4. Yet, in both cases the courts emphasized the right of the customer to rely on the forthrightness of the bank in dealing with its customers; for example, the courts suggested that a bank's overwhelmingly superior status in the community induces customer reliance on the good faith of the bank and obligates the bank to avoid arbitrary abuse of this position.\textsuperscript{162}

The \textit{Riviera}\textsuperscript{163} case also illustrates the reliance point. That case, apparently decided contrary to the provisions of the U.C.C.\textsuperscript{164} and otherwise without extensive authoritative support,\textsuperscript{165} was based solely on the theory that the public at large relies on bank cashier's checks as being essentially the same as cash,\textsuperscript{166} that is, not subject to bank defenses. While the court's statement that "scrutiny in the law is irrelevant"\textsuperscript{167} may strike some as extraordinary coming from a United States Court of Appeals, it makes clear that the public's reliance on the "aura" of bank cashier's checks was deemed to supercede the otherwise applicable law. Essentially the same can be said for \textit{Tonelli},\textsuperscript{168} where the bank's issuance of a cashier's check in return for an unendorsed certified check payable to the same payee was viewed as the determinative factor, allowing the holder to perpetrate a subsequent fraud.

Admittedly, not all of the cases are so easy to categorize. For example, \textit{Reynolds-Wilson}\textsuperscript{169} may represent nothing beyond a mere liberal imposition of U.C.C. rules on demand

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\item[163.] 768 F.2d 1201.
\item[164.] See U.C.C. §§ 3-302 & 3-306.
\item[165.] 768 F.2d at 1204.
\item[166.] "In commercial circles, cashier's checks have the aura of cash." 768 F.2d at 1204 citing 10 AM. JUR. 2d Banks § 544 (1965); Lawrence, \textit{Making Cashier's Checks and Other Bank Checks Cost-Effective: A Plea for Revision of Articles 3 and 4 of the Uniform Commercial Code}, 64 MINN. L. REV. 275 (1980). Also: "Whether that aura bears scrutiny in the law is irrelevant here. It is important only that there is a universal commercial reverence for cashier's checks . . ." 768 F.2d at 1204.
\item[167.] 768 F.2d at 1204.
\item[169.] 699 P.2d 146.
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\end{footnotesize}
items payable by payor banks; and Perdue,\textsuperscript{170} while resting on the bank's duty of "good faith and fair dealing,"\textsuperscript{171} may be only a dispute over the reasonableness of a six dollar returned check charge. Yet Perdue, like Commercial Cotton, depends at least inferentially on the theory that this duty of good faith and fair dealing arises because the bank's status induces customer reliance on the reasonableness of bank decisions. Jackson\textsuperscript{172} falls into the same category.

The credit reporting cases fit even more easily into this mold. Maley,\textsuperscript{173} General Motors Acceptance,\textsuperscript{174} and Central States Stamping\textsuperscript{175} are all cases where creditor reliance led to liability for a bank disclosing credit information. Similarly, the "watchdog" cases, where a bank has been made liable for failure to monitor the activities of its customer and to protect the public from those activities,\textsuperscript{176} are founded on the public's need to rely on the good faith and fair dealing of banks. Finally, the "course of conduct" cases are the clearest example of all, based as they are on one party's reliance on the past conduct of a bank.\textsuperscript{177}

But how do these cases compare with the most famous "lender liability" cases?\textsuperscript{178} Are the lender liability cases another facet of this reliance-based theory of the bank-customer relationship? Consider some examples. Perhaps the best known of the lender liability cases is State National Bank v. Farah Manufacturing Co.\textsuperscript{179} This case could be loosely described as one involving creditor control of the debtor, inasmuch as the lenders blocked Mr. Farah's election as president and Chief Executive Officer of Farah Manufacturing (as well as two directors friendly to Farah), and subsequently engineered the election of a lender's employee as chairman of the

\textsuperscript{170} 38 Cal. 3d 913, 702 P.2d 503, 216 Cal. Rptr. 345.
\textsuperscript{171}  Id. at 923, 702 P.2d at 510, 216 Cal. Rptr. at 352.
\textsuperscript{172} 55 Tenn. App. 545, 403 S.W.2d 109.
\textsuperscript{173} 361 F.2d 393.
\textsuperscript{174} 773 F.2d 771.
\textsuperscript{175} 727 F.2d 1405.
\textsuperscript{176} Supra notes 91-106 and accompanying text.
\textsuperscript{177} See, e.g., Metge, 762 F.2d 621; Richfield, 244 N.W.2d 648; Klein, 293 Minn. 418, 196 N.W.2d 619.
\textsuperscript{178} See, e.g., Merrill Lynch, 774 F.2d 909; see also, Vogel, 711 P.2d 708; National Livestock, 653 P.2d 1243.
\textsuperscript{179} 678 S.W.2d 661 (Tex. Ct. App. 1984).
board. The lenders also requested that a specific consultant be hired, objected to Mr. Farah’s serving as a consultant, suggested an auction of company assets, named the auction company to be used and financed the auction purchase of Farah assets by a competitor.\textsuperscript{180} Farah Manufacturing suffered under the tutelage of the banks, but later Mr. Farah regained control and led the company to an economic turnaround.\textsuperscript{181} He then sued the banks on various theories involving fraud, duress and interference with corporate government. He was awarded damages of approximately $19 million.\textsuperscript{182}

\textit{Farah} clearly involves issues of excessive creditor control, and as such could be viewed as an example of liability to a bank customer who relied on the banks’ duties of good faith and fair dealing, but the case goes much further than that. The means by which the creditor influenced Farah’s board of directors was through a provision in the loan agreement allowing the creditor banks to accelerate the loan in the event of any management change deemed adverse by the lenders. The apparent basis for the decision was not the existence or even the exercise of this clause, but rather the untruthful threat that the clause would be exercised if Mr. Farah was elected. In effect, the lender’s crucial failing was the unfounded threat that the loan would be “called” upon Farah’s election, when in reality no such decision had been made. The result was that the Farah board was induced to rely on a factual representation by the banks which was clearly and knowingly incorrect. In this respect, the \textit{Farah} case resembles the credit disclosure cases where parties were induced to rely to their detriment on incorrect representations by the bank.\textsuperscript{183}

Other lender liability cases also fit this pattern. In \textit{K.M.C. Co. v. Irving Trust Co.},\textsuperscript{184} $7.5 million in damages were awarded due to the bank’s failure to advance funds under a discretionary credit agreement. The decision was based on the bank’s breach of the implied covenants of good faith and fair

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\item \textsuperscript{180} \textit{Id.} at 667-68.
\item \textsuperscript{181} \textit{Id.} at 668.
\item \textsuperscript{182} \textit{Id.} at 699.
\item \textsuperscript{183} \textit{See, e.g., General Motors Acceptance, 773 F.2d 771; Central States Stamping, 727 F.2d 1405.}
\item \textsuperscript{184} 757 F.2d 752 (6th Cir. 1985).
\end{itemize}
\end{footnotesize}
dealing, relied upon by the debtor to its detriment. In *Pecos Construction Co. v. Mortgage Investment Co.*,¹⁸⁵ the lender made last minute demands inconsistent with a previous loan commitment made by the lender and relied on by the borrower. In *re American Lumber Company*,¹⁸⁶ a case ostensibly involving equitable subordination in bankruptcy due to improper creditor control, emphasized that unsecured creditors had relied on the bank’s representations that the debtor would not go into bankruptcy.

This is not to say that all lender liability cases are based, purely or even largely, on reliance; clearly there are significant lender liability cases that rest essentially on agency or other “control” theories, without reliance constituting a significant factor.¹⁸⁷ No one should suggest that reliance is a central or even relevant factor in all lender liability cases, but it seems to be the central factor in many of those cases involving the bank-customer relationship and the related issues of good faith and fair dealing. This is often the case regardless of which side prevails in the case. For example, in *Oregon Bank v. Nautilus Crane & Equipment Corp.*,¹⁸⁸ the bank was accused of manipulating the debtor by having a receiver appointed. The court agreed with the bank, that the bank did not seek a role in corporate governance and had a legal right to seek appointment of a receiver. The bank had done nothing to induce detrimental reliance on the part of the debtor.

Cases involving course of conduct have already been discussed in the context of both lending and depository transactions.¹⁸⁹ A number of lender liability cases also involve course

¹⁸⁶. 7 Bankr. 519 (Bankr. D. Minn. 1979).
¹⁸⁷. See, e.g., *Krivu Indus. Supply v. National Distillers and Chem. Corp.*, 483 F.2d 1098 (5th Cir. 1973), modified, 490 F.2d 916 (1974); A. Gay. *Jenson Farms Co. v. Cargill, Inc.*, 309 N.W.2d 285 (Minn. 1981); *Credit Managers Ass’n of So. Cal. v. Superior Court*, 51 Cal. App. 3d 352, 124 Cal. Rptr. 242 (1975); *Connor v. Great Western Sav. & Loan Ass’n*, 69 Cal.2d 850, 447 P.2d 609, 73 Cal. Rptr. 369 (1968). In cases such as these, the creditor typically has assumed such direct control over the debtor’s activities that for all purposes relating to third parties the creditor becomes the debtor, and hence becomes liable under a theory of agency or fiduciary duty as any officer or director of the debtor would be liable.
¹⁸⁹. See, e.g., *Merrill Lynch*, 774 F.2d 909; *Vogel*, 711 P.2d 708.
of conduct theories, typically relating to an unexpected acceleration of debt or a bank's refusal to continue a discretionary credit line.\textsuperscript{190} In \textit{Centerre Bank v. Distributors, Inc.},\textsuperscript{191} the borrower unsuccessfully claimed that the bank violated its duty of good faith in demanding payment of a note. The court rejected the debtor's argument that the bank's right to demand payment was conditioned on a duty of good faith, distinguishing \textit{Skeels v. Universal C.I.T. Credit Corp.}\textsuperscript{192} and \textit{K.M.C.},\textsuperscript{193} on grounds that in those cases the banks withdrew credit "suddenly and without notice." The clear implication is that in these cases one deciding factor was whether the bank had done anything to induce the customer to rely on continuing credit availability from the bank. Similar conclusions result from comparison of the cases involving creditor tolerance of late payments\textsuperscript{194} and other cases involving enforcement of security interests.\textsuperscript{195}

\textbf{Summary and Conclusion}

These concepts are not necessarily limited to bank liability cases\textsuperscript{196} and are not necessarily a new development.\textsuperscript{197}

\textsuperscript{190} See, \textit{e.g.}, \textit{K.M.C.}, 757 F.2d 752.
\textsuperscript{191} 705 S.W.2d 42 (Mo. Ct. App. 1985).
\textsuperscript{192} 335 F.2d 846 (3d Cir. 1964).
\textsuperscript{193} 757 F.2d 752.
\textsuperscript{194} Compare, \textit{Postal Sav.}, 10 Kan. App. 2d 286, 698 P.2d 382, with \textit{Alaska Statebank v. Fairco}, 674 P.2d 288 (Alaska 1983). In \textit{Alaska Statebank} the creditor formally extended the due date of late payments, establishing a course of dealing relied on by the debtor. In contrast, \textit{Postal Sav.} had a specific written anti-waiver clause which precluded customer reliance.
\textsuperscript{195} Compare \textit{National Livestock}, 653 P.2d 1243, with Van Bibber v. Norris, 419 N.E.2d 115 (Ind. 1981). \textit{National Livestock} was viewed as having consented to sales of collateral by a course of conduct permitting such sales, while in \textit{Van Bibber} a specific, written anti-waiver clause precluded reliance on the bank's past practice of accepting late payments as protection against enforcement of security interest.
\textsuperscript{196} See, \textit{e.g.}, \textit{Reserve Oil, Inc. v. Dixon}, 711 F.2d 951, 953 (10th Cir. 1983), holding that the relationship between the oil and gas operator and the non-operator interest owners creates a "trustee type relationship imposing a duty of fair dealing" between the parties; see also Note, \textit{Reserve Oil v. Dixon: Giving Unexpected Meaning to Trust Law in a Contractual Relationship and its Impact upon Bankruptcy}, 11 \textit{Okla. City U.L. Rev.} 437 (1986).
\textsuperscript{197} See, \textit{e.g.}, \textit{Continental Supply Co. v. Marshall}, 152 F.2d 300 (10th Cir. 1945), where a senior mortgagee, with notice of the claim of a subordinate mortgagee to the same collateral, had collected proceeds from the collateral and distributed them to the debtor.
However, the dramatic increase in the number of recent bank liability cases, with continual emphasis on the unique nature of the bank-customer relationship, suggests that something special is happening and that banks are at the center of the storm. A large number of the cases dwell on the special duty of banks (because of their unique position in society) to deal with customers, creditors and even the public at large in a way that is always evenhanded and above reproach.

While this special duty may be stated in terms of a “special relationship,” “good faith and fair dealing,” a “quasi-fiduciary” obligation, a “course of dealing,” “creditor control” or simple fraud and misrepresentation, two things are clear. First, the traditional common law theories of liability suggested by use of the foregoing terminology are not sufficient to explain the phenomenon currently sweeping the law in the area of bank liability. Second, vague generalities about “quasi-fiduciary duty” or “good faith and fair dealing” or the unique “status” of banks are equally inadequate as either an explanation or a description of these recent developments. While the apparent revolution in bank liability cases may be too new to permit accurate formulation of a descriptive central theory, it is clear that the direction of the trend needs to be clarified so that banks and bank lawyers will have some guidance as to the new duties and liabilities. Hopefully, as the case law evolves the courts will elaborate more thoroughly on the legal principles that underlie the bank liability decisions. In the meantime, an analysis of existing cases suggests that some guideposts may be helpful to bankers and bank counsels in navigating through this maze.

As noted, the liability often focuses on the unique nature of the bank-customer relationship. But, it derives not from the legal nature of the relationship itself, but rather from the

The court concluded that:
the Bank as senior mortgagee is accountable to Continental as junior mort-
gagee, for the application of all proceeds derived from the mortgaged secur-
ity coming into its possession and control, to the satisfaction of its prior
mortgage indebtedness, and failure to do so renders its lien junior to that of
Continental to the extent of the applicable proceeds which came into its
possession and control, and which were not applied to the satisfaction of its
mortgage indebtedness

Id. at 307.
impact of the bank's status within the relationship. It is the bank's superior stature within the community and in relation to its customers which is perceived as creating an aura of expertise and reliability that is greater than that of the ordinary commercial enterprise. Like doctors and lawyers, bankers traditionally enjoy prestige in the community and a deference to their judgment in the area of their specialty (finance, in the case of banks) which induces ordinary persons to rely on that judgment in matters relating to that specialty. In essence, banks have a perceived level of expertise somewhat akin to that of the traditional professions. Like the traditional professions, this tends to induce reliance on that expertise. Whether it is the result of the federalized bank regulatory system, or bank public relations campaigns, or sheer financial size and power or whether or not it is deserved is largely irrelevant. If this perception exists and is recognized by the courts, it can become the basis for new developments in commercial law.

In conclusion, the tried and true concept of detrimental reliance may be the mechanism by which this new development is given direction and effect. That is, the bank-customer relationship may have evolved in such a way that the courts are receptive to the argument that the societal perception of the bank's role in society induces customers and others to rely on the unique expertise and trustworthiness of banking institutions. The result can be liability for banks in a variety of non-traditional ways, nearly always involving some justifiable and detrimental reliance by a member of the public on something the bank has done.

It may be, as some have suggested, that the emerging theories of bank liability are not new or novel, but are merely the result of a new willingness by borrowers to sue their banks. Surely, this is a part of what these cases mean. But, it is possible that they represent something more far reaching than merely increased borrower litigiousness. It is possible that these cases may be the introduction to a new stage in the evolution of the bank-customer relationship, a stage that will

198. Flick & Replansky, supra note 4, at 258.
elevate bank responsibility to the level of a quasi-professionalism,\textsuperscript{199} based on a new application of the legal theory of detrimental reliance. Whatever the outcome, the results could have far reaching impact on bank operations, and it will be incumbent on bankers and bank counsels to closely monitor these developments as they continue to unfold.