Articles

NOW YOU HAVE IT, NOW YOU DON'T: THE DEPOSITARY BANK'S RIGHTS OF CHARGE-BACK AND SET-OFF

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The purpose of this Article is to examine the right of a depositary bank to charge back a customer's account when an item deposited for collection is returned to the depositary bank unpaid.[1] Little scholarly attention has been paid to the problems that are generated by a bank's statutory charge-back right,[2] despite its difficulty and the lack of agreement in the courts regarding its treatment.[3] Through a series of hypothetical cases,[4] this Article will probe the nature of the charge-back right and its interpretation in the courts. Further, the Article will demonstrate how the courts have often misunderstood and misapplied the charge-back provision, permitting banks to exercise their right of charge-back in inappropriate circumstances. Finally, it will examine the depositary bank's right to set off the funds in a customer's account in related circumstances.

I. THE RIGHT OF CHARGE-BACK

A. *Introductory Issues*

Section 4-212(1) of the Uniform Commercial Code (Code) describes the basic right of a collecting bank to charge back an item deposited for collec-

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1. The right to "charge back" is merely the right of a bank to deduct from a customer's balance the amount of an instrument which the customer has deposited to his account and which has been returned unpaid.

2. While there is some discussion of the problems associated with the charge-back right in various commercial code treatises, *see, e.g.*, A. BAILEY, BRADY ON BANK CHECKS ¶ 21.4 (6th ed. 1986); B. CLARK, THE LAW OF BANK DEPOSITS, COLLECTIONS, AND CREDIT CARDS ¶ 4.8 (Rev. ed. 1981), there has been no comprehensive treatment of the provision.

3. *See infra* text accompanying notes 27-116.

4. Some of the hypotheticals are simplified versions of actual cases.

tion by a customer. In essence, the Code provides that if a bank has given a customer credit for an item which the customer deposited in his account for collection, the bank can revoke that credit and deduct the amount of the credit from the customer's account balance.[5] If there are insufficient funds in the account to cover the item, the bank is entitled to a refund of the deficiency from the customer. In order to exercise this right, the bank must meet certain timeliness requirements.

Example 1. Dan Drawer draws a check payable to Pam Payee on his account at Payor Bank. Pam deposits the check in her account at First Bank. First Bank forwards the check to Payor who refuses to pay the check because of insufficient funds in Dan's account. The day after First Bank learns the check has been dishonored, it sends notice to Pam that it is revoking the provisional credit to her account represented by the check.

This is a simple example of section 4-212 in operation. Upon receiving the check for deposit, First Bank gives Pam a provisional credit to her account in the amount of the check prior to forwarding it to Payor for payment. When Payor Bank dishonors the check, First Bank reverses this provisional credit by giving notice to its customer within the period prescribed in section 4-212.

Example 2. Same facts as above, except that Pam is permitted to withdraw all or a portion of the check's proceeds prior to the time that First Bank is notified of the check's dishonor.

This example, along with some slight variations, results in a number of complications, some difficult and some easily resolved. The mere fact that First Bank permitted all or a portion of the funds represented by the check to be withdrawn prior to collection does not, in itself, defeat the right of the bank to charge back the customer's account.[6] Section 4-212 expressly permits a collecting bank to obtain a *refund* as well as charging back a credit. Despite the fact that it has allowed a withdrawal against the check,[7] the

5. The somewhat cumbersome language of the statute provides:

> If a collecting bank has made provisional settlement with its customer for an item and itself fails by reason of dishonor, suspension of payments by a bank or otherwise to receive a settlement for the item which is or becomes final, the bank may revoke the settlement given by it, charge back the amount of any credit given for the item to its customer's account or obtain refund from its customer whether or not it is able to return the items if by its midnight deadline or within a longer reasonable time after it learns the facts it returns the item or sends notification of the facts. These rights to revoke, charge back and obtain refund terminate if and when a settlement for the item received by the bank is or becomes final (subsection (3) of section 4-211 and subsections (2) and (3) of section 4-213).

U.C.C. § 4-212(1) (1977).

6. Brannon v. First Nat'l Bank of Atlanta, 137 Ga. App. 275, 223 S.E.2d 473, 19 U.C.C. Rep. Serv. 234 (1976); Lamson v. Commmercial Credit Corp., 187 Colo. 382, 53 P.2d 966, 16 U.C.C. Rep. Serv. 756 (1975); Isaacs v. Chartered New Eng. Corp., 378 F. Supp. 370, 14 U.C.C. Rep. Serv. 1191 (S.D.N.Y. 1974).

7. Whether the withdrawal is determined to be drawn from the proceeds of the check, or from other funds in the customer's account, depends upon a number of factors. It may, for example, depend upon the wording of the customer's deposit slip, or upon the Code's "first in, first out" (FIFO) principle articulated in section 4-208(2). It will not matter in cases where there are already sufficient funds in the account to cover the dishonored check, since the bank is entitled to recover its "refund" by setting off the debt against any funds in the depositor's account. Thus, as a practical matter, it makes no difference in most cases whether the bank is merely charging back a provisional credit for the entire amount of the check, while allowing the customer to retain the funds withdrawn

bank remains a collecting bank and is therefore a beneficiary of the right of charge-back under section 4-212.[8]

A variation on the above example introduces further complications. What if the customer takes the check to her bank and "cashes" it? The customer completes no deposit slip; she merely indorses the check, and, after checking her account to determine whether there are sufficient funds to cover the check, the bank gives her the amount of the check in return. Can the customer argue that the depositary bank is no longer a "collecting bank," but is the owner of the item, and, therefore, has lost its charge-back rights under section 4-212?[9]

Section 4-201(1) would seem to address this situation. The last sentence of this section states that "[w]hen an item is handled by banks for purposes of presentment, payment and collection, the relevant provisions of this Article apply even though action of the parties clearly establishes that a particular bank has purchased the item and is the owner of it."[10] This language seems to indicate that the bank would not lose its charge-back right even if it could be established that it was the "owner" of the item. Unfortunately, this conclusion results from a superficial reading of the statute and is probably wrong. The first sentence of section 4-201(1) states that "[u]nless a contrary intent clearly appears . . . the bank is an agent or sub-agent of the owner of the item and any settlement given for the item is provisional."[11] Thus, by "clearly indicating to the contrary" the parties can create a relationship in which the bank is not only the owner of an item, but in which the credit given by the bank is not provisional. In such a case one can argue that since section 4-212 applies only to *provisional* credits, the bank has no charge-back rights. In fact, in the variation of Example 2, in which the bank "cashes" the check, no "credit" has been given for the check, and therefore, section 4-212 is not applicable.

Similarly, the last sentence of section 4-201(1) applies only when "an item is handled by banks for purposes of presentment, payment, and collection."[12] It can be argued that since there were no indicia of a deposit to the customer's account, the bank was not acting for collection purposes. Consequently, while the bank may have rights against its customer on her indorsement contract, it has no right of charge-back under section 4-212. While this may not matter in the majority of cases, there are some circumstances where it may matter greatly.[13]

(on the basis that they represented other funds), or whether the bank is obtaining a "refund" of the amount it allowed to be withdrawn against the check by setting off the customer's account.

8. This is due to the provisions of section 4-201(1). This section provides that "[u]nless a contrary intent clearly appears" any settlement given by a collecting bank prior to final payment is provisional "even though credit given for the item is subject to immediate withdrawal as of right or is in fact withdrawn." U.C.C. § 4-201(1) (1977).

9. Of course, the bank would still have rights on the indorsement contract and for breach of warranty in any event.

10. U.C.C. § 4-201(1) (1977).

11. *Id.*

12. *Id.*

13. While both the section 4-212 charge-back right and the right to recover on an indorsement contract are subject to "midnight deadlines," the midnight deadline limitations are not identical. Section 4-212(1) permits a depositary bank to charge back the customer's account if the bank pro-

The final, and perhaps most problematic, case under Example 2 involves a situation where a portion of the amount of the check is paid to the customer over the counter, and a portion is deposited to the customer's account. This transaction can be viewed from a number of different perspectives. First, it can be seen as a deposit of the entire item, and an immediate withdrawal of a portion of the credit. In this case, if the check were returned unpaid, there would be a right to charge back the entire amount of the check. The transaction can also be interpreted, however, as a purchase of the item by the bank and a deposit of a portion of the proceeds in the customer's account. In this case, if the above analysis is correct, the right of charge-back would not be available to the bank.[14] Finally, it can be interpreted as a "split" transaction, in which a portion of the item is deposited for collection and a portion is paid in cash. Presumably, in this case, only the portion deposited would be subject to the charge-back right.

The case law provides very little assistance on this issue. The only reasonably analogous case is *Kirby v. First & Merchants National Bank.*[15] In *Kirby*, the payee presented a check at the drawee bank, which was also the payee's bank. A portion of the amount represented by the check was deposited in the payee's account and a portion was given to the payee in cash. The check was drawn on insufficient funds and was dishonored. The bank charged back the account of the payee, which created an overdraft, and attempted to recover the overdraft in a suit. Because the deposit slip listed the deposit as "currency" rather than "checks," the court held that the bank had paid the check and that final payment could not be reversed.[16]

Because the same bank was both the drawee and the depositary bank in *Kirby*, the case is not directly on point. The finality of payment by a payor has a long history dating from the case of *Price v. Neal,*[17] and the hypothetical under consideration does not involve final payment by a payor. Nonetheless, the court's treatment of the deposit is instructive. If, because of the nature of the deposit slip or otherwise, the deposit in the example was treated as a purchase of the check and a deposit of currency, a strong argument could be made, as indicated above, that the right of charge-back would not exist because the depositary bank was not a collecting bank. While the

vides notice to the customer by its midnight deadline or within "a longer reasonable time." U.C.C. § 4-212(1) (1977). Thus, a bank need merely show that a delay was reasonable in order to avoid losing its charge-back rights. There is no similar language of reasonableness in sections 3-502 and 3-508, governing liability on an indorsement contract. Only by satisfying the impracticability standard of section 3-511 can the discharge of an indorser be avoided when the notice of dishonor is late. This section requires not only that the bank act reasonably, but that the cause of any delay be beyond its control. Courts have been reluctant to permit excuse under the provisions of section 3-511; in fact there are no reported cases where the claim ultimately succeeded. In Rich v. Franklin Sav. Bank of N.Y., 18 U.C.C. Rep. Serv. 451 (N.Y. Sup. Ct. 1975), the court did permit a claim of excuse to survive a motion for summary judgment, but the case apparently did not proceed further. In the analogous context of section 4-108, which provides for excuse from final payment under section 4-302, courts have often described the midnight deadline in terms of strict liability rather than reasonableness. *See, e.g,* Engine Parts, Inc. v. Citizens Bank of Clovis, 92 N.M. 37, 582 P.2d 809, 23 U.C.C. Rep. Serv. 1248 (1978); State and Sav. Bank of Monticello, Ind. v. Meeker, 469 N.E.2d 55, 39 U.C.C. Rep. Serv. 1391 (Ind. App. 1984).

14. *See supra* notes 9-13 and accompanying text.

15. 210 Va. 88, 168 S.E.2d 273, 6 U.C.C. Rep. Serv. 694 (1969).

16. *Kirby,* 210 Va. at 90, 168 S.E.2d at 275, 6 U.C.C. Rep. Serv. at 697.

17. 3 Burr. 1354, 97 Eng. Rep. 871 (1762).

result in *Kirby* is questionable, and has been the object of some scholarly criticism,[18] it remains the only case providing guidance on the issue.

Example 3. Same facts as Example 1, except that the depositary bank notifies Pam by telephone rather than sending written notice.

Despite the fact that section 4-212 requires that a depositary bank *send* notice of dishonor, most cases have held that oral notice, so long as it is timely provided, will suffice under section 4-212,[19] though this result is by no means uniform. Because "send" is defined in the Code to mean "in connection with any writing or notice . . . to deposit in the mail or deliver for transmission by any other usual means . . ."[20] it can be argued that oral notice cannot suffice for a bank to exercise its charge-back rights. While section 3-508 permits oral notice of dishonor, section 4-102 provides that whenever Articles 3 and 4 conflict, Article 4 shall prevail. This line of reasoning convinced the court in *Valley Bank & Trust Co. v. First Security Bank of Utah, N.A.*[21] to preclude a depositary bank from charging back its customer's account when it provided only verbal notice of dishonor.

Others have relied upon section 4-104(3) to reach a different result.[22] This section indicates that the definition of "notice of dishonor" for purposes of Article 4 is provided by section 3-508.[23] Since section 3-508 permits notice of dishonor to be given orally, oral notice should suffice for purposes of section 4-212.[24] Furthermore, although it has not been explicitly recognized in most of the cases, the charge-back right under section 4-212 and the liability of the customer as an *indorser* are independent bases upon which the customer may be liable for a dishonored check.[25] Even if the right of charge-back is lost because notice was oral, in most cases it will not matter because indorsement liability will remain. Only where indorsement liability has otherwise been lost will the issue become important.

B. *The Timing of the Notice*

Example 4. Same facts as Example 1, except that the notice to the customer is not provided within the bank's midnight deadline.

Both the language of section 4-212 and the official comments thereto seem to provide a simple resolution to this problem: the depositary bank loses its right of charge-back unless the delay in notification was reason-

18. *See, e.g.*, B. CLARK, *supra* note 2, at ¶5.3(4).

19. *See, e.g.*, Yoder v. Cromwell State Bank, 478 N.E.2d 131, 41 U.C.C. Rep. Serv. 173 (Ind. App. 1985); Salem Nat'l Bank v. Chapman, 64 Ill. App. 3d 625, 381 N.E.2d 741, 25 U.C.C. Rep. Serv. 234 (1978). *But see* Valley Bank & Trust Co. v. First Sec. Bank of Utah, 538 P.2d 298, 17 U.C.C. Rep. Serv. 480 (Utah 1975).

20. U.C.C. § 1-201(38) (1977).

21. 538 P.2d 298, 17 U.C.C. Rep. Serv. 480 (Utah 1975).

22. *See, e.g.*, Sun River Cattle Co. v. Miners' Bank of Mont., N.A., 164 Mont. 479, 525 P.2d 19 (1974); B. CLARK, *supra* note 2, ¶ 4.6[2], at 4-46.

23. U.C.C. § 4-104(3) (1977).

24. This argument is not completely persuasive. While section 4-104(3) refers to section 3-508 for the *definition* of notice of dishonor, arguably the portion of section 3-508 allowing oral notice of dishonor is not part of the definition of the term. On the other hand, there is not much, if anything, in section 3-508 which *can* be called a definition. U.C.C. § 3-508 (1977).

25. U.C.C. § 4-212(5) (1977).

able.[26] Section 4-212 of the Code states that a collecting bank can charge back the amount of an unpaid item *"if by its midnight deadline or within a longer reasonable time* after it learns of the facts it returns the item or sends notification of the facts."[27] The use of the language "if" strongly indicates that the availability of the charge-back right is dependent upon prompt notification. The language is not merely precatory, nor does it only make the collecting bank liable for damages caused by late notification. Rather, it seems to make the charge-back right *contingent* upon prompt notification. Official comment 3 to section 4-212 confirms this interpretation. It states that the right of charge-back or refund "must" be exercised promptly after the bank learns of the facts.[28] Moreover, the "right [of charge-back] exists (*if so promptly exercised*) whether or not the bank is able to return the item."[29] The italicized language, while parenthetical, clearly makes the right of charge-back contingent upon its prompt exercise.

The history of the provision supports this interpretation. The bank's charge-back right went through numerous drafts before attaining its present form.[30] In only one of these drafts was language limiting the time to exercise the set-off right omitted.[31] This draft prompted very sharp criticism from the Reporter for the Bank Deposits sections, Fairfax Leary. Leary stated that at some point the charge-back right should expire automatically, and the depositary bank should be relegated to actions that it might have on the

26. U.C.C. § 4-212 (1977).
27. U.C.C. § 4-212(1) (1977)(emphasis added).
28. U.C.C. § 4-212, official comment 3 (1977).
29. *Id.* (emphasis added).
30. The collected papers of Karl Llewellyn disclose at least seven different drafts of the charge-back section. The first draft was proposed in 1947. *See* F. Leary, Article IV, Chapter II, Bank Collections 12 (Jan. 1947)(unpublished manuscript in Llewellyn Papers, available at University of Chicago and on microfilm) [hereinafter Llewellyn Papers] (proposed UCC charge-back provision was "§ 10. Reversal of Credit Given for Cash Item"); F. Leary, Notes and Comments to Article IV, Chapter II, Bank Collections 19 (Jan. 1947), Llewellyn Papers, *supra* (commentary on purposes of proposed § 10).

The charge-back provisions next appeared as § 711 in 1948. *See* Minutes of A.L.I. Meeting 13 (May 20-22, 1948), Llewellyn Papers, *supra*. In 1949, the proposed charge-back provision was § 3-617. *See* F. Leary, Proposed Revision for Submission to Nat'l Conf. of Comm'rs on Uniform State Laws at the 1949 Session in St. Louis 5 (1949), Llewellyn Papers, *supra* (§ 3-617, "Right of Charge-Back or Refund," was included in U.C.C., Part 6 of Article 3); Nat'l Conf. of Comm'rs on Uniform State Laws of A.L.I., Proc. in Comm. of the Whole 141 (Sept. 2-3, 1949), Llewellyn Papers, *supra* (Leary defending § 3-617).

By October 1949, the charge-back provision had been revised again and renumbered § 3-619. *See* A.L.I. Nat'l Conf. of Comm'rs on Uniform State Laws, Uniform Commercial Code: October 1949 Revisions of Section 1-105, Bank Collections Part of Article 3, Section 6-303 and Articles on Secured Transactions and Bulk Transfers 31-33 (Oct. 1949), Llewellyn Papers, *supra* (text and comments, first use of the term "midnight deadline").

In 1950, the charge-back section was § 4-207. *See* A.L.I. Nat'l Conf. of Comm'rs on Uniform State Laws, Uniform Commercial Code Proposed Final Draft Text Edition and Comments 468-70 (Spring 1950), Llewellyn Papers, *supra*. In the September 1950 draft, charge-back appeared in § 4-213. *See* A.L.I. Nat'l Conf. of Comm'rs on Uniform State Laws, Uniform Commercial Code: September 1950 Revisions of Article 2, Article 4, Article 9, at 21-22 (Sept. 1950).

The charge-back provision first appeared in its present form as § 4-212 in 1951. *See* A.L.I. Nat'l Conf. of Comm'rs on Uniform State Laws, Uniform Commercial Code: Final Text Edition 150-51 (Nov. 1951), Llewellyn Papers, *supra*.

31. This was proposed in section 3-617, brought forward at a meeting of the American Law Institute in St. Louis in 1949. *See* F. Leary, Proposed Revision for Submission to Nat'l Conf. of Comm'rs on Uniform State Laws at the 1949 Session in St. Louis, Llewellyn Papers, *supra* note 30, at 5.

indorsement contract, for breach of warranty, or for foreclosure of its banker's lien.[32] The time limitation was promptly reinserted in the next draft,[33] where it has remained until the present. In every draft in which a time limitation on the right to charge-back appears, it is phrased in conditional language similar to the present provision.[34] There is no indication in this history that the consequence of missing the deadline for providing notice was to be limited to damages for negligence.

During the study of the Code by the New York State Law Revision Commission, a lengthy analysis of Article 4 was done. This analysis indicates that section 4-212 was meant to preclude charge-back unless notice was timely provided.[35] Further, the comments of the witnesses made during

32. *See* Nat'l Conf. of Comm'rs on Uniform State Laws of A.L.I., Proc. in Comm. of the Whole, Llewellyn Papers, *supra* note 30, at 141-42. Leary did not, however, feel that the bank would be without remedies in a case where it failed to give timely notice of the charge-back. His primary concern was that the depositor be given prior notice once the charge-back right expired, and before the bank was allowed to collect the funds from the depositor. *See id.* at 141. Professor Leary did not appear to consider that without the statutory right of charge-back, the bank would be hard-pressed to find a substantive basis for recovery. The three grounds suggested by him—indorsement contract, warranty, and foreclosure of a banker's lien—are all problematic. In the typical case where the payor refuses payment because there are insufficient funds in the drawer's account nor because the drawer stopped payment, there would be no breach of warranty. *See* U.C.C. §§ 3-417, 4-207 (1977). Further, once the charge-back right had expired, the right to recover on the indorsement contract would also have elapsed, since both are premised on the same midnight deadline. *See* U.C.C. § 3-508(2) (1977). Finally, in order to foreclose on a banker's lien, there must be some underlying obligation owed by the depositor to the bank. If neither warranty, indorsement, nor the statutory right of charge-back is available to supply that obligation, it is hard to see where it would come from, except perhaps in restitution or quasi-contract. Unfortunately, Professor Leary does not discuss these difficulties in his comments contained in the various proceedings documented in the Llewellyn Papers, *supra* note 30.

33. *See* proposed § 3-619, which appeared in October 1949. A.L.I. Nat'l Conf. of Comm'rs on Uniform State Laws, Uniform Commercial Code: October 1949 Revisions of Section 1-105, Bank Collections Part of Article 3, Section 6-303 and Articles on Secured Transactions and Bulk Transfers, Llewellyn Papers, *supra* note 30, at 31-33.

34. *See, e.g.*, the 1947 draft of proposed section 10, permitting the bank to charge back "*if* notice of the debit is mailed to the depositor before the close of the business day next following the day on which the bank obtained knowledge of the facts," F. Leary, Article IV, Chapter II, Bank Collections, Llewellyn Papers, *supra* note 30, at 12 (emphasis added); proposed section 711 stating that "*to be effective*, such reversal must be made and notice given its transferor by midnight of the collecting bank's next banking day following receipt of the item or knowledge," Minutes of A.L.I. Meeting, Llewellyn Papers, *supra* note 30, at 133 (emphasis added); proposed section 3-619 permitting charge back "*if* [the bank] makes such charge-back or claims refund and returns the item or sends notice of the facts to its transferor within a reasonable time after it learns the facts," A.L.I. Nat'l Conf. of Comm'rs on Uniform State Laws, Uniform Commercial Code: October 1949 Revisions of Section 1-105, Bank Collections Part of Article 3, Section 6-303 and Articles on Secured Transactions and Bulk Transfers, Llewellyn Papers, *supra* note 30, at 31 (emphasis added).

35. *E.g.*, "[t]he right of charge-back exists irrespective of whether the collecting bank is able to return the item, *provided* the bank after it learns of the facts, returns the item or sends notification of the facts by its midnight deadline or within a longer reasonable time." 2 N.Y. L. Revision Comm'n Rep. 1363 (1955)(emphasis added).

> [T]he right of charge-back or refund exists whether or not the bank is able to return the item, *but only if* the bank either does return the item or sends notice of its failure to receive final payment by its midnight deadline or within a longer reasonable time after it learns the fact."

Id. (Emphasis added). Later, however, the commission concluded that a question exists as to whether the failure of the bank to observe the time limits fixed in section 4-212 and section 4-301 forfeits the right of charge-back or whether it is merely a factor of ordinary care, while recognizing that under the prior law the right to revoke a provisional settlement would be cut off by delay past the stated time limits. *Id.* at 1376. This author is unable to find any indication that the drafters intended to change prior law in this respect.

the hearings of the Law Revision Commission uniformly indicate an interpretation which would preclude charge-back in the event of untimely notice.[36] The *Conference Pamphlet* of the Commercial Code Committee of the National Conference of Commissioners on Uniform State Laws describes section 4-212 as giving a collecting bank the right of charge-back "if it acts within certain time limitations."[37]

1. *The Early Cases*

The early cases consistently concluded that a bank lost its right of charge-back if not timely exercised. For example, in *First Security Bank of Utah v. Ezra C. Lundahl, Inc.*,[38] the defendants deposited a check in the depositary bank. The payor dishonored the check, but the depositary bank failed to give notice until about two months later. When the depositary bank finally charged back the account, there were insufficient funds in the account to cover the check, and the depositary bank sued for the deficiency. In holding the depositary bank was not entitled to recover for the overdraft, the court stated:

> It is true that under the Uniform Commercial Code there is a presumption that a collecting bank acts as agent for its depositor. However, this presupposes that the bank acts in accordance with its duty imposed by law; and this requires presentation to the payor bank in the due course of business, and, if the check is dishonored, notice to its depositor "by its midnight deadline or within a longer reasonable time" under the circumstances. *If there is a substantial failure of the bank to perform this duty, it loses its right of charge-back.*[39]

A number of other early cases reach similar results and contain language indicating that timely notice acts as a condition precedent to the right of charge-back.[40]

Manufacturers Hanover Trust Co. v. Akpan[41] is probably the most cited case asserting that the right of charge-back is lost unless timely exercised. In *Akpan*, the drawer gave the defendant a $2500 check to deposit in the defendant's account. The payee was to give the drawer the cash proceeds of the check. The check was returned unpaid to the depositary bank on August

36. *See, e.g.*, the comments of J.M. McCloy. "The Code rule would eliminate the presumption that the credit is provisional and would place a time limit on the right of charge-back even though the proceeds have not been received and unconditional credit has not been given." 2 N.Y. L. Revision Comm'n Rep. 1319 (1954). *See also* Comments of Milbank, Tweed, Hope and Hadley, 1 N.Y. L. Revision Comm'n Rep. 304 (1954); comments of Robert H. Brome, 1 N.Y. L. Revision Comm'n Rep. 315 (1954).

37. Nat'l Conf. of Comm'rs on Uniform State Laws, *Conference Pamphlet* 37 (A copy of the *Conference Pamphlet* is on file with the author.).

38. 22 Utah 2d 433, 454 P.2d 886, 6 U.C.C. Rep. Serv. 765 (1969).

39. *Lundahl*, 22 Utah 2d at 435, 454 P.2d at 888, 6 U.C.C. Rep. Serv. at 767 (citations omitted)(emphasis added).

40. *See, e.g.*, North Carolina Nat'l Bank v. Harwell, 38 N.C. App. 190, 247 S.E.2d 720, 25 U.C.C. Rep. Serv. 225 (1978)(depositor will prevail over depositary bank unless the depositary bank gave notice of charge-back within its midnight deadline); Salem Nat'l Bank v. Chapman, 64 Ill. App. 3d 625, 381 N.E.2d 741, 25 U.C.C. Rep. Serv. 234 (1978). *Cf.* Dozier v. First Ala. Bank of Montgomery, 363 So. 2d 781, 25 U.C.C. Rep. Serv. 802 (Ala. Civ. App. 1978)(applying § 4-212(3) because depositary bank and payor bank were the same).

41. 91 Misc. 2d 622, 398 N.Y.S.2d 477, 22 U.C.C. Rep. Serv. 1009 (Civ. Ct. 1977).

19. On August 22, the defendant wrote a check for $2490 from her account and received cash for it which she gave to the drawer of the deposited check. On August 25, the bank gave the defendant notice that the check had been returned and charged back her account, creating an overdraft.

The court refused to permit the bank to recover on the overdraft because the charge-back was too late. The court stated that the remedy of charge-back was "conditioned" upon its timely exercise, and that since the notice was five days late, the bank could not charge back the customer's account. The court further rejected the bank's argument that it should recover on grounds of unjust enrichment or mistake. Since the customer had paid over funds to the drawer on the "implied representation" that the check had been paid, the customer had detrimentally relied on the failure to give notice and, therefore, could not be charged.[42]

2. *The Recent Trend*

Recently, however, the cases have retreated from the position that the depositary bank is accountable for a check which is returned dishonored unless it gives timely notice to its customer. The majority of the cases since 1983 permit the depositary bank to charge its customer for a check returned unpaid despite the fact that timely notice under section 4-212 was not provided to the customer. These decisions have a number of underlying theories, and their facts are often distinguishable from the earlier cases discussed above. Nonetheless, they represent a clear circumscription of the prior cases, and appear to perceive the charge-back right in a fundamentally different manner.

Appliance Buyers Credit Corp. v. Prospect National Bank of Peoria[43] is prominent among these cases. In *Appliance Buyers* the plaintiff deposited checks with the depositary bank for collection. Because of insufficient funds the checks were not paid, but the depositary bank did not notify the plaintiff within the time provided in section 4-212. The depositary bank nevertheless charged back the amount of the unpaid checks. The drawer had become insolvent, the checks were not collectible, and the plaintiff sued the depositary bank for the amount of the checks.

The court held that the depositary bank's failure to meet its midnight deadline did not mean that it was absolutely accountable for the item.[44] Rather, the customer must prove that actual damages resulted from the delay. The court reached this conclusion by placing great emphasis on the fact that section 4-212 does not use the word "accountable," which is used in the final payment rules of sections 4-302 and 4-213.[45] The cases have generally held that once a *payor* bank has failed to settle for an item by its midnight

42. It should be noted that the *Akpan* court cited no evidence to show that the customer had in fact assumed on August 22 that the check had been paid because she had received no notice of dishonor by that time. *Id. See also* Lufthansa Ger. Airlines v. Bank of Am. Nat'l Trust Sav. Ass'n, 478 F. Supp. 1195, 27 U.C.C. Rep. Serv. 1067 (N.D. Cal. 1979), *aff'd*, 652 F.2d 835, 31 U.C.C. Rep. Serv. 1426 (9th Cir. 1981).

43. 708 F.2d 290, 36 U.C.C. Rep. Serv. 231 (7th Cir. 1983).

44. *Appliance Buyers*, 708 F.2d at 293, 36 U.C.C. Rep. Serv. at 235-36.

45. *Id.*

deadline, it is responsible for paying the item even though the delay has caused no provable damage.[46] The court said that it was

> obvious that if the drafters of the Uniform Commercial Code had intended to make a bank liable for the face value of a check under section 4-212, they would have held the bank 'accountable' in specific language for the face amount of the check as they have under other Code sections.[47]

The *Appliance Buyers* court attempted to distinguish the *Akpan* case in three ways. First, it stated that in *Akpan* the customer had been allowed to withdraw against the check.[48] Second, the depositor in *Akpan* "had detrimentally relied on the fact that the bank had allowed her to draw against the provisionally credited item."[49] Finally, the court stated that in *Akpan*, the issue of the depositor's damages was not before the court.[50]

None of these distinctions is particularly convincing. Whether the bank permitted withdrawal against the provisional credit in *Akpan* is irrelevant. By its own terms, section 4-212 permits the depositary bank to obtain a "refund" of amounts paid to the customer for the instrument as well as to charge back the customer's account. The fact that the bank has permitted withdrawal against the item does not destroy the provisional nature of the credit.[51] Further, it is unclear what the court meant by its second distinction. The court does not say how the customer in *Akpan* relied upon the bank permitting her to withdraw against the provisional credit. Perhaps the court meant that she relied upon it by paying the proceeds of the unpaid check to the drawer. There is, however, no indication in section 4-212 that the right of the bank to obtain refund turns on whether the customer has disposed of the proceeds of the check. In fact, reliance of this sort would appear to be irrelevant in determining the effect of late notice. The customer could just as easily have disbursed the proceeds immediately upon receiving them, that is, *prior* to the expiration of the period that section 4-212 gives to the depositary bank to provide its customer with notice of dishonor.

What the *Appliance Buyers* court probably meant is that the customer in *Akpan* had assumed that the check had been paid because she had received no notice of dishonor, and had disbursed the proceeds in reliance upon this assumption. Thus, *Appliance Buyers* was unlike *Akpan* because the customer in the present case had not relied upon the fact that she had received no notice of dishonor. While this is a plausible basis for distinction, there was no finding in *Akpan* that the customer actually had relied upon the failure of the depositary bank to give notice. That is, there was no finding that the *reason* the customer disbursed the proceeds to the drawer was that she had not received notice and thereby assumed the check had been paid.

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46. *See, e.g.*, Rock Island Auction Sales, Inc. v. Empire Packing Co., 32 Ill. 2d 269, 273, 204 N.E.2d 721, 723, 2 U.C.C. Rep. Serv. 319, 322 (1965); New Ulm State Bank v. Brown, 558 S.W.2d 20, 23 U.C.C. Rep. Serv. 389 (Tex. Civ. App. 1977); Southern Cotton Oil Co. v. Merchants Nat'l Bank, 670 F.2d 548, 33 U.C.C. Rep. Serv. 632 (5th Cir. 1982).

47. *Appliance Buyers*, 708 F.2d at 293, 36 U.C.C. Rep. Serv. at 235-36.

48. *Id.* at 295, 36 U.C.C. Rep. Serv. at 238.

49. *Id.*

50. *Id.*

51. U.C.C. § 4-201 (1977); *see supra* text accompanying notes 6-13.

More importantly, there are no facts in *Akpan* that even suggest this was the case. Consequently, it is unlikely that the cases are actually distinguishable on this basis. The court's final distinction, that the customer's damages were not before the *Akpan* court, is disingenuous. Given its interpretation of section 4-212, the issue of the customer's damages could not have been before the court in *Akpan*. On the contrary, the issue in *Akpan* was whether the plaintiff bank could recover from the customer. In deciding that the timeliness requirements of section 4-212 acted as a condition precedent to the bank's right to recover, there was no issue of the customer's damages to discuss.[52] The court in *Appliance Buyers*, apart from noting the absence of the word "accountable," made little effort to reconcile its interpretation with the apparently conditional language of section 4-212.[53]

About the same time as the *Appliance Buyers* case, the Arizona Court of Appeals decided *Great Western Bank & Trust v. Nahat*.[54] *Nahat* exemplifies the second line of reasoning through which depositary banks have avoided the effect of the time constraints of section 4-212. In *Nahat*, the payee of a check attempted to deposit it but the depositary bank refused to take it because the check was drawn against insufficient funds.[55] The payee attempted again to deposit it a month later and was told he would have to wait ten days until the check cleared. After more than ten days had passed, the payee called the bank and was erroneously told the check had cleared. Based upon this advice, the payee wired money to another account and also transferred money to his mother's account. The depositary bank found out that it had mistakenly paid the customer and applied the funds in the customer's savings account to offset the claim. The depositary bank then sued for the balance.

Unlike the court in *Appliance Buyers*, the *Nahat* court held that the depositary bank had lost its statutory right of charge-back because of the late notice.[56] The court went on, however, to hold that the bank could nonetheless recover from the customer on restitutionary principles if it could prove the appropriate facts.[57] To justify this conclusion, the court cited section 4-212(5), which states that a "failure to charge-back or claim refund does not

52. Perhaps the court merely meant that the bank had not proffered the interpretation adopted by the *Appliance Buyers* court. This point is correct, but that is hardly a factual basis upon which to distinguish the cases.

53. The dissent attempted, with limited success, to confront the problem. The dissent stated that the "plain language of the statute in question here preconditions a collecting bank's right to charge back upon its giving notice of dishonor to its customer before midnight of the next banking day," and further that "[q]uite clearly, the intent of the Code's drafters, reflected in plain language, was to precondition the right of charge back under section 4-212 upon timely notice of dishonor." *Appliance Buyers*, 708 F.2d at 295-96, 36 U.C.C. Rep. Serv. at 240 (Cudahy, J., dissenting). Despite this clear indication that the bank has no right to reverse a provisional settlement unless timely notice was provided, the dissent views the failure to provide timely notice as merely raising a *presumption* of liability which can be rebutted by evidence that the item would have been uncollectible even if timely notice had been provided. The dissent provides no statutory support for this interpretation, nor does the dissent explain the bank's basis for recovery of the funds if it is not the right of charge-back, which it found *conditioned* upon timely notice. In short, the dissent's argument appears to be a *non-sequitur*.

54. 138 Ariz. 260, 674 P.2d 323, 37 U.C.C. Rep. Serv. 209 (Ct. App. 1983).

55. *Nahat*, 138 Ariz. at 262, 674 P.2d at 325, 37 U.C.C. Rep. Serv. at 210.

56. *Id.* at 263, 674 P.2d at 326, 37 U.C.C. Rep. Serv. at 212.

57. *Id.* at 264, 674 P.2d at 327, 37 U.C.C. Rep. Serv. at 214.

affect other rights of the bank against the customer or any other party."[58] The court relied upon section 34 of the *Restatement of Restitution* and indicated that, upon retrial, if the bank could show that the customer was a "knowing wrongdoer" the bank could recover on that basis.[59]

Like *Appliance Buyers*, the *Nahat* case is suspect for a number of reasons. First, although the court relied on the *Restatement of Restitution*, it does not appear that the criteria of section 34 of the *Restatement* were satisfied, even under the bank's asserted facts.[60] By its terms, *Restatement of Restitution* section 34 applies only to "payors." Under the Code, a depositary bank is not a "payor" bank unless the check is drawn on that bank.[61] Further, it is clear that neither subsection (a) nor (c) of *Restatement* section 34 applies, since the customer has not made a misrepresentation causing the payment nor has any failure to notify the bank precluded the bank from obtaining restitution from a third party. Therefore, subsection (b) appears to be the only applicable provision. This provision is satisfied by showing that at the time of payment the customer had reason to know that the payor was mistakenly paying the check. This subsection, however, does not appear satisfied by the facts. When the customer deposited the check, the bank informed him that he would have to wait ten days for the check to clear. Despite the fact that the depositary bank had refused a prior check, it nonetheless took this check and told its customer that he would have to wait for ten days. At this point, the customer may have had reason to believe that the check ultimately might not be paid. However, the depositary bank did not permit the customer to withdraw funds at this time. After the ten days had passed, the customer called the bank to see if the check had cleared and was told that it had. Only then did the customer actually withdraw funds.

Whether the customer should have reasonably believed that the check would not be paid when he withdrew the funds is certainly problematic. In fact, the depositary bank had informed him to the contrary. The bank was in a much better position to know the facts than the customer. If these are the only facts,[62] it is hard to see how the customer's actions satisfy the stan-

58. U.C.C. § 4-212(5) (1977).

59. *Nahat*, 138 Ariz. at 265, 674 P.2d at 328, 37 U.C.C. Rep. Serv. at 215-16.

60. RESTATEMENT OF RESTITUTION § 34 (1936) provides:

> The holder of a bill of exchange or promissory note who, under the rules stated in §§ 30-33, otherwise would be entitled to retain the amount received in payment thereof, is under a duty of restitution to the payor who paid because of a mistake of fact, if
>
> (a) he made a misrepresentation causing the mistake, or
>
> (b) at the time of payment he suspected or had reason to know of the mistake of the payor, except where before such time he had acquired a contractual right to receive payment, or
>
> (c) having received payment, he learned facts from which he had reason to know of the payor's mistake and failed to use care to notify the payor, to the extent that the payor has been thereby prevented from obtaining restitution from a third person.

61. Section 4-105(b) defines "payor bank" as "a bank by which an item is payable as drawn or accepted." U.C.C. § 4-105(b) (1977).

62. The case was decided on appeal from the granting of a directed verdict by the trial court and was remanded for a new trial. The court, in its remand, stated that the bank "alleges that Nahat had knowledge of the mistake made by Great Western." *Nahat*, 138 Ariz. at 265, 674 P.2d at 328, 37 U.C.C. Rep. Serv. at 215. It is not clear whether this simply refers to the fact that the customer, at the time of presenting the check, should have had some reason to think that the bank might not

dard of the *Restatement of Restitution* section 34 or are sufficient to categorize the customer as a "knowing wrongdoer."[63]

Also, if reliance is the key, as suggested in *Appliance Buyers*, the customer in *Nahat* relied in a much more convincing way than the customer in *Akpan*, where the bank was denied recovery. As previously mentioned, there was no showing in *Akpan* that the customer relied upon the failure to receive notice in disbursing the proceeds of the deposited check.[64] In *Nahat*, the customer clearly relied upon the bank's positive assurance that the check had been paid and the court nonetheless refused recovery. These cases can be reconciled only if the court in *Akpan* did not consider restitution as an alternative to section 4-212 in deciding whether the bank should be permitted to recover from the customer.

Three other cases decided in 1983 and 1984 also found for the depositary bank despite the failure of the bank to give timely notice.[65] Two merit detailed discussion. In *Northpark National Bank v. Bankers Trust Co.*,[66] a malefactor deposited a worthless check with an incorrect routing number, hoping to take advantage of any delay in processing this defect would cause. The check went on a lengthy journey before being finally dishonored. By this time, the malefactor had been allowed to withdraw the funds.[67] The depositary bank, Northpark, sued, among others, the Federal Reserve Bank of New York (FRBNY), an intermediate collecting bank, claiming that the FRBNY could not charge back the account of the depositary bank for the dishonored check because it had failed to comply with the time period of section 4-212.

The court framed the issue as whether section 4-212 establishes a condition precedent to the right of charge-back or whether it merely defines a duty of care for which actual damages must be proved.[68] If the time limit in section 4-212 were a condition precedent to charge-back, a collecting bank failing to meet the condition would be absolutely liable for the item. The court decided, however, that this was not the intent of the provision, and gave four reasons for its conclusion.[69] First, the court cited the 1948 pro-

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pay, or whether the bank made other allegations the court did not refer to in its recitation of the facts.

63. The result in *Nahat* is also questionable on policy grounds. The customer who has some reason to believe that a check may not be paid should not be treated differently from any other holder. It is hardly "knowing wrongdoing" to present a check for payment with some uncertainty as to whether it will be paid, relying on the payor and the depositary bank to properly perform their responsibilities under Article 4. Certainly, if the customer and the drawer are in collusion and the customer presents a worthless check in the hope that the banks will make an error that results in payment, the customer can easily be characterized as a knowing wrongdoer, but there is no indication that facts such as these were present in the case.

64. *See supra* text accompanying notes 51-52.

65. Two of the cases will be discussed: Northpark Nat'l Bank v. Bankers Trust Co., 572 F. Supp. 524 (S.D.N.Y. 1983) and Greer v. White Oak State Bank, 673 S.W.2d 326, 39 U.C.C. Rep. Serv. 929 (Tex. App. 1984). The third case is Royal Trust Bank of Orlando v. All Fla. Fleets, Inc., 431 So. 2d 1043, 36 U.C.C. Rep. Serv. 596 (Fla. App. 1983).

66. 572 F. Supp. 524, 37 U.C.C. Rep. Serv. 385 (S.D.N.Y. 1983).

67. By the time of the litigation, however, the perpetrator was in prison in Pennsylvania for an apparently unrelated offense. *Northpark Nat'l Bank*, 572 F.2d at 526 n.5, 37 U.C.C. Rep. Serv. at 389 n.5.

68. *Id.* at 529, 37 U.C.C. Rep. Serv. at 393.

69. *Id.* at 529-30, 37 U.C.C. Rep. Serv. at 393-95.

posed final drafts and observed that neither the drafts, nor their notes and comments, provide any help in interpreting the provision.[70] Second, "[c]omment 1 to UCC § 4-108 specifically refers to UCC § 4-212 as 'prescrib[ing] . . . time limits . . . within which a bank, *in fulfillment of its obligation to exercise ordinary care*, must handle items entrusted to it for collection.' "[71] This was a clear indication to the court that the time limits of section 4-212 were not conditions precedent, but merely established a standard of care. Third, the court noted that the primary purpose of notification is to advise an unsuspecting customer and protect him from having subsequent checks dishonored which were written on the assumption that the deposited check had been paid.[72] Finally, the court concluded that all of the cases it had found in which a charge-back had not been permitted were cases in which the failure of the bank to notify the customer caused a detrimental change of position which could have been avoided by prompt notice.[73]

Each of these justifications deserves comment. While it is true that the history cited by the court is of little assistance, other history already discussed in this Article suggests a conclusion contrary to that reached by the court.[74] At the very least, legislative history which proves "unhelpful" hardly justifies a conclusion which deviates from the apparent meaning of the language of the statute. Further, comment 1 to section 4-108 is not as supportive of the court's conclusion as its discussion suggests.[75] A collecting bank has responsibilities to its customers, including other banks, both as a check moves "forward" in the system to the payor bank and as credits or dishonor move from the payor bank "backward" in the system. Clearly, the negligence standard of ordinary care governs the duties of a collecting bank to move promptly and properly in "forwarding" items for collection. Moreover, section 4-212 establishes no specific time limits with respect to this aspect of the process, nor does it contain any suggestion that timeliness in this part of the process is a condition to charging back the provisional credit if the instrument is dishonored. Additionally, this same comment also refers to the section 4-302 time limitations in the same context, and courts have, almost uniformly, held these time limitations to impose liability on a payor for failing to meet its midnight deadline without regard to negligence or proof of loss.

The court's statement that the primary purpose of the charge-back notice provision is to insure that the customer does not write checks on the amount that has been charged back, and thus run the risk of "bouncing" these checks, is also problematic, and does not necessarily support the

70. *Id.* at 530 n.15, 37 U.C.C. Rep. Serv. at 394 n.15.
71. *Id.* at 530, U.C.C. Rep. Serv. at 394 (emphasis added).
72. *Id.*
73. *Id.*
74. *See supra* text accompanying notes 30-37.
75. Sections 4-202(2), 4-212, 4-301 and 4-302 prescribe various time limits for the handling of items. These are the limits of time within which a bank, in fulfillment of its obligation to exercise ordinary care, must handle items entrusted to it for collection or payment. Under Section 4-103 they may be varied by agreement or by Federal Reserve regulations or operating letters, clearing house rules, or the like.
U.C.C. § 4-108 comment 1 (1977).

court's conclusion. While this is certainly one purpose of the notice provision, there are a number of other plausible justifications which might support a different conclusion. The notice provision also serves to insure that the customer has the maximum opportunity to recover from the drawer or from indorsers of the instrument.[76]

In addition, as will be discussed later,[77] virtually all of the policies behind the final payment rule, and the resulting liability of a payor bank without regard to negligence, apply equally to the charge-back provision of section 4-212.[78] Further, even if we accept the court's statement that the notice provision is designed to prevent the customer from bouncing checks, a rule of strict liability for failing to provide such notice would accomplish the same deterrent effect. Finally, the notice provision is, to some degree, logically unrelated to the court's concern about the customer bouncing checks, since *any* notice to the customer *prior* to the actual set-off of funds would prevent this from occurring, even if the charge-back did not occur until months after the deposit. If this were the provision's primary purpose, one would expect that, rather than imposing a midnight deadline time limitation, the drafters would have been more concerned with insuring that notice was given to the customer prior to setting off the customer's funds.

Finally, the court stated that all of the earlier cases in which recovery had been permitted were cases in which the lack of timely notice had caused the customer to act detrimentally.[79] The cases do not support such a categorical statement. There is no indication of reliance, for example, in *Dozier v. First Alabama Bank of Montgomery.*[80] Further, there is no suggestion in many of the earlier cases that the presence or absence of reliance is of any relevance.[81]

The other two cases in which courts have permitted recovery by a depositary bank despite its failure to give timely notice of charge-back are *Greer v. White Oak State Bank*[82] and *Royal Trust Bank of Orlando v. All Florida Fleets, Inc.*[83] In *Greer*, the customer deposited an insurance check in his account.[84] The check also named three others as payees, all of whom were lienors of the customer. The check bounced because the drawer had become insolvent, and the depositary bank sued both its customer and the indorsers since it gave the customer immediate credit for the check. The court held that the bank could not recover against the indorsers since they

76. The collecting bank's failure to give its customer timely notice may make it difficult or impossible to locate indorsers or the drawer, or late notice may preclude recovery from one of these parties because of intervening insolvency. While the present case law generally permits recovery against the depositary bank where the late notice actually precluded the customer from recovering from someone else, *see supra* text accompanying notes 43-63, avoiding this situation is certainly a plausible purpose of the notice provision, since it results in one of two innocent parties having to bear the loss.

77. *See infra* text accompanying notes 103-106.

78. *See infra* text accompanying notes 117-140.

79. *Northpark Nat'l Bank*, 572 F. Supp. at 530, 37 U.C.C. Rep. Serv. at 394.

80. 363 So. 2d 781, 25 U.C.C. Rep. Serv. 804 (Ala. Civ. App. 1978).

81. *See, e.g.*, Lufthansa Ger. Airlines v. Bank of Am. Nat'l Trust & Sav. Ass'n, 478 F. Supp. 1195, 27 U.C.C. Rep. Serv. 1067 (N.D. Cal. 1979).

82. 673 S.W.2d 326, 39 U.C.C. Rep. Serv. 929 (Tex. App. 1984).

83. 431 So. 2d 1043, 36 U.C.C. Rep. Serv. 596 (Fla. App. 1983).

84. *Greer*, 673 S.W.2d at 328, 39 U.C.C. Rep. Serv. at 930.

had not received timely notice of dishonor.[85] The bank could, however, recover against its customer even though it did not proceed under section 4-212 in a timely manner. The court also held that the right of charge-back under section 4-212 is not exclusive, and that the depositary bank was entitled to recover on a theory of unjust enrichment.[86] Finally, the court held that restitution was available even though the customer had committed no wrongdoing and the funds from the check had already gone to pay off the lienors.[87]

Greer presents a clear case where one of two innocent parties will have to bear the loss resulting from the drawer's insolvency. From the customer's point of view, there is no reason to treat him any differently from the indorsers. He has not received a "windfall" as a result of receiving the check's proceeds. Presumably, he paid for the insurance policy and is only receiving the return to which he is entitled. He is not getting "something for nothing" which characterizes many unjust enrichment cases. More importantly, the customer might legitimately ask why the bank should occupy a special status simply because it is a depositary bank. Were it simply another subsequent holder of the check, rather than a depositary bank, it would have no rights against any of the payees because it failed to give timely notice of dishonor. It is difficult to see why the depositary bank's rights should be greater simply because it is a depositary bank, particularly since it chose to give immediate value for the item just as any other holder would normally do.

Similarly, it is difficult to see why the other lienors are not equally "unjustly enriched" as the customer by their receipt of the funds from the check. The late notice has the same effect on them as the customer, but no court has found restitutionary rights to exist in a bank against an indorser when the bank has missed its midnight deadline in providing notice of dishonor.

The bank, of course, views the situation differently. Why should it suffer the loss when its only "fault"—the failure to give timely notice—in no sense caused the customer's loss? Had the bank given timely notice, and thus prevented distribution of the proceeds to the lienors, the customer would remain liable to the lienors. Thus, the failure to give timely notice caused no loss. While the Code clearly indicates that late notice of dishonor discharges indorsers,[88] the defendant is not merely an indorser, but is also the bank's customer. Even though the bank actually permitted withdrawal of the proceeds, it remains only the agent of its depositor for collection[89] and thus occupies a different status than a non-depositary bank holder. While agents are liable to their principals for harm caused by their negligence,[90] where no loss is caused by the negligence there can be no recovery.[91]

85. *Id.* at 329, 39 U.C.C. Rep. Serv. at 932.
86. *Id.*
87. *Id.*
88. U.C.C. § 3-502 (1977).
89. U.C.C. § 4-201 (1977).
90. RESTATEMENT (SECOND) OF AGENCY § 401 comment a (1958).
91. A failure of the agent to perform his duties which results in no loss to the principal may subject the agent to liability for nominal damages for breach of contract, . . . to liability for any profits he has thereby made . . ., to discharge . . ., or to loss of compensation . . ., but not to an action of tort.

3. *The Proper Perspective: Analogy to Final Payment*

Upon close analysis, none of the cases in which a depositary bank has been permitted to charge back a customer's account despite the failure to give timely notice is analytically sound. The first series of cases, those in which the courts indicate that section 4-212 incorporates only negligence liability, suffers from a number of defects.[92] The language of the section itself indicates a contrary conclusion, as does the history of the provision. Similarly, the official comments suggest that a failure to give timely notice acts as a condition to charge-back. The one official comment that does suggest that section 4-212 incorporates negligence liability can be otherwise explained.[93]

Cases that rely on an unjust enrichment theory avoid these problems, but have their own set of difficulties. First, none of them explores with any depth the issue of why a restitutionary recovery is not displaced by the particular provisions of section 4-212. While there is no language in section 4-212 that expressly makes charge-back the exclusive means of recovery for a depositary bank, one can argue that permitting a restitutionary recovery despite the language of section 4-212 sufficiently undercuts the policy of providing timely notice that it should be deemed pre-empted.[94] Further, the provisions of the *Restatement of Restitution* do not appear to support a restitutionary recovery.[95] Finally, the courts are not clear as to what kind of reliance is required to preclude a restitutionary recovery.

Appliance Buyers[96] suggests that it is sufficient that the customer have withdrawn the proceeds of the check. This, however, is contrary to the result in *Greer*, and is an inappropriate determinant. What, for example, should be the result if the customer has withdrawn the funds but still has them on hand? Why should restitution be precluded in this case and not in the case where they are still in the account? Similarly, what if the customer has spent the funds, but retains what was purchased with them? Should it make any difference what was purchased with the funds?[97] In virtually every case the customer will have obtained some benefit from the proceeds of the check.[98] On the whole, it is difficult to justify a rule which considers withdrawal of the proceeds sufficient "detrimental reliance" to bar restitu-

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RESTATEMENT (SECOND) OF AGENCY § 401 comment b (1958).

92. *See supra* text accompanying notes 43-45.

93. *See supra* text accompanying note 75.

94. *Cf.* State & Sav. Bank of Monticello, Ind. v. Meeker, 469 N.E.2d 55, 58, 39 U.C.C. Rep. Serv. 1391, 1395 (Ind. App. 1984)(permitting restitution in favor of payor bank which misses midnight deadline would undermine "crucial" values of finality and certainty).

95. *See supra* text accompanying note 60.

96. *Appliance Buyers*, 708 F.2d 290, 36 U.C.C. Rep. Serv. 231.

97. *E.g.*, a TV set vs. a certificate of deposit with another bank.

98. This may not be the case in a situation such as *Akpan* where the drawer simply gave the check to the payee so that the payee could obtain funds for the drawer, and the proceeds were merely given to the drawer. *See Akpan*, 91 Misc. 2d 622, 398 N.Y.S.2d 477, 22 U.C.C. Rep. Serv. 1009. The payee in such a case, however, gives nothing for the check in the first place, and is therefore in no different position than someone who parted with some value to obtain the check. In both cases, if restitution is permitted, the payee will have to seek payment from the drawer or suffer a loss. On the other hand, if restitution is not permitted, the payee will be "made whole," having parted with something to obtain the check and receiving its proceeds in return.

tion. Furthermore, the remedy will be of little practical effect since withdrawal of the proceeds has generally occurred in these cases.

If, however, the customer must do something more than simply withdraw the proceeds, the nature of the requisite additional "reliance" is not at all clear. Certainly, if what was acquired can be traced and recovered, the mere expenditure of the proceeds itself should not be sufficient. Must the customer rely by writing additional checks on the assumption that the deposited check has been paid, and then have them bounce before the reliance is sufficient? The customer may suffer no damages from this occurrence. For example, the only check written may have been to the customer's daughter. Why should the customer in this instance be any better off than the customer who has not written any such checks? If, in order to preclude a restitutionary recovery, the customer must show that he bounced checks in reliance on the check being paid and also suffered damage as a result, the restitutionary remedy will virtually swallow the condition of timeliness in section 4-212.

The Code offers little help and conflicting guideposts in resolving these questions. A useful analogy, however, might be drawn to the rules relating to payment by a payor bank. As mentioned earlier,[99] section 4-302 holds a payor bank "accountable" for an item which is held past the payor's midnight deadline without payment or dishonor.[100] A number of issues that have arisen in connection with this provision may provide some guidance in interpreting section 4-212. First, the cases are uniform in not requiring proof of negligence or damages in order for a holder to recover from a payor who has missed its midnight deadline, at least where the holder is a holder in due course or someone who has in good faith relied upon payment.[101] There is no doubt that section 4-302 imposes more than negligence liability. In addition to the cases, the history of the provision makes it clear that the drafters intended more than negligence liability.[102] The cases and commentators have suggested numerous policies to justify this rule. In a recent case, the Minnesota Supreme Court stated that the overarching advantage of the finality rule was simplicity, obviating the need for courts to be "forever wrestling with fine fact questions involving reliance, negligence, notice, damages and the concept of holder in due course."[103]

Similarly, the Fifth Circuit said that one of the policies behind the final payment rule was to inject certainty into the collection process by providing

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99. *See supra* text accompanying notes 45-47.

100. U.C.C. § 4-302 (1977).

101. *See, e.g.*, Rock Island Auction Sales, Inc. v. Empire Packing Co., 32 Ill. 2d 269, 204 N.E.2d 721 (1965).

102. For example, in its analysis of Article 4, the New York Law Revision Commission concluded that

> except for the undefined and therefore ambiguous term 'pay' in the case of a demand item received by a payor bank which is also the depositary bank, and except for the restriction to items 'properly payable' where they are not demand items, *mere lapse of time*, under section 4-302 will result in liability for the payor bank.

State of New York, 2 LAW REVISION COMM'N STUDY OF THE UNIFORM COMMERCIAL CODE: ARTICLE 4—BANK DEPOSITS AND COLLECTIONS 165 (1955). *See also id.* at 238.

103. Town & Country State Bank of Newport v. First State Bank of St. Paul, 358 N.W.2d 387, 39 U.C.C. Rep. Serv. 1740 (Minn. 1984).

a bright line for payor bank liability.[104] The same court indicated that imposing absolute liability on the payor bank for holding a check past its midnight deadline helped speed the collection of checks through the system.[105] The commentators offer similar justifications for the rule. Professor Clark, in his superb treatise on bank deposits and collections, states that the policy behind the final payment rule is "to reduce float and to encourage the prompt return of dishonored checks so that there will be a minimum amount of sand in the collection system."[106]

The justifications are essentially efficiency justifications: the system will operate in a less costly manner if difficult and expensive administrative costs (such as the cost of resolving disputes concerning negligence, damages, causation, etc.) are removed, and if there are appropriate incentives for the bank to have an efficient collection system. The drafters have determined that the efficient operation of the collection system is furthered by the accountability rule, and that these advantages outweigh occasional inequities that may occur as a result. The question remains, however: to what extent is this rationale applicable to section 4-212?

Generally, these policies are relevant to section 4-212 as well as to section 4-302. Although, by the terms of the statute, factual questions involving notice cannot be avoided, an interpretation that makes a depositary bank accountable for a check when it misses its midnight deadline without excuse would remove the issues of reliance, causation, and damages. Also, the rule would provide maximum incentive to give prompt notice in those instances where checks are dishonored, since the depositary bank could not rely upon the difficulty of proving negligence, reliance, damages, or causation to avoid liability. Moreover, imposing this responsibility upon depositary banks seems no more, and probably less, inequitable than imposing it upon payor banks. After all, under section 4-212, depositary banks are permitted "a longer reasonable time" after their midnight deadline if they can show the longer period was justified. Payor banks have generally been accorded no such advantage under section 4-302.[107]

Rather, payor banks are governed by the stricter impracticability standard of section 4-108. Further, the return of a check unpaid is, in a relative sense, both an infrequent and isolated occurrence.[108] It is unlikely that a bank will miss the midnight deadline for charge-back on a large number of items at once.[109] In any event, there seems to be no reason to believe that

104. Starcraft Co. v. C.J. Heck Co. of Tex., 748 F.2d 982, 40 U.C.C. Rep. Serv. 215 (5th Cir. 1984).

105. *Id.* at 986, 40 U.C.C. Rep. Serv. at 221.

106. B. CLARK, *supra* note 2, ¶ 3.4[1], at 3-21.

107. There are no cases which have permitted payor banks to avoid liability for missing their midnight deadline upon a simple showing that it was reasonable for them to delay past the deadline. On the other hand, a number of cases make it clear that liability attaches regardless of whether the delay was negligent or not. *See, e.g.*, State Sav. Bank of Monticello, Ind. v. Meeker, 469 N.E.2d 55, 39 U.C.C. Rep. Serv. 1391 (Ind. App. 1984) and cases cited *infra* at note 112.

108. A leading authority has estimated that no more than 0.5% of all checks are returned unpaid, and that half of those are eventually paid. A. BAILEY, *supra* note 2, ¶ 18.1, at 18-4.

109. Banks may, however, simultaneously miss the final payment deadline on a large number of items. *See, e.g.*, First Wyo. Bank v. Cabinet Craft Distrib., Inc., 624 P.2d 227, 30 U.C.C. Rep. Serv. 1194 (Wyo. 1981).

applying something like the final payment rule to depositary banks would be *more* inequitable than its application to payors.

Courts also have been reluctant to grant relief to payors on restitutionary grounds when they have failed to make payment or dishonor by their midnight deadlines. While two courts have held that a payor can recover on restitutionary grounds if the holder is not a holder in due course,[110] only one case has held that a general right of restitution survives a payor bank's failure to meet its midnight deadline, and that case involved highly atypical circumstances.[111] On the other hand, the courts in two cases have clearly rejected the availability of restitutionary theories after final payment has been made, including a failure to dishonor by the midnight deadline.[112] Moreover, a third case is strongly supportive of this position.[113] Similarly, most scholars have taken the position that once payment is final, at least in favor of a holder in due course, it should not be subject to reversal on restitutionary grounds.[114]

Contrary to the language of most of the cases which allow a restitutionary recovery, the issue generally is not that of permitting the depositor a "windfall" if the bank is not permitted to charge back the depositor's account. Instead, the issue in these cases is either (1) which of two innocent

110. Maplewood Bank and Trust Co. v. F.I.B., Inc., 142 N.J. Super. 480, 362 A.2d 44, 19 U.C.C. Rep. Serv. 1164 (1976); National Sav. and Trust Co. v. Park Corp., 722 F.2d 1303, 37 U.C.C. Rep. Serv. 817 (6th Cir. 1983), *cert. denied*, 466 U.S. 939 (1984).

111. *See* Bank Leumi Trust Co. of N.Y. v. Bally's Park Place, Inc., 528 F. Supp. 349, 32 U.C.C. Rep. Serv. 1542 (S.D.N.Y. 1981). The court in this case indicated that actions for restitution could survive sections 4-302 and 3-418 if the proper circumstances were present. Drawee wrote Bally's a check for $60,000 to cover his losses, using a check supplied by Bally's rather than one of his own. Because the payor bank's computer was unable to read the check, the bank processed it by hand. Processing was not completed by the midnight deadline. The bank was nonetheless permitted to recover, despite the fact that Bally's would seem to qualify as a holder in due course. A number of circumstances, however, caution against an expansive reading of the case. First, the court emphasized that Bally's knew that the check could not be mechanically processed, and thus "set a trap for an unwary bank." *Id.* at 354, 32 U.C.C. Rep. Serv. at 1549. Secondly, when Bally's presented the check, the drawer had died and Bally's was aware that the estate was insolvent. Thus, in effect, Bally's only hope was that the bank would accidentally pay the check, which it did. Also, under section 4-405, the bank, upon learning of the death of the drawer, no longer had any authority to pay the check, presumably something that Bally's knew or should have known. Finally, the court was not particularly taken with Bally's practice of having blank checks on hand for the purpose of providing them to gamblers who often intentionally avoided bringing their own personal checks along to avoid temptation. *Id.* at 351 n.3, 32 U.C.C. Rep. Serv. at 1545 n.3. While perhaps a step short of fraudulent, the actions of Bally's in this case are far different from those of an innocent payee.

112. State & Sav. Bank of Monticello, Ind. v. Meeker, 469 N.E.2d 55, 39 U.C.C. Rep. Serv. 1391 (Ind. App. 1984); Citizens & S. Nat'l Bank v. Youngblood, 135 Ga. App. 638, 219 S.E.2d 172, 18 U.C.C. Rep. Serv. 180 (1975). *See also* Northwestern Nat'l Ins. Co. v. Midland Nat'l Bank, 96 Wis. 2d 155, 292 N.W.2d 591, 29 U.C.C. Rep. Serv. 940 (1980). The court in *Northwestern* did not explicitly reject a restitutionary theory, but refused to reverse final payment even though the holder was not a holder in due course and did not rely on the final payment in circumstances where a restitutionary argument would appear strong.

113. *See* Sunshine v. Bankers Trust Co., 34 N.Y.2d 404, 412 n.3, 358 N.Y.S.2d 113, 120 n.3, 314 N.E.2d 860, 865 n.3, 14 U.C.C. Rep. Serv. 1416, 1423 n.3 (1974)(discussing restitution in the context of § 4-407).

114. *See* J. WHITE & R. SUMMERS, UNIFORM COMMERCIAL CODE 613-18 (2d ed. 1980)(arguing that once payment is final under § 4-302 it should only be reversed if the holder has acted in bad faith regardless of whether the holder is a holder in due course or has relied on the payment); B. CLARK, *supra* note 2, ¶ 3.6[3], at 3-38 to 3-40 (adopting the same approach as J. WHITE & R. SUMMERS, *supra*). Both of these scholarly authorities suggest that the advantages of certainty and simplicity outweigh any disadvantages.

parties will be required to pursue other parties (such as the drawer), or (2) which of two innocent parties will be required to suffer a loss (if, for example, the drawer is insolvent). It is much more difficult to say that a party has been "unjustly enriched," thereby entitling the other party to restitution, if payment of the check does no more than make the depositor whole.[115] Further, the depositary bank may have remedies against its depositor or others for breach of warranty, a cause of action which is clearly not precluded by the failure to give timely notice of charge-back.[116] Also, there is the provision in section 4-212 permitting the depositary bank a "longer reasonable time" to provide notice where circumstances preclude notice by the midnight deadline. Finally, as indicated above, there are strong policy considerations supporting a rule of finality in these circumstances. Consequently, in the absence of bad faith or fraud, the failure of a depositary bank to provide notice of charge-back by its midnight deadline or a longer reasonable time should preclude charge-back or other recovery by a depositary bank.

C. *Effect of Final Payment on Charge-back*

Example 6. Charlie deposits a check in his account at First Bank, and First Bank forwards it to the payor for payment. The payor fails to pay or dishonor the check by its midnight deadline, although it does dishonor the check shortly thereafter for insufficient funds. It notifies the depositary bank that it is reversing the credit given to the depositary bank for the check, and the depositary bank charges back the amount of the check against the customer's account. The depositary bank provides timely notice of the charge-back under section 4-212. Is the charge-back valid?

The appropriate analysis, while somewhat circuitous, is not difficult. Section 4-212(1), in appropriate part, provides: "These rights to revoke, charge-back and obtain refund terminate if and when a settlement for the item received by the bank is or becomes final (subsection (3) of section 4-211 and subsections (2) and (3) of section 4-213)."[117] Thus, the right of charge-back ends when settlement for the item becomes final. Has settlement become final in example 6? The answer appears to be that it has. Under section 4-213(1) an item is "finally paid" when the earliest of four events occurs: (a) payment by the payor in cash for the item;[118] (b) settlement by the payor for the item without reserving a right to revoke the settlement and without having a right to revoke under statute, clearinghouse rule or agreement;[119] (c) completion of the process of posting the item by the payor;[120] or (d) failure to revoke a provisional settlement in the time and manner pro-

115. This analysis is premised on the assumption that the depositor has given value for the instrument.

116. *See* B. CLARK, *supra* note 2, ¶ 3.6[3], at 3-40; City Nat'l Bank v. Crocker Nat'l Bank, 150 Cal. App. 3d 290, 197 Cal. Rptr. 721, 37 U.C.C. Rep. Serv. 1228 (1983); Dozier v. First Ala. Bank of Montgomery, 363 So. 2d 781, 25 U.C.C. Rep. Serv. 802 (Ala. Civ. App. 1978); Sunshine v. Bankers Trust Co., 34 N.Y.2d 404, 358 N.Y.S.2d 113, 314 N.E.2d 860, 14 U.C.C. Rep. Serv. 1416 (1974).

117. U.C.C. § 4-212 (1977).

118. U.C.C. § 4-213(1)(a) (1977).

119. U.C.C. § 4-213(1)(b) (1977).

120. U.C.C. § 4-213(1)(c) (1977).

vided by statute, clearinghouse rule, or agreement.[121] Typically, a payor bank will make a provisional settlement for an item by crediting the presenting bank's account prior to midnight of the banking day of receipt. This provisional credit may be given to a depositary bank if the depositary bank directly presented the item to the payor, or it may be given to an intermediary bank which has itself given a provisional credit to the depositary bank, or perhaps to another intermediary bank. Section 4-301 permits this initial credit to be revoked, so long as the item is returned or written notice of dishonor is given prior to its midnight deadline.[122] If the item is not returned or notice of dishonor given, the bank becomes "accountable" for the item under section 4-302, and the settlement is no longer provisional. Under section 4-213(1)(d) above, this failure to revoke a provisional settlement in the time provided by statute results in the item being finally paid.[123] Comment 6 to section 4-213 confirms this analysis in a simple illustration. It states that if a provisional settlement made on Monday is not revoked before midnight on Tuesday as permitted by section 4-301, the item is finally paid on Tuesday.[124] Thus, in our example, since the provisional settlement made on the day of receipt was not properly revoked the following day either by return of the item or notice of dishonor, final payment would occur. And, under section 4-212(1), final payment precludes charge-back.

A number of courts, however, have reached results inconsistent with the Code's clear direction. For example, in *Mercantile Bank & Trust Co. v. Hunter*,[125] the defendant deposited a check for collection and was allowed to withdraw the amount of the check the following day. Months later, the check was dishonored, and the depositary bank gave the defendant timely notice. The defendant claimed that since the payor had not returned or dishonored the item by its midnight deadline, the payor was accountable for the item under section 4-302 and the depositary bank had lost its right of charge-back. The *Hunter* court, however, held for the plaintiff depositary bank.[126] It stated that simply because the payor bank was accountable for the item under section 4-302 did not mean that there had been a final settlement for the item such as would preclude charge-back by the depositary bank.[127] The court said that there is "no provision that mere accountability of a payor bank for a check is a final settlement unless the check is actually paid by the payor bank."[128]

The court could not have been more misdirected in its analysis. While recognizing that section 4-213 is the appropriate section for determining whether final payment has occurred, the court simply ignored section 4-213(1)(d) and the analysis suggested above, including the illustration in comment 6 to section 4-213.[129] In addition, contrary to the court's suggestion,

121. U.C.C. § 4-213(1)(d) (1977).
122. That is, midnight of the day following receipt of the item. *See* U.C.C. § 4-104(1)(h) (1977).
123. U.C.C. §§ 4-301, 4-302 (1977).
124. U.C.C. § 4-213 comment 6 (1977).
125. 31 Colo. App. 200, 501 P.2d 486, 11 U.C.C. Rep. Serv. 545 (1972).
126. *Hunter*, 31 Colo. App. at 204, 501 P.2d at 488, 11 U.C.C. Rep. Serv. at 548.
127. *Id.*
128. *Id.*
129. *See supra* text accompanying notes 118-121.

section 4-213(1) itself indicates that "accountability" and "final payment" are synonymous in the context of bank credits.[130] There is little doubt that the drafters intended congruity between the concepts of final payment and accountability.

A similarly misguided decision is that of the Indiana Court of Appeals in *Yoder v. Cromwell State Bank.*[131] In that case, the defendant deposited checks with the depositary bank for collection. The payor gave notice of their dishonor, and the depositary bank gave the defendant timely notice of charge-back. Because the depositor's account contained insufficient funds to cover the full amount, the depositary bank sued for a refund of the balance. The depositor defended against summary judgment on a number of grounds, one of which was that final payment might have occurred because the payor had completed the process of posting. Therefore, summary judgment was inappropriate because a material issue of fact remained unresolved.

Relying expressly on *Hunter*, the court rejected the defendant's argument.[132] The court found that it was irrelevant whether the payor had made final payment by completing the process of posting.[133] Given the volume and speed of check processing, it would be unrealistic to require the collecting bank to inquire and ascertain the grounds for and propriety of every dishonored item, and the collecting bank must be able to rely upon receipt of the items or notice of dishonor in order to act seasonably in notifying the customer. The *Yoder* court quoted from *Hunter*'s holding that because a payor is "accountable" for an item does not mean that there has been final settlement for purposes of section 4-212 unless the check is actually paid.[134]

The *Yoder* court's reasoning is flawed for a number of reasons. There is nothing "unrealistic" about precluding charge-back in this situation. The depositary bank, upon receiving notice of dishonor from the payor, can simply provide notice of charge-back to its depositor on the assumption that the payor has not made final payment. If this assumption is wrong, the depositor will be entitled to have the charge-back reversed. The depositary bank, however, will have recourse against the payor since the payor bank will be accountable for the item to the depositary bank as a result of the final payment.[135] It is no more "unrealistic" to require the depositary bank to assume this responsibility than to require the depositor to seek a remedy directly against the payor bank, which may be located in a distant city or state. Also, the reasoning of *Yoder* is as untenable in the circumstances of this case as it was in *Hunter*. Section 4-213(1) specifically equates "accountability" and "final payment" in the context of completion of the posting pro-

130. U.C.C. section 4-213(1) provides that upon final payment under paragraphs (b), (c), or (d) the payor bank is accountable for the amount of the item. U.C.C. § 4-213(1) (1977). The only reason subsection (a) is not included is explained in comment 7. "[A payor bank] is not made accountable if it has paid the item in cash because such payment is itself a sufficient accounting." *Id.* at comment 7.

131. 478 N.E.2d 131, 41 U.C.C. Rep. Serv. 173 (Ind. App. 1985).

132. *Yoder*, 478 N.E.2d at 135, 41 U.C.C. Rep. Serv. at 180.

133. *Id.* at 134, 41 U.C.C. Rep. Serv. at 179.

134. *Id.* at 135, 41 U.C.C. Rep. Serv. at 180.

135. U.C.C. § 4-213(2) (1977).

cess.[136] There is no basis for the proposition that final payment for purposes of section 4-212 occurs only when a check is finally paid in cash.[137]

Fortunately, other cases have reached the correct conclusion. In both *Fromer Distributors, Inc. v Bankers Trust Co.*[138] and *Capital City First National Bank v. Lewis State Bank*,[139] the courts held that the failure of a payor bank to dishonor prior to its midnight deadline precluded charge-back by the depositary bank. Language supporting this result is also found in other cases and in commentaries.[140] The results reached by the *Hunter* and *Yoder* cases are unfortunate. The clear mandate of the statute, as well as sound policy, supports a contrary result. Hopefully, the analysis in this article will help to prevent courts from making similar errors.

D. *Set-off*

Example 7. Doug sells his stereo to a person he believes is Sam Smith, and receives Smith's indorsed paycheck in return. Doug deposits the check in his account, and the check is processed and paid by the payor. Sometime thereafter the payor notifies the depositary bank that it has determined that Smith's indorsement is a forgery and requests reimbursement from the depositary bank. The depositary bank reimburses the payor and then deducts the amount of the check from Doug's account. This causes a number of checks to bounce. Doug sues to have his account recredited and also for wrongful dishonor of those checks that bounced.

Although the cases have sometimes failed to recognize it,[141] this is not a situation involving the bank's right of charge-back. The language of section

136. "Upon final payment under subparagraphs (b), (c) or (d) the payor bank is accountable for the amount of the item." U.C.C. § 4-213(1) (1977). Subparagraph (c) covers completion of the posting process.

137. There is a technical argument that might plausibly be asserted when a claimed final payment is based upon completing the posting process, at least where some very unusual circumstances are present. Under section 4-212, the right of charge-back terminates if and when a *settlement* for an item is or becomes final. To "settle" is defined in section 4-104(j) as "to pay in cash, by clearing house settlement, in a charge or credit or by remittance, or otherwise as instructed." U.C.C. § 4-104(j) (1977). If final payment occurs through completion of the posting process before *any* settlement (either provisional or final) occurs, it could be argued that a "settlement" has not become final under section 4-212 even though final payment has occurred. Therefore, the right of charge-back is not lost. This argument is bolstered to some degree by the parenthetical in the last sentence of section 4-212(1) which mentions subparagraphs (2) and (3) of section 4-213, but not subparagraph (1).

Even if this argument were tenable, the circumstances under which it could be asserted would arise *very* rarely. The process of posting an item to the drawer's account will almost always occur after there has been a provisional settlement. See the explanation of the posting process in official comments 3 and 4 to section 4-213 for more detail. According to section 4-213(2) "final payment" will cause this provisional settlement to become final and thus section 4-212 will be satisfied. There is no reason to believe, however, from anything in the Code or comments that the drafters intended to distinguish between situations where the process of posting was completed prior to provisional settlement and where it was completed after provisional settlement. It is hard to find any rationale which would justify such a conclusion. In any event, the *Yoder* court did not rely upon this distinction.

138. 36 A.D.2d 840, 321 N.Y.S.2d 428, U.C.C. Rep. Serv. 1298 (1971).

139. 341 So. 2d 1025, 21 U.C.C. Rep. Serv. 183 (Fla. App. 1977).

140. *See* North Carolina Nat'l Bank v. Harwell, 38 N.C. App. 190, 247 S.E.2d 720, 25 U.C.C. Rep. Serv. 225 (1978); B. CLARK, *supra* note 2, ¶ 4.12[2], at 4-70.

141. *See* 622 West 113th St. Corp. v. Chemical Bank N.Y. Trust Co., 52 Misc. 2d 444, 276 N.Y.S.2d 85, 3 U.C.C. Rep. Serv. 1148 (1966).

4-212 makes it clear that the right of charge-back exists only prior to final payment. Consequently, any deduction must come as a result of the common law right of set-off.[142] The basis for this set-off must be that the collecting bank has breached its presentment warranty of good title[143] to the payor bank, and is therefore liable to it, and that the customer has likewise breached its transfer warranties of good title and genuineness of signatures[144] to the depositary bank and is in turn liable to it.

While not always discussing the issue in these terms,[145] the courts have reached the correct conclusion that the depositary bank cannot unilaterally choose to recognize the claim of forgery of the payor and debit the customer's account in the absence of proof of forgery.[146] That is, unless the bank can prove a forgery existed, the customer is entitled to have his account recredited, and presumably to be compensated for wrongful dishonor for those checks that bounced as a consequence of the bank's unjustified debit of the customer's account. The bank is a debtor to the creditor for the funds in the checking account[147] and cannot extinguish all or a portion of the debt without a legal basis. Checks that "bounce" as a result of the debit have been wrongfully dishonored since the bank has not legally decreased the amount of the depositor's funds on hand to pay his checks.

Some interesting issues also arise if a forgery *in fact* exists (assuming the depositor is not the culprit). For example, consider if the depositor, Doug in Example 7, had received the check in exchange for value from a thief who had stolen it and forged the payee's indorsement. Notwithstanding the depositor's good faith, he has breached his warranty of good title and his warranty of genuine signatures to the depositary bank. Does this alone entitle the depositary bank to set off the funds in his account? If so, is there not some duty on the part of the bank to give notice at the time it exercises its set-off right in order to prevent the depositor from "bouncing" checks on his account after the bank has deducted the amount of the check from his account?

There is a strong argument that the bank should be liable in negligence if the customer unknowingly writes checks after the set-off which then "bounce." While there are no cases which firmly establish liability in this case, banks do have a statutory responsibility to exercise ordinary care toward their customers in sending notice of dishonor or non-payment.[148] Fur-

142. *See* B. CLARK, *supra* note 2, ¶ 11.1, at 11-2.

> The legal right of a financial institution to approporiate the deposit of its customer upon the customer's default has long been considered holy writ. Setoff can be traced back to the doctrine of "compensatio"—the extinction of cross-demands—which found its way into Roman law about the time of Christ.

Id.

143. U.C.C. §§ 3-417(1), 4-207(1) (1977).

144. U.C.C. §§ 3-417(2), 4-207(2) (1977).

145. *See* 622 West 113th St. Corp. v. Chemical Bank N.Y. Trust Co., 52 Misc. 2d 444, 276 N.Y.S.2d 85, 3 U.C.C. Rep. Serv. 1148 (1966).

146. *Id. See also* Boggs v. Citizens Bank and Trust Co. of Md., 32 Md. App. 500, 363 A.2d 247, 20 U.C.C. Rep. Serv. 148 (Ct. Spec. App. 1976).

147. *See* B. CLARK, *supra* note 2, ¶ 2.1, at 2-2. "Although Article 4 does not say so in so many words, it is fundamental that the relationship is, at bottom, one between creditor and debtor." *Id.*

148. U.C.C. § 4-202(1)(b) (1977). While a set-off for breach of warranty is not technically a notice of dishonor or non-payment, the ultimate effect is the same.

ther, the bank is the customer's agent for collection,[149] and owes a duty of ordinary care to its principal, the customer.[150] Assuming that the customer was not aware of the forgery, the customer would have no reason to anticipate the set-off. In fact, since the check already would have been paid, the customer probably has forgotten all about it, and a set-off because of a breach of warranty would take the customer completely by surprise. It is certainly not unreasonable under these circumstances to impose a duty to notify the customer in advance so the customer does not unnecessarily bounce checks with the attendant embarrassment and potential damages.[151]

There are a number of cases, however, which have stated that no notice is required prior to the bank exercising its right of set-off,[152] and there appear to be none which have held to the contrary.[153] These cases, however, should be viewed with caution. First, in only one case was it asserted that the bank's failure to notify the customer prior to set-off constituted a breach of the bank's duty of care, and in this case the court decided that the bank had breached this duty because it gave earlier assurance that the funds would be available.[154] Thus, there are no cases in which a court has specifically held that the failure to give prior notice is not a breach of the duty of due care. Second, the traditional reason given for not requiring notice of set-off is inapplicable in this context. When set-off is applied against an overdue debt, the usual context in which set-off arises, it should not take the customer by surprise to find that the bank has used the funds on hand to satisfy the debt.[155] Therefore, it is arguable that the bank is not negligent by failing to notify the customer first. This is not the case, however, in the context of a breach of warranty by an innocent depositor. The depositor would generally have no way of knowing that the check contained a forgery, and thus would have no reason to expect that the bank would divert the funds. There are simply no cases which have dealt with the issue in this context, and it is, therefore, imprudent to assume that the general rule not requiring notice will be applied.

While the Code does not specifically require prior notice with respect to set-off,[156] the structure of the Code certainly suggests the implication of such

149. U.C.C. § 4-201 (1977).

150. RESTATEMENT (SECOND) OF AGENCY § 401 comment a (1958).

151. A similar case would involve a customer who draws checks prior to the set-off which are not presented for payment until a set-off has been made. In this case as well, the bank's duty of ordinary care should include a responsibility to notify the customer prior to dishonoring such checks for the reasons argued in the text above.

152. *See, e.g.*, Elizarraras v. Bank of El Paso, 631 F.2d 366 (5th Cir. 1980); Federal Deposit Ins. Corp. v. First Mortgage Investors, 485 F. Supp. 445 (E.D. Wis. 1980).

153. In a case in which the bank interpleaded a depositor's funds, the court analogized the interpleader, which caused a subsequent check to bounce, to a set-off for notice purposes. *Elizarraras*, 637 F.2d at 372. It recited the general rule that notice is not required prior to set-off, but held that since the bank gave earlier assurance that the funds would be available, it was required to give prior notice before interpleading them. *Id.*

154. *Id.*

155. *See, e.g., id.*

156. In fact, it does not deal with the set-off right at all except in section 4-303. Section 4-303 merely states that a payor bank cannot set off funds in the drawer's account to the extent that those funds represent items which have been "finally paid" under section 4-213 or items which have been accepted or certified by the bank. U.C.C. § 4-303 (1977). This is the only provision in Article 4 dealing with set-off and is not relevant in the context under consideration.

a requirement within the bank's obligation of reasonable care. As indicated above, the Code requires timely notice to a depositor if a provisional credit is charged back under section 4-212.[157] At a minimum, a failure to provide such notice will result in negligence liability.[158] Because a set-off, unlike a typical charge-back, will usually involve an item which has already been paid, the customer probably has a greater expectation that the funds represented by the check are available to him, and, thus, notice is even more important in the set-off context. In a similar context, compliance with stringent notice requirements is necessary to hold prior indorsers on their indorsement contracts,[159] the purpose of which, at least in part, is to prevent them from reasonably assuming from the passage of time that the check has been paid.[160] Certainly, there is little cost or risk to the bank in imposing such a duty; since its purpose is to preclude the customer from writing checks on funds which he does not have, the notice can be given concurrently with the actual set-off. Thus, there is little risk that the customer could withdraw the funds before the set-off is accomplished. Since the bank would provide notice of the set-off in any event,[161] there is little inconvenience in requiring it to be done prior to the actual reduction in the customer's account.

It has thus far been assumed that the bank's common law right of set-off permits it to deduct the amount of the check from the account if a breach of warranty has actually occurred. This assumption is problematic. The right of set-off is generally applied to cases involving an explicit contractual debt running from the customer to the bank.[162] There are, however, a few cases that deal explicitly with a bank's right to set off funds for a breach of warranty, although the results vary. Two cases from the 1960s permit the bank to set off a customer's funds for the damages caused by a breach of warranty.[163] In contrast, two Georgia cases indicate that while a bank may freeze a depositor's account pending a final determination of breach of warranty, it may not set off the depositor's funds in the absence of an express agreement permitting it to do so.[164]

More broadly, there are a number of cases that hold that the right of

157. *See supra* text accompanying notes 27-29.

158. *See supra* text accompanying notes 45-53.

159. U.C.C. §§ 3-502, 3-508 (1977).

160. *Cf.* B. CLARK, *supra* note 2, ¶ 1.3[4], at 1-22. The Code's distinction in subsections (a) and (b) of section 3-502 between discharge of indorsers and drawers in the case of unexcused delay "seems to be a reasonable distinction between indorsers, who never expected to have to respond on the check, and drawers, who should be discharged only if the delay injures them." *Id.*

161. Obviously, the customer's monthly statement would reflect the set-off. More likely, the bank would provide a separate notice of the set-off, along with notice of a "service charge" for depositing a forged instrument.

162. *See* Marine Midland Bank—N.Y. v. Graybar Elec. Co., 51 A.D.2d 903, 380 N.Y.S.2d 238 (1976), *aff'd*, 41 N.Y.2d 703, 395 N.Y.S.2d 403, 363 N.E.2d 1139, 21 U.C.C. Rep. Serv. 1094 (1977); Otto v. Lincoln Sav. Bank, 268 A.D. 400, 51 N.Y.S.2d 561 (1944), *aff'd*, 294 N.Y. 798, 62 N.E.2d 236 (1945).

163. Krinsky v. Pilgrim Trust Co., 149 N.E.2d 665 (Mass. 1958); F.I.N.N.E., Inc. v. National State Bank of Newark, 74 N.J. Super. 86, 180 A.2d 532 (Ct. App. Div. 1962).

164. *See* Friedland Properties, Inc. v. Citizens & S. Nat'l Bank, 148 Ga. App. 259, 251 S.E.2d 143 (1978); First National Bank of Gainesville v. Appalachian Indus., Inc., 146 Ga. App. 630, 247 S.E.2d 422 (1978).

set-off does not apply to an unmatured or contingent debt.[165] It can be argued that a claim of breach of warranty is more like a contingent or unliquidated debt than one which has matured. In the typical case involving a mature debt, there is little question whether a default actually occurred. It is generally clear that the depositor failed to make a payment when due, or breached some other provision of the loan agreement, causing the debt to mature. In warranty cases, there is often a hotly disputed question of fact as to whether a warranty has actually been breached, and thus whether the bank is entitled to damages.[166] For example, the result may turn upon the credibility of witnesses, including experts such as handwriting analysts, whether the payor acted in good faith in paying the check, and whether the person whose signature was "forged" authorized the signature, either actually or apparently. Thus, at the time the bank sets off the funds it is unlikely to be clear whether facts exist which make the depositor liable to the bank. This is especially unlikely where the depositor defaults on an express obligation to the bank.

E. *Alteration by Agreement*

Example 8. Hal opens a checking account with First Bank. He signs an agreement which states

> Customer agrees that First Bank shall have the right to charge back to the customer the amount of any item deposited for collection which is not actually collected by the bank. Customer agrees that the Bank shall have the right to charge back such amounts notwithstanding the failure of the bank to provide notice to the customer that it has charged the customer's account for such amounts.

Example 8 presents the obvious issue of whether the bank can avoid the notice obligation of section 4-212(1) via the deposit agreement. While there are no cases directly on point, a closely analogous case strongly suggests that a bank cannot contractually avoid the time limits of section 4-212(1). In *Sunshine v. Bankers Trust Co.*,[167] the bank was both the depositary and payor bank. The payee deposited a check in her account with the bank and was given a provisional credit. The same day, the bank was notified by the drawer that payment should be stopped. Three days later, the bank revoked the credit. The payee sued the bank to have her account recredited.

The New York Court of Appeals correctly recognized that the proper

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165. *See, e.g.*, Dockendorf v. Dakota County State Bank, 673 F.2d 961 (8th Cir. 1981); First Nat'l Bank of Gaylord v. Autrey, 9 Kan. App. 96, 673 P.2d 448, 37 U.C.C. Rep. Serv. 1329 (1983); Walter v. National City Bank, 42 Ohio St. 2d 524, 330 N.E.2d 425 (1975); Gillett v. Williamsville State Bank, 310 Ill. App. 395, 34 N.E.2d 552 (1941); Kane v. First Nat'l Bank of El Paso, 56 F.2d 534 (5th Cir.), *cert. denied*, 287 U.S. 603 (1932). There is authority, however, that this can be varied by agreement. *See, e.g.*, First Nat'l Bank of Gainesville v. Appalachian Indus., Inc., 146 Ga. App. 630, 247 S.E.2d 422 (1978).

166. Leonard Smith, Inc. v. Merrill Lynch, Pierce, Fenner, and Smith, 129 A.D.2d 397, 518 N.Y.S.2d 55 (1987); Capital Dist. Tel. Employees Fed. Credit Union v. Berthiaume, 105 Misc. 2d 529, 432 N.Y.S.2d 435 (Sup. Ct. 1980); Seattle-First Nat'l Bank v. Pacific Nat'l Bank of Wash., 22 Wash. App. 46, 587 P.2d 617, 25 U.C.C. Rep. Serv. 821 (1978); Sunshine v. Bankers Trust Co., 34 N.Y.2d 404, 358 N.Y.S.2d 113, 314 N.E.2d 860, 14 U.C.C. Rep. Serv. 1416 (1974).

167. 34 N.Y.2d 404, 358 N.Y.S.2d 113, 314 N.E.2d 860, 14 U.C.C. Rep. Serv. 1416 (1974).

section with which to begin its analysis was section 4-212(3).[168] This section permits a depositary bank which is also a payor to charge back the account of a depositor only if it does so within the time limits of section 4-301 (that is, by its midnight deadline). The *Sunshine* court stated that since the bank had not revoked the provisional credit within this time period, the check had been finally paid.[169] The bank attempted to avoid this result by pointing to two provisions in its agreement with the depositor which it argued gave it the right to charge back the account.[170] The court observed that "to the extent that either of the agreements attempts to extend the period during which the Bank can charge back a depositor's account in a situation such as the one before us now, they are invalid."[171] Accordingly, the court held that to permit this contractual alteration of the Code's payment structure in this manner would violate the portion of section 4-103 which precludes a bank from contractually disclaiming its responsibility to exercise ordinary care.[172]

Because the *Sunshine* decision involved a depositary bank which was also a payor and because the court determined that final payment had occurred, it is not precisely the same situation as Example 8. There are, however, no convincing reasons why the results should differ. Like subsection (1) of section 4-212, subsection (3) establishes time limits by which a collecting bank must charge back its depositor's account. There is no reason to believe from the Code or its comments that the reasons for the time limits in subsection (3) are any different from those established in subsection (1). In both cases the bank must notify the depositor within the same time period after the bank learns of the non-payment, that is, by its midnight deadline. Subsection (3), however, merely recognizes the fact that when a depositary bank is also the payor, it does not have to wait for notification of non-payment by the payor before it can notify the depositor. The reasons for not permitting the bank to extend the time period for charging back a depositor's account are no different or more compelling in *Sunshine* than they are in Example 8.

There are a number of cases in which the courts have permitted agreements between the payee of a check and the payor to extend the midnight deadline for payment,[173] but these are inapposite for a number of reasons.

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168. *Sunshine*, 34 N.Y.2d at 409, 358 N.Y.S.2d at 118, 314 N.E.2d at 863, 14 U.C.C. Rep. Serv. at 1421.

169. *Id.*

170. The first provision was in the bank's "Regulations Governing Special Check Accounts" which the depositor had signed and which stated:

> If claim is made to the bank for the recovery of any part of any collected items (including any item cashed for depositor) after final payment thereof, on the ground that such item was altered or bore a forged endorsement or was otherwise not properly payable, the Bank may withhold the amount thereof from the account until final determination of such claim.

The second provision was on the deposit slip and read:

> All items are credited subject to final collection and receipt of proceeds in cash or by unconditional credit to and accepted by Bankers Trust Company.

Id.

171. *Id.* at 410, 358 N.Y.S.2d at 119, 314 N.E.2d at 863, 14 U.C.C. Rep. Serv. at 1421.

172. *Id.*

173. *See, e.g.*, Idaho Forest Indus., Inc. v. Minden Exch. Bank & Trust Co., 212 Neb. 820, 326 N.W.2d 176, 35 U.C.C. Rep. Serv. 201 (1982); Western Air & Refrigeration, Inc. v. Metro Bank of Dallas, 599 F.2d 83, 26 U.C.C. Rep. Serv. 1248 (5th Cir. 1979); David Graubart, Inc. v. Bank Leumi Trust Co., 48 N.Y.2d 554, 423 N.Y.S.2d 899, 399 N.E.2d 930, 27 U.C.C. Rep. Serv. 1184 (1979).

These cases generally involve situations where a check is dishonored and the payee and payor expressly agree that the check will be resubmitted and be held by the payor for a reasonable period of time to await the deposit by the drawer of funds to pay it. When the funds are not deposited, the check is again dishonored and the payee then claims that the check has been paid because the bank has kept it beyond the midnight deadline. The differences between this situation and Example 8 are obvious. The cases do not involve a wholesale waiver of the midnight deadline, but rather a waiver involving a specific individual check *made for the convenience of the payee*, not the payor bank. Also, there is no possibility that the payee will assume merely from the passage of time that the check has been paid; rather, the payee is aware that the check has already been dishonored once and cannot assume that it will be paid in the ordinary course. Finally, permitting waiver of the midnight deadline by agreement in such a case does not undermine the incentive effect of the midnight deadline to process items quickly and efficiently. While superficially similar, these cases are fundamentally different from the kind of case presented by Example 8, a fact which some courts have appeared to recognize.[174]

CONCLUSION

This Article has illustrated some difficult problems which arise when a depositary bank attempts to recapture funds from a customer, and has suggested possible approaches and resolutions. The most difficult issue, and the one which most frequently appears in the cases, involves the failure to provide timely notice under section 4-212. This issue merits some final comment. Notwithstanding the confusion, one thing is relatively clear: the drafters intended the time limitations imposed by Article 4 to provide a substantial incentive for timely processing of items and the smooth and efficient operation of the collections system.[175] That the Code's structure and the time limitations therein may occasionally result in a loss to the bank and a "windfall" to someone else was also clearly understood and contemplated by the drafters.[176] It is the conclusion of this author that short of bad faith or fraud, the opportunity for a bank to restore its position after it has missed a clear and explicit time limitation established in Article 4 should be extremely limited or should not exist at all. The incentive effect of this approach can-

174. *See Western Air & Refrigeration*, 599 F.2d at 90 n.8, 26 U.C.C. Rep. Serv. at 1257 n.8; *David Graubart*, 48 N.Y.2d at 560-61, 423 N.Y.S.2d at 903-04, 339 N.E.2d at 934, 27 U.C.C. Rep. Serv. at 1191.

175. *See, e.g.*, Fairfax Leary's 1947 general commentary on proposed Article IV, Chapter II, Bank Collections. F. Leary, Notes and Comments to Article IV, Chapter II, Bank Collections, Llewellyn Papers, *supra* note 30, at 4.

> § 1. Finding and Declaration of Policy, [stating that] speed and certainty in the processes of bank collection are of advantage to depositors in banks and to the stability and safety of their accounts, . . . and that reduction of the quantity of uncollected float to safe, effective, and speedy use . . . is a purpose which both justifies and requires standardization of contracts of deposit and collection as provided in this chapter.

Proceedings of the Larger Editorial Board of the American Law Institute 239 (Jan. 1951), Llewellyn Papers, *supra* note 30 (comments of Mr. Malcolm).

176. *See, e.g.*, Minutes of A.L.I. Meeting (May 20-22, 1948), Llewellyn Papers, *supra* note 30, at 129, 150.

not be denied; it can even be argued that an interpretation imposing absolute liability on the banks is inappropriate because it is an incentive to take "too much" care. That is, it imposes costs on the bank for losses which it did not cause, and is, therefore, both inequitable and inefficient.[177]

But, as has been demonstrated, the rule certainly imposes no great inequities and may, in fact, result in the prevention of some losses which would be unprovable if proof were required. Moreover, there are corresponding efficiencies, particularly administrative and adjudicative, which are fostered by a bright line rule with fewer difficulties of proof. The drafters' choice as to the final payment rules is clear: a holder should not be required to show a loss in order to hold the bank accountable for an item if the payment time limits are not met. There is no compelling argument distinguishing this case from the ability of a depositary bank to charge back a depositor's account under section 4-212.

At the very least, the failure to meet the midnight deadline established in section 4-212 should raise a strong presumption in favor of the customer that the depositary bank's delay has caused him to detrimentally rely on the payment, thus shifting the burden of proving, perhaps by clear and convincing evidence, whether reliance occurred as a result of the delay. Unfortunately, many of the recent cases that have allowed the depositary bank to recover apparently place this burden on the customer,[178] while others are unclear.[179] To place this burden on the customer is inappropriate in view of the purpose of the time limitation and the liberal grant in section 4-212 of a "longer reasonable time" to provide the necessary notice. While there is nothing in the Code which specifically sanctions the imposition of this heavy burden of proof on the bank, there is certainly nothing to preclude it.

More generally, this Article has attempted to demonstrate that serious difficulties exist in the Code's treatment of the charge-back and set-off rights

177. It could be argued that such a rule is inequitable because it requires the bank (and ultimately its customers) to be responsible for losses unrelated to its behavior. It is a fundamental tenet of tort law that unless careless behavior actually causes a loss, it is unfair to impose liability. W. KEETON, PROSSER & KEETON ON THE LAW OF TORTS § 41 (5th ed. 1984). Arguably, where those who ultimately bear the loss (the customers) are completely innocent, liability is even more inappropriate.

Such a rule may be inefficient in that the bank may expend resources to prevent late notice where no loss would be suffered if the notice had been late and the resources were not expended. For example, assume that if the bank expended no funds to prevent late notice, depositors would suffer $5000 in damages as a result of late notice. If the bank is liable for these losses it will be willing to spend an amount to prevent such losses up to a point where the prevention costs and the cost of losses just equal $5000. This expenditure will be "efficient" because the gains through prevention will necessarily be no greater than the costs associated with the prevention. Assume, however, that the bank will have to pay out $50,000 to its depositors if it is made strictly liable for late notice and it takes no preventive measures. Again, it will expend funds to prevent these payments up to a point where the prevention funds plus payments just equals $50,000. Forty-five thousand dollars of these funds, however, will be expended with no corresponding reduction in losses to others. These expenditures are non-productive; they represent funds expended to prevent a transfer payment which could be prevented simply by changing the rule imposing liability. Thus, the rule is inefficient since these funds could be expended in productive ways if the rule were otherwise.

178. *See, e.g.*, Appliance Buyers Credit Corp. v. Prospect Nat'l Bank of Peoria, 708 F.2d 290, 36 U.C.C. Rep. Serv. 231 (7th Cir. 1983); Northpark Nat'l Bank v. Bankers Trust Co., 572 F. Supp. 524, 37 U.C.C. Rep. Serv. 385 (S.D.N.Y. 1983).

179. *See, e.g.*, Greer v. White Oak State Bank, 673 S.W.2d 326, 329, 39 U.C.C. Rep. Serv. 929, 933 (Tex. Civ. App. 1984).

of depositary banks. Some of these difficulties result from erroneous court decisions, while others result from omissions or ambiguities in the Code itself. This Article is intended to provide a starting point for the development of a more consistent and coherent body of law dealing with these important rights.