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Dexter Delony

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THE PRESENTMENT PROBLEM IN THE COLLECTION OF CHECKS THROUGH BANKS

DEXTER DELONY*

The drawer on a check wants to pay a debt, frequently for goods purchased, and proceeds to accomplish this through his agent, the drawee bank. The payee wants to receive payment for the goods sold and proceeds to accomplish this through his agents, the depository bank and subcollecting banks. Visually, and to a degree functionally, one may think of the drawer and his agent as lined up on one side and the payee and his agents on the other. Presentment is the process by which the two groups are brought together for the purpose of accomplishing check collection. A check collection is payment that may (1) discharge the drawee's obligation to the drawer, (2) discharge the drawer's obligation to the payee, (3) discharge the collection agent's obligation to the payee, and (4) incidentally discharge the liability of sureties, including the liabilities of the drawer and the indorsers on the check. It is worth noting that many if not most of the aspects of these obligations, except perhaps those of the indorsers, rest upon law or contract beyond the check itself. For instance, the drawee's obligations to the drawer spring from the depositor's contract; a large part of the drawer's obligation to the payee comes from an underlying debt, for example, the purchase price owed under a sales contract; the surety's duties flow from suretyship law; and the collection agent's obligation to the payee is, in addition to negotiable instruments law, founded on agency, contract, negligence, and other law. Obviously a number of parties have an interest in the presentment process, which is the legal responsibility of the payee-holder; the objective of this responsibility is to demand payment at a time, under circumstances, and in a manner most likely to produce payment. The collection agent assumes this responsibility on behalf of the payee in the sense of fulfilling the payee's duties to the other parties and in the interest of the payee, in the sense of going beyond his bare duties to others and pursuing with due diligence the payee's primary objective of converting the check into value acceptable to him.

*B.S. 1936, LL.B. 1939, University of Alabama; LL.M. 1941, Harvard University; Professor of Law, University of Florida.

This paper will discuss the trouble spots in the presentment process, with particular attention drawn to the special problems of the bank collection agent, caused largely by rapid economic growth and the resulting increase in the use of checks with too little adjustment of the law applicable to check collections.

FACTUAL BACKGROUND

No doubt the present-day economy could not operate without the tremendous service afforded by banks. But the significance of this fact and its importance to an understanding and analysis of the law applicable to the presentment problem in check collections make it worth emphasizing. The economy rests on commercial transactions, and commercial transactions are largely made up of the sale of merchandise and the payment therefor, usually by the use of credit. In our credit economy, banks, primarily through the negotiable instrument tool, provide the means for credit, with the resulting mass distribution of goods.¹ The history of the growth of the economy could well be written around the development of the efficiency of the means of payment for goods purchased — “means” in the sense of the mechanics available for payment, and only indirectly in the sense of economic wealth. The responsibility for this means rests heavily on the law.

Since social stability to a degree is desirable, one can appreciate the often repeated remark that in order to gain social stability the law must lag behind the other sciences by refusing to accept and apply newly developed theories until thoroughly tried and proved to be good for society. There are eminent physicians today who cry out in protest at the law's refusal to utilize theories developed by medical science that, in their opinion, would greatly aid the administration of justice. We know how tenaciously Chief Justice Holt at the turn of the seventeenth century held to strict common law contract principles in opposition to the use of negotiable instruments, referring to them as things “invented in Lombard Street which attempted in these matters of bills of exchange to give laws to Westminster Hall.” This effort by merchants and their lawyers, according to Chief Justice Holt, “proceeded from obstinacy and opinionativeness.”² Long before 1700 merchants watched the stifling of trade, the braking of distribution of

¹For a study of the history and function of the modern market see POLANYI, *THE GREAT TRANSFORMATION* (1944).

²*Clerke v. Martin*, 2 Ld. Raym. 758, 92 Eng. Rep. 6 (K.B. 1702). Lombard Street, referred to by Justice Holt, was at that time the business and financial district of London.

goods and thus the slowing of a rising living standard by such cumbersome means of payment as the hauling of gold or money from one place to another, with all the risks and limitations involved. Merchants somewhat overcame this obstacle to payment for goods purchased, not with the aid of the law but to a degree in spite of its opposition, by the development of the bill of exchange. It was a method of transferring funds; its function as a significant credit instrument came later. The need of people in trade caused the development of the check, and this same need demanded that banks or some similar institutions serve the economy through the check. It is agreed that the law should lag, but the interests of society require that it not lag too far, hence the necessity for the law constantly to take a critical attitude in the application of set rules to changing circumstances. Are the principles of law that are applicable to a particular social or economic problem, presentment, for instance, the best, or even adequate? To determine this, a view must be taken of what society needs or — better perhaps, considering the limitations on our power to determine that tall order — what society wants.

There is every indication that the social values of the present time and place highly regard the benefits of mass distribution of goods. Payment for goods purchased involves two problems: making the necessary funds available, which most frequently today means making credit available, and transferring the funds or credit from one place to another. Banks serve heavily in both areas; and, although checks are used primarily in the second problem area, their use also involves availability of credit. As of December 31, 1952, there were 4,909 national banks and 1,889 state banks that were members of the Federal Reserve System, a total of 6,798 members. The non-member banks numbered 7,248, plus 529 mutual savings banks, making a total of 14,575 banks in the United States. From 1941 to 1952 the number of members of the Federal Reserve System increased by nearly 200, whereas the total number of banks decreased during this period by almost 250.³ Of this number not many were failures. Part of the decrease resulted from the large expansion of branch banking, consolidations, and the like. On December 31, 1952, the total amount of money in circulation in the United States was \$30,430,000,000.⁴ Five years later this amount had increased by a mere \$184,000,000.⁵ In

³Trade and Securities Statistics on Banking and Finance (June 1957) (Standard & Poor).

⁴U.S. TREAS. DEP'T REP. (1952).

⁵FED. RESERVE BULL. (July 1957).

centers that reported to the Federal Reserve System alone, debits to demand deposit accounts, not including interbank and federal government accounts, amounted in the year 1952 to \$1,642,853,000,000, and in the month of January 1957 amounted to \$204,435,000,000.⁶ It is estimated that the number of checks issued in the United States in 1953 was around eight billion, with a value of \$1,900,000,000,000.⁷ This means that within this period of time eight billion separate payments in the amount of nearly two trillion dollars were made through bank operations by the use of money and credit, but primarily the latter. The 1957 rate of bank debits to demand deposit accounts suggests a total for the year of well over two trillion dollars.⁸

These figures give some indication of the magnitude of check collections. Since an appreciation of the functions of banks and their interrelation in the economic objective of mass distribution of goods is important to an examination of only one or two of the legal problem areas involving collections, it should be noted that banks facilitate distribution of goods not only by the tremendous check collection volume but also by supplying credit and collecting promissory notes and bills of exchange other than checks, with or without documents of title attached such as bills of lading or warehouse receipts, all of which involve the law applicable to presentment for payment.

Bills of exchange other than checks, or drafts as they are more commonly called in the business world, are used extensively in business for a variety of purposes, such as transferring funds, including collecting accounts and financing the movement of goods and commodities. Usually the services of banks are needed in each of these cases.

For example, assume that X Company of Jacksonville has sold goods to Y in Chicago on credit and is experiencing difficulty in collecting the account. As a final measure, it may decide to draw a draft on him, thereby definitely putting it up to him to agree to pay by a certain time. The X Company, the drawer, gives the draft to the Z National Bank of Jacksonville for collection, and the latter indorses and forwards it to its correspondent bank in Chicago. The Chicago bank presents it to Y, the drawee, and requests his acceptance. Y is, of course, under no legal obligation to accept the draft, since the owing of a debt imposes no duty upon the debtor to make a new form

⁶*Ibid.*

⁷72 BANKING L.J. 251 (1955).

⁸FED. RESERVE BULL. (July 1957).

of contract for its payment. If, however, *Y* values his business reputation, he may not wish to go on record as being unwilling to pay his debts. If he decides to accede to the demand, he will accept the draft. Suppose that he accepts it payable at the Cook County National Bank, Chicago. The correspondent bank in Chicago either returns the draft to the *Z* National Bank or holds it for collection, in accordance with instructions. In the latter event, it presents the draft at the Cook County National Bank at maturity and demands payment. If paid, it remits to the *Z* National Bank, which credits the *X* Company's account. If the acceptance is not honored, the *X* Company at least possesses a written acknowledgment of the debt, upon which it can sue with greater facility. Even if a drawee debtor refuses to accept a draft, the drawer creditor is in no worse position than he was originally, since he may still sue on the original debt.

Banks and bills of exchange or drafts also greatly facilitate the financing of shipments of goods. A merchant, manufacturer, or dealer is always faced with the problem of obtaining as promptly as possible payment for goods sold. In a few lines of business, sales are for cash only; in others credit is extended in the form of charge accounts; in many, payment upon delivery or within a certain number of days is demanded in the form of a draft. The shipment of goods accompanied by a draft offers a very satisfactory method of collecting accounts, and it is widely used. Suppose that the *A* Company of Philadelphia sells goods to *B*, a partnership firm of Cleveland. The shipment is a large one, and the *A* Company is not entirely satisfied with the credit rating of *B*, or its business is such that it must keep its funds liquid by quick collections. It therefore arranges for payment by draft upon delivery of the goods. Accordingly, the goods are shipped, and the company obtains a bill of lading from the railroad. It then draws a bill of exchange or draft on *B*, payable on sight. The *A* Company delivers the draft, with bill of lading attached, to its bank and directs that it be forwarded to a Cleveland correspondent bank for presentation to the drawee, *B*, upon arrival and inspection of the goods by him. If the shipment is satisfactory, the drawee pays the draft and the bank surrenders the bill of lading to him. The Cleveland bank remits to *A* Company's bank, and the transaction is closed.

Another common scheme for the extension of credit is the use of the trade acceptance. Here again the purpose is to obtain payment for goods sold, but this time credit is extended for a certain period agreed upon by the buyer and the seller. Assume that the Acme

Manufacturing Company of New York sells goods to the New Bedford Company in New Bedford, Massachusetts, payment to be by sixty-day draft. The goods are shipped; a bill of lading is obtained, and the Acme Manufacturing Company draws a draft on the New Bedford Company, payable sixty days after sight. This draft with bill of lading attached is delivered to Acme's bank, which forwards it to its correspondent bank in New Bedford. The New Bedford bank presents the draft to the New Bedford Company, and if the goods are as ordered the company will accept the draft. The bill of lading is surrendered to the acceptor; and the draft, now a trade acceptance, is returned through the banks to the Acme Manufacturing Company, which may hold it until maturity or discount it at its bank, thereby getting immediate cash for the sale. Such paper is highly regarded by banks. It has behind it the credit of the acceptor and the credit of the drawer, the acceptor having sold his credit for presently received goods that afford the means of making money as opposed to financing an old debt. It may be discounted readily at a federal reserve bank.

An additional method of financing the movement of goods is the use of the bank acceptance. For instance, suppose that George Buyer of Philadelphia wishes to buy goods from Aaron Sellers of Baltimore. Buyer's credit standing is not sufficiently good in his own name, but he is in good standing at the Exchange National Bank of Philadelphia, which agrees to finance him within certain limits. Sellers is willing to sell the goods on the well-known credit of the Exchange National Bank. Accordingly, after notification by Buyer, Sellers ships the goods and draws a bill of exchange on the Bank for the amount of the shipment. This bill, with negotiable bill of lading attached, is then sent through Sellers' bank to the Exchange National Bank, which writes its acceptance across the face and returns it to Sellers. Sellers may hold it or discount it, as he sees fit. It is readily salable because of the high standing of the acceptor, the Exchange National Bank. Meanwhile, the Exchange National Bank and Buyer have made arrangements for disposition of the bill of lading. Buyer has already agreed to provide the Bank with funds to pay the acceptance when it falls due. The Bank, having confidence in Buyer, lets him have the bill of lading, carrying with it possession of the goods. The Bank may require a trust receipt; if so, it holds the trust receipt until the transaction is closed. It will be noted that the bank acceptance accomplishes several useful results: (1) it enables Sellers to make a sale that he would otherwise be unwilling to make; (2) it secures payment in a highly desirable negotiable form; (3) it enables Buyer to buy goods

in places where his credit is unknown; and (4) it provides a medium for the use of bank funds.

Banks perform other types of collection services, including installment contracts, bonds, and the bond-a-month club, whereby the bank collects from its depositors the cost of bonds that the depositors have previously agreed to buy. In fact, over seventy life insurance companies, including some of the most prominent ones in the country, offer policies that permit the collection of premiums by the companies through banks without "bothering" the policyholder. It amounts simply to the premium payer giving the insurance company authority to collect premiums, usually at monthly periods, directly from the bank that carries the policyholder's checking account. Some companies refer to the plan as a "painless" way to pay insurance. In any event, the companies are convinced that the plan has increased insurance sales; it apparently is another demonstration of the promotion of commercial transactions by improvement of the mechanics of payment.⁹ Some banking circles, however, look with disfavor on the plan. A special commission of the American Bankers' Association states: "We believe it to be fundamentally wrong for the depositor, in a sense, to lose control of his account and operationally wrong from the point of view of the banks." Further, the Association believes that the plan makes checking accounts expensive and cumbersome to handle and makes the problems of forgery and overdraft more acute.

Consider the tremendous task of a bank that must process 100,000 checks each business day, processing that may involve more than mere detection of forgery if it stays within prudent bounds from the point of view of its potential legal liabilities. The Atlantic National Bank of Jacksonville, Florida, reports that it processed a daily average, during the 182 business days from January through July, 1957, of 102,208 checks, which included checks drawn on it as well as those in transit to other banks for collection. The bank further reports that

⁹According to a syndicated newspaper column covering business affairs which appeared in Jan. 1958, the oil companies have found a method for the improvement of the mechanics of payment by their customers that has promoted sales. The method is the extensive use of the plastic embossed credit card, which cuts the time needed for a service station transaction and permits the handling of accounts through electro-mechanical computers. The companies report that nearly one third of the service station sales are handled through the credit card device. Three companies alone report that 6,250,000 customers use these cards. The practice is also spreading to hotels, the American Hotel Association having issued about 120,000 cards.

it inspected each check for indorsements and irregularities and placed its guaranteed indorsement on checks forwarded for collection.¹⁰ Many banks carry even heavier loads, under laws in most instances formulated without the perspective of the great demands made on banks today. For instance, the present negotiable instrument law relating to collections fundamentally envisions personal presentment over the counter for money,¹¹ with little or no thought of mail presentment for collection. A good guess, however, is that, just as banks have met many demands in the past for collection services by performance, they will meet this demand from insurance companies and many more from other sources that are bound to come; and if the results are desirable from society's point of view the law should make reasonable adjustments to implement the service.

Some of the services demanded of banks, such as the bond-a-month plan, can be implemented satisfactorily by contract; but others need definitive laws especially designed to meet the problems involved. To be an improvement this special design must recognize the need in certain areas for definiteness, achieved through clearly defined non-waiver provisions, and in other areas for flexibility, achieved through clearly defined waiver provisions,¹² the latter effectuated by contract in a form that will avoid such pitfalls as the "small print" or against-public-policy or no-consideration type of litigation.¹³ New and more efficient mechanical means of payment are in the same general category, from the point of view of the development of society, as the automatic calculator and other instruments of automation now available or on the horizon. Perhaps soon some device may be developed that can better perform the jobs of paper money and the check. The law will have to be on its toes to keep from lagging further behind than society's interests require.

In the meantime the law should face up to the present facts of

¹⁰Letter from Comptroller, Atlantic Nat'l Bank of Jacksonville, Aug. 14, 1957. The Citizens Bank of Gainesville, Fla., a relatively small bank, reported that it handled 7,497 checks during one business day in Aug. 1957, 2,633 drawn on it and 4,864 in transit drawn on other banks.

¹¹*E.g.*, National Reserve Bank v. National Bank, 172 N.Y. 102, 64 N.E. 799 (1902); Winchester Milling Co. v. Bank of Winchester, 120 Tenn. 225, 111 S.W. 248, 18 L.R.A. (n.s.) 441 (1907).

¹²In order to gain flexibility in certain relationships the law should practice silence, so that there would be no necessity for contractual waiver.

¹³*E.g.*, Reinhardt v. Passaic-Clifton Nat'l Bank and Trust Co., 16 N.J. Super. 430, 84 A.2d 741 (1951), *aff'd*, 9 N.J. 607, 89 A.2d 242 (1952).

payment, which means primarily check collections, and most particularly the presentment aspect. *S* in Xville sells merchandise to *B* in Yville. *S* wants the bargained-for equivalent, that is, money or comparable value. How does he get it? Usually commercial necessity, convenience, custom, or all three require that *S* take a check from *B* drawn on *B*'s bank in Yville. The result *S* wants is collection, namely, the turning of the check into money or comparable value in *S*'s hands with assurance that it cannot be taken away from him so far as this transaction is concerned. No collection should be considered complete until *S* gets money or something, usually bank credit, that he elects to take in lieu of money. Election involves identification of the thing elected, such as credit or other item of value, and, if credit, what type of credit and to what bank or other legal entity the credit is extended. Yet is it not often true that commercial necessity, convenience, and custom require that *S* take bank credit, with the risks attaching thereto, in lieu of money as payment?¹⁴ Does an active businessman elect to have a bank checking account? But risk in this aspect of the commercial transaction is another story; attention here is directed to a few of the problems of *S*, and particularly of his collection agents, from the time he receives the check to the time of collection, or perhaps discharge, of the check.

Payment for goods is a function that society needs to have performed efficiently; hence this function is the key to the analysis of the laws applicable to payment, including presentment. As indicated above, *S*, the payee-seller of goods, is helpless regarding many of his "elections." Services now performed by banks as check collection agents are essential; the law in distributing the risks involved should adjust to these facts. Collecting a check involves risks. *S* should be able to get his bargained-for value without undue risks or costs. Risks placed on collection agents increase the cost of collection. Collection agents are not public utilities; costs are paid by the principals. Increased cost operates against the efficiency of payment and thus bears upon the efficiency of the distribution of goods.

THE BASIC PROBLEM

Presentment for payment is not necessary in order to charge par-

¹⁴To a degree the federal government has recognized an economic need and lack of true election in many cases involving acceptance of bank credit by providing for insurance coverage of certain risks and regulatory laws designed to reduce risks.

ties primarily liable.¹⁵ This common law principle was codified by section 70 of the Negotiable Instruments Law.¹⁶ Primary parties are liable for the period of the statute of limitations, which begins to run at the time of the maturity of the paper. Ordinarily it is held that a demand obligation is due at the time it comes into being, and therefore the statute of limitations starts running against the liability of the primary party on the date of the creation of the demand obligation.¹⁷ An exception is the liability that a bank owes its depositor under the depositor's contract. In this case the statute does not start running against the bank's liability until demand is made.¹⁸ This conclusion is based upon the function performed by the bank deposit.

Unless the right to presentment is waived, parties secondarily liable — the drawer¹⁹ and the indorsers²⁰ — will be discharged from liability if the holder fails to make due presentment of the paper for payment to the party primarily liable²¹ — the maker or the acceptor. In the case of an unaccepted draft or check due presentment must be made to the drawee.²² The discharge applies to the liability of secondary parties as sureties and as warrantors of payment.²³ Presentment is not a requisite for the creation or continuation of liability on a warranty of genuineness or warranty of legal capacity of the parties to the instrument.²⁴ The position of secondary parties on negotiable instruments is comparable in many respects to the rights and duties of sureties under suretyship law, but it should be noted that by the weight of authority a surety in the ordinary case has no right to have

¹⁵Rottman v. Hevener, 54 Cal. App. 474, 202 Pac. 329 (1921); Binghamton Pharmacy v. Memphis First Nat'l Bank, 131 Tenn. 711, 176 S.W. 1038 (1915).

¹⁶Rodriguez & Arieux v. Hardouin, 15 La. App. 112, 131 So. 593 (1930).

¹⁷State Trust & Sav. Bank v. Malitz, 44 S.W.2d 1070 (Tex. Civ. App. 1932).

¹⁸Harris v. Neuman, 179 Ga. 879, 177 S.E. 698 (1934); Missouri Pac. Ry. v. Continental Nat'l Bank, 212 Mo. 505, 111 S.W. 574 (1908); Koelzer v. First Nat'l Bank, 125 Wis. 595, 104 N.W. 838 (1905).

¹⁹NEGOTIABLE INSTRUMENTS LAW §61, Simonoff v. Granite City Nat'l Bank, 279 Ill. 248, 116 N.E. 636 (1917).

²⁰NEGOTIABLE INSTRUMENTS LAW §66, Eastman v. Pelletier, 114 Vt. 419, 47 A.2d 298 (1946).

²¹NEGOTIABLE INSTRUMENTS LAW §70, Gilman v. F. O. Bailey Carriage Co., 125 Me. 108, 131 Atl. 138 (1925).

²²County Board of Educ. v. Slaughter, 230 Ala. 229, 160 So. 758 (1935); Haefner v. First Nat'l Bank, 70 Ohio App. 293, 44 N.E.2d 489 (1942).

²³Lyons v. Hager's Adm'r, 278 Ky. 99, 128 S.W.2d 196 (1939); cf. Brown v. Peoples Bank, 59 Fla. 163, 52 So. 719 (1910).

²⁴See NEGOTIABLE INSTRUMENTS LAW §66, Security Trust Co. v. Giglio, 4 N.J. Misc. 350, 132 Atl. 651 (Sup. Ct. 1926).

the creditor make demand on the primary debtor for payment.

As far as the date and place are concerned, due presentment, in the case of time paper, means demand for payment on the day it falls due,²⁵ at a reasonable hour, at the place specified; and, if no place is specified, then at the business or residence address of the person to whom presentment is to be made.²⁶ If the instrument provides that it is payable at a designated bank, presentment should be made at the bank. This does not mean that the holder has to wait at the bank for the payor. It simply means that the bank is agent of the payor for the purpose of receiving presentment.²⁷ In the case of death of the party primarily liable or the drawee, presentment must be made to his personal representative.²⁸ It is emphasized that due presentment, among other things, requires timely presentment; however, there is a provision in the law, not too liberally construed, to the effect that delay may be excused if it is caused by circumstances beyond the control of the holder, or his agent, and is not imputable to his default, misconduct, or negligence.²⁹ Also the drawer has no right to have presentment made if he has no reason to expect the drawee to pay the instrument,³⁰ for example when the drawer of a check has no money in the drawee bank. Likewise the indorser would have no right to have presentment made if the instrument were made by the maker or accepted by the acceptor for the indorser's accommodation, leaving the indorser with no reason to expect that the instrument would be paid if it were presented to these parties.³¹

TIMELY PRESENTMENT OF DEMAND PAPER

The problem of timely presentment of demand paper is one of the most serious and troublesome of all the presentment problems, largely because of the uncertainty and unreasonableness of the law regarding what constitutes timeliness.

²⁵NEGOTIABLE INSTRUMENTS LAW §71.

²⁶*Id.* §§72, 73.

²⁷*Id.* §§75, 87; *cf.* *German Amer. Bank v. Milliman*, 31 Misc. 87, 65 N.Y. Supp. 242 (County Ct. 1900).

²⁸NEGOTIABLE INSTRUMENTS LAW §76, *Piper v. Hayward*, 71 Misc. 41, 127 N.Y. Supp. 240 (Sup. Ct. 1911).

²⁹NEGOTIABLE INSTRUMENTS LAW §81, *Joerns Bros. Mfg. Co. v. Burns*, 173 Minn. 389, 217 N.W. 506 (1928).

³⁰NEGOTIABLE INSTRUMENTS LAW §79.

³¹*Id.* §80.

The Promissory Note

Indorsers are the only parties to a promissory note who are secondarily or contingently liable.³² In order for the holder to preserve the liability of an indorser on a demand note, he must present it to the maker for payment within a reasonable time after the note is issued.³³

The question is, what is a reasonable time? The best help that one can get from the Negotiable Instruments Law is the reference to reasonable time in section 193. This section provides that in determining what is a "reasonable time" or an "unreasonable time" regard is to be had to the nature of the instrument, the usage of trade or business, if any, with respect to such instrument, and the facts of the particular case. As to what is a reasonable time within which a demand note must be presented to the maker in order to preserve the secondary liability of indorsers, the cases vary from two months,³⁴ and in a few extreme cases even less,³⁵ up to one year,³⁶ and in some cases more.³⁷ Perhaps this wide spread of cases can be explained on the basis of proof of custom or usage in the particular business in which the note was used and the facts of the particular case, such as whether the note bore interest. The nature of a demand note, which differs from that of a draft or check, makes the period of reasonable time for presentment longer than that for a draft or check. For instance, although the holder of a demand note can demand payment and enforce the note against the maker immediately after it is issued, obviously neither the maker nor the payee expects demand to be made. If they did, the maker would pay money and the

³²See *id.* §66.

³³See *id.* §71.

³⁴*Plymouth County Trust Co. v. Scanlan*, 227 Mass. 71, 116 N.E. 468 (1917); *Merritt v. Jackson*, 181 Mass. 69, 62 N.E. 987 (1902); see *Eastman v. Pelletier*, 114 Vt. 419, 47 A.2d 298 (1946).

³⁵See *Bank of Mt. Airy v. Greensboro Loan and Trust Co.*, 159 N.C. 85, 74 S.E. 747 (1912).

³⁶See *White v. Wadhams*, 204 Mich. 381, 170 N.W. 60 (1918); *Schlesinger v. Schultz*, 110 App. Div. 356, 96 N.Y. Supp. 383 (1st Dep't 1905); *Patchogue Bank v. Ambrose*, 278 App. Div. 582, 101 N.Y.S.2d 979 (2d Dep't 1951); *New Rochelle Securities Co. v. International Thrift Soc'y*, 244 App. Div. 810, 279 N.Y. Supp. 772 (2d Dep't 1935); *Kurt v. Defren*, 76 N.Y.S.2d 634 (Sup. Ct. 1947).

³⁷*In re Dashnau's Estate*, 194 Misc. 156, 88 N.Y.S.2d 13 (Surr. Ct. 1948); *Van Buren v. Wensley*, 102 Misc. 248, 169 N.Y. Supp. 789 (Sup. Ct. 1918); *Hussey v. Sutton*, 96 Misc. 552, 160 N.Y. Supp. 934 (Sup. Ct. 1916).

payee would demand money, and neither would resort to a demand note. Clearly, then, a demand note is a credit instrument by which all parties intend that some time shall elapse between the date of issue and the date of demand. Therefore, as the indorser, who voluntarily became a party to such an instrument, passes it on to another party he has no right to expect presentment within the next day or even few days. The best test as to what he does have a right to expect is the custom and usage pertaining to such instruments in the particular locality in which the case arises. The fact should not be overlooked that the heart of the problem under consideration is protection of the interest of the indorser without undue prejudice to the interests of others. Some insight may be gained by asking the question, What does the indorser have a right to expect? A good rule of thumb for use in practice is that presentment should be made within three months from the date of issue unless there is a clear fact, such as the interest clause in the note, indicating a longer period. The rule is nothing but a suggested course of procedure that seems reasonably safe. The law is not clear as to what the holder's duty really is. The number of negotiations has no bearing on it.

The Bill of Exchange Other Than the Check

By the nature of a demand bill, the drawer and the indorsers have a right to expect that the holder will present the paper to the drawee or to the acceptor within a period of time normally less than that of a note. Again, the heart of the problem is the protection of the interests of the drawer and the indorsers. What do they have a right to expect? The demand bill may perform the function of a credit instrument, but more likely its chief function is the transfer of funds. The holder must assume that the drawee owes the drawer money and that the drawer may be prejudiced unless demand is made on the drawee forthwith. In a sense one may think of the holder as an agent for the drawer for the purpose of making demand on the drawee for money owed by the drawee to the drawer. Probably the holder is not a true agent; but, by electing to take the draft, he assumes the obligation to make the demand in order to prevent the drawer from being prejudiced. Theoretically the drawer's reliance on the holder induces the drawer not to make demand personally. Failure to make demand on the drawee forthwith may also prejudice indorsers on the theory that if demand on the drawee had been made forthwith after indorsement the drawee might have paid; in that event the liability

of the indorser, other than the contingent liability, would never have arisen. Hence there is a resulting rule of law that the drawer and the indorsers are discharged on a demand bill unless presentment for payment to the drawee is made within a reasonable time.

What is a reasonable time? The Negotiable Instruments Law again leads to the vague standards of section 193. In order to preserve the liability of the drawer, courts have held that if the holder and the drawee are in the same locality presentment must be made before the close of the next business day after issue, and that if the drawee and the holder are in different localities the holder must, before the close of the next business day, initiate the normal process of collection, such as transferring the instrument to a local bank for collection.³⁸ In some cases the period is extended if there is evidence that prompt presentment is not contemplated by the parties,³⁹ but generally the law has been entirely too rigid in applying the next business day rule. In the case of an indorser on a demand bill, the cases are reasonably consistent in holding that the holder of the instrument must present to the drawee by the close of the next business day after indorsement and delivery if the drawee and holder are in the same locality; if not, then he must start the normal process of collection before the close of the next business day after indorsement.⁴⁰ Again, if the evidence shows that the parties do not contemplate the usual time for presentment, a longer period may be allowed in accordance with the special evidence.⁴¹ It is to be noted that in the case of the drawer the reasonable time starts running at the time of issue, whereas in the case of the indorser the reasonable time starts running from the date of indorsement.

The "except clause" in section 71 of the Negotiable Instruments Law provides that a demand instrument must be presented within a reasonable time after its issue, "except that in the case of a bill of exchange, presentment for payment will be sufficient if made within a reasonable time after the last negotiation thereof." The demand draft, other than a check, that has had one or more negotiations falls, it

³⁸*Northern Lumber Co. v. Clausen*, 201 Iowa 701, 208 N.W. 72 (1926); *Moore v. Warren*, 1 Strange 415, 93 Eng. Rep. 605 (K.B. 1760).

³⁹*Prescott Bank v. Caverly*, 73 Mass. (7 Gray) 217 (1856); *Nutting v. Burked*, 48 Mich. 241, 12 N.W. 184 (1882).

⁴⁰See *Wallace v. City Nat'l Bank*, 202 Ala. 323, 80 So. 405 (1918); *Nuzum v. Sheppard*, 87 W. Va. 243, 104 S.E. 587 (1920).

⁴¹*Muncy Borough School Dist. v. Commonwealth*, 84 Pa. 464 (1877); *National Network Banking Co. v. Erie Second Nat'l Bank*, 63 Pa. 404 (1869).

seems, within the control of this "except clause." It appears, to some extent, inconsistent with the reasoning that the drawer has a right to expect the holder to make demand on the drawee forthwith after issue. It would seem to apply to a drawer in the sense that, if the drawer is discharged by failure to present within a reasonable time after issue, presentment forthwith after the last negotiation will revive the drawer's liability, or that a negotiation once every twenty-four hours after issue will prevent the drawer's discharge based on failure to present. Several cases dealing with the revival point were decided after adoption of the Negotiable Instruments Law, but none was found that gives an authoritative interpretation of the "except clause" of section 71. One case⁴² gets the result of the explicit language of the "except clause," but it is not clear as to what weight it gave to the clause in reaching its decision. Two writers⁴³ argue that the revival aspect of the "except clause" should be limited to a holder who can qualify as a holder in due course. In other words, no holder should be able to revive the previously discharged secondary liability of the drawer or indorser unless he bought the instrument before it was stale, counting from the date of issue. Since this view would limit the duration of the liability of the drawer and indorser to the period that the instrument is not stale, one can have sympathy for the view, since it protects to this degree the presentment right, assuming the presentment right has justification. In view of the language of the statute, including sections 53, 58, and others dealing with the holder in due course, it is most difficult to accept this view. It has been suggested that the "except clause" should be limited to the liability of the last indorser, so that prompt presentment after the last negotiation will not revive the liability of the drawer or prior indorsers if it has lapsed.⁴⁴ From the point of view of the reason behind the presentment right this result may be preferred; however, the language of the statute is against this conclusion.⁴⁵ The fairly clear language of the statute seems to indicate that under the "except clause" of section 71⁴⁶ the drawer and indorsers of a demand bill other

⁴²Columbia Banking Co. v. Bowen, 134 Wis. 218, 114 N.W. 451 (1908).

⁴³BEUTEL, BRANNAN NEGOTIABLE INSTRUMENTS LAW 999 (7th ed. 1948); BRITTON, BILLS AND NOTES 867 (1943).

⁴⁴Greeley, *The Uniform Negotiable Instruments Law in the Light of Recent Criticism*, 10 ILL. L. REV. 265, 275 (1915).

⁴⁵BIGELOW, BILLS, NOTES AND CHECKS §355 (Lile ed. 1928); Greeley, *supra* note 44.

⁴⁶Several states have eliminated the "except clause" or amended it, e.g., Massachusetts, Nebraska, New Hampshire, Vermont.

than a check remain contingently liable as long as each holder negotiates it before the close of the next business day after he receives it. It also appears that a holder who holds the instrument for more than a reasonable period after it was negotiated to him cannot enforce the secondary liability of the drawer or the indorsers. But, if a holder who has held the bill too long negotiates it to an indorsee and the latter presents it to the drawee within a reasonable time thereafter, the previously extinguished contingent liability of the drawer and prior indorsers is revived.⁴⁷ From the statutory language it would seem that the drawer and indorsers on a demand bill may be held liable indefinitely; however, if they have a personal defense, it will become effective as against a holder who cannot qualify as a holder in due course; and a holder who buys after the instrument is stale cannot qualify as a holder in due course.⁴⁸ In determining staleness the date of issue is the starting point.⁴⁹ It is sometimes easy to confuse the reasonable time for presentment of demand paper with the period in which demand paper becomes stale; therefore some emphasis should be given to the distinction between the two. Not only may the periods be different but the concepts involved are different. The presentment right applies against a holder in due course as well as a holder not in due course, and failure to present properly is a valid defense against a holder in due course, whether a personal defense is available or not. The issue as to whether the holder is a holder in due course will not arise unless a personal defense is available. The breach of the duty to present does not fall in the category of personal defenses; therefore the status of holder in due course cannot cut it off.

The Check

Section 186 of the Negotiable Instruments Law provides: "A check must be presented for payment within a reasonable time after its issue or the drawer will be discharged from liability thereon to the extent of the loss caused by the delay."

Note that section 71 of the law is a general provision dealing with bills of exchange and that section 186 is a specific provision dealing with checks. Therefore, as to checks, when section 186 conflicts with section 71 the former prevails. As to check problems not covered by

⁴⁷See 40 MICH. L. REV. 418 (1942).

⁴⁸*La Due v. First Nat'l Bank*, 31 Minn. 33, 16 N.W. 426 (1883).

⁴⁹See NEGOTIABLE INSTRUMENTS LAW §53.

the specific provisions, the general provisions prevail.⁵⁰ In regard to presentment of checks within a reasonable time in order to preserve the contingent liability of secondary parties, three things should be emphasized:

- (1) The special provision does not deal with indorsers but with the drawer only; therefore, indorsers on checks are left to the control of section 71.⁵¹
- (2) As to the drawer of a check, section 186 definitely dates the running of the reasonable time from the date of issue and not from the time of the last negotiation.⁵²
- (3) As to the drawer of a check, failure to make due presentment does not result in automatic discharge but discharge only to the extent of loss resulting from the failure to make due presentment.⁵³

For the first time in the presentment problem loss becomes a material factor.

First, consider the point regarding discharge only to the extent of loss. This means that the drawer is liable to the holder of a check for the period of the statute of limitations, which starts at the time the check is issued, except to the extent that he can prove loss resulting from failure to make due presentment.⁵⁴ This rule distinguishing the drawer's position on checks from that on bills other than checks has a fairly reasonable basis. The drawer of a bill other than a check simply represents to the holder that he has a right to expect the drawee to pay, and the holder must assume that the drawer may be relying upon the holder to make appropriate demand on the drawee in order to prevent the drawer from being prejudiced. The drawer, but for his reliance upon the holder, theoretically would have made

⁵⁰*Deal v. Atlantic C.L.R.R.*, 225 Ala. 533, 144 So. 81, 86 A.L.R. 455 (1932).

⁵¹NEGOTIABLE INSTRUMENTS LAW §185; *Swift v. Miller*, 62 Ind. App. 312, 113 N.E. 447 (1916); *Columbian Banking Co. v. Bowen*, 134 Wis. 218, 114 N.W. 451 (1908); *Commercial Inv. Trust v. Lundgren-Wittensten Co.*, 173 Minn. 83, 216 N.W. 531 (1927); see *Annot.*, 56 A.L.R. 494 (1928). *But see* NEGOTIABLE INSTRUMENTS LAW §120 (3); *Arterburn v. Wakefield*, 309 Ky. 212, 217 S.W.2d 203, 6 A.L.R.2d 982 (1949); *BIGELOW, BILLS, NOTES AND CHECKS* §354 (Lile ed. 1928).

⁵²*Millett v. Miller*, 135 Neb. 123, 280 N.W. 442 (1938).

⁵³*Marx & Co. v. Bankers' Credit Life Ins. Co.*, 224 Ala. 249, 139 So. 421 (1931); see *Baldwin's Bank v. Smith*, 215 N.Y. 76, 109 N.E. 138 (1915).

⁵⁴*Roberts v. School Dist.*, 99 Colo. 484, 63 P.2d 1232 (1936); *Gainesville News v. Harrison*, 58 Ga. App. 744, 199 S.E. 559 (1938).

due demand on the drawee. The drawer on a check, however, represents that he has maintained with the drawee bank funds for payment of the check. By the nature of bank deposit accounts, it is not likely that the drawer will be prejudiced if demand for payment is not made on the bank within a particularly short time. For instance, a bank's position is different from that of the usual drawee other than a bank, and no statute of limitation is running against the drawer on a bank deposit account, whereas it may well be running against the drawer on a debt owed him by a drawee other than a bank. So usually the only way that the drawer on a check can suffer loss as a result of the holder's failure to present to the drawee bank within the reasonable time period is by the drawee bank becoming insolvent after the lapse of the reasonable time. It has been argued, though unsuccessfully, that the protection afforded the drawer by section 186 should cover loss to the drawer resulting from the situation in which the drawer delivers to the payee a second check on the claim that the first one was lost when in fact both checks were cashed.⁵⁵ But one case has held that the drawer is discharged under section 186 on a check issued to payee for consideration from a third party, which consideration was returned to the third party after the lapse of about two and one-half months without presentment of the check.⁵⁶

The burden of proof of the fact and the extent of loss is on the drawer.⁵⁷ And proof of the drawee's insolvency after the lapse of a reasonable time but before presentment of the check for payment is not sufficient to discharge the drawer, since the insolvent drawee may pay the drawer dividends based on the amount on deposit at the time the drawee closed its doors in insolvency, thus preventing complete loss of the full amount of the check resulting from failure of timely presentment.⁵⁸ In order to be discharged at all the drawer must go forward with the proof and establish the amount of loss. However, if a drawee bank that has certified the check becomes insolvent after the lapse of a reasonable time and before presentment, the drawer is entirely discharged on his liability as surety for the certifying bank.⁵⁹ The reason for this is that any debt owed by the insolvent bank in re-

⁵⁵*Pan American Petroleum Corp. v. American Nat'l Bank*, 165 Tenn. 66, 52 S.W.2d 149 (1932).

⁵⁶*In re Pascal's Estate*, 146 N.Y.S.2d 364 (Sup. Ct. 1955).

⁵⁷*Sims v. Hunter*, 44 Idaho 505, 258 Pac. 550 (1927). *But see* *Dehoust v. Lewis*, 128 App. Div. 131, 112 N.Y. Supp. 559 (2d Dep't 1908).

⁵⁸*Mars, Inc. v. Chubriilo*, 216 Wis. 313, 257 N.W. 157 (1934).

⁵⁹*Seager v. Dauphinee*, 284 Mass. 96, 187 N.E. 94 (1933).

lation to the amount of the check is primarily owed to the holder, as opposed to the case of the uncertified check, so that any dividends that may be paid in relation to the amount of the check will go to the holder rather than the drawer.

Once the drawer is discharged by loss resulting from failure to present within a reasonable time after issue, his liability cannot be revived. Of course the Negotiable Instruments Law refers to discharge of the drawer on the check; so, in case of discharge, since a check normally is conditional payment of the underlying debt for which the check was given,⁶⁰ why cannot the holder-creditor ignore the check and sue the drawer-debtor on the underlying debt? That has been tried without success, the holding being that the underlying debt becomes paid absolutely when the drawer is legally discharged on the check, whether by payment from the drawee or by loss to the drawer resulting from the holder's failure to present within a reasonable time.⁶¹

As to the liability of indorsers on checks, the law is identical with that pertaining to indorsers on bills other than checks. It appears that section 71 controls; an indorser may be discharged from liability completely, not merely to the extent of provable loss, by failure to present within a reasonable time after the last negotiation. However, this liability may be revived by further negotiation and presentment within a reasonable time thereafter. Thus it would be possible to have a situation in which the indorser of a check is liable and the drawer completely discharged. This possibility is another argument against the revival point of section 71, since normally the drawer is surety to protect the indorsers.⁶² As indicated in the discussion of the revival point in regard to bills of exchange other than checks, in spite of the holder's ability in some cases to revive discharged secondary liability, if he buys the instrument after it becomes stale he cannot be a holder in due course; therefore, any personal defense that the parties may have is effective against him. And checks usually become stale quicker than any other type of instrument.

What is the reasonable time in which a check must be presented? The law appears quite settled on this point and unreasonably rigid. It is the same as the period most frequently applied in the case of a

⁶⁰McRae Grocery Co. v. Independence Indemnity Co., 33 F.2d 494 (4th Cir. 1929).

⁶¹Mars, Inc. v. Chubriilo, 216 Wis. 313, 257 N.W. 157 (1934).

⁶²An exception would be when the drawer executes the instrument as an accommodation for the indorser; see note 51 *supra*.

bill other than a check. If the holder and the drawee are in the same town, presentment must be made before the close of the next business day after issue in the case of the drawer, and in the case of the indorser before the close of the next business day after the last negotiation.⁶³ If the holder and the drawee are not in the same town, the holder must within the next business day start the check in the normal course of collection, which usually means turn it over to a local bank.⁶⁴ This period, which is used most frequently by the courts, is entirely too short if consideration is given to the actual use and function of the check today. What check holder is aware that he assumes the risks of discharging the drawer and the indorsers by keeping the check in his pocket for two business days?

OTHER ASPECTS OF THE PROBLEM

Although the date of the demand of payment looms as one of the largest aspects of due presentment from the problem standpoint, it is not the whole story of the duties that the holder must perform in order to preserve the liabilities of secondary parties. In addition to such usual things as physical display of the instrument, identification of the presenter, and perhaps receipt, discussed later, there are the duties to protest and give notice of dishonor in certain cases. It may well be said that the duties to protest and to give notice follow the duty of due presentment and are not part of it; however, they are all so closely connected functionally that frequently they are considered as only separate aspects of the due presentment problem. Consequently a brief word at this point about protest and notice of dishonor seems appropriate.

The law gives the right to notice of dishonor to secondary parties in order to afford them an opportunity to protect themselves against the party primarily liable.⁶⁵ So the rule is simply that parties secondarily liable, drawer and indorsers, are discharged unless notice of dishonor is duly given to them.⁶⁶ The rule is applicable equally to time paper, demand paper, promissory notes, bills of exchange other than

⁶³National Plumbing & Heating Supply Co. v. Stevenson, 213 Ill. App. 49 (1918); Viles v. S. D. Warren Co., 132 Me. 277, 170 Atl. 501 (1934); Farm and Home Sav. and Loan Ass'n v. Stubbs, 231 Mo. App. 87, 98 S.W.2d 320 (1936).

⁶⁴Swift & Co. v. Miller, 62 Ind. App. 312, 113 N.E. 447 (1916); Nuzum v. Shepard, 87 W. Va. 243, 104 S.E. 587 (1920).

⁶⁵In re Taylor's Estate, 174 Misc. 457, 21 N.Y.S.2d 245 (Surr. Ct. 1940).

⁶⁶NEGOTIABLE INSTRUMENTS LAW §89.

checks, and checks.⁶⁷ An indorser who receives notice may protect himself by giving notice to the prior indorsers and the drawer within a reasonable time after he receives notice.⁶⁸ The Negotiable Instruments Law defines reasonable time for notice. It provides that if the parties live in the same locality notice must be given before the close of business on the date following dishonor if given at the secondary party's place of business; but if notice is given at his residence it must be given before the usual hours of rest on the day following dishonor.⁶⁹ If the parties do not live in the same locality and notice is sent by mail, the notice must be sent so that it will leave the locality before the close of the day following dishonor. If notice is given by means other than mail, it must be as effective as mail.⁷⁰ The right to notice is dispensed with, however, if after the exercise of reasonable diligence it cannot be given.⁷¹

The rule pertaining to discharge of parties secondarily liable unless the instrument is protested in the event of dishonor applies only to bills that appear on their face to be foreign bills, that is, bills drawn in one state or country and payable in another. If the foreign nature of the bill does not appear on its face, or if the bill is a domestic one, for instance drawn in Michigan and payable in Michigan, protest is not necessary.⁷² Any negotiable instrument may be protested,⁷³ and quite frequently both domestic and foreign instruments are protested for the reason that the certificate of protest is admissible in court as prima facie evidence of presentment and dishonor. Protest is a notarized statement made on the instrument by the presenter specifying the time and place of presentment, the fact that presentment was made and the manner thereof, the demand made and the answer given, including language of dishonor. The notary may be dispensed with by the use of two or more witnesses.⁷⁴

⁶⁷*Gainesville News v. Harrison*, 58 Ga. App. 744, 199 S.E. 559 (1938); *Chelsea Park Garage v. Neuberger*, 200 N.Y. Supp. 265 (Sup. Ct. 1923); *National Life and Accid. Ins. Co. v. Varner*, 171 Tenn. 95, 100 S.W.2d 662 (1937). *But see Deal v. Atlantic C.L.R.R.*, 225 Ala. 533, 144 So. 81 (1933).

⁶⁸*Williams v. Paintsville Nat'l Bank*, 143 Ky. 781, 137 S.W. 535 (1911).

⁶⁹NEGOTIABLE INSTRUMENTS LAW §§102-3.

⁷⁰See *id.* §104.

⁷¹*Id.* §112.

⁷²*Id.* §152, *Gorsche v. Manistique First Nat'l Bank*, 233 Mich. 428, 206 N.W. 992 (1926).

⁷³NEGOTIABLE INSTRUMENTS LAW §118, *Shickshinny First Nat'l Bank v. Tustin*, 246 Pa. 151, 92 Atl. 119 (1914).

⁷⁴See NEGOTIABLE INSTRUMENTS LAW §§153-54.

The most effective method of doing away with the rights of secondary parties to presentment, notice of dishonor, and protest is by agreement. They may effectively waive all of these rights in the body of the instrument. If a waiver clause appears, it applies to all parties to the instrument.⁷⁵ Usually foreign bills and foreign notes contain waiver clauses, but they seldom occur in the case of checks. A waiver of protest, without mentioning the other rights, on any negotiable instrument, whether foreign or domestic, is deemed to be a waiver not only of formal protest but also of presentment and notice of dishonor.⁷⁶ Waiver of notice may waive protest, and waiver of presentment may waive notice and protest; but it has been held that waiver of notice will not waive presentment.⁷⁷ From the point of view of making the clause an undoubtedly effective waiver, the only wise course is to refer to each of the rights separately. One single secondary party may waive the rights by appropriate waiver language prior to signature; however, such language probably will affect only the particular party.⁷⁸

Although consideration of the conditions for preservation of the liability of secondary parties on negotiable instruments might tempt one toward the conclusion that without a waiver such liability could never last long enough to involve the statute of limitations, it would not be true. The statute of limitations may become material to the liability of secondary parties in any one of the following situations:

- (1) when presentment, dishonor, notice of dishonor, and protest have been duly made, in other words, when the conditions have been fulfilled;
- (2) when presentment, notice of dishonor, and protest have been waived;
- (3) when the drawer has no right to expect the drawee to pay, as in the case of insufficient funds in the drawee bank, or in the case of an indorser when he is an accommodated party;
- (4) when the indorsee has the capacity to present forthwith after he receives the instrument and revive under section 71 of the Negotiable Instruments Law previously discharged liability of secondary parties;

⁷⁵See *id.* §§82 (3), 109-110, *Hall v. Crane*, 213 Mass. 326, 100 N.E. 554 (1913).

⁷⁶NEGOTIABLE INSTRUMENTS LAW §111.

⁷⁷*Hayward v. Empire State Sugar Co.*, 105 App. Div. 21, 93 N.Y. Supp. 449 (4th Dep't 1905).

⁷⁸NEGOTIABLE INSTRUMENTS LAW §110.

- (5) in the case of a drawer on a check, when the failure to duly present or give notice of dishonor does not cause any loss to the drawer.

All of these situations may involve the question of whether in the case of demand paper the statute of limitations will start running against secondary liability without demand on either the primary or the secondary party, or whether the running of the statute against the primary debt will discharge secondary parties.

SPECIAL ASPECTS OF THE PROBLEM PARTICULARLY APPLICABLE TO THE BANK CHECK COLLECTION AGENT

TIMELY PRESENTMENT

The bank check collection agent is legally responsible to the check holder for the diligent fulfillment of its collection duties, such as the protection of the holder's interest by making due presentment, including timely presentment, protest, and giving notice of dishonor in accordance with the law.⁷⁹ Usually this means preservation of the liability of secondary parties, but it should be noted that it may also include prevention of loss to the holder from such things as the freezing of the drawer's bank account by bankruptcy after the lapse of a reasonable time for presentment. The bank's problem regarding timely presentment flows from two conditions: (1) the unreasonableness and rigidity of the requirement that the law makes in view of the facts involved in check collection operations, and (2) the lack of clarity as to what the law requires.

As previously noted, the Negotiable Instruments Law does not set up an unreasonably short and rigid time rule, but many of the cases do. A few examples will aid in getting a perspective of the problem. Usage or custom regarding the sending of checks through several bank correspondents for collection may be considered in determining whe-

⁷⁹First Nat'l Bank v. Fourth Nat'l Bank, 77 N.Y. 320, 33 Am. Rep. 618 (1879); Williams v. Brown, 53 App. Div. 486, 65 N.Y. Supp. 1049 (2d Dep't 1900); McEwen Bros. v. Cobb, 104 Misc. 477, 172 N.Y. Supp. 44 (Sup. Ct. 1918); First Guaranty State Bank v. Meyer & Kiser, 287 S.W. 1110 (Tex. Civ. App. 1926); see Notes, 77 Am. St. Rep. 616 (1899), 34 Am. Dec. 308 (1839).

ther presentment was timely,⁸⁰ but evidence of the custom cannot be admitted on the issue unless it is shown that the custom was known to the secondary parties on the check.⁸¹ If the collection agent and the drawee are in the same city, presentment must be made during banking hours of the next business day after receipt of the check by the agent, notwithstanding the size of the city, clearing house arrangements, or collection customs.⁸² Keeping the check on the move in the collection process is not sufficient. Suppose a payee receives on Monday a check drawn on a local bank. If he follows normal procedure he will deposit the check in the local bank that carries his account, and if the banking procedures are normal the check most likely will reach the drawee for payment on Wednesday. There are cases that hold that this is too late, that Tuesday was the last day for timely presentment.⁸³ The custom of presenting and collecting checks through clearing houses, indeed the necessity of doing so in metropolitan areas, will not extend the time in which the agent must accomplish presentment beyond the day after its receipt by the agent.⁸⁴ It is said that the rules of a clearing house do not affect the rights of a drawer in his relation to the holder or the rights of the holder in his relation to his collection agent, since these parties are not members of the clearing house.⁸⁵ It has been held that there was failure of timely presentment when the bank collection agent presented the check on the second business day after its receipt, even though the agent strictly followed local custom when the drawee did not belong to the local clearing house.⁸⁶ Numerous cases rigidly apply the next business day rule to check collections,⁸⁷ and evidence of economy regarding collection costs or business custom or good business procedure or business

⁸⁰*Plover Sav. Bank v. Moodie*, 135 Iowa 685, 113 N.W. 476 (1906).

⁸¹*First Nat'l Bank v. Mackey*, 157 Ill. App. 408 (1910).

⁸²*Farm and Home Sav. and Loan Ass'n v. Stubbs*, 231 Mo. App. 87, 98 S.W.2d 320 (1936); see 2 PATON'S DIGEST OF LEGAL OPINIONS 1272-76 (1942).

⁸³*Rosenblatt v. Haberman*, 8 Mo. App. 486 (1880); *Edmisten v. Herpolsheimer Co.*, 66 Neb. 94, 92 N.W. 138 (1901), *aff'd*, 66 Neb. 98, 92 N.W. 140 (1902); *Dorchester v. Merchants Nat'l Bank*, 106 Tex. 201, 163 S.W. 5 (1914).

⁸⁴See note 82 *supra*. But see *Marrett v. Brackett*, 60 Me. 524 (1872).

⁸⁵See note 84 *supra*.

⁸⁶*Lowell Cooperative Bank v. Sheridan*, 284 Mass. 594, 188 N.E. 636 (1933).

⁸⁷*Wallace v. City Nat'l Bank*, 202 Ala. 323, 80 So. 405 (1918); *Village of Lombard v. Anderson*, 280 Ill. App. 283 (1935); *National Plumbing & Heating Supply Co. v. Stevenson*, 213 Ill. App. 49 (1918); *Swift & Co. v. Miller*, 62 Ind. App. 312, 113 N.E. 447 (1916); *Viles v. S. D. Warren Co.*, 132 Me. 277, 170 Atl. 501 (1934); *Brookside Mills v. Railway Exp. Agency*, 170 Tenn. 325, 95 S.W.2d 301 (1936).

needs or the demands of practical banking operations is not sufficient to extend the time for presentment for even three or four days.⁸⁸

There is language in *First National Bank of Meadville v. Fourth National Bank of the City of New York*⁸⁹ that suggests that the bank collection agent may have a stricter presentment duty than that imposed on the holder, resulting apparently in a situation in which there may be a shift of risk from the drawer to the collection agent when, but for the use of the collection agent, the risk would be on the drawer for a longer period. Admittedly, however, this is an improper conclusion from the whole case, since the full opinion indicates that the court meant to restrict the language to duties owed by the collection agent to the holder and was primarily interested in pointing out that the collection agent has duties beyond preserving the liabilities of the secondary parties on the check. Nevertheless, there are cases suggesting that if the collection agent has knowledge indicating that the *drawer* or holder may lose unless immediate presentment is made, knowledge of the precarious financial position of the drawee, for instance, then the bank collection agent owes the duty to present on the same day it receives the check.⁹⁰ One case⁹¹ states that the time in which a collection agent may forward a check by mail for collection does not include the whole of the next business day after receipt unless the last mail of that day goes at the close of business, and if there is but one mail a day the check must leave by it unless the mail leaves at an unreasonably early hour.

⁸⁸*Chadwick First Nat'l Bank v. Mackey*, 157 Ill. App. 408 (1910); *Northern Lumber Co. v. Clausen*, 201 Iowa 701, 208 N.W. 72 (1926); *Farm and Home Sav. and Loan Ass'n v. Stubbs*, 231 Mo. App. 87, 98 S.W.2d 320 (1936); *Woods Bros. Corp. v. Francke*, 122 Neb. 672, 241 N.W. 88 (1932); *Brookside Mills v. Railway Exp. Agency*, *supra* note 87; *Mars, Inc. v. Chubriilo*, 216 Wis. 313, 257 N.W. 157 (1934).

⁸⁹77 N.Y. 320, 33 Am. Rep. 618, 619 (1879). For an interesting case regarding the duty of the holder's collection agent to the drawer, see *Cohen v. Tradesmen's Nat'l Bank*, 69 Pa. Super. 28 (1918).

⁹⁰See *Wallace v. City Nat'l Bank*, *supra* note 87; *Blackwelder v. Fergus Motor Co.*, 80 Mont. 374, 260 Pac. 734 (1927); *Henderson Chevrolet Co. v. Ingle*, 202 N.C. 158, 162 S.E. 219 (1932); *Bennett v. American Nat'l Bank*, 130 Okla. 23, 264 Pac. 912 (1928); *Holbrook v. W. L. Moody & Co.*, 45 S.W.2d 685 (Tex. Civ. App. 1931); *Pinkney v. Kanawha Valley Bank*, 68 W. Va. 254, 69 S.E. 1012 (1910); *Boddington v. Schlencker*, 4 B. & A. 752, 110 Eng. Rep. 639 (1833); 6 MICHIE, BANKS AND BANKING 144 (1952). *But see* *Continental Bank and Trust Co. v. Detroit Trust Co.*, 262 Mich. 497, 247 N.W. 728 (1933).

⁹¹*Pinkney v. Kanawha Valley Bank*, *supra* note 90.

Although the rigid authorities referred to above dominate the case reports, there are cases that allow an extension of time for presentment on the basis of the facts of the collection process;⁹² and there are a few cases that extend the time because of circumstances or habits of the holder or other reasons.⁹³ Admittedly these decisions recognize a problem and attempt to meet it, but their efforts fall far short of the need. In spite of conflict of laws rules, which sometimes afford a little help, the cases and certain statutory provisions, the "except clause" of section 71 of the Negotiable Instruments Law, for instance, result in considerable confusion and uncertainty.⁹⁴

Now the question: what is the solution of the timely presentment problem? The drawer and the indorsers on negotiable paper perform a function quite similar to that of a surety, who has no right in the usual case to a demand by the creditor on the principal debtor or to a notice of refusal of payment. Perhaps, then, the presentment rights of drawers and indorsers cannot be justified, particularly if these rights unreasonably clog the collection process. Should the drawer or indorser be required to follow up each negotiable instrument transaction into which he enters and check it out to its conclusion, or at least to his satisfaction at his own risk, as a surety must? Obviously not. Consider what one's thoughts would be if he signed a contract as a surety as opposed to signing a negotiable instrument as drawer or indorser. In the former transaction he would devote much more time to entering into it and following it up; hence it is a cumbersome transaction. How often would he wake at night and wonder whether the negotiable instrument that he signed were still a club of liability over his head? He would not, and he is not supposed to. If he did he would not use the negotiable device often and it would lose much of its functioning service to the economy. Therefore, to protect the usefulness of the negotiable instrument the law must provide for presentment rights designed to prevent unnecessary

⁹²Maryland Title Guarantee Co. v. Alter, 167 Md. 244, 173 Atl. 200 (1934); Bay City Bank v. Concordia Mutual Fire Ins. Co., 260 Mich. 611, 245 N.W. 532 (1932); see Andrews, *Validity and Time of Presentment Through the Clearing House*, 2 WESTERN RES. L. REV. 97 (1949).

⁹³Berry v. Harris, 186 Ark. 481, 54 S.W.2d 289 (1932); Peterson v. School Dist., 162 Minn. 357, 203 N.W. 46 (1925); Coolidge v. Rueth, 209 Wis. 458, 245 N.W. 186 (1932).

⁹⁴The "except clause" of section 71 of the Negotiable Instruments Law is considered in the discussion of the bill of exchange other than a check under the heading "The Basic Problem" *supra*.

prejudice to the drawer and the indorser without infringing on a reasonable collection process.

Some help for the check collection agent's position would result from a more general recognition by the courts that the agent is liable to the principal only for the direct loss resulting from the agent's breach of duty, as opposed to holding that by breach of duty the agent becomes liable to the principal for the amount of the instrument as a purchaser. This loss may be cut down from the amount of the instrument by recognition of the rule that the drawer of a check is discharged only to the extent of loss resulting from failure to present timely,⁹⁵ instead of complete discharge irrespective of loss as in the case of indorsers⁹⁶ and also drawers on bills other than checks, and therefore may still be liable to the principal on his guaranty of payment, at least for part of the amount of the instrument. It is doubtful that the possibility of revival of the indorser's guaranty liability under section 71 of the Negotiable Instruments Law should be considered in determining the principal's loss; however, in cases in which there is a failure of capacity of parties or other defect affecting the genuineness of the check that strikes at the principal's rights,⁹⁷ this fact plus the liability of the drawer and the indorsers to the principal on their admissions and warranties should be considered in determining the liability of the collection agent to the principal.

If the liability of the agent for failure to present timely is limited to the loss of the holder not covered by the holder's rights against secondary parties, this limitation would be more effective in protecting the agent if the law were changed as to indorsers to do away with the automatic discharge of their suretyship liability;⁹⁸ that is, to

⁹⁵NEGOTIABLE INSTRUMENTS LAW §186.

⁹⁶*Id.* §71, *Swift & Co. v. Miller*, 62 Ind. App. 312, 113 N.E. 447 (1916).

⁹⁷See *Bank of Washington v. Triplett*, 1 Pet. 25, 77 Am. St. Rep. 618 (1899); 6 MICHIE, BANKS AND BANKING §§60, 62 (1952); 2 PATON'S DIGEST OF LEGAL OPINIONS, *Collections*, §§2, 6 (1942). There are cases that hold that the collecting bank is not necessarily liable for the face amount of the check, although the bank has breached its duty in the collection process. *Balsa Ecuador Lumber Corp. v. Security Nat'l Bank*, 141 F. Supp. 470 (E.D.N.C. 1956).

⁹⁸*Nuzum v. Sheppard*, 87 W. Va. 243, 104 S.E. 587 (1920). Consider the factual situation in which there is a failure of timely presentment but the drawer becomes insolvent before the reasonable time period has elapsed. Should not the indorser carry this risk as opposed to the holder or agent? Of course it may be argued that the indorser is not discharged for the reason that he cannot expect payment if it is presented. But this situation is hardly analogous to the cases in which the indorser is an accommodated party. See NEGOTIABLE INSTRUMENTS LAW §80; note 51

limit their discharge to the actual loss resulting from the breach of the timely presentment duty. This change in the law as to indorsers, as well as a similar change in the case of a drawer on a bill other than a check, would be desirable not only for the collection agent but for the holder. Thus one may be tempted to suggest that such a change could promote the use of the negotiable device, since the holder would feel more comfortable in his position, the risks of the collection agent would be reduced, and the indorser would have some protection — the protection of a surety who under suretyship law usually is discharged if at all only to the extent of actual loss resulting from the creditor's laches. But indorsers are essential in most instances in order to fulfill the functions of the negotiable instrument, and few indorsers would feel that their interests were protected adequately if the law were changed to agree with the suretyship scheme of permitting discharge only to the extent of loss resulting from the failure of timely presentment. What loss? Has an indorser suffered loss if there is a solvent drawer or prior indorser? What is the extent of his loss if the drawer and all prior indorsers are insolvent? Think of the difference between the situation of the indorser on a check that was presented timely and therefore paid and the situation of the indorser on a check that was not presented timely and therefore not paid. The former is entirely freed from the transaction, and the latter most likely feels chagrin if not despair with at least the very-difficult-to-determine costs of litigation, emotion, time, and effort confronting him. Even if it is assumed that the loss intended can be defined it would be most difficult to prove, as has been found in cases involving the discharge of the drawer on a check under section 186 of the Negotiable Instruments Law. Another good reason for not applying the extent of loss idea to the indorser is the nature of the position of the indorser and the function he performs on the check. Contrast the position of the drawer having an obligation due him with that of the indorser having at most a potential obligation due him that matures only upon the happening of conditions subsequent, most of which are beyond his control. The Uniform Commercial Code permits the indorser to be completely discharged and attempts to solve the difficulties of proof when the drawer is discharged to the extent of loss by providing that the drawer is discharged only when the drawee bank becomes insolvent

supra. Under suretyship law there is authority for the discharge of the surety only to the extent of his actual loss resulting from the improper action or inaction by the creditor. *Commercial Credit Corp. v. Joseph Greco Motor Co.*, 16 So.2d 660, *modified*, 18 So.2d 49 (La. App. 1944); RESTATEMENT, LAW OF SECURITY §132 (1941).

during the delay, so that the drawer is deprived of funds which he maintained with the closed bank to cover the instrument. In this event the drawer can have the benefit of his discharge to the extent of loss only by making a written assignment to the check holder of the drawer's rights against the closed bank regarding funds maintained in the bank for payment of the check.⁹⁹ Thus the holder who has delayed will receive whatever dividend is paid by the insolvent drawee bank on funds maintained for payment of the check. This solution of the proof problem in cases involving drawers has merit, but probably it would work only to the most limited degree if at all in cases involving indorsers. One may think there is just as much reason to limit discharge of indorsers to loss not including amounts collectible by the exercise of indorsers' rights against prior parties argued against in this paragraph as there is reason to limit liability of the collection agent to the loss of the holder not including amounts collectible by the exercise of the holder's rights against prior parties, suggested in the immediately preceding paragraph as a possibility leading toward some alleviation of the collection agent's situation. Put in another way, if it is not appropriate to permit the holder to force a repurchase of the instrument by the indorser for a price equal to amounts collectible by the exercise of indorser's rights against prior parties, why is it appropriate to permit the collection agent, the one guilty of the breach of duty, to resist a forced purchase of the instrument and thereby compel the holder to exercise his rights against prior parties with the loss of time and effort connected therewith? The difference between the relationship of the indorser to the holder and the relationship of the collection agent to the holder, including the risk incidents of title vested in the holder, can justify a distinction. However, any significant aid to the legal position of the collection agent with the objective of an efficient collection process must come from reappraisal and revision of the presentment duty owed by the agent to the holder and of the presentment duty owed by the holder to secondary parties, since much of the former is based on the latter. It is not sufficient merely to change the rules as to the amount of recovery in the event of a breach of duty.

Although the revival aspect of the "except clause" of section 71 of the Negotiable Instruments Law¹⁰⁰ may be an indication of a de-

⁹⁹UNIFORM COMMERCIAL CODE §§3-501, 3-502 (1957).

¹⁰⁰For a consideration of the "except clause" see the discussion of the bill of exchange other than a check under the heading "The Basic Problem" *supra*.

preciation of the presentment right in the legislatures, it has not had this result in the courts, and its potency and effect still stand as an unknown quantity. Its purpose seems to be a matter of pure speculation,¹⁰¹ but undoubtedly it was not designed to help the bank collection process; in the interest of the elimination of unnecessary uncertainty it should be repealed, as has been done by several states¹⁰² and the Uniform Commercial Code.¹⁰³

A few states have recognized the timely presentment problem in the check collection context, providing by statute that a check in the possession of any bank for collection may be handled according to current bank custom and usage.¹⁰⁴ Florida has attempted to help the situation, providing by statute¹⁰⁵ that if a bank handles a check in its possession for collection "in the usual commercial way in use according to the regular course of business of banks" it exercises due diligence. *Montsedoca v. Highlands Bank and Trust Co.*¹⁰⁶ utilized this statute when it held the defendant bank collection agent not liable for loss even though it did not forward the check for collection until the second business day after its receipt. Sections 5 and 6 of the Bank Collection Code¹⁰⁷ tried to alleviate the problem by providing that the responsibility of the collecting bank is to exercise ordinary care, presumptively nothing more, and that ordinary care is exercised when the collection agent forwards nonlocal checks not later than the business day next following their receipt "to another bank collection agent according to the usual banking custom, either located in the

¹⁰¹See 40 MICH. L. REV. 418 (1942).

¹⁰²See note 46 *supra*.

¹⁰³§3-503 (1957).

¹⁰⁴*E.g.*, ALA. CODE ANN. tit. 5, §130(1) (Supp. 1955).

¹⁰⁵FLA. STAT. §674.74 (1957).

¹⁰⁶85 Fla. 158, 95 So. 666 (1923). Several items of fact, such as the receipt of the check after business hours and the early hour at which the last mail left on the next business day, keep this case from being as authoritative as it otherwise would be.

¹⁰⁷The Bank Collection Code was sponsored by the American Bankers Association and adopted by about 19 states. It was held unconstitutional as to national banks in *Jennings v. United States Fidelity and Guaranty Co.*, 294 U.S. 216 (1935), and the courts of two states have suggested that it may be unconstitutional as to state banks. See *People ex rel. Barrett v. Union Bank and Trust Co.*, 362 Ill. 164, 199 N.E. 272 (1935), and *In re Riverton State Bank*, 48 Wyo. 372, 49 P.2d 637 (1935). The holdings were not based on the coverage of the presentment problem by the statute.

town or city where the check is payable or in another town or city." In the case of local checks ordinary care is exercised if the collecting bank presents the check no later than the next business day after its receipt "through the local clearing house under the regular established procedure, or according to the usual banking custom" if the collecting bank or the payor bank is not a member of the clearing house. However, the Bank Collection Code has been interpreted to apply only to rights between the holder and his bank collection agent and to affect in no way the duty of the holder to the drawer and indorsers to present the local check for payment within the next business day after the holder receives it.¹⁰⁸ Specifically it is held that, under the Bank Collection Code, bank customs or clearing house rules do not affect the drawer's relationship to the holder and that custom does not extend the time for presentment beyond the next business day as far as the drawer is concerned.¹⁰⁹ A solution that affects only the agent-holder relationship and not the holder-secondary party relationship is hardly satisfactory; it virtually tells the holder that he had better not use the banking system, the only efficient means available for the collection of checks.

The conclusion is justified that the timely presentment rules as applied by many courts to check collections through the banking system are unreasonable. It may be rationalized that by the holder's election to use the banking system as a means for collection he consents to the use of usual and reasonable bank collection processes, so that risks that may shift from the drawer to the holder as a result of the usual timely presentment rules will not be passed on to the collection agent. As far as the promotion of efficient check collections is concerned, the difficulties inherent in this reasoning, as well as in the interpretation of the Bank Collection Code, are (1) that it fails to come to grips with the holder-secondary party relationship, and (2) that from the point of view of practical business operations the holder has no real election; he must use the banking system. A much better rationalization, supported by some cases, is that when the secondary party elects to become a party to the instrument, presumptively knowing that the banking system is the only feasible means for collection, he consents to usual and reasonable bank collection processes, including clearing house rules, so that the risks do not leave him until after

¹⁰⁸*Farm and Home Sav. and Loan Ass'n v. Stubbs*, 231 Mo. App. 87, 98 S.W.2d 320 (1936).

¹⁰⁹*Ibid.*

these processes have had a reasonable time in which to be completed.¹¹⁰ This reasoning has merit; and, although it is subject to the argument that drawer and indorser have no real opportunity to make an election and that modern business methods require that they use the check, the drawer at least initiates the instrument and should remain liable during its normal life, and the indorser consents to remain liable.¹¹¹ The best way to put the rationale, as opposed to theoretical consent to a particular collection process, however, is simply that the primary aspect of the liability of the secondary party, entered into for consideration, is to remain liable during the normal processes in the life of a check. This solution approaches the problem on the basis of the fundamental relationship involved, that of the holder and secondary parties. The conclusion that the secondary liability should not be terminated by the lapse of a period made unreasonably short by the demands of modern uses of the negotiable device is supported by the same reasoning as that which supports the imposition of secondary liability on the drawer and indorser in the first place. This secondary liability is usually the vital support to the willingness of one to buy and own a check, and the promotion of this willingness to buy or own a check or other negotiable instrument is the objective of the heart of the policy of the Negotiable Instruments Law. Hence in the light of the realities of the collection process it is scarcely possible to overemphasize the need for an adjustment of the timely presentment duty toward allowing a longer period of time in which to make demand for payment.

The personal defenses of a secondary party may be cut off by the status of holder in due course. According to many decisions,¹¹² one may buy a check up to twenty-five and more days after issue and still qualify as a holder in due course; that is, he may presume that there is no personal defense even though the check is still outstanding, has not been presented for payment, and is twenty-five or more days old. Such a holder is protected from the personal defenses of the secondary party in order to promote the policy objective of making the in-

¹¹⁰There are authorities supporting this reasoning and also holding that it is not necessary to show that the secondary party had actual knowledge of the bank's customs and rules when he became a party to the check. *Jett Bros. Stores v. McCullough*, 188 Ark. 1108, 69 S.W.2d 863 (1934); *Federal Land Bank v. Goodman*, 173 Ark. 489, 292 S.W. 659 (1927).

¹¹¹*Johannsen v. Evans*, 271 Ill. App. 372 (1933); *Cox v. Citizens State Bank*, 73 Kan. 789, 85 Pac. 762 (1906).

¹¹²*E.g.*, see *Anderson v. Elem*, 111 Kan. 713, 208 Pac. 573 (1922).

strument more acceptable and therefore more negotiable; why not extend the time for presentment in order to achieve the same policy objective? It would aid the logic of the law if the period in which a check becomes stale, after which one cannot buy it and qualify as a holder in due course, and the period in which presentment for payment should be made were brought closer together. How can it be reasonable to say that one can buy a twenty-five-day-old check and be entitled to presume that there is no personal defense when he knows that there was a duty to present for payment twenty-four days earlier? Admittedly they are separate points of law, and one may be supported by argument over the other; nevertheless they are related, and the policy objective, promotion of negotiation with reasonable protection of parties' interests, that supports one supports the other.

Since a reasonable extension of the time for presentment probably will not prejudice the interests of secondary parties, any revision in the law should reach for certainty also, as the Uniform Commercial Code has done.¹¹³ The code sets up the reasonable time standard for presentment and affords flexibility by providing that a reasonable time is determined by the nature of the instrument, usage of banking or trade, and the facts of the particular case. Further, however, in the case of a check it creates a presumption that a reasonable period for presentment is thirty days after the date or issue of the check, whichever is later, with respect to the liability of the drawer; with regard to the indorser's liability a reasonable time is presumed to be seven days after his indorsement.¹¹⁴ A collecting bank may make presentment through a clearing house¹¹⁵ and, in a good faith effort to secure payment, may extend time limits otherwise imposed by the code by one additional banking day without discharging secondary parties.¹¹⁶ And any check for collection received after a cut-off hour of two P. M. or later, established by the bank, may be treated for purposes of collection as being received on the next business day.¹¹⁷ As far as the collection problem is concerned the presumption of thirty days in the case of the drawer is longer than is needed; nevertheless when business customs are considered the position taken by the Uniform Commercial Code may not be too far out of line. In any event the

¹¹³§3-503 (1957).

¹¹⁴*Ibid.*

¹¹⁵UNIFORM COMMERCIAL CODE §3-504 (2) (1957).

¹¹⁶*Id.* §4-108.

¹¹⁷*Id.* §4-107.

position appears to be an improvement over the present state of the law applicable to the time when checks should be presented, especially since it comes to grips with the holder-secondary party relationship as opposed to dealing only with the holder-collection agent relationship.

WARRANTIES BY THE CHECK COLLECTION AGENT

Does the proper presentment duty owed by the holder to the drawer and the indorsers include warranty of title or warranty of right to receive payment, either expressly or by implication of law? At least two lines of reasoning, supported by authority, say no, for the reason that the drawee is not entitled to warranty. One argument is that a warranty attaches to sales or negotiations only and that, since the payment transaction between the holder-creditor and the drawee-debtor is not a sale or negotiation, no warranty attaches.¹¹⁸ The second is that the position of the drawee is analogous to that of a debtor whose tender is invalidated by a demand made to the creditor for a receipt or other commitment showing payment in full, that the drawer owes no comparable duty to the drawee either directly or through the holder, and therefore the drawee has no right to demand a warranty as a condition to payment.¹¹⁹ If it does, it has dishonored the check and is subject to suit by the drawer for breach of contract, libel, or whatever other ground the particular jurisdiction permits for wrongful dishonor. Also worth noting are related cases that reach the conclusion described above, in which the court gives special attention to the fact that the drawee has notice that the presenter is acting as a collection agent, for instance, when a check bears restrictive indorsement or when a check is in the process of bank collection in a state that has a statute providing that there is a presumption that a bank is acting as a collection agent regarding checks it is handling that are not drawn on it.¹²⁰ The idea is that the drawee knows that the collection

¹¹⁸State Planters Bank & Trust Co. v. Fifth-Third Union Trust Co., 56 Ohio App. 309, 10 N.E.2d 935 (1937); see East India Co. v. Tritton, 3 B. & C. 280, 107 Eng. Rep. 738 (1824); Ames, *The Doctrine of Price v. Neal*, 4 HARV. L. REV. 297, 302 (1891).

¹¹⁹See Osborn v. Gheen, 16 D.C. 189 (1886); McCurdy v. The Society of Savings, 6 Ohio Dec. 1169, 11 Am. L. Rec. 156 (1882); Klaus, *Identification of the Holder and Tender of Receipt on the Counter-Presentation of Checks*, 13 MINN. L. REV. 281 (1928).

¹²⁰E.g., see FLA. STAT. §674.74 (1957); Leonardi v. Chase Nat'l Bank, 263 App. Div. 552, 33 N.Y.S.2d 706 (2d Dep't), cert. denied, 289 N.Y. 852, 43 N.E.2d 357 (1942).

agent presumptively received no warranty, since it gave up no value for the check, and therefore is in no position to give a warranty;¹²¹ hence, one from the agent should not be presumed in favor of the drawee¹²² or a collecting subagent. This conclusion flows from the assumption that the drawee is not entitled to a warranty without bargaining for it. So this group of cases does not form a third line of reasoning in any sense but simply indicates a basis on which the court finds it easier to presume no warranty to the drawee or a collecting subagent. An argument pointing in the other direction could be built by turning the above idea around and saying that, since the court seems to base the presumption of no warranty on the drawee's knowledge of the agency, a warranty may be presumed when there is no knowledge; but this argument does not appear to have been used effectively.

In looking further at the second line of reasoning it will be noted that, although the duty regarding timely presentment flows from the drawer-holder and indorser-holder relationships, other aspects of the proper presentment duty flow not only from these relationships but also from the drawer-drawee relationship, including the depositor's contract; therefore, proper presentment may also include the fulfillment of certain duties that the drawer may owe the drawee.¹²³ It is perfectly proper, however, to say that the drawer-drawee relationship is that of creditor-debtor, and some courts have reasoned that the debtor must pay its debts in accord with its contract, namely, pay proper orders at its peril with no conditions as to payment, and refuse at its peril to pay improper orders,¹²⁴ carefulness and diligence being immaterial factors.¹²⁵ In other words, risks of alteration, forged indorsements, and the like are the drawee's risks, with no recourse against the drawer, by virtue of their relationship and contract.¹²⁶

¹²¹When the restrictive indorser receives value it is not improper to hold that he warrants title. *In re Ziegenhein*, 187 S.W. 893 (Mo. App. 1916). Otherwise the warranty should not be presumed. See NEGOTIABLE INSTRUMENTS LAW §66. Normally the restrictive indorser is not a vendor, but a better reason when applicable for the implication that he does not warrant to his agent is that the agent gives up no value and runs no risks that should be covered by a warranty.

¹²²*United States v. American Exch. Nat'l Bank*, 70 Fed. 232 (S.D.N.Y. 1895).

¹²³See 1 MORSE, BANKS AND BANKING §§289e, 322 (6th ed. 1928).

¹²⁴*McCurdy v. The Society of Savings*, 6 Ohio Dec. 1169, 11 Am. L. Rec. 156 (1882).

¹²⁵*Reinhardt v. Passaic-Clifton Nat'l Bank & Trust Co.*, 16 N.J. Super. 430, 84 A.2d 741 (1951), *aff'd*, 9 N.J. 607, 89 A.2d 242 (1952).

¹²⁶See Klaus, *supra* note 119.

Hence, since the drawer owes the drawee no assurances regarding these risks, such assurances do not fall within the area of proper presentment, the duty owed by holder to the drawer and the indorser. Likewise there is no duty owed by the collection agent to the holder to give such assurances to the drawee in order to promote the conversion of the check into acceptable value.

Thus the weight of authority seems to be that there is no warranty of title or warranty of right to payment made to the drawee,¹²⁷ the collection agent, or the collection subagent, especially if the drawee or collection subagent has knowledge of the agency of the presenter or transferor, as by a restrictive indorsement, unless the warranties are specially contracted for.¹²⁸ It is said that holdings to this effect startled the banks,¹²⁹ particularly in regard to the risk of forged indorsements. Suppose *H* in Gainesville, Florida, who holds a check drawn on *D* Bank in New York, follows the usual collection procedure by depositing it in *A* Bank, in Gainesville, which forwards it to its correspondent, *B* Bank in Jacksonville, which forwards it to its correspondent, *C* Bank in New York, which presents it to *D* through the clearing house. How can *D* know that *H* is entitled to payment? Specimens of the indorsers' signatures are not in its records, and the rationale of the well-known *Price v. Neal*¹³⁰ situation is not available. It seems that *D* must either charge the cost of the risks or insurance to cost of business, thus increasing the cost of collection, or go out of the bank depositing business. Check collections in which holder and drawee are in different localities become stymied. Would it not be better for *H* to warrant his right to payment to *A*, which knows and trusts *H*, for *A* to warrant the right to *B*, which knows and trusts *A*, for *B* to warrant the right to *C*, which knows and trusts *B*, and for *C* to warrant to *D*, which knows and trusts *C*? *C*, through its chain of correspondents, is in far better position than *D* to verify the title to this check. Since the law does not afford the warranty by implication, many drawees and collection agents get it by express warranty¹³¹ or clearing house

¹²⁷*South Boston Trust Co. v. Levin*, 249 Mass. 45, 143 N.E. 816 (1924); *First Nat'l Bank v. City Nat'l Bank*, 182 Mass. 130, 65 N.E. 24 (1902).

¹²⁸*National Park Bank v. Seaboard Bank*, 114 N.Y. 28, 20 N.E. 632 (1889); see *Clearfield Trust Co. v. United States*, 318 U.S. 363 (1943).

¹²⁹See *United States v. American Exch. Nat'l Bank*, 70 Fed. 232 (S.D.N.Y. 1895); *First Nat'l Bank of Belmont v. First Nat'l Bank of Barnesville*, 58 Ohio St. 207, 50 N.E. 723 (1898).

¹³⁰3 Burr. 1354, 97 Eng. Rep. 871 (1762).

¹³¹*District Nat'l Bank v. Washington Loan and Trust Co.*, 65 F.2d 831 (D.C. Cir. 1933); *First Nat'l Bank v. New Jersey Trust Co.*, 18 N.J. Misc. 449, 14 A.2d

regulations.¹³² True, *D* may not be entitled under the law to a warranty from *C* regarding prior indorsements, and it has the penalties of wrongful dishonor hanging over it;¹³³ nevertheless, it frequently gets an express warranty from *C* either by *C* being denied the use of clearing house facilities for presenting checks unless it warrants to the drawees the genuineness of indorsements, or by *C* being told by *D* that if it will not take care of *D* by assuring it regarding title to the check, when *D* has a check for collection drawn on *C*, *D* will not take care of *C*. This usually gets results: *C* tells *B* that it will act as *B*'s correspondent and receive checks from *B* for collection only on condition that *B* makes express warranty to *C*; *B* tells *A* that it will act as *A*'s correspondent and receive checks from *A* for collection only on condition that *A* makes the express warranty to *B*; and *A* will receive the check for collection only on *H*'s warranty. In view of *D*'s obligation to the drawer, it may run some risk in making demand for a warranty, but not so *C*, *B*, and *A*; they are not public utilities and can deal with whomever they please on agreed-upon terms.

In addition to these risks of the drawee, which support the widespread practice of bargaining for warranties to collection agents and drawees, there are special risks that lend additional support to the practice. The foremost of these is the power of the true titleholder of a check to bring an action in conversion or for money had and received against the drawee¹³⁴ or any collection agent¹³⁵ that handled

765 (Sup. Ct. 1940); *Real Estate Land Title & Trust Co. v. United Sec. Trust Co.*, 303 Pa. 273, 154 Atl. 593 (1931).

¹³²For a statement regarding the existence of such regulations and the reason for them, see *First Nat'l Bank of Belmont v. First Nat'l Bank of Barnesville*, *supra* note 129, and for an example of such regulation and its effect see *First Nat'l Bank v. United States Nat'l Bank*, 100 Ore. 264, 197 Pac. 547 (1921).

¹³³*But see* notes 147, 149 *infra*.

¹³⁴*Schweitzer v. Bank of America*, 42 Cal. App.2d 536, 109 P.2d 441 (1941); *Blacker and Shepard Co. v. Granite Trust Co.*, 284 Mass. 9, 187 N.E. 53 (1933); *Henderson v. Lincoln Rochester Trust Co.*, 303 N.Y. 27, 100 N.E.2d 117 (1951); *Hartford Accid. & Indemnity Co. v. Bear Butte Valley Bank*, 63 S.D. 262, 257 N.W. 642 (1934). *But see* *Strickland Transp. Co. v. First State Bank*, 147 Tex. 193, 214 S.W.2d 934 (1948).

¹³⁵*Atlanta & St. A.B. Ry. v. Barnes*, 96 F.2d 18 (5th Cir. 1938); *Henderson v. Lincoln Rochester Trust Co.*, 303 N.Y. 27, 100 N.E.2d 117 (1951); *House-Evans Co. v. Mattoon Transfer and Storage Co.*, 275 P.2d 268 (Okla. 1954); *Bell-Wayland Co. v. Bank of Sugden*, 95 Okla. 67, 218 Pac. 705 (1923); *Lindsley v. First Nat'l Bank*, 325 Pa. 393, 190 Atl. 876 (1937); *Bell v. Citizens Nat'l Bank*, 122 W. Va. 312, 9 S.E.2d 143 (1940); see 7 AM. JUR., *Banks* §597 (1937).

the check under a forged indorsement. Another risk to the collection agent is the power of a drawee that paid a check under a forged indorsement to recover the proceeds from the agent on the "payment under mistake of fact" theory.¹³⁶ This risk to the agent is far from being removed entirely by the holding that the drawee may not recover if it knew that the party receiving the funds was an agent and the agent had already in good faith paid over the proceeds to the forwarding agent or principal.¹³⁷ This holding may ameliorate the risk to the agent but to that extent adds further need for the warranty to the drawee by the agent, which in turn should have a warranty from the forwarding agent or principal. Although a collection agent should not lose sight of the general concept that an agent is entitled to indemnity from his principal for normal loss resulting from the execution of the agency, this remedy is not adequate to meet the needs of the collection process. In any event the custom among banks of giving an express warranty of right to payment is so well established that it is difficult if not impossible to believe that a bank could voluntarily take a check for collection and then refuse to give a warranty without breaching duty to make proper presentment, particularly if it has recourse against the forwarder on an express warranty.

In spite of some authorities it can easily be shown that the drawer-drawee relationship is more than the simple creditor-debtor relationship. When the deposit contract is created both parties know that normally the demand for payment will be made by a third party, the payee or the indorsee, whose identity most likely will not be known to the drawee-debtor. In recognition of this situation, plus the idea that the drawee owes a duty to the depositor to use due care and good faith in paying checks, many cases have held that the drawee is entitled to have the presenter identify himself.¹³⁸ This right has

¹³⁶*Canal Bank v. Bank of Albany*, 1 Hill 287 (N.Y. 1841); *P. & H. Finance Co. v. First State Bank*, 185 Okla. 558, 94 P.2d 894 (1939); see *Withers v. Jefferson Trust Co.*, 123 N.J. Eq. 113, 196 Atl. 442 (1938); *W. E. Richmond & Co. v. Security Nat'l Bank*, 16 Tenn. App. 414, 64 S.W.2d 863 (1933); 5 WILLISTON, CONTRACTS §1574 (rev. ed. 1937).

¹³⁷*United States v. American Exch. Nat'l Bank*, 70 Fed. 232 (S.D.N.Y. 1895); *National Park Bank v. Seaboard Bank*, 114 N.Y. 28, 20 N.E. 632 (1889); see *Jefferson County Bank v. Hansen Lumber Co.*, 246 Ky. 384, 55 S.W.2d 54 (1932); 5 WILLISTON, *supra* note 136, §1595. Such paying over to the principal will not help the agent if suit is by the true owner. *Bell v. Citizens Nat'l Bank*, 122 W. Va. 312, 9 S.E.2d 143 (1940).

¹³⁸An example is *Citizens Nat'l Bank v. Reynolds*, 72 Ind. App. 611, 126 N.E. 234 (1919).

been limited to identification of the person only,¹³⁹ however, as opposed to identification of the person as the titleholder, which is the all-important thing to the drawee. Identification usually has been accomplished by the cumbersome process of finding some third party mutually known to the drawee and the presenter. Thus, identification on request is a right drawn by implication from the contract between the drawer and the drawee with which the holder and his agents are presumed to be familiar, at least to the extent of usual terms. The same type of need which led to this implication has caused some courts¹⁴⁰ and legislatures¹⁴¹ to take the position that the drawee is entitled to a receipt for payment. There are a number of holdings to the effect that an indorsement by a presenter performs the function of a receipt, but incidentally, probably by the weight of authority, an indorsement that does not contain an express warranty amounts to nothing more than a receipt.¹⁴² The provision of the Negotiable Instruments Law that the drawee is entitled to have the check physically presented and delivered to it is a type of identification and receipt, carrying recognition that a drawee's status is a bit more than that of an obligor with a pure duty to pay at its peril.¹⁴³ It is fraud on the drawee for presentment to be made by one with knowledge that he is not entitled to payment in his own right or as agent. There are holdings to the effect that the drawee has a right to rely on the assumption that the presenter exercised due care in receiving the check,¹⁴⁴ and if the drawee can show lack of due care and subsequent loss by paying under a forged indorsement it may recover on the negligence theory.

¹³⁹As to the effect of identifier's indorsement see *Commercial Press v. Crescent City Nat'l Bank*, 26 La. Ann. 744 (1874); *Smith v. State Bank*, 54 Misc. 550, 104 N.Y. Supp. 750 (Sup. Ct. 1907); *Judge v. West Philadelphia Title & Trust Co.*, 68 Pa. Super. 310 (1917).

¹⁴⁰*Eichner v. Bowery Bank*, 24 App. Div. 63, 48 N.Y. Supp. 978 (1st Dep't 1897); *Pickle v. Muse*, 88 Tenn. 380, 12 S.W. 919 (1890).

¹⁴¹A number of states have statutes which provide that whoever pays money is entitled to a receipt from the person receiving payment, e.g., California, Iowa, New York, North Dakota, and Oregon. FLA. STAT. §687.08 (1957) requires a receipt only on payment of a secured loan or part thereof.

¹⁴²*But see* P. & H. Finance Co. v. First State Bank, 185 Okla. 558, 94 P.2d 894 (1939); 2 PATON'S DIGEST OF LEGAL OPINIONS, *Collection*, §25.2 (1942). An example of the opposite view is *Keene v. Beard*, 8 C.B.N.S. 372, 141 Eng. Rep. 1210 (1860).

¹⁴³NEGOTIABLE INSTRUMENTS LAW §74, *Gilpin v. Savage*, 201 N.Y. 167, 94 N.E. 656 (1911); *Cuddy v. Sarandrea*, 52 R.I. 465, 161 Atl. 297 (1932).

¹⁴⁴E.g., *Citizens' Bank v. J. Blach & Sons, Inc.*, 228 Ala. 246, 153 So. 404 (1934).

Thus, in view of these rights of the drawee, created by operation of law in many jurisdictions, it seems that proper presentment in these jurisdictions involves more than a bare timely demand of payment; it includes identification, physical display and surrender of the check on payment, and may include the giving of a receipt, at least to the extent of an indorsement on the check. It may also include a warranty that the presenter has used due care in acquiring possession of the check, and certainly it includes a representation that the presenter has no knowledge of a lack of the right to receive payment and thereby discharge the check. Consequently, the drawee's tender conditioned on one or more of the above items may constitute valid tender, and if the presenter fails to perform the conditions the result is failure of proper presentment, with discharge of secondary parties under section 120 (4) of the Negotiable Instruments Law. So, let it be said again that the statutes, as well as the cases, recognize that the drawee differs from a mere debtor who must pay at his peril. Note, however, how far short the recognition falls in fulfilling the function that supports it. The identification is of the person and not the titleholder; the receipt does not necessarily make the receiver liable for the return of the proceeds; physical possession of the check by the drawee does not destroy the interest of the unpaid titleholder; and success in suit on the theory of fraud or negligence is limited to the narrow situations in which *scienter* or lack of due care can be established. When applied to nonlocal check collections performed in the volume handled by the banking system today, these limitations are so magnified that the protections afforded the drawee are so archaic that they are in most cases useless, except in the small area in which fraud or negligence can be established.

An implied warranty to collection agent and drawee, covering forged indorsements and alterations, that does not depend on *scienter* or a particular standard of care is the answer to the needs of the collection process, particularly for nonlocal checks.¹⁴⁵ In view of the essential requirements of a modern check collection process, the well-

¹⁴⁵Indeed, there is some authority to the effect that an implied warranty is made to the drawee regarding forged indorsements and alterations. *Security Sav. Bank v. First Nat'l Bank*, 106 F.2d 542 (6th Cir. 1939); *Wellington Nat'l Bank v. Robbins*, 71 Kan. 748, 81 Pac. 487 (1905); *American Exch. Nat'l Bank v. Yorkville Bank*, 122 Misc. 616, 204 N.Y. Supp. 621 (Sup. Ct. 1924). For a recommendation of such warranty to drawee see Turner, *Bank Collections—The Direct Routing Practice*, 39 YALE L.J. 468, 477, n.40 (1930). As to the need for warranty in view of the policy of the Negotiable Instruments Law, the opinion in *Atlantic Nat'l Bank v.*

established custom among banks of expressly warranting right to payment, the requirements of such warranty by many clearing house regulations, the recognition by the law that the position of the drawee is more than that of a simple debtor who must pay on bare demand, and the fact that, notwithstanding some authorities, warranties do attach by operation of law to a number of transactions other than sales of tangibles and negotiations of intangibles, such as bailments,¹⁴⁶ the sound position seems to be that warranty of the genuineness of indorsements and terms of the check is a part of the proper presentment duty owed by the holder to the drawer and the indorser and in turn by the collection agent to the holder. Indeed, such warranty should arise by operation of law,¹⁴⁷ subject to disclaimer.¹⁴⁸ There is no question that the presentment duty is designed to protect the interests of the drawer and the indorser; and the conclusion might be drawn that warranty, receipt, and the like have no place in the presentment duty for the reason that the drawer or indorser cannot lose, regardless of whether the holder warrants or gives a receipt. But this is not true

United States, 250 F.2d 114, 118 (5th Cir. 1957), states: "The ready fluid circulation of negotiable commercial paper requires the assurance to the drawee that the payee's endorsement has not been forged because the drawer's engagement is that the drawee will pay only when the person to whose order the instrument is drawn shall have endorsed it." See *National Metropolitan Bank v. United States*, 323 U.S. 454 (1944).

¹⁴⁶*Standard Oil Co. v. Boyle*, 231 App. Div. 101, 246 N.Y. Supp. 142 (4th Dep't 1930); see 2 VAND. L. REV. 675 (1949); 4 VAND. L. REV. 921 (1951).

¹⁴⁷Chief Judge Ruger in *Parker v. Stroud*, 98 N.Y. 379, 385, 50 Am. Rep. 685, 688 (1885), followed by *Gilpin v. Savage*, 201 N.Y. 167, 171, 94 N.E. 656, 657 (1911), stated: "It is essential to the validity of a demand, that it shall be made by a person authorized to receive payment . . ." Then it should follow that the duty to present includes a duty to warrant authority to receive payment. Also §72 (1) of the Negotiable Instruments Law provides that presentment by one not entitled to payment is not valid presentment. From this it can be argued that the drawee has a right not to have presentment made by one not authorized to receive payment. Hence the drawee is entitled to assume from the act of presentment a representation that the presenter is authorized to receive payment. No attempt should be made to bring the warranty within the scope of §65 or §66 of the Negotiable Instruments Law. That is not necessary; the common law is still applicable to negotiable instruments in a number of areas. See §196.

¹⁴⁸2 PATON'S DIGEST OF LEGAL OPINIONS, *Forged Paper*, §2B:8 (1942), suggests that if a collecting bank used a disclaimer clause it is doubtful that the drawee would honor the check. This could be interpreted to imply that the drawee is entitled to the warranty; otherwise it would not dishonor in the face of the severe penalties for wrongful dishonor. Therefore, the disclaimer by the collecting agent in the ordinary situation should constitute a breach of the presentment duty.

if the drawee and the collection agents are entitled to them.¹⁴⁹ The drawer and the indorser have an interest in the payment of the check, and they run risks when it is not paid. From these risks flows the rule that failure of proper presentment discharges them. Clearly the argument for imposing the duty to give a warranty to the collection agents and the drawee regarding title or right to payment is an argument for increasing the burden of the presentment obligation. It is submitted that the answer is not necessarily to decrease the presentment burden but to adjust it, upward or downward when needed and appropriate, to achieve check collection efficiency with reasonable protection of the interests of the parties, and thereby to promote the policy of the Negotiable Instruments Law by making the check a more serviceable device. It may be argued that requiring the warranty is just one step removed from the drawee requiring security of reimbursement from the drawer, or perhaps even a bond from the presenter. It may be only one step, but it is a big one, and not needed in order adequately to protect the drawee's interest. But the most significant objection is that it would be an unnecessary burden on the use of the negotiable device and against the policy of its being a "courier without luggage."¹⁵⁰

The Uniform Commercial Code¹⁵¹ recognized the problem and met it by providing that the collection agent shall receive the warranty of right to payment automatically by operation of law upon transfer to it and that the drawee shall receive the same warranty upon presentment.¹⁵² In other words, the warranty does not even depend upon

¹⁴⁹Before the drawer has a cause of action against the drawee for wrongful dishonor there must be a proper demand for payment by the drawer or one entitled to make the demand on his behalf. The holder of the check is such a person, and he assumes the obligation to the drawer and the indorser of making proper demand, that is, fulfilling the drawer's duty to drawee, the duty of presentment owed drawer and indorser. See *Joachimson v. Swiss Bank Corp.*, [1921] 3 K.B. 110; 1 MORSE, BANKS AND BANKING §§289c, 322 (6th ed. 1928).

¹⁵⁰See *Overton v. Tyler*, 3 Pa. 346, 45 Am. Dec. 645 (1846); Note, 28 MICH. L. REV. 1023 (1930).

¹⁵¹See also BANK COLLECTION CODE §4, which provides that a restrictive indorsement that puts a check in the collection process constitutes a warranty of right to payment to all subsequent holders, including collection agents, and to the drawee unless the indorsement specifically disclaims the warranty.

¹⁵²UNIFORM COMMERCIAL CODE §§4-207 (1) (a) (3), 3-417 (a) (1957). See LAW REVISION COMMISSION OF STATE OF NEW YORK, LEGISLATIVE DOCUMENT NO. 65 (c) (1954); Andrews, *Should Article 3 of the Uniform Commercial Code Be Adopted in Ohio?*, 14 OHIO ST. L.J. 32, 49 (1953); Beutel, *Comparison of the Proposed Commercial Code, Article 3, and the Negotiable Instruments Law*, 30 NEB. L. REV. 531,

an indorsement but is automatically made a part of presentment; it arises from the single act of putting the check in the bank collection process or the act of presentment. It would seem, however, that a collection agent could still violate its presentment duty by expressly disclaiming the warranty upon its demand of payment from the drawee. The code also provides that the drawee may require receipt and identification of the presenter, together with evidence of the authority to make presentment.¹⁵³

As far as the drawee's interest and the resulting interest of the drawer and the indorser are concerned, the problem could be met by doing violence to the rights of titleholders, as is done to a considerable degree in England¹⁵⁴ and generally in civil law countries,¹⁵⁵ namely, by providing that a good faith payment to the presenter of the check, even though he holds under a forged indorsement, discharges the check, including the liabilities of the drawee, the drawer, and the indorsers. The idea is to promote the principle of free circulation by protecting the bona fide purchaser and payor rather than the real owner. It involves the old contest between the policy of protecting titles and property interests and the policy of promoting trade by decreeing finality of transactions. Business tends to want the latter but with a reasonable degree of the former, hence the struggle of the law to strike a compromise between the two. The tendency in the United States has been generally to go slow in giving up protection to property interests in order to promote business; for instance, this country never adopted the true English Market *Overt* doctrine, wherein the law protects purchasers of even stolen goods if the sale occurred at a business "fair."

Although the Uniform Commercial Code does not go as far as the civil law countries in permitting the destruction of an owner's interest in a check, it goes much further than the holder in due course concept of the present law by providing that the payor's liability, including a drawee, is discharged by payment to the presenter, even

554 (1951); Brome, *Bank Deposits and Collections*, 16 LAW & COMTEMP. PROB. 308, 317 (1951); Leary, *Article 4: Bank Deposits and Collections under the Uniform Commercial Code*, 15 U. PITT. L. REV. 565, 591 (1954); Note, 27 IND. L.J. 561 (1952).

¹⁵³UNIFORM COMMERCIAL CODE §3-505 (1) (d) (1957).

¹⁵⁴See Bills of Exchange Act, 1882, 45 & 46 VICT. c. 61, §§60, 80; Charles v. Blackwell, 2 C.P.D. 151 (1877); HOLDEN, *HISTORY OF NEGOTIABLE INSTRUMENTS IN ENGLISH LAW* (1955).

¹⁵⁵See Hudson and Feller, *The International Unification of Laws Concerning Bills of Exchange*, 44 HARV. L. REV. 333 (1931).

though made with knowledge of the claim of another person.¹⁵⁶ In other words, the code seems to eliminate the payment in due course concept of the Negotiable Instruments Law¹⁵⁷ by permitting destruction of the true owner's title in a check payable to bearer by the drawee's payment to a presenter who is a thief, in spite of knowledge or suspicion that he is a thief. This position of permitting bad faith payment to destroy interest in negotiable paper is open to serious question policywise, even from a businessman's standpoint. Perhaps the policy of the code in promoting ease of circulation and collection has not gone too far, but there is no question that this tendency to destroy interests in negotiable paper can go too far. Who wants to hold a check if his interest can be so easily destroyed? If potential holders resist becoming holders the service of the check to the business world will be curtailed to that extent. Whatever the cause may be, the fact remains that the check is used far more in the United States than in civil law countries. It should not be concluded, however, that, since the code destroys the payment in due course concept, the warranty in the presentment process is not needed under the code. This conclusion would be erroneous for the reason that the code, like the Negotiable Instruments Law, preserves the property interest of the payee or special indorsee on a check as opposed to the true owner of a check payable to bearer; in other words, the payee or indorsee does not lose his interest by a forged indorsement.¹⁵⁸

Making warranty of right to payment, perhaps with the exception of the forgery of drawer's signature, an implied part of the due presentment act, including transfers in the collection channel, probably would meet the needs of the collection process regarding certainty as to the titleholder without further diluting the protection to owners afforded by the present law.

DIRECT ROUTING BY MAIL

The common law is clear that it is negligence for a bank collection agent to send a check directly to the drawee for collection,¹⁵⁹ and

¹⁵⁶UNIFORM COMMERCIAL CODE §3-603 (1) (1957). Of course there is present authority for giving greater protection to a good faith drawee than to a holder in due course. *E.g.*, see the refusal to apply NEGOTIABLE INSTRUMENTS LAW §15 to the drawee by *Weiner v. Pennsylvania Co.*, 160 Pa. Super. 320, 51 A.2d 385 (1947).

¹⁵⁷NEGOTIABLE INSTRUMENTS LAW §88.

¹⁵⁸UNIFORM COMMERCIAL CODE §§3-204, 3-404 (1957).

¹⁵⁹*Marx & Co. v. Bankers' Credit Life Ins. Co.*, 224 Ala. 249, 139 So. 421 (1931);

the fact that the drawee is the only bank in town is no excuse.¹⁶⁰ It is generally held that a collecting agent has a duty to select subcollecting agents "with judgment and care, and one of the first elements of care is to select a subagent who is not adversely interested in the subject matter."¹⁶¹ Mr. Justice Sutherland, in *Federal Reserve Bank of Richmond v. Malloy*,¹⁶² suggests that the basis of the rule that forbids the use of the drawee as a collection agent is that the drawee is not a suitable agent for the enforcement of his own obligation. There are two aspects of the collection agent's obligation worth noting. One is the duty to the holder to make reasonable effort to get the holder's interest in the check converted to cash or other acceptable value. The other aspect is the duty to the holder to properly execute the holder's duty to secondary parties, namely, make presentment in a manner that will prevent the discharge of secondary parties in any way other than by payment. There are cases holding that secondary parties are entitled to persuasive presentment and that this cannot be accomplished by mail or telephone.¹⁶³ The duty owed secondary parties by the holder is something more than demand of payment; it involves an exhibition of the instrument¹⁶⁴ at the drawee's place of business with a personal demand of payment by the holder or his agent, accompanied by the usual persuasive elements associated with a personal presentation as opposed to mail or telephone presentment. Generally the right to waive persuasive presentment is restricted to secondary parties;¹⁶⁵ however, it has been held that the rule requiring exhibition of the instrument in presentment is for the benefit of the

see Turner, *Bank Collections—The Direct Routing Practice*, 39 YALE L.J. 468 (1930); 7 AM. JUR., *Banks* §§674-78 (1937). But see *McEwen v. Cobb*, 104 Misc. 477, 172 N.Y. Supp. 44 (Sup. Ct. 1918).

¹⁶⁰*First Nat'l Bank v. Bank of Whittier*, 221 Ill. 319, 77 N.E. 563 (1906); *Leach v. Citizens' State Bank*, 203 Iowa 782, 211 N.W. 522 (1926); *American Exch. Nat'l Bank v. Metropolitan Nat'l Bank*, 71 Mo. App. 451 (1897); *Bank v. Floyd*, 142 N.C. 187, 55 S.E. 95 (1906); *Winchester Milling Co. v. Bank of Winchester*, 120 Tenn. 225, 111 S.W. 248 (1908); *Pinkney v. Kanawha Valley Bank*, 68 W. Va. 254, 69 S.E. 1012 (1910); see 7 AM. JUR., *Banks* §675 (1937).

¹⁶¹*Marx & Co. v. Bankers' Credit Life Ins. Co.*, 224 Ala. 249, 257, 139 So. 421, 427 (1931).

¹⁶²264 U.S. 160 (1923).

¹⁶³*Robinson v. Lancaster Foundry Co.*, 152 Md. 81, 136 Atl. 58 (1927); 11 MINN. L. REV. 554 (1927); 37 YALE L.J. 258 (1927).

¹⁶⁴NEGOTIABLE INSTRUMENTS LAW §74. But see UNIFORM COMMERCIAL CODE §3-504 (1957).

¹⁶⁵*Robinson v. Lancaster Foundry Co.*, 152 Md. 81, 136 Atl. 58 (1927).

drawee and may be waived by him.¹⁶⁶ One court, although holding that routing the obligor out of bed near midnight constituted improper presentment, suggested that the conclusion might be different if the obligor indicated a waiver of any objection to the time and manner of the presentment.¹⁶⁷ Certainly the court is not giving much thought to personal persuasion or a climate or setting that would tend to induce payment. The inducing motivations associated with embarrassment from personal confrontation would not likely be present at a midnight presentment.

Many cases involving the direct routing problem deal with the duty of the collecting agent to the holder to take reasonable steps to convert the check to cash, and conclude that the bank with the duty to pay the holder cannot be a proper agent of the holder to handle the check on his behalf.¹⁶⁸ A collecting agent that mails the check directly to the drawee must bear any loss that results to the holder.¹⁶⁹ And this loss usually is held to be the amount of the check. A clear situation occurs when the collecting bank sends the check by mail to the drawee, which receives the check while still paying instruments presented over the counter but suspends operations without paying the check. Not only does this result in a breach of duty owed by the agent to the holder to convert the check to acceptable value, but also the drawer and the indorsers are discharged, not because the check failed to arrive at the drawee quickly enough¹⁷⁰ but because of the failure of personal presentment.¹⁷¹ Often courts give no consideration to the holder's right to recover part of the amount of the instrument from the drawer in the event the drawer's loss does not equal the entire amount.¹⁷² A custom or usage cannot successfully justify the sending of a check directly to the drawee bank by mail, for the reason that customary negligence cannot justify negligence.¹⁷³

¹⁶⁶Porter v. East Jordan Realty Co., 210 Mich. 398, 177 N.W. 987 (1920).

¹⁶⁷Dana v. Sawyer, 22 Me. 244, 39 Am. Dec. 574 (1843).

¹⁶⁸German Nat'l Bank v. Burns, 12 Colo. 539, 13 Am. St. Rep. 247 (1889); Drovers' Nat'l Bank v. Anglo-American Packing Co., 18 Ill. App. 191 (1885).

¹⁶⁹Western Wheeled Scraper Co. v. Sadilek, 50 Neb. 105, 61 Am. St. Rep. 550 (1897); see Louisville & N.R.R. v. Federal Res. Bank, 157 Tenn. 497, 10 S.W.2d 683 (1928).

¹⁷⁰See the discussion of timely presentment *supra*.

¹⁷¹See German Nat'l Bank v. Burns, 12 Colo. 539, 13 Am. St. Rep. 247 (1889).

¹⁷²For a consideration of the extent of the drawer's discharge see discussion of the check under heading "The Basic Problem" *supra*. Also see Pinkney v. Kanawha Valley Bank, 68 W. Va. 254, 69 S.E. 1012 (1910).

¹⁷³Whitney v. Esson, 99 Mass. 308, 96 Am. Dec. 762 (1868); American Exch.

Just how valid is this idea that a drawee on a check is not a suitable agent of the holder for collection of an obligation against itself? It brings to mind the old precept that one cannot serve two masters, the holder and the drawer, at the same time, and also the basic principle of agency law that one cannot properly serve himself and a third party in conflict of interest matters. When sent by mail, the drawee has on occasion lost or destroyed the check and quite frequently, if not usually, given less attention or priority to mail presentments than counter presentments. For instance, in *Anderson v. Rodgers*¹⁷⁴ the drawee received a check by mail on the evening of December 12 and continued to do business during all of the following day, receiving deposits and paying checks over the counter. At the end of banking hours on the second day, although the drawer had enough money on deposit to cover the check, the drawee returned the check, unpaid, by mail to the collecting bank, did not open for business thereafter, and paid nothing to either the holder or the drawer. In addition, since banks are not public utilities and may choose their customers and the persons with whom they deal, it has been suggested that this may be a further impediment to direct routing¹⁷⁵ for the reason that a bank may refuse to deal with the forwarding bank and thus cause a unwarranted delay in presentment and potential loss. Although it is clear that an intermediate collecting bank may refuse to handle a check drawn on a particular bank,¹⁷⁶ nevertheless it would seem that refusal by a drawee to deal with any agent of the holder would constitute dishonor, and that the only impediment noticeable in such case would be that caused by wrongful dishonor. It may be questionable whether there are some agents of a holder with whom a drawee may refuse to deal without suffering the penalties of wrongful dishonor.

For years banks have resisted the requirement that checks be presented to the drawee over the counter by their messengers or those of a subagent correspondent other than the drawee. There are two primary reasons for this: (1) it saves time to present directly to the drawee, on the average about twenty-four hours, which, incidentally,

Nat'l Bank v. Metropolitan Nat'l Bank, 71 Mo. App. 451 (1897); Pinkney v. Kanawha Valley Bank, *supra* note 172; see Note, 77 Am. St. Rep. 613, 623 (1901). *But see* Marx & Co. v. Bankers' Credit Life Ins. Co., 224 Ala. 249, 139 So. 421 (1931).
¹⁷⁴53 Kan. 542, 36 Pac. 1067 (1895).

¹⁷⁵See Turner, *supra* note 159, at 476.

¹⁷⁶McEnelly v. American Nat'l Bank, 172 Minn. 204, 214 N.W. 922 (1927).

operates in favor of the policy behind the requirement of timely presentment;¹⁷⁷ and (2) it reduces the "float" by one day on an average. When the tremendous amount of "float" involved in check collections¹⁷⁸ is considered, it is easy to see that the interest charges on the amount for one day are enormous. Direct routing reduces the time needed for collection and therefore the time needed for the operation of the commercial transaction; and it reduces the cost of the collection and therefore the cost of the transaction, both highly desired objectives of the economy and presumably of commercial law. It should take compelling reasons to prevent a change in the law, and reasons of this caliber just do not exist. Admittedly a drawee bank about to become insolvent may be motivated to act not entirely in the best interests of the check holder; nevertheless the drawee's position is not that which traditionally forms the basis for the rule against an agent operating in a situation involving a conflict of interest. Most of the fiduciary elements are lacking: the great volume of the drawee's payments are routine; the obligation is clear; there is no discretion, no bargaining; and there are government regulations and considerable insurance protection against the drawee's insolvency. The force of the drawer's contract with the drawee and the law of libel,¹⁷⁹ absent in the usual conflict of interest cases, are in most instances strong factors motivating proper treatment by the drawee of the holder's interest. Conceivably a conflict of interest could occur between the drawee's duty to the drawer and its duty to the holder, as in the case of a stop payment order in relation to the finality of payment problem; but if the law comes to grips with these problems with the certainty that it should this conflict of interest is not likely to arise in practical operation. Potent protection for the holder is provided by section 137 of the Negotiable Instruments Law,¹⁸⁰ which provides that if the drawee destroys the check or refuses to return it within twenty-four hours the check becomes certified. Probably a check presented over the counter will be handled more quickly than one arriving by mail if the timing process is started from the time the check reaches the drawee's premises. But if the timing is started when the collection process starts, the direct mail presentment usually will re-

¹⁷⁷See note 169 *supra*.

¹⁷⁸See the discussion of the use of checks and the magnitude of the "float" under the heading "Factual Background" *supra*.

¹⁷⁹*Reinish v. Consolidated Nat'l Bank*, 45 Pa. Super. 236 (1911).

¹⁸⁰*Wisner v. First Nat'l Bank*, 220 Pa. 21, 68 Atl. 955 (1908).

sult in payment or dishonor quicker than presentment through a local subagent correspondent. It is worth noting that the longer time that the check presented by mail remains on the drawee's premises before payment often results from the sheer volume handled in this way; counters could not be built long enough to handle a similar volume over the counter, and even if they could the cost would be prohibitive.¹⁸¹ Perhaps this will be considered an exaggeration, since in practice the local subagent correspondent probably will present huge batches of checks at one time either directly or through the clearing house. But is that proper presentment?¹⁸² What happens to the argument for persuasive presentment?¹⁸³ The point noted here is the distinction between law and practice, practice no doubt necessitated by the demands of the economy.

Some courts have given legal sanction to direct routing if it is a customary banking practice, reasonable under the circumstances, and so well known and established that the custom becomes a part of the contract between the bank and the holder when the bank receives the check for collection.¹⁸⁴ On the assumption that the holder has impliedly agreed to the practice, these cases shift the risk to him, since by the weight of authority this practice does not constitute proper legal presentment from the standpoint of the drawer and the indorsers. If one needs the ground that the holder has impliedly consented in order to justify the conclusion, it is not a very pretty rationale, since the holder has no real alternative.

Courts have upheld the direct routing practice when the holder expressly agreed to it in his contract with the collection agent;¹⁸⁵ consequently banks usually provide for direct routing in all their contracts with their customers, including deposit slips. Frequently the deposit slip is the only source of agreement between the collection agent and the holder, since usually the agent and the holder also have

¹⁸¹See the discussion under the heading "Factual Background" *supra*.

¹⁸²See the discussion of timely presentment *supra*, wherein the effect of clearing house presentment is considered.

¹⁸³See note 163 *supra*.

¹⁸⁴*South Jacksonville v. Jacksonville Traction Co.*, 50 F.2d 839 (5th Cir. 1931); *Transcontinental Oil Co. v. Federal Res. Bank*, 172 Minn. 58, 214 N.W. 918 (1927); *Kershaw v. Ladd*, 34 Ore. 375, 56 Pac. 402 (1899); *Chicago, M. & St. P. Ry. v. Federal Res. Bank*, 70 Utah 310, 260 Pac. 262 (1927).

¹⁸⁵*Marx & Co. v. Bankers' Credit Life Ins. Co.*, 224 Ala. 249, 139 So. 421 (1931); *Fergus County v. Federal Res. Bank*, 75 Mont. 582, 244 Pac. 883 (1926); *Oklahoma Gas & Elec. Co. v. First Nat'l Bank*, 179 Okla. 475, 66 P.2d 29 (1937); *Jones v. Clark*, 30 S.W.2d 577 (Tex. Civ. App. 1930).

the relationship of bank and depositor; if they do not, there may or may not be express collection agreements.¹⁸⁶ Much of the collection efficiency of the Federal Reserve System rests upon direct routing, and the only real legal support for this very important aspect of Federal Reserve operations is the forwarding bank's agreement, and in turn the holder's agreement. Direct routing is provided for by Federal Reserve regulations,¹⁸⁷ which are binding on the forwarding bank because of its membership and resulting agreement, but on the holder, if at all, only because the regulations are read into his contracts.¹⁸⁸ Three things are disturbing here:

- (1) Usually the holder is in no position to refuse to agree; thus the bottom falls from under the rationale.
- (2) Although the courts usually uphold Federal Reserve regulations against banks and holders who have "agreed" to them, member banks, and especially nonmember banks that do not have the backing of the dignity of a Federal Reserve regulation and must rely on clauses in deposit slips and the like, are forced by the practical demands of the collection process to operate on a legal foundation that is not only lacking in certainty but also so flimsy that on occasion it may not exist at all. This is particularly true in view of the cases holding deposit slip clauses and other types of bank contracts unenforceable because the print is too small, or the clauses are not called to the depositor's attention, or the depositor lacks bargaining power, or no consideration is received, or the clauses are against public policy.¹⁸⁹

¹⁸⁶For terms of a standard collection agreement see 2 PATON'S DIGEST OF LEGAL OPINIONS, *Collections* §26:2 (Supp. 1954).

¹⁸⁷§§5 (2) and 6 of Regulation J as to checks and Regulation G as to noncash items, promulgated by the Board of Governors of the Federal Reserve System.

¹⁸⁸*Early v. Federal Res. Bank*, 281 U.S. 84 (1930), *affirming* 30 F.2d 198 (4th Cir. 1929); *Transcontinental Oil Co. v. Federal Res. Bank*, 172 Minn. 58, 214 N.W. 918 (1927); *Massey-Harris Harvester Co. v. Federal Res. Bank*, 226 Mo. App. 916, 48 S.W.2d 158 (1932), *aff'd*, 340 Mo. 1133, 104 S.W.2d 385 (1937); *Carson v. Federal Res. Bank*, 254 N.Y. 218, 172 N.E. 475 (1930). The lower court in *Louisville & N.R.R. v. Federal Res. Bank*, 157 Tenn. 497, 10 S.W.2d 683 (1928), suggested that the Federal Reserve regulations had the force of federal statute, but the appellate court refused expressly to rule on this point. In this case the victory of the defendant bank on a negligence charge for direct forwarding was based on the failure to establish a loss resulting from the direct forwarding.

¹⁸⁹See *Hiroshima v. Bank of Italy*, 78 Cal. App. 362, 248 Pac. 947 (1926); *Cala-*

- (3) Most disturbing of all, the failure of these cases to meet the real problem: on the basis of the facts and interests involved where should the risk of direct routing be placed — on the collection agent, on the holder, or on the drawer?

These cases place the risk on the holder based on his fictional agreement. Direct routing should be recognized by the law as part of proper presentment, and the risk should be on the drawer for the same reason that the law made the drawer liable during the period of proper presentment.

If there is anything to the argument that nothing less than an independent correspondent subagent must be used as opposed to direct routing for the reason that the secondary parties are entitled to persuasive presentment, it would be only one more step, and in a sense about as logical, to say that the secondary parties are entitled to personal presentment by the holder for the reason that he would have much more emotional verve than any of his agents could have. This would be just about on a par with the conclusions that a breach of the duty owed by drawer to drawee occurs when the drawer draws a check on paper other than sensitized paper designed to guard against alterations,¹⁹⁰ or leaves a signed blank check with a female.¹⁹¹ Just as these extreme positions would defeat the policy of the Negotiable Instruments Law by unduly encumbering the use of the negotiable de-

mita v. Tradesmen's Nat'l Bank, 135 Conn. 326, 64 A.2d 46 (1949); Reinhardt v. Passaic-Clifton Nat'l Bank and Trust Co., 16 N.J. Super. 430, 84 A.2d 741 (1951), *aff'd*, 9 N.J. 607, 89 A.2d 242 (1952); Speroff v. First-Central Trust Co., 149 Ohio St. 415, 79 N.E.2d 119, (1948).

¹⁹⁰Although an instrument on tree bark may satisfy the "writing" requirement of NEGOTIABLE INSTRUMENTS LAW §1 (1), it would seem to be a breach of duty that the drawer owes to the drawee. And in view of the volume of check collections it would seem to promote the efficiency of the use of checks to prohibit advertising matter on them, such as a facsimile of the front page of a newspaper, with the drawer's signature, the name of the drawee, and the amount of the check tucked away inconspicuously. The argument for requiring sensitized paper has been made unsuccessfully in litigation, and in the light of present facts should be unsuccessful; however, it is not inconceivable that as advancements occur this requirement may become reasonable.

¹⁹¹In *Young v. Grote*, 4 Bing. 253, 130 Eng. Rep. 764 (1827), the suggestion appears that it is a breach of duty owed by drawer to drawee for the drawer to leave a signed blank check with a female, for the reason that she is a female and therefore inexperienced. It is inconceivable that this pronouncement can ever prevail again. According to a popular radio newscaster, today over 50% of all bank officials and employees in this country are women, and there are 150 bank presidents who are women.

vice in proportion to the resulting protection of the interests of parties, so also does the rule against direct routing in the light of present-day operative facts in check collections.

From the point of view of certainty and uniformity of the basic aspects of the relationships of not only holder and drawer but also those of holder and collection agent and holder and collection sub-agent, including the drawee, who may not be in privity with the holder's deposit slip contract, legislation is needed to provide for direct routing. The Bank Collection Code to a degree provides for direct routing of checks,¹⁹² but its unconstitutional status¹⁹³ makes it unsound even to lean upon, much less rest upon.¹⁹⁴ Quite a few state legislatures have tried, with varying degrees of success, to do something about the problem, such as by adoption of the Bank Collection Code or the Forwarding Check Direct to Payor Act.¹⁹⁵ Florida and a number of other states have not adopted either act; however, Florida has a statute that permits forwarding "in the usual commercial way in use according to the regular course of business of banks . . ."¹⁹⁶ The statute was used in *South Jacksonville v. Jacksonville Traction Co.*¹⁹⁷ as a basis for holding that direct routing to the drawee was not negligent presentment, since the circumstances and conditions provided for by the statute, such as customs and practices, were adequately established. This points in the right direction but is risky. The result of the Florida statute seems to be that an act that is negligent at common law becomes not negligent by virtue of the statute if it can be shown that such common law negligent acts were customary.

The Uniform Commercial Code hits the problem head on by providing that a collecting bank may present a check by mail or through a clearing house¹⁹⁸ direct to the drawee bank.¹⁹⁹ Since the economy

¹⁹²BANK COLLECTION CODE §6.

¹⁹³See note 107 *supra*.

¹⁹⁴For an application and discussion of the statute, see Massey-Harris Harvester Co. v. Federal Res. Bank, 340 Mo. 1133, 104 S.W.2d 385 (1937), and Witt v. Peoples State Bank, 166 S.C. 1, 164 S.E. 306 (1932).

¹⁹⁵This act was recommended by the American Bankers Association before it recommended the Bank Collection Code, which, from the Association's point of view, supplemented the former act.

¹⁹⁶FLA. STAT. §674.74 (1957). For similar statutes see GA. CODE ANN. §13-2035 (1953); KY. REV. STAT. ANN. §3720c (1936), supplanted by KY. REV. STAT. ANN. §357.060 (1955) (§6 of Bank Collection Code).

¹⁹⁷50 F.2d 839 (5th Cir. 1931).

¹⁹⁸UNIFORM COMMERCIAL CODE §3-504(2)(a) (1957).

¹⁹⁹*Id.* §4-204(2).

demands speed and a routinized mass collection process and since there are available to meet the demand responsible institutions partially government regulated and insured for the individual's protection, the advantages of the position of the code outweigh the dangers pointed out by the case decisions. The widespread present practice of direct routing, so often in derogation of the law, is one of the main reasons why check collections in fact today are so much more efficient than collections of other types of instruments, drafts for instance. The experience of those engaging in this practice, including an apparent readiness of some with bargaining power to expressly agree to direct routing, is evidence of the business world's recognition of banks as responsible institutions. Indeed, in view of the institutional position given banks by the Uniform Commercial Code, which reflects the opinions of many people in business, and in view of the functions actually performed by banks, one may be inclined to suggest that the recognition goes further, to include the status of public service institutions, at least public-conscious business-service institutions, as to many of their operations, including the collection process. Often business people consider a bank as a type of community financial center, where they meet personally or by agent to terminate commercial transactions by payments. This is evidenced by the practice of some parties, insurance companies for example, of making instruments payable at a bank when no bank appears as a party on the instrument. The practice is recognized by the Negotiable Instruments Law²⁰⁰ and the Uniform Commercial Code.²⁰¹ The code further recognizes the banks as a community financial center by providing that a draft is not varied so as to constitute dishonor by an acceptance to pay at a designated bank,²⁰² even though this type of acceptance requires presentment at that bank.²⁰³ In addition, the code took an especially long step — some have felt a rather dramatic one — toward recognizing a bank as a community institution by changing the presentment law in certain situations to provide for presentment by notice.²⁰⁴ This section of the code makes an effort to ap-

²⁰⁰ §§ 73 (1), 75.

²⁰¹ § 3-504 (4) (1957).

²⁰² *Id.* § 3-412 (3).

²⁰³ *Id.* § 3-504 (4).

²⁰⁴ *Id.* § 4-210. For a discussion of types of paper and their uses which would be benefited regarding collection efficiency by this section, see "Factual Background" *supra*.

proach the same type of efficiency in the collection of instruments that are not payable at a bank that the code attempts to get for the collection of checks and other items payable at a bank. The provision is to the effect that a bank with such an instrument for collection may satisfy the presentment law by sending to the payor written notice that the bank holds the instrument for payment. The idea is that the payor after receiving notice will pay the instrument on the due date by either mailing the payment and trusting the bank to forward the canceled instrument or coming in to the bank personally or by agent. Perhaps today the usual payor would rather have notice by mail instead of by doorbell, since the risks are little. Admittedly the code does not trust a payor other than a bank in that the instrument is not included with the notice as is done in the case of direct routing of checks,²⁰⁵ but, as indicated above, there is good reason for this distinction. In any event the payor by return notice to the bank can receive the protection of what may be the more time consuming and inconvenient doorbell type of presentment, such as exhibition and surrender of the instrument simultaneously with payment at a place other than the community financial center.²⁰⁶ Admittedly also, this is a far cry from persuasive presentment, an interest of secondary parties²⁰⁷ and perhaps the holder too, but in view of the job to be done something has to give, just as the old grocery store with the delivery truck has given way in most instances to the supermarket.

THE DRAWEE AS A COLLECTION AGENT

The concept of the drawee as collection agent of the holder, an idea that seems to be shocking in some quarters,²⁰⁸ is designed to give

²⁰⁵UNIFORM COMMERCIAL CODE §3-504 (1957) seems to permit a collecting bank to send an instrument directly to a payor other than a bank, but to this extent it appears in conflict with §4-204 (2), which is the more specific section and probably should control this point. Sec. 4-204, however, does clearly provide for sending the instrument directly to a nonbank payor if certain conditions are met, such as authorization by the transferor, or by a federal reserve regulation or operating letter, or clearing house rule, or the like.

²⁰⁶UNIFORM COMMERCIAL CODE §3-505 (1957).

²⁰⁷See note 163 *supra*.

²⁰⁸See Federal Res. Bank v. Malloy, 264 U.S. 160 (1924); Marx & Co. v. Bankers' Credit Life Ins. Co., 224 Ala. 249, 139 So. 421 (1931); Leach v. Citizens State Bank, 203 Iowa 782, 211 N.W. 522 (1926); McGoldrick Lumber Co. v. Farmers Lumber Co., 64 N.D. 544, 254 N.W. 281 (1934); Reinisch v. Consolidated Nat'l Bank, 45 Pa. Super. 236 (1911); NEGOTIABLE INSTRUMENTS LAW §189; 9 C.J.S., *Banks and Banking* §§232, 235 (1938).

the holder a basis for action against the drawee for improper handling of the holder's interest, for instance, a delay in presentment to itself for payment until after the drawer becomes insolvent. It is easier to support the practice of direct routing by mail if the drawee can be considered an agent of the holder for some purposes instead of exclusively either as the "right arm" of the drawer, in which case the collection agent owes the duty to the holder to recognize the conflict of interest between holder and drawer and act accordingly to protect the holder's interest, or as the debtor of the drawer, in which case the collection agent owes a duty to the holder, based on the holder's duty to the drawer, to recognize the conflict of interest between drawer and drawee and act accordingly to protect the drawer's interest. However, a number of authorities take a position against the conclusion that the drawee may act in the dual capacity of agent for the drawer to make payment and agent for the holder to present the check to itself for payment, with resulting liability for breach of duties. These authorities point out that there is a conflict of interest involving a fiduciary relationship, that there is no privity whatever between the holder and the drawee, and that the Negotiable Instruments Law provides that the drawee shall not be liable to the holder.²⁰⁹ The rationale used by these authorities includes their idea of the function and operation of a check. The drawer wants to pay a debt, say for goods purchased, and proceeds to accomplish this through his agent, the drawee; he should therefore bear the risks resulting from the failure of the drawee to perform its payment functions properly. The payee wants to receive payment for the goods and proceeds to accomplish this through his agent, the depository bank; therefore he should bear the risks resulting from the failure of the depository bank to perform its presentment functions properly. So, the authorities point out, it is appropriate to line the drawer and his agent, the drawee, up on one side and the payee and his agents on the other, which is in accord with the concept that no one agent can properly represent two different parties in a conflict of interest situation.

Some authorities contend that there is no contractual privity between drawee and holder from which agency duties may be inferred.²¹⁰ There is no question that no privity on the check exists between drawee and holder. Section 127 of the Negotiable Instruments Law

²⁰⁹See note 208 *supra*.

²¹⁰Sec 7 A.M. JUR., *Banks* §545 (1937).

specifically provides that a bill does not operate as an assignment of the funds in the hands of the drawee available for payment of the check and that the drawee is not liable "on the bill" unless it accepts it. Of course this result that a check is not an assignment to the payee of the drawee's obligation, or part thereof, is absolutely necessary to the operation of a large segment of the law applicable to banking procedures; for examples — the law applicable to the order in time in which checks may be paid, and the power of the drawer to stop payment. But the Negotiable Instruments Law does not stop there. Section 189, which is specifically applicable to checks, provides that the drawee "is not liable to the holder, unless and until it accepts or certifies the check." Section 127 leaves an implication that the drawee could be liable to the holder before acceptance on some basis other than the check; but, since section 189 seems deliberately to use more sweeping language, some authorities suggest that the drawee is not liable to the holder in tort or contract.²¹¹

Obviously such a conclusion is not tenable in a situation in which the drawee commits a clear tort against the interest of the holder, destruction of the check for instance. For a century or more the problem of protecting the holder against loss or destruction while the check or bill is physically in the possession of the drawee was recognized by law. In some of the civil law countries the drawee was deemed to have accepted the bill or check if it did not pay it or return it within twenty-four hours. Section 137 of the Negotiable Instruments Law provides that, when the drawee has possession of a bill on presentment for acceptance and destroys it or refuses to return it to the holder within twenty-four hours or other agreed upon period,²¹² he will be deemed to have accepted it. It is to be noted that the result is not in conflict with section 189, since the remedy is in assumpsit and not tort; but obviously it is purely a statutory fiction as far as the acceptance is concerned. There is authority that mere retention beyond twenty-four hours will constitute acceptance; however, the weight of authority requires demand and refusal before

²¹¹See *Elyria Sav. and Banking Co. v. Walker Bin Co.*, 92 Ohio St. 406, 111 N.E. 147 (1915); Aigler, *Rights of Holder of Bill of Exchange Against the Drawee*, 38 HARV. L. REV. 857, 883 (1925).

²¹²*Safety Motors, Inc. v. Elk Horn Bank and Trust Co.*, 217 F.2d 517 (8th Cir. 1954), held that, when the holder authorizes the drawee to hold the check longer than 24 hours for the purpose of trying to collect it, the drawee acts as agent of the holder and not as acceptor.

finding acceptance.²¹³ Generally the statutory fiction has been limited to presentments for acceptance, but some courts recognize that the same type of problem regarding the protection of the holder exists when checks are presented for payment by direct mail routing, and apply section 137 to that situation.²¹⁴ In any event it should be clear that the drawee owes the holder a duty to handle the check with care so as not to lose, destroy, or retain it an unreasonable length of time, and should, on breach of this duty, respond in damages.²¹⁵ The Uniform Commercial Code destroyed the statutory fiction of acceptance in such circumstances but went far toward accomplishing the same result by fixing the liability of the drawee as a converter at the face amount of the check.²¹⁶

A large number of courts have had to meet the question of the liability of the drawee to the true titleholder in the situation in which the drawee pays the check under a forged indorsement. Although there is some authority holding that payment under a forged indorsement constitutes constructive acceptance and recovery can be had by the rightful owner against the drawee in assumpsit,²¹⁷ the weight of authority holds that assumpsit will not lie²¹⁸ but that the drawee is liable to the owner in conversion.²¹⁹

The next step in setting up a relationship involving duties and liabilities between the drawee and the holder was the recognition by

²¹³See *Mt. Vernon Nat'l Bank v. Canby State Bank*, 129 Ore. 36, 276 Pac. 262 (1929); *Westberg v. Chicago Lumber and Coal Co.*, 117 Wis. 589, 94 N.W. 572 (1903).

²¹⁴*Mt. Vernon Nat'l Bank v. Canby State Bank*, 129 Ore. 36, 276 Pac. 262 (1929).

²¹⁵See Ames, *The Negotiable Instruments Law*, 14 HARV. L. REV. 241 (1900).

²¹⁶See UNIFORM COMMERCIAL CODE §§3-419, 4-302 (1957).

²¹⁷*Dawson v. National Bank*, 196 N.C. 134, 144 S.E. 833 (1928). Note that in view of the finding of constructive acceptance the holding is not in conflict with §189 of the Negotiable Instruments Law.

²¹⁸*Henderson v. Lincoln Rochester Trust Co.*, 303 N.Y. 27, 100 N.E.2d 117 (1951); *Elyria Sav. and Banking Co. v. Walker Bin Co.*, 92 Ohio St. 406, 111 N.E. 147, (1915); *Baltimore & O.R.R. v. First Nat'l Bank*, 102 Va. 753, 47 S.E. 837 (1904); *Whorf v. Seattle Nat'l Bank*, 173 Wash. 629, 24 P.2d 120 (1933).

²¹⁹*Louisville & N.R.R. v. Citizens and Peoples Nat'l Bank*, 74 Fla. 385, 77 So. 104, (1917); *Blacker and Shepard Co. v. Granite Trust Co.*, 284 Mass. 9, 187 N.E. 53 (1933); *Kansas City Cas. Co. v. Westport Ave. Bank*, 191 Mo. App. 287, 177 S.W. 1092 (1915). For the effect of these holdings on the warranty problem see the discussion under the heading "Warranties by the Check Collection Agent" *supra*. Note that in order to reach the conclusion of these cases one must interpret NEGOTIABLE INSTRUMENTS LAW §189 to apply only to contract liability. *Contra*, *Strickland Transp. Co. v. First State Bank*, 147 Tex. 193, 214 S.W.2d 934 (1948).

the courts that the drawee held the proceeds of the check as agent and trustee on behalf of the holder after collecting or conditionally collecting the check from itself but before remitting.²²⁰ This holding is especially helpful to a holder when the drawer is discharged and the drawee becomes insolvent after "collecting" but before remitting; it establishes the holder with priority over the trustee in bankruptcy.²²¹

The final step made, by probably what is the weight of authority today, is direct recognition that the drawee acts as agent of the holder for the purpose of presentment to itself for payment, with resulting duties to the holder to make due and proper presentment.²²² This position may seem to be strong medicine if it gives the impression that it makes the drawee just about as liable before acceptance as after.²²³ But there is a big difference; under the position taken the only occasion when there may be a similarity between the liability of the drawee before acceptance and his liability after acceptance is when the drawer's account has adequate funds and no stop order exists. Even when these conditions are present the theory of recovery is in damages for breach of duty, and some courts make the point that the recovery is not necessarily the face amount of the check.²²⁴

²²⁰Miami v. First Nat'l Bank, 58 F.2d 561 (5th Cir. 1932), *certificates dismissed per curiam*, 289 U.S. 707, 290 U.S. 594 (1933), on second appeal, 69 F.2d 346 (5th Cir. 1934); Edwards v. Lewis, 98 Fla. 956, 124 So. 746 (1929); see Nineteenth Ward Bank v. First Nat'l Bank, 184 Mass. 49, 67 N.E. 670 (1903); City Bank v. Hart, 102 Fla. 529, 136 So. 446 (1931); Myers v. Federal Res. Bank, 101 Fla. 407, 134 So. 600 (1931). *But see* Bohlig v. First Nat'l Bank, 233 Minn. 523, 48 N.W.2d 445 (1951).

²²¹Miami v. First Nat'l Bank, *supra* note 220.

²²²*Ibid.*; Standard Trust Co. v. Commercial Nat'l Bank, 240 Fed. 303 (4th Cir. 1917); Bank of Poplar Bluff v. Millspaugh, 313 Mo. 412, 281 S.W. 733 (1926); see 2 PATON'S DIGEST OF LEGAL OPINIONS, *Collections* §17 (1942). New York by statute makes the drawee, which receives a check by mail or through a clearing house, a subagent of the holder with the duty to present to itself. See N.Y. Negotiable Instr. Law §350a; UNIFORM COMMERCIAL CODE §§3-419, 4-302, 4-105 (d), 4-213, 4-303 (1957). *Contra*, Leach v. Citizens' State Bank, 203 Iowa 782, 211 N.W. 522 (1926).

²²³Florida Citrus Exch. v. Union Trust Co., 244 App. Div. 68, 278 N.Y. Supp. 313 (4th Dep't 1935); Standard Trust Co. v. Commercial Nat'l Bank, 166 N.C. 112, 81 S.E. 1074 (1914). The former case was decided under the Bank Collection Code. See 2 PATON, *op. cit. supra* note 222, at 1306-07, 1314-16. It is suggested in *Scotts-bluff Nat'l Bank v. First State Bank*, 162 Neb. 475, 76 N.W.2d 445 (1956), that a drawee may refuse the duties of a collection agent and becomes liable to the holder only upon voluntarily assuming the duties. 2 PATON, *op. cit. supra*, at 1307, suggests that a drawee may refuse to act as collection agent, particularly if there are collection instructions that it does not wish to follow.

²²⁴See note 223 *supra*.

Just what duties does the agency position place on the drawee? Briefly, they are the duty to make proper presentment to itself, or perhaps more clearly put, to the department responsible for payment, plus the duty to remit or protest and give notice of dishonor in appropriate cases.²²⁵ The presentment part is the duty not to delay presentment to the paying department, by returning the check without legal cause or by waiting an unreasonable time, until the drawer becomes insolvent, or until the drawee pays checks received at a later time, resulting in insufficient funds to pay the check, or until the drawer files a stop payment order, or until the drawee is served with garnishment or levying papers by the drawer's creditors, or until the drawee gets around to charging the deposit account with obligations the drawer owes to the drawee, resulting in insufficient funds to pay the check.²²⁶

These duties flow from the interest of the holder in getting payment, not from the duty to protect the holder from loss of rights against the drawer, as in the case of the holder's duty to the drawer to make timely presentment to avoid loss from the drawee's insolvency. Now the question arises, should the drawer or the holder bear the risk of loss for the drawee's breach of its agency duty not to delay presentment to the paying department, by returning the check without cause or waiting an unreasonable time, until the drawee becomes insolvent? Perhaps either or both may have a cause of action against the drawee, but neither wants it. At least each wants something more: the holder wants the benefit of the liability of the drawer on the check, and on the underlying debt if the holder is the payee; and the drawer wants discharge of his liability on the check and on the underlying debt.²²⁷ If this breach of duty by drawee constitutes a breach of presentment duty owed by holder to drawer, the risks rest on the holder; but, if it is only a breach of duty owed by the drawee to the

²²⁵Regarding the duty to protest and give notice of dishonor see 2 PATON, *op. cit. supra* note 222, at 1315; Turner, *Bank Collections—The Direct Routing Practice*, 39 YALE L.J. 468, 474 (1930). Testimony taken by the New York Law Revision Commission, recorded on p. 203 in N.Y. LEGISLATIVE DOCUMENT No. 65 (c) (1954), suggests that it is customary in Massachusetts for the drawee to protest and give notice of dishonor.

²²⁶See note 222 *supra*. Although a delay in presentment may result in priority going to a stop payment order, or garnishment papers, etc., which makes the duty of proper presentment a most substantial duty, the priority problem is essentially a part of the finality of payment problem, which is another story and a big one too.

²²⁷See *Mars, Inc. v. Chubriilo*, 216 Wis. 313, 257 N.W. 157 (1934).

drawer and the holder, risks rest on the drawer. The problem should be solved by a determination of who has the responsibility for presentment to the paying department, the drawer or the holder. Whose agent is the drawee when it performs this function? To be consistent it would seem that the weight of authority should be that it is the holder's agent. This is usually the case when the issue is whether the holder has a cause of action against the drawee; in other words, when the issue is whether the drawee has breached its duty to the holder in those situations in which the duty is not founded on the holder's duty to the drawer, for instance, when the drawer becomes insolvent. But when the issue is whether the holder has breached its duty to the drawer by the drawee's bad handling of the check, the courts are very reluctant to reason in terms of the drawee as the agent of the holder. Probably this reluctance comes from the thought that there is a strong sense of loyalty felt by the drawee toward the drawer resulting from a business relationship closer than that between the drawee and holder and from the operation of some rather potent laws pertaining to the right of the drawer to stop payment,²²⁸ the effect of forgery, and the concept of payment in good faith.²²⁹ Some courts have held that the drawer is discharged when there is a loss resulting from the drawee's delay in processing the check, but the basis of these holdings is that the holder or his intermediate bank collecting agent was negligent in making the presentment because it sent the check directly by mail to the drawee; perhaps some authorities would say by failure of persuasive presentment.²³⁰ In direct mail routing cases holding that such routing constitutes negligence, the practical result is very close to if not the same as an across-the-board holding that the presentment function of the drawee is performed as the agent of the holder, who bears the risk of loss for its breach of agency duties, including the risk flowing from the drawee's insolvency. Such a holding would seem to be more realistic than placing the risk on the holder by the use of the negligence theory based on direct mail routing — perhaps a bit clearer if not more honest as to

²²⁸See *Olds Motor Works v. First State Sav. Bank*, 258 Mich. 269, 241 N.W. 813 (1932); *Bohlig v. First Nat'l Bank*, 233 Minn. 523, 48 N.W.2d 445 (1951).

²²⁹The payment in due course concept has been destroyed by the Uniform Commercial Code, so under the code there is no difficulty regarding the drawee's dual agency pertaining to the duty of the drawee to the drawer to make payment only in good faith, such as refuse payment when it has notice of a claim by drawer against holder, although there is no stop payment order.

²³⁰See *Robinson v. Lancaster Foundry Co.*, 152 Md. 81, 136 Atl. 58 (1927).

what is being done, since the great majority of all checks collected through banks are routed directly by mail or through clearing houses.²³¹

According to the probable weight of authority the holder has a cause of action against the drawee for loss resulting from the latter's failure to use due care in processing a check. Whether the drawer or the holder should bear the risks of the drawee's insolvency when it fails to handle the check forthwith is a question largely of policy; it can be rationalized either way. It may be said that the drawer by using the check accepts the drawee as his agent, and that the holder by receiving the check accepts the drawee as his agent for forthwith presentment. However, if the policy of allowing the holder to have a cause of action against the drawee for delay in processing the check is correct, and if there is strength in the policy behind the holdings that the interests of the drawer require that the holder not make presentment to the drawee directly by mail and that the drawer is entitled to persuasive presentment, it would seem that the best rule would be that the drawee's function of presentment to the paying department is exclusively within its duties as agent of the holder.

The draftsmen of the Uniform Commercial Code made a detailed study of the usual life of a check after it reaches the premises of the drawee. This life, assuming normal processing through remittance, may be divided into three rather distinct phases: (1) the progress through the receiving and presenting department, which receives the check over the counter, from the clearing house, or through the mail; sorts, records, and perhaps photographs the check, and presents it to the bookkeeping department; (2) the progress through the bookkeeping or paying department, which verifies the check, the drawer's account, and the nonexistence of stop orders, garnishment papers, and the like, and finally completes the posting process to the drawer's account, usually terminating the life of a check as a check; and (3) the progress of the proceeds of the check through the remitting department, which delivers cash, a remittance draft, or other payment item, such as notice of credit, back over the counter, through the clearing house, or by mail to the party from whom the check

²³¹This is not to say that there are no authorities holding that direct mail routing is not a breach of duty by the holder to the drawer, or that there are no holdings that the drawee is exclusively the agent of the drawer. Combining these two holdings, the result may be honestly obtained that the risk of loss in the usual bank collection process arising from the malfunctioning of the drawee after the check reaches the drawee's premises rests on the drawer.

was received.²³² These departments normally perform their functions in a most routine and impersonal manner. The tremendous check volume requires this; the law by eliminating most discretion tends to require it. The discretion involved in the fiduciary or confidential relationships is not present as far as the rigid steps of check collection are concerned. No court has shown any concern about fiduciary aspects when the drawee also happens to be the holder's depository bank, with the duty to collect for the holder and the duty to pay on behalf of the drawer. The climate is quite different from that of the schemes designed to accomplish chattel security in sale of goods situations, in which the collecting bank holds a draft, drawn on a purchaser of goods with bill of lading attached, such as those discussed under "Factual Background." It does not seem difficult to consider the presentment department of the drawee as acting as collection agent for the check holder.

CONCLUSION

Bank procedures have developed to meet the tremendous growth in the demand for collection services, almost, it would seem in some instances, in callous disregard of much of the case law, direct routing by mail, for instance. It would not be surprising to find this conclusion borne out by a conversation between a lawyer with some familiarity with banking laws and a bank official well versed in actual banking practices. The conversation could end easily with the lawyer being frightened and the bank official being convinced that the lawyer does not have the slightest idea of what banking is all about. So the lawyer attempts to protect his client by contract, and as far as its terms are concerned does a pretty thorough job,²³³ to the extent that

²³²See UNIFORM COMMERCIAL CODE §4-213, comment (1957). The code utilizes these three rather distinct phases for the purpose of resolving (by pinpointing final payment at the completion of the posting process) the formidable problems involved in the question of finality of payment, such as which gets priority: payment of the check, stop payment order, garnishment papers, notice of drawer's bankruptcy, etc.

²³³See note 186 *supra*. As Professor Roscoe Steffen points out in COMMERCIAL AND INVESTMENT PAPER 542 (1954), collecting banks generally have succeeded in making themselves not liable for malfunctioning of subcollecting banks, whereas carriers, such as railroads, after vigorous effort failed to gain a similar advantage when Congress adopted the Carmack Amendment to the Interstate Commerce Act, which makes the initial carrier liable for losses occurring on connecting lines. Although the case decisions indicate that danger to banks exists in exclusive reliance

some people feel that banks often demonstrate a callous disregard of their customers.

Perhaps the risks involved in check collections are really small and for that reason parties should not be concerned. It has been indicated by use of figures of Federal Reserve banks that one-half of one per cent of all collection items handled by banks are bad; however, about one-half of this number are made good by subsequent collection efforts.²³⁴ As pointed out earlier, a single city bank in a single day frequently will handle more than 100,000 checks in the course of collection. Using these figures, it appears that such a bank in a single day may experience 500 bad checks, 250 of which may ultimately be uncollectible, at least without extraordinary procedures, the extra costs of which are a part of the risks involved. Appropriate presentment procedure should be concerned with an adjustment among the drawer, the drawee, the holder, and the collection agent of the risks from losses that are most likely to occur today: by the drawer's account becoming insufficient, particularly if he is also insolvent; by stolen checks, particularly when forged indorsements are involved; by the drawer returning consideration for which the check was given; and by the drawee's insolvency. The automatic loss of the holder's rights against indorsers by failure to follow the present rigid and unrealistic timely presentment rule is not listed for the reason that it is not a real loss that the law has the task of distributing; it is manufactured by the law and of course should be taken care of by the adjustment.

Who should bear the increase in the real risks caused by the use of the banking system as a collection tool when loss results from the banking system requiring a longer time in which to demand payment, from the practical necessity of direct routing by mail, from payment to one who has no right to it? As indicated in the closing paragraph under the heading "Factual Background," the payee-seller of goods

on contract, there is considerable evidence that generally banks want the flexibility afforded by contract and perhaps the advantage of their bargaining power over the rather helpless positions of the drawer and the holder. Note the suggestions made in favor of contract by banks and their organizations during the preparation of the Uniform Commercial Code. See Gilmore, *The Uniform Commercial Code*, 61 YALE L.J. 364 (1952).

²³⁴See Leary, *Article 4: Bank Deposits and Collections Under the Uniform Commercial Code*, 15 U. PITT. L. REV. 565, 569 (1954). The Todd Company of Rochester, N.Y., a supplier of materials for banks, compiled a report which indicates that check fraud is the fastest growing crime in America, that the upward trend in check fraud is more than double the increase in check usage, and that the loss in the United States from bad checks totaled \$535,000,000 in 1956 alone.

is entitled to his bargained-for value, which he fails to receive if he assumes risks and costs of collection. Perhaps it is not inappropriate to say that the drawer-buyer of goods is responsible for supplying a legal tender medium of exchange, and for that reason when he uses something less, such as a check, he should shoulder the extra costs and risks; but to the extent that he does he pays more than his bargain provided for. The costs of the service, including the risks that the law places on the collecting bank, will to the extent of the power of the bank be passed on to the holder or other customer. Certainly it is nonsense to say that either the drawer or the payee should bear the risks and costs because he elects to use the check. The economy requires the function performed by the check as a medium of exchange. Checks cannot perform this function without the collection services of banks, and the economy suffers from lack of an efficient medium to the extent of the costs and risks of this collection service. Sometimes a great cry is raised to the effect that banks are monsters preying on little people; if so, let the law regulate them more, turn them into public utilities or government agencies,²³⁵ but not injure the economy by crippling the bank collection services on the theory of protecting the little man. Perhaps the government has a duty to supply an adequate medium of exchange; then the government should bear the risks and costs resulting from the use of the banking system.²³⁶ During the past few decades the government, in recognition of the vital economic functions of banks, has through regulation and insurance eliminated much of the risk in check collections formerly borne by the customers of banks. A revision and clarification of the law regarding the presentment duty can adjust the remaining risks among the parties involved in such fashion that their interests will be adequately protected and that the present cloud on the check collection process and therefore on the efficiency of the check as an exchange device will be removed without changing the character of the banking system and without further inroads by the government into private business with the resulting evils that flow therefrom.

Many of the difficulties with the presentment situation today arise from the great divergence of case holdings and from the application

²³⁵This is no recommendation, in view of actual facts, and is in no sense considered necessary. However, since banks solve problems that must be solved, in a very real sense they are sanctioned by government.

²³⁶See note 235 *supra*.

of general law, the law of bills and notes for instance, to a particular industry or business, such as banking; the application of general law to some extent causes the case conflicts. This is a common problem and is frequently noticed in the application of contract law to the marketing of goods of a particular industry. Adjustments must be made, and often a very adequate job is done by the case law. An examination of the application of sales law to different types of businesses occasionally leaves one very pleased with the court's recognition of the peculiar problems of the industry and its adjustment of the law to meet them; on other occasions the feeling is one of disappointment at the court's rigidity in applying the general law. Generally the legislative process is more responsive than the judicial process to a need that arises within a relatively short period of time. Contract law is too uncertain regarding application, too unjust regarding bargaining power of the parties, and too lacking in uniformity to be the exclusive remedy. The rapid and tremendous growth of the need for bank collections requires special legislation that affords uniformity and definiteness, to gain routineness among other things, tempered with a degree of flexibility in certain areas; in other words, legislation that faces up to the peculiar problems of the industry's collection process. The Bank Collection Code is special legislation, but its lack of depth and lack of general acceptance leaves the great majority of collection problems at the mercy of a most confused and inadequate body of law. As far as method and depth of coverage are concerned, Article 4 of the Uniform Commercial Code²³⁷ proceeds in the right direction; whether it leans too heavily on flexibility based on contract is another question.

The following are suggestions for revision and clarification of the present body of law applicable to the presentment of checks for collection through the banking system:

- (1) Extend the period of time for presentment of checks to a definite period that is reasonable under today's circumstances. The interests of the drawer and the indorsers require that the period be limited; however, these parties have agreed to be liable on the check, and the law certainly should not imply liability for a period less than that reasonably necessary to cover the usually appropriate col-

²³⁷The title of the article, "Bank Deposits and Collections," is descriptive of the special nature of the proposed legislation.

lection process. If extending the period violates justice, probably any other alternative would violate it more, except perhaps the creation of another medium of exchange that would do the job without any risks and costs of collection. The inventiveness of man has not yet been so productive. A reasonable though limited extension of the period for presentment will afford needed protection of the holder's interests against secondary parties with appropriate and adequate consideration for the interests of secondary parties; in addition it will in a practical sense eliminate any injustice to the holder that may otherwise result from the conclusion that the presenting department of the drawee is the agent of the holder as opposed to the agent of the drawer.

- (2) Clearly make the drawee a collection agent of the holder for the function of presentment, thus affording the basis for a cause of action by the holder against the drawee for delaying presentment to the paying department by returning the check without legal cause or by waiting an unreasonable time. This affords needed protection to the holder's interest, for instance against the risks of the drawer's insolvency, in two ways: (a) by motivating the drawee to expedite the conversion of the check into acceptable value, and (b) by giving the holder a cause of action in the event of some types of loss, which cause of action would otherwise not exist. It also tends to increase the speed of the check collection process, all without unduly prejudicing the drawee's duties to the drawer or the practical necessities of the functional operations of the drawee bank.
- (3) Create a definite duty of the holder to the collection agent, and the collection agent in its turn to the drawee, to give warranty of right to payment covering situations other than, perhaps, that of *Price v. Neal*.²³⁸ This gives needed protection to the interest of the drawee, reduces in many cases the time needed for check collections, for instance by often avoiding cumbersome identification procedures and the like, with appropriate protection of the interest of the collection agent and without unjust treatment of the holder.
- (4) Establish direct routing by mail as an appropriate part of

²³⁸Burr. 1354, 97 Eng. Rep. 871 (1762).

one method of due presentment. The sheer pressure of the volume of checks makes this a virtual necessity, and in any event it results in improved collection efficiency, which operates in the interests of the economy and in most cases of all parties to the check, without undue prejudice to the drawer and the indorsers. The added speed may operate in favor of the holder and the indorsers by beating the drawer's insolvency and in favor of the drawer and the indorsers by beating the drawee's insolvency.

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