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BANKS AND BANKING - DUTY OF DEPOSITOR TO DETERMINE STATUS OF HIS ACCOUNT

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BANKS AND BANKING — DUTY OF DEPOSITOR TO DETERMINE STATUS OF HIS ACCOUNT — Plaintiff's bookkeeper, who, as defendant bank admittedly knew, had authority only to indorse and deposit commission checks to plaintiff's account, embezzled considerable money between 1926 and 1931 by taking some of the proceeds in cash or drafts. In the passbook and in defendant's own records only the net transactions, not the total amount of the checks, were recorded. Plaintiff discovered the fraud in 1936 and now sues the receiver five years after the bank closed. *Held*, that plaintiff, charged with constuctive knowledge of the fraud, which reasonable examination would have revealed, is guilty of negligence and therefore barred from now asserting his claim, which would injure defendant bank by reducing dividends to depositors. *Mattison-Greenlee Service Corporation v. Culhane*, (C. C. A. 7th, 1939) 103 F. (2d) 608.

A depositor generally is chargeable only with those payments made in conformity with his orders,[1] but that is more acceptable as a starting point for discussion than as a reliable, immutable rule. An important qualification, simply stated, is that its application is in practice dependent to some extent upon the reasonable conduct of the depositor. If the depositor knows about, or from the available sources of information should have discovered, irregularities in his account and yet fails to give reasonably prompt notice to the bank, the bank will be relieved of liability, provided, of course, the bank was not negligent or the loss might otherwise have been prevented.[2] Whatever the theory by which this result is explained,[3] the more practical problem is to translate the vague require-

[1] Shipman v. Bank of New York, 126 N. Y. 318, 27 N. E. 371 (1891).

[2] Arant, "Forged Checks—The Duty of the Depositor to his Bank," 31 YALE L. J. 598 (1922); Leather Manufacturer's Nat. Bank v. Morgan, 117 U. S. 96, 6 S. Ct. 657 (1886).

[3] The theories which have been applied are legion, among them being adoption, ratification, and estoppel. As Arant has pointed out, however, "the objection that one cannot ratify what he does not know of seems conclusive against the ratification theory." Arant, "Forged Checks—The Duty of the Depositor to his Bank," 31 YALE L. J. 598 at 625 (1922). Estoppel is acceptable as far as it goes, but its requirement of affirmative proof of damage or prejudice to the bank has been regarded as an undesirable limitation. The right promptly to proceed against a forger is in itself valuable, for even though the forger is insolvent or beyond reach, "others may become interested in him and come to his assistance, who, after delay, may not do so." McNeely Co. v. Bank of North America, 221 Pa. 588, 70 A. 891 (1908). And since quite clearly the whole problem is simply one of requiring due diligence on the part of the depositor where indispensable to prevention of loss, the duty theory, which, properly applied, will every time induce a reasonable result, is to be preferred. In any event, "the

ment of "reasonable care" into specific acts.[4] From the numerous reported cases it appears that the depositor is obliged at least to examine the vouchers and statements returned to him by the bank from time to time,[5] thus verifying the correctness of the debits and credits in the statement with a view to detecting forgeries and alterations.[6] The duty may be delegated to and discharged by a competent employee; there is conflict, however, on the question of constructive knowledge when the delegate is himself the forger.[7] Ordinarily the examination does not extend to forged indorsements, since the depositor is not expected to know the payee's signature.[8] Where, as in the principal case, the problem arises from a misapplication of funds intended for deposit, a forged indorsement as a cause for suspicion does not enter the picture. But the depositor is bound to act prudently, and failure to give reasonable attention to suspicious circumstances of whatever source may give rise to a valid defense in the bank.[9] Although an

effect . . . is to recognize the business sense of an implied contractual obligation. . . ." 32 HARV. L. REV. 287 (1919).

[4] "It is not possible to give an exact definition of the term 'reasonable care.' All that can be done is to refer to the decisions in which the question has arisen." BRADY, BANK CHECKS, 2d ed., 293 (1926).

[5] First Nat. Bank v. Allen, 100 Ala. 476, 14 So. 335 (1893); 6 ZOLLMAN, BANKS AND BANKING, § 4144 (1936); 5 MICHIE, BANKS AND BANKING, § 284 (1932). In Stump v. Bank of New York, 212 App. Div. 608, 209 N. Y. S. 396 (1925), three steps are suggested: 1. Compare vouchers returned by the bank with check stubs; 2. Compare balance entered in the statement with balance in stub book; 3. Compare returned vouchers with list of checks entered in the statement. For further aspects of this matter, see 15 A. L. R. 159 (1921) and 67 A. L. R. 1121 (1930).

[6] The three months limitation statutes have uniformly been interpreted to apply only "to facts . . . within the knowledge of the drawer at the time of the return of the check to him, namely, whether his name has been forged, or the check raised, or the name of the payee changed." Detroit Piston Ring Co. v. Wayne County & Home Sav. Bank, 252 Mich. 163 at 171, 233 N. W. 185 (1930). Similar qualifications apply to the usual receipt from the depositor. Ibid.

[7] BRADY, BANK CHECKS, 2d ed., § 181 (1926); Detroit Piston Ring Co. v. Wayne County & Home Sav. Bank, 252 Mich. 163, 233 N. W. 185 (1930).

[8] Nat. Surety Co. v. Bank of Manhattan Co., 133 Misc. 48, 231 N. Y. S. 389 (1928); New Amsterdam Casualty Co. v. Albia State Bank, 214 Iowa 541, 239 N. W. 4, 242 N. W. 538 (1932); 67 A. L. R. 1121 at 1125 (1930).

[9] "We will not say the maker never is required to look at the indorsements. If as in the Erickson case [C. E. Erickson Co. v. Iowa Nat. Bank, 211 Iowa 495, 230 N. W. 342 (1930)], the fifty checks had been further indorsed by Tschupp personally, showing all the money was going to or through him; if, as in the Detroit Piston Ring case [Detroit Piston Ring Co. v. Wayne County & Home Sav. Bank, 252 Mich. 163, 233 N. W. 185 (1930)], the expense of [plaintiff] had so unduly increased as to attract attention; if the plaintiff had known of part of the forgeries and failed to caution the trust company; if the forged indorsements had even been crude and obviously all in the same handwriting—in any of these circumstances we will concede *arguendo* there might be substance to this defense." American Sash & Door Co. v. Commerce Trust Co., 332 Mo. 98 at 121, 56 S. W. (2d) 1034 (1932). See Arant, "Forged Checks—The Duty of the Depositor to his Bank," 31 YALE L. J. 598 at 613, note 37 (1922). In Goodyear Tire & Rubber Co. v. Nat. Bank of Denver, 95 Colo. 34, 32 P. (2d) 268 (1934), plaintiff could probably

arguable point, certain facts in the principal case indicate that the depositor's conduct was not necessarily unreasonable and that a decision in his favor might not have been amiss.[10] But possibly an explanation for an apparent extension of the rule in this instance can be found in the court's feeling that a bank closed for five years "may have a more appealing and persuasive argument than an individual," especially when the depositor knew that the receiver had been operating on the basis of the depositor's claim as filed several years before and not containing the present claim. *James D. Ritchie*

have detected nothing from the indorsements, but "there were in its exclusive possession sources of information which upon an audit would have revealed" errors in the account.

[10] E.g., defendant's admitted fault in giving cash to the agent and the recording of only the net transactions in the passbook. This case clearly differs from those wherein a fraudulent clerk used names of former or fictitious employees and from the situation in Potts & Co. v. Lafayette Nat. Bank, 269 N. Y. 181, 199 N. E. 50 (1935), where "any employee who examined the statements would have discovered" the discrepancy.