

**DISTRICT OF COLUMBIA**  
**OFFICIAL CODE**

**TITLE 28.**  
**COMMERCIAL INSTRUMENTS AND**  
**TRANSACTIONS.**

**ARTICLE 4.**  
**BANK DEPOSITS AND COLLECTIONS.**

**2001 Edition**

# DISTRICT OF COLUMBIA OFFICIAL CODE

## ARTICLE 4. BANK DEPOSITS AND COLLECTIONS.

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# ARTICLE 4. BANK DEPOSITS AND COLLECTIONS.

*Refs & Annos*

*HISTORICAL AND STATUTORY NOTES*

*Editor's Notes*

Many of the cases appearing in the notes to this article were decided under the former statutes in effect prior to the 1995 revision. These earlier cases have been moved to pertinent sections of the revised material where they may be useful in interpreting the current statutes.

## PART 1. GENERAL PROVISIONS AND DEFINITIONS.

### § 28:4-101. SHORT TITLE.

This article may be cited as "Uniform Commercial Code -- Bank Deposits and Collections".

(Dec. 30, 1963, 77 Stat. 695, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. The great number of checks handled by banks and the country-wide nature of the bank collection process require uniformity in the law of bank collections. There is needed a uniform statement of the principal rules of the bank collection process with ample provision for flexibility to meet the needs of the large volume handled and the changing needs and conditions that are bound to come with the years. This Article meets that need.

2. In 1950 at the time Article 4 was drafted, 6.7 billion checks were written annually. By the time of the 1990 revision of Article 4 annual volume was estimated by the American Bankers Association to be about 50 billion checks. The banking system could not have coped with this increase in check volume had it not developed in the late 1950s and early 1960s an automated system for check collection based on encoding checks with machine-readable information by Magnetic Ink Character Recognition (MICR). An important goal of the 1990 revision of Article 4 is to promote the efficiency of the check collection process by making the provisions of Article 4 more compatible with the needs of an automated system and, by doing so, increase the speed and lower the cost of check collection for those who write and receive checks. An additional goal of the 1990 revision of Article 4 is to remove any statutory barriers in the Article to the ultimate adoption of programs allowing the presentment of checks to payor banks by electronic transmission of information captured from the MICR line on the checks. The potential of these programs for saving the time and expense of transporting the huge volume of checks from depository to payor banks is evident.

3. Article 4 defines rights between parties with respect to bank deposits and collections. It is not a regulatory statute. It does not regulate the terms of the bank-customer agreement, nor does it prescribe what constraints different jurisdictions may wish to impose on that relationship in the interest of consumer protection. The revisions in Article 4 are intended to create a legal frame-work that accommodates automation and truncation for the benefit of all bank customers. This may raise consumer problems which enacting jurisdictions may wish to address in individual legislation. For example, with respect to Section 4-401(c), jurisdictions may wish to examine their unfair and deceptive practices laws to determine whether they are adequate to protect drawers who postdate checks from unscrupulous practices that may arise on the part of persons who induce drawers to issue postdated checks in erroneous belief that the checks will not be immediately payable. Another example arises from the fact that under various truncation plans customers will no longer receive their cancelled checks and will no longer have the cancelled check to prove payment. Individual legislation might provide that a copy of a bank statement along with a copy of the check is prima facie evidence of payment.

**Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

1981 Ed., § 28:4-101.

1973 Ed., § 28:4-101.

Law 10-249, the "Uniform Commercial Code--Negotiable Instruments Act of 1994," was introduced in Council and assigned Bill No. 10-240, which was referred to the Committee on Consumer and Regulatory Affairs. The Bill was adopted on first and second readings on November 1, 1994, and December 6, 1994, respectively. Signed by the Mayor on January 18, 1995, it was assigned Act No. 10-396 and transmitted to both Houses of Congress for its review. D.C. Law 10-249 became effective on March 23, 1995.

## **§ 28:4-102. APPLICABILITY.**

(a) To the extent that items within this article are also within Articles 3 and 8, they are subject to those articles. If there is conflict, this Article governs Article 3, but Article 8 governs this article.

(b) The liability of a bank for action or nonaction with respect to an item handled by it for purposes of presentment, payment, or collection is governed by the law of the place where the bank is located. In the case of action or nonaction by or at a branch or separate office of a bank, its liability is governed by the law of the place where the branch or separate office is located.

(Dec. 30, 1963, 77 Stat. 695, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. The rules of Article 3 governing negotiable instruments, their transfer, and the contracts of the parties thereto apply to the items collected through banking channels wherever no specific provision is found in this Article. In the case of conflict, this Article governs. See Section 3-102(b).

Bonds and like instruments constituting investment securities under Article 8 may also be handled by banks for collection purposes. Various sections of Article 8 prescribe rules of transfer some of which (see Sections 8-108 and 8-304) may conflict with provisions of this Article (Sections 4-205, 4-207, and 4-208). In the case of conflict, Article 8 governs. Amendments approved by the Permanent Editorial Board for Uniform Commercial Code November 4, 1995.

Section 4-210 deals specifically with overlapping problems and possible conflicts between this Article and Article 9. However, similar reconciling provisions are not necessary in the case of Articles 5 and 7. Sections 4-301 and 4-302 are consistent with Section 5-112. In the case of Article 7 documents of title frequently accompany items but they are not themselves items. See Section 4-104(a)(9).

In *Clearfield Trust Co. v. United States*, 318 U.S. 363 (1943), the Court held that if the United States is a party to an instrument, its rights and duties are governed by federal common law in the absence of a specific federal statute or regulation. In *United States v. Kimbell Foods, Inc.*, 440 U.S. 715 (1979), the Court stated a three-pronged test to ascertain whether the federal common-law rule should follow the state rule. In most instances courts under the *Kimbell* test have shown a willingness to adopt UCC rules in formulating federal common law on the subject. In *Kimbell* the Court adopted the priorities rules of Article 9.

In addition, applicable federal law may supersede provisions of this Article. One federal law that does so is the Expedited Funds Availability Act, 12 U.S.C. § 4001 et seq., and its implementing Regulation CC, 12 CFR Pt. 229. In some instances this law is alluded to in the statute, e.g., Section 4-215(e) and (f). In other instances, although not referred to in this Article, the provisions of the EFAA and Regulation CC control with respect to checks. For example, except between the depository bank and its customer, all settlements are final and not provisional (Regulation CC, Section 229.36(d)), and the midnight deadline may be extended (Regulation CC, Section 229.30(c)). The comments to this Article suggest in most instances the relevant Regulation CC provisions.

2. Subsection (b) is designed to state a workable rule for the solution of otherwise vexatious problems of the conflicts of laws:

a. The routine and mechanical nature of bank collections makes it imperative that one law govern the activities of one office of a bank. The requirement found in some cases that to hold an indorser notice must be given in accordance with the law of the place of indorsement, since that method of notice became an implied term of the indorser's contract, is more theoretical than practical.

b. Adoption of what is in essence a tort theory of the conflict of laws is consistent with the general theory of this Article that the basic duty of a collecting bank is one of good faith and and the exercise of ordinary care. Justification lies in the fact that, in using an ambulatory instrument, the drawer, payee, and indorsers must know that action will be taken with respect to it in other jurisdictions. This is especially pertinent with respect to the law of the place of payment.

c. The phrase "action or non-action with respect to any item handled by it for purposes of presentment, payment, or collection" is intended to make the conflicts rule of subsection (b) apply from the inception of the collection process of an item through all phases of deposit, forwarding, presentment, payment and remittance or credit of proceeds. Specifically the subsection applies to the initial act of a depository bank in receiving an item and to the incidents of such receipt. The conflicts rule of *Weissman v. Banque de Bruxelles*, 254 N.Y. 488, 173 N.E. 835 (1930), is rejected. The subsection applies to questions of possible vicarious liability of a bank for action or non-action of sub-agents (see Section 4-202(c)), and tests these questions by the law of the state of the location of the bank which uses the sub-agent. The conflicts rule of *St. Nicholas Bank of New York v. State Nat. Bank*, 128 N.Y. 26, 27 N.E. 849, 13 L.R.A. 241 (1891), is rejected. The subsection applied to action or non-action of a payor bank in connection with handling an item (see Sections 4-215(a), 4-301, 4-302, 4-303) as well as action or non-action of a collecting bank (Sections 4-201 through 4-216); to action or non-action of a bank which suspends payment or is affected by another bank suspending payment (Section 4-216); to action or non-action of a bank with respect to an item under the rule of Part 4 of Article 4.

d. In a case in which subsection (b) makes this Article applicable, Section 4-103(a) leaves open the possibility of an agreement with respect to applicable law. This freedom of agreement follows the general policy of Section 1-105.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-102.

1973 Ed., § 28:4-102.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-103. VARIATION BY AGREEMENT; MEASURE OF DAMAGES; ACTION CONSTITUTING ORDINARY CARE.**

(a) The effect of the provisions of this article may be varied by agreement, but the parties to the agreement cannot disclaim a bank's responsibility for its lack of good faith or failure to exercise ordinary care or limit the measure of damages for the lack or failure. However, the parties may determine by agreement the standards by which the bank's responsibility is to be measured if those standards are not manifestly unreasonable.

(b) Federal Reserve regulations and operating circulars, clearing-house rules, and the like have the effect of agreements under subsection (a) of this section, whether or not specifically assented to by all parties interested in items handled.

(c) Action or nonaction approved by this article or pursuant to Federal Reserve regulations or operating circulars is the exercise of ordinary care and, in the absence of special instructions, action or nonaction consistent with clearing-house rules and the like or with a general banking usage not disapproved by this article, is prima facie the exercise of ordinary care.

(d) The specification or approval of certain procedures by this article is not disapproval of other procedures that may be reasonable under the circumstances.

(e) The measure of damages for failure to exercise ordinary care in handling an item is the amount of the item reduced by an amount that could not have been realized by the exercise of ordinary care. If there is also bad faith it includes any other damages the party suffered as a proximate consequence.

(Dec. 30, 1963, 77 Stat. 695, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Section 1-102 states the general principles and rules for variation of the effect of this Act by agreement and the limitations to this power. Section 4-103 states the specific rules for variation of Article 4 by agreement and also certain standards of ordinary care. In view of the technical complexity of the field of bank collections, the enormous number of items handled by banks, the certainty that there will be variations from the normal in each day's work in each bank, the certainty of changing conditions and the possibility of developing improved methods of collection to speed the process, it would be unwise to freeze present methods of operation by mandatory statutory rules. This section, therefore, permits within wide limits variation of the effect of provisions of the Article by agreement.

2. Subsection (a) confers blanket power to vary all provisions of the Article by agreements of the ordinary kind. The agreements may not disclaim a bank's responsibility for its own lack of good faith or failure to exercise ordinary care and may not limit the measure of damages for the lack or failure, but this subsection like Section

1-102(3) approves the practice of parties determining by agreement the standards by which the responsibility is to be measured. In the absence of a showing that the standards manifestly are unreasonable, the agreement controls. Owners of items and other interested parties are not affected by agreements under this subsection unless they are parties to the agreement or are bound by adoption, ratification, estoppel or the like.

As here used "agreement" has the meaning given to it by Section 1-201(3). The agreement may be direct, as between the owner and the depositary bank; or indirect, as in the case in which the owner authorizes a particular type of procedure and any bank in the collection chain acts pursuant to such authorization. It may be with respect to a single item; or to all items handled for a particular customer, e.g., a general agreement between the depositary bank and the customer at the time a deposit account is opened. Legends on deposit tickets, collection letters and acknowledgments of items, coupled with action by the affected party constituting acceptance, adoption, ratification, estoppel or the like, are agreements if they meet the tests of the definition of "agreement." See Section 1-201(3). *First Nat. Bank of Denver v. Federal Reserve Bank*, 6 F.2d 339 (8th Cir.1925) (deposit slip); *Jefferson County Bldg. Ass'n v. Southern Bank & Trust Co.*, 225 Ala. 25, 142 So. 66 (1932) (signature card and deposit slip); *Semingson v. Stock Yards Nat. Bank*, 162 Minn. 424, 203 N.W. 412 (1925) (passbook); *Farmers State Bank v. Union Nat. Bank*, 42 N.D. 449, 454, 173 N.W. 789, 790 (1919) (acknowledgment of receipt of item).

3. Subsection (a) (subject to its limitations with respect to good faith and ordinary care) goes far to meet the requirements of flexibility. However, it does not by itself confer fully effective flexibility. Since it is recognized that banks handle a great number of items every business day and that the parties interested in each item include the owner of the item, the drawer (if it is a check), all nonbank indorsers, the payor bank and from one to five or more collecting banks, it is obvious that it is impossible, practically, to obtain direct agreements from all of these parties on all items. In total, the interested parties constitute virtually every adult person and business organization in the United States. On the other hand they may become bound to agreements on the principle that collecting banks acting as agents have authority to make binding agreements with respect to items being handled. This conclusion was assumed but was not flatly decided in *Federal Reserve Bank of Richmond v. Malloy*, 264 U.S. 160, at 167, 44 S.Ct. 296, at 298, 68 L.Ed. 617, 31 A.L.R. 1261 (1924).

To meet this problem subsection (b) provides that official or quasi-official rules of collection, that is Federal Reserve regulations and operating circulars, clearing-house rules, and the like, have the effect of agreements under subsection (a), whether or not specifically assented to by all parties interested in items handled. Consequently, such official or quasi-official rules may, standing by themselves but subject to the good faith and ordinary care limitations, vary the effect of the provisions of Article 4.

*Federal Reserve regulations.* Various sections of the Federal Reserve Act (12 U.S.C. § 221 et seq.) authorize the Board of Governors of the Federal Reserve System to direct the Federal Reserve banks to exercise bank collection functions. For example, Section 16 (12 U.S.C. § 248(o)) authorizes the Board to require each Federal Reserve bank to exercise the functions of a clearing house for its members and Section 13 (12 U.S.C. § 342) authorizes each Federal Reserve bank to receive deposits from nonmember banks solely for the purposes of exchange or of collection. Under this statutory authorization the Board has issued Regulation J (Subpart A—Collection of Checks and Other Items). Under the supremacy clause of the Constitution, federal regulations prevail over state statutes. Moreover, the Expedited Funds Availability Act, 12 U.S.C. Section 4007(b) provides that the Act and Regulation CC, 12 CFR 229, supersede "any provision of the law of any State, including the Uniform Commercial Code as in effect in such State, which is inconsistent with this chapter or such regulations." See Comment 1 to Section 4-102.

*Federal Reserve operating circulars.* The regulations of the Federal Reserve Board authorize the Federal Reserve banks to promulgate operating circulars covering operating details. Regulation J, for example, provides that "Each Reserve Bank shall receive and handle items in accordance with this subpart, and shall issue operating circulars governing the details of its handling of items and other matters deemed appropriate by the Reserve Bank." This Article recognizes that "operating circulars" issued pursuant to the regulations and concerned with operating details as appropriate may, within their proper sphere, vary the effect of the Article.

*Clearing-House Rules.* Local clearing houses have long issued rules governing the details of clearing; hours of clearing, media of remittance, time for return of mis-sent items and the like. The case law has recognized these rules, within their proper sphere, as binding on affected parties and as appropriate sources for the courts to look to in filling out details of bank collection law. Subsection (b) in recognizing clearing-house rules as a means of preserving flexibility continues the sensible approach indicated in the cases. Included in the terms "clearing houses" are county and regional clearing houses as well as those within a single city or town. There is, of course, no intention of authorizing a local clearing house or a group of clearing houses to rewrite the basic law generally. The term "clearing-house rules" should be understood in the light of functions the clearing houses have exercised in the past.

*And the like.* This phrase is to be construed in the light of the foregoing. "Federal Reserve regulations and operating circulars" cover rules and regulations issued by public or quasi-public agencies under statutory authority. "Clearing-house rules" cover rules issued by a group of banks which have associated themselves to perform through a clearing house some of their collection, payment and clearing functions. Other agencies or associations of this kind may be established in the future whose rules and regulations could be appropriately looked on as constituting means of avoiding absolute statutory rigidity. The phrase "and the like" leaves open

possibilities for future development. An agreement between a number of banks or even all the banks in an area simply because they are banks, would not of itself, by virtue of the phrase "and the like," meet the purposes and objectives of subsection (b).

4. Under this Article banks come under the general obligations of the use of good faith and the exercise of ordinary care. "Good faith" is defined in Section 3-103(a)(4). The term "ordinary care" is defined in Section 3-103(a)(7). These definitions are made to apply to Article 4 by Section 4-104(c). Section 4-202 states respects in which collecting banks must use ordinary care. Subsection (c) of Section 4-103 provides that action or non-action approved by the Article or pursuant to Federal Reserve regulations or operating circulars constitutes the exercise of ordinary care. Federal Reserve regulations and operating circulars constitute an affirmative standard of ordinary care equally with the provisions of Article 4 itself.

Subsection (c) further provides that, absent special instructions, action or non-action consistent with clearing-house rules and the like or with a general banking usage not disapproved by the Article, *prima facie* constitutes the exercise of ordinary care. Clearing-house rules and the phrase "and the like" have the significance set forth above in these Comments. The term "general banking usage" is not defined but should be taken to mean a general usage common to banks in the area concerned. See Section 1-205(2). In a case in which the adjective "general" is used, the intention is to require a usage broader than a mere practice between two or three banks but it is not intended to require anything as broad as a country-wide usage. A usage followed generally throughout a state, a substantial portion of a state, a metropolitan area or the like would certainly be sufficient. Consistently with the principle of Section 1-205(3), action or non-action consistent with clearing-house rules or the like or with banking usages *prima facie* constitutes the exercise of ordinary care. However, the phrase "in the absence of special instructions" affords owners of items an opportunity to prescribe other standards and although there may be no direct supervision or control of clearing houses or banking usages by official supervisory authorities, the confirmation of ordinary care by compliance with these standards is *prima facie* only, thus conferring on the courts the ultimate power to determine ordinary care in any case in which it should appear desirable to do so. The *prima facie* rule does, however, impose on the party contesting the standards to establish that they are unreasonable, arbitrary or unfair as used by the particular bank.

5. Subsection (d), in line with the flexible approach required for the bank collection process is designed to make clear that a novel procedure adopted by a bank is not to be considered unreasonable merely because that procedure is not specifically contemplated by this Article or by agreement, or because it has not yet been generally accepted as a bank usage. Changing conditions constantly call for new procedures and someone has to use the new procedure first. If this procedure is found to be reasonable under the circumstances, provided, of course, that it is not inconsistent with any provision of the Article or other law or agreement, the bank which has followed the new procedure should not be found to have failed in the exercise of ordinary care.

6. Subsection (e) sets forth a rule for determining the measure of damages for failure to exercise ordinary care which, under subsection (a), cannot be limited by agreement. In the absence of bad faith the maximum recovery is the amount of the item concerned. The term "bad faith" is not defined; the connotation is the absence of good faith (Section 3-103). When it is established that some part or all of the item could not have been collected even by the use of ordinary care the recovery is reduced by the amount that would have been in any event uncollectible. This limitation on recovery follows the case law. Finally, if bad faith is established the rule opens to allow the recovery of other damages, whose "proximateness" is to be tested by the ordinary rules applied in comparable cases. Of course, it continues to be as necessary under subsection (e) as it has been under ordinary common law principles that, before the damage rule of the subsection becomes operative, liability of the bank and some loss to the customer or owner must be established.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-103.

1973 Ed., § 28:4-103.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-104. DEFINITIONS AND INDEX OF DEFINITIONS.**

(a) In this article, unless the context otherwise requires, the term:

(1) "Account" means any deposit or credit account with a bank, including a demand, time, savings, passbook, share draft, or like account, other than an account evidenced by a certificate of deposit.

(2) "Afternoon" means the period of a day between noon and midnight.

(3) "Banking day" means the part of a day on which a bank is open to the public for carrying on substantially all of its banking functions.



- (4) "Clearing house" means an association of banks or other payors regularly clearing items.
- (5) "Customer" means a person having an account with a bank or for whom a bank has agreed to collect items, including a bank that maintains an account at another bank.
- (6) "Documentary draft" means a draft to be presented for acceptance or payment if specified documents, certificated securities (section 28:8-102) or instructions for uncertificated securities (section 28:8-102), or other certificates, statements, or the like are to be received by the drawee or other payor before acceptance or payment of the draft.
- (7) "Draft" means a draft as defined in section 28:3-104 or an item, other than an instrument, that is an order.
- (8) "Drawee" means a person ordered in a draft to make payment.
- (9) "Item" means an instrument or a promise or order to pay money handled by a bank for collection or payment. The term does not include a payment order governed by Article 4A or a credit or debit card slip.
- (10) "Midnight deadline", with respect to a bank, means midnight on its next banking day following the banking day on which it receives the relevant item or notice or from which the time for taking action commences to run, whichever is later.
- (11) "Settle" means to pay in cash, by clearing-house settlement, in a charge or credit or by remittance, or otherwise as agreed. A settlement may be either provisional or final.
- (12) "Suspends payments", with respect to a bank, means that it has been closed by order of the supervisory authorities, that a public officer has been appointed to take it over, or that it ceases or refuses to make payments in the ordinary course of business.

(b) Other definitions applying to this article and the sections in which they appear are:

"Agreement for electronic presentment".	Section 28:4-110.
"Bank".	Section 28:4-105.
"Collecting bank".	Section 28:4-105.
"Depository bank".	Section 28:4-105.
"Intermediary bank".	Section 28:4-105.
"Payor bank".	Section 28:4-105.
"Presenting bank".	Section 28:4-105.
"Presentment notice".	Section 28:4-110.

(c) The following definitions in other articles apply to this article:

"Acceptance".	Section 28:3-409.
"Alteration".	Section 28:3-407.
"Cashier's check".	Section 28:3-104.
"Certificate of deposit".	Section 28:3-104.
"Certified check".	Section 28:3-409.
"Check".	Section 28:3-104.
"Good faith".	Section 28:3-103.
"Holder in due course".	Section 28:3-302.
"Instrument".	Section 28:3-104.
"Notice of dishonor".	Section 28:3-503.
"Order".	Section 28:3-103.
"Ordinary care".	Section 28:3-103.
"Person entitled to enforce".	Section 28:3-301.
"Presentment".	Section 28:3-501.
"Promise".	Section 28:3-103.
"Prove".	Section 28:3-103.
"Teller's check".	Section 28:3-104.
"Unauthorized signature".	Section 28:3-403.

(d) In addition, Article 1 contains general definitions and principles of construction and interpretation applicable throughout this article.

(Dec. 30, 1963, 77 Stat. 696, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467; Apr. 9, 1997, D.C. Law 11-240, § 3(d), 44 DCR 1087.)

#### *HISTORICAL AND STATUTORY NOTES*

##### *UNIFORM COMMERCIAL CODE COMMENT*

1. Paragraph (a)(1): "Account" is defined to include both asset accounts in which a customer has deposited money and accounts from which a customer may draw on a line of credit. The limiting factor is that the account must be in a bank.

2. Paragraph (a)(3): "Banking day." Under this definition that part of a business day when a bank is open only for limited functions, e.g., to receive deposits and cash checks, but with loan, bookkeeping and other departments closed, is not part of a banking day.

3. Paragraph (a)(4): "Clearing house." Occasionally express companies, governmental agencies and other nonbanks deal directly with a clearing house; hence the definition does not limit the term to an association of banks.

4. Paragraph (a)(5): "Customer." It is to be noted that this term includes a bank carrying an account with another bank as well as the more typical nonbank customer or depositor.

5. Paragraph (a)(6): "Documentary draft" applies even though the documents do not accompany the draft but are to be received by the drawee or other payor before acceptance or payment of the draft.

6. Paragraph (a)(7): "Draft" is defined in Section 3-104 as a form of instrument. Since Article 4 applies to items that may not fall within the definition of instrument, the term is defined here to include an item that is a written order to pay money, even though the item may not qualify as an instrument. The term "order" is defined in Section 3-103.

7. Paragraph (a)(8): "Drawee" is defined in Section 3-103 in terms of an Article 3 draft which is a form of instrument. Here "drawee" is defined in terms of an Article 4 draft which includes items that may not be instruments.

8. Paragraph (a)(9): "Item" is defined broadly to include an instrument, as defined in Section 3-104, as well as promises or orders that may not be within the definition of "instrument." The terms "promise" and "order" are defined in Section 3-103. A promise is a written undertaking to pay money. An order is a written instruction to pay money. But see Section 4-110(c). Since bonds and other investment securities under Article 8 may be within the term "instrument" or "promise," they are items and when handled by banks for collection are subject to this Article. See Comment 1 to Section 4-102. The functional limitation on the meaning of this term is the willingness of the banking system to handle the instrument, undertaking or instruction for collection or payment.

9. Paragraph (a)(10): "Midnight deadline." The use of this phrase is an example of the more mechanical approach used in this Article. Midnight is selected as a termination point or time limit to obtain greater uniformity and definiteness than would be possible from other possible terminating points, such as the close of the banking day or business day.

10. Paragraph (a)(11): The term "settle" has substantial importance throughout Article 4. In the American Bankers Association Bank Collection Code, in deferred posting statutes, in Federal Reserve regulations and operating circulars, in clearing-house rules, in agreements between banks and customers and in legends on deposit tickets and collection letters, there is repeated reference to "conditional" or "provisional" credits or payments. Tied in with this concept of credits or payments being in some way tentative, has been a related but somewhat different problem as to when an item is "paid" or "finally paid" either to determine the relative priority of the item as against attachments, stop-payment orders and the like or in insolvency situations. There has been extensive litigation in the various states on these problems. To a substantial extent the confusion, the litigation and even the resulting court decisions fail to take into account that in the collection process some debits or credits are provisional or tentative and others are final and that very many debits or credits are provisional or tentative for awhile but later become final. Similarly, some cases fail to recognize that within a single bank, particularly a payor bank, each item goes through a series of processes and that in a payor bank most of these processes are preliminary to the basic act of payment or "final payment."

The term "settle" is used as a convenient term to characterize a broad variety of conditional, provisional, tentative and also final payments of items. Such a comprehensive term is needed because it is frequently difficult or unnecessary to determine whether a particular action is tentative or final or when a particular credit shifts from the tentative class to the final class. Therefore, its use throughout the Article indicates that in that particular context it is unnecessary or unwise to determine whether the debit or the credit or the payment is tentative or final. However, if qualified by the adjective "provisional" its tentative nature is intended, and if qualified by the adjective "final" its permanent nature is intended.

Examples of the various types of settlement contemplated by the term include payments in cash; the efficient but somewhat complicated process of payment through the adjustment and offsetting of balances through clearing houses; debit or credit entries in accounts between banks; the forwarding of various types of

remittance instruments, sometimes to cover a particular item but more frequently to cover an entire group of items received on a particular day.

11. Paragraph (a)(12): "Suspends payments." This term is designed to afford an objective test to determine when a bank is no longer operating as a part of the banking system.

#### **Reason for 1990 Change [D.C. Law 10-249]**

The definition of "account" is amended to make clear that it includes both asset accounts in which a customer has deposited money and accounts from which a customer may draw on a line of credit. The remainder of the definition is amended to bring it more into conformity with the definition of "deposit account" in Section 9-105(1)(e).

The definition of "documentary draft" is amended to recognize the existence of uncertificated securities. The reference to "accompanying documents" is deleted as obsolete. It is enough that the documents are to be received by the drawee or other payor before acceptance or payment of the draft.

The definition of "draft" is new and is explained in the Official Comment.

The definition of "drawee" is new and is explained in the Official Comment.

The definition of "item" is amended because the term "instrument" as defined in Section 3-104 and as used in Article 4 is narrower than the term "item." See the Official Comment.

The definition of "properly payable" is deleted. In former Article 4 there is no affirmative definition of the term "properly payable." Former Section 4-104(1)(i) merely implies that if the customer's account is insufficient to pay the item the item is not properly payable. The phrase is defined in proposed Section 4-401(1) in terms of the items authorized by the customer and in accordance with the bank-customer agreement. This is done to give meaning to "properly payable" in Sections 4-401(1) and 4-402(1). The latter provision makes clear that a bank that fails to pay an overdraft has not wrongfully dishonored unless it had agreed to pay the overdraft.

The definition of "settle" is amended in changing "instructed" to "agreed" to conform to Section 4-213.

The terms "remitting bank," "protest," and "second party" are deleted because they are not used in Article 4.

The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-104.

1973 Ed., § 28:4-104.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

Law 11-240, the "Uniform Commercial Code Investment Securities Revision Act of 1996," was introduced in Council and assigned Bill No. 11-576, which was referred to the Committee on Consumer and Regulatory Affairs. The Bill was adopted on first and second readings on November 7, 1996, and December 3, 1996, respectively. Signed by the Mayor on December 24, 1996, it was assigned Act No. 11-500 and transmitted to both Houses of Congress for its review. D.C. Law 11-240 became effective on April 9, 1997.

### **§ 28:4-105. "BANK"; "DEPOSITARY BANK"; "PAYOR BANK"; "INTERMEDIARY BANK"; "COLLECTING BANK"; "PRESENTING BANK".**

In this article, the term:

- (1) "Bank" means a person engaged in the business of banking, including a savings bank, savings and loan association, credit union, or trust company.
- (2) "Depositary bank" means the first bank to take an item even though it is also the payor bank, unless the item is presented for immediate payment over the counter.
- (3) "Payor bank" means a bank that is the drawee of a draft.
- (4) "Intermediary bank" means a bank to which an item is transferred in course of collection except the depositary or payor bank.
- (5) "Collecting bank" means a bank handling an item for collection except the payor bank.
- (6) "Presenting bank" means a bank presenting an item except a payor bank.

(Dec. 30, 1963, 77 Stat. 697, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. The definitions in general exclude a bank to which an item is issued, as this bank does not take by transfer

except in the particular case covered in which the item is issued to payee for collection, as in the case in which a corporation is transferring balances from one account to another. Thus, the definition of "depository bank" does not include the bank to which a check is made payable if a check is given in payment of a mortgage. This bank has the status of a payee under Article 3 on Negotiable Instruments and not that of a collecting bank.

2. Paragraph (1): "Bank" is defined in Section 1-201(4) as meaning "any person engaged in the business of banking." The definition in paragraph (1) makes clear that "bank" includes savings banks, savings and loan associations, credit unions and trust companies, in addition to the commercial banks commonly denoted by use of the term "bank."

3. Paragraph (2): A bank that takes an "on us" item for collection, for application to a customer's loan, or first handles the item for other reasons is a depository bank even though it is also the payor bank. However, if the holder presents the item for immediate payment over the counter, the payor bank is not a depository bank.

4. Paragraph (3): The definition of "payor bank" is clarified by use of the term "drawee." That term is defined in Section 4-104 as meaning "a person ordered in a draft to make payment." An "order" is defined in Section 3-103 as meaning "a written instruction to pay money . . . An authorization to pay is not an order unless the person authorized to pay is also instructed to pay." The definition of order is incorporated into Article 4 by Section 4-104(c). Thus a payor bank is one instructed to pay in the item. A bank does not become a payor bank by being merely authorized to pay or by being given an instruction to pay not contained in the item.

5. Paragraph (4): The term "intermediary bank" includes the last bank in the collection process if the drawee is not a bank. Usually the last bank is also a presenting bank.

#### **Reason for 1990 Change [D.C. Law 10-249]**

The definition of "bank" is added and is in conformity with that found in Section 4A-105(a)(2). See the Official Comment.

The definition of "depository bank" is amended. The term "transferred for collection" is too limiting as the purpose for which the item is taken. The amendment makes clear that a payor bank is not also a depository bank with respect to an item presented for immediate payment over the counter.

The definition of "payor bank" is amended to require that in order for a bank to be a payor bank it must be instructed rather than authorized to pay and that the instruction must be contained in the item. As explained in the Official Comment, this result follows from the use of the defined terms "drawee" and "draft."

The definition of "remitting bank" is deleted because the term is not used in Article 4.

The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-105.

1973 Ed., § 28:4-105.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-106. PAYABLE THROUGH OR PAYABLE AT BANK; COLLECTING BANK.**

(a) If an item states that it is "payable through" a bank identified in the item, (i) the item designates the bank as a collecting bank and does not by itself authorize the bank to pay the item, and (ii) the item may be presented for payment only by or through the bank.

(b) If an item states that it is "payable at" a bank identified in the item, the item is equivalent to a draft drawn on the bank.

(c) If a draft names a nonbank drawee and it is unclear whether a bank named in the draft is a co-drawee or a collecting bank, the bank is a collecting bank.

(Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. This section replaces former Sections 3-120 and 3-121. Some items are made "payable through" a particular bank. Subsection (a) states that such language makes the bank a collecting bank and not a payor bank. An item identifying a "payable through" bank can be presented for payment to the drawee only by the "payable through" bank. The item cannot be presented to the drawee over the counter for immediate payment or by a collecting bank other than the "payable through" bank.

2. Subsection (b) retains the alternative approach of the present law. Under Alternative A a note payable at a bank is the equivalent of a draft drawn on the bank and the midnight deadline provisions of Sections 4-301 and 4-302 apply. Under Alternative B a "payable at" bank is in the same position as a "payable through" bank under subsection (a).

3. Subsection (c) rejects the view of some cases that a bank named below the name of a drawee is itself a drawee. The commercial understanding is that this bank is a collecting bank and is not accountable under Section 4-302 for holding an item beyond its deadline. The liability of the bank is governed by Sections 4-202(a) and 4-103(e).

*Prior Codifications*

1981 Ed., § 28:4-106.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-107. SEPARATE OFFICE OF BANK.**

A branch or separate office of a bank is a separate bank for the purpose of computing the time within which and determining the place at or to which action may be taken or notice or orders must be given under this article and under Article 3.

(Dec. 30, 1963, 77 Stat. 697, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. A rule with respect to the status of a branch or separate office of a bank as a part of any statute on bank collections is highly desirable if not absolutely necessary. However, practices in the operations of branches and separate offices vary substantially in the different states and it has not been possible to find any single rule that is logically correct, fair in all situations and workable under all different types of practices. The decision not to draft the section with greater specificity leaves to the courts the resolution of the issues arising under this section on the basis of the facts of each case.

2. In many states and for many purposes a branch or separate office of the bank should be treated as a separate bank. Many branches function as separate banks in the handling and payment of items and require time for doing so similar to that of a separate bank. This is particularly true if branch banking is permitted throughout a state or in different towns and cities. Similarly, if there is this separate functioning a particular branch or separate office is the only proper place for various types of action to be taken or orders or notices to be given. Examples include the drawing of a check on a particular branch by a customer whose account is carried at that branch; the presentment of that same check at that branch; the issuance of an order to the branch to stop payment on the check.

3. Section 1 of the American Bankers Association Bank Collection Code provided simply: "A branch or office of any such bank shall be deemed a bank." Although this rule appears to be brief and simple, as applied to particular sections of the ABA Code it produces illogical and, in some cases, unreasonable results. For example, under Section 11 of the ABA Code it seems anomalous for one branch of a bank to have charged an item to the account of the drawer and another branch to have the power to elect to treat the item as dishonored. Similar logical problems would flow from applying the same rule to Article 4. Warranties by one branch to another branch under Sections 4-207 and 4-208 (each considered a separate bank) do not make sense.

4. Assuming that it is not desirable to make each branch a separate bank for all purposes, this section provides that a branch or separate office is a separate bank for certain purposes. In so doing the single legal entity of the bank as a whole is preserved, thereby carrying with it the liability of the institution as a whole on such obligations as it may be under. On the other hand, in cases in which the Article provides a number of time limits for different types of action by banks, if a branch functions as a separate bank, it should have the time limits available to a separate bank. Similarly if in its relations to customers a branch functions as a separate bank, notices and orders with respect to accounts of customers of the branch should be given at the branch. For example, whether a branch has notice sufficient to affect its status as a holder in due course of an item taken by it should depend upon what notice that branch has received with respect to the item. Similarly the receipt of a stop-payment order at one branch should not be notice to another branch so as to impair the right of the second branch to be a holder in due course of the item, although in circumstances in which ordinary care requires the communication of a notice or order to the proper branch of a bank, the notice or order would be effective at the proper branch from the time it was or should have been received. See Section 1-201(27).

5. The bracketed language ("maintaining its own deposit ledger") in former Section 4-106 is deleted. Today banks keep records on customer accounts by electronic data storage. This has led most banks with branches to centralize to some degree their record keeping. The place where records are kept has little meaning if the

information is electronically stored and is instantly retrievable at all branches of the bank. Hence, the inference to be drawn from the deletion of the bracketed language is that where record keeping is done is no longer an important factor in determining whether a branch is a separate bank.

#### **Reason for 1990 Change [D.C. Law 10-249]**

The bracketed language in former Section 4-106 is deleted. Today banks keep records on customer accounts by electronic data storage. This has led most banks with branches to centralize to some degree their record keeping. The place where records are kept has little meaning if the information is electronically stored and is instantly retrievable at all branches of the bank. Hence, the inference to be drawn from the deletion of the bracketed language is that where record keeping is done is no longer an important factor in determining whether a branch is a separate bank.

##### *Prior Codifications*

1981 Ed., § 28:4-107.

1973 Ed., § 28:4-106.

##### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-108. TIME OF RECEIPT OF ITEMS.**

(a) For the purpose of allowing time to process items, prove balances, and make the necessary entries on its books to determine its position for the day, a bank may fix an afternoon hour of 2 p.m. or later as a cutoff hour for the handling of money and items and the making of entries on its books.

(b) An item or deposit of money received on any day after a cutoff hour so fixed or after the close of the banking day may be treated as being received at the opening of the next banking day.

(Dec. 30, 1963, 77 Stat. 697, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

##### *HISTORICAL AND STATUTORY NOTES*

##### *UNIFORM COMMERCIAL CODE COMMENT*

1. Each of the huge volume of checks processed each day must go through a series of accounting procedures that consume time. Many banks have found it necessary to establish a cutoff hour to allow time for these procedures to be completed within the time limits imposed by Article 4. Subsection (a) approves a cutoff hour of this type provided it is not earlier than 2 P.M. Subsection (b) provides that if such a cutoff hour is fixed, items received after the cutoff hour may be treated as being received at the opening of the next banking day. If the number of items received either through the mail or over the counter tends to taper off radically as the afternoon hours progress, a 2 P.M. cutoff hour does not involve a large portion of the items received but at the same time permits a bank using such a cutoff hour to leave its doors open later in the afternoon without forcing into the evening the completion of its settling and proving process.

2. The provision in subsection (b) that items or deposits received after the close of the banking day may be treated as received at the opening of the next banking day is important in cases in which a bank closes at twelve or one o'clock, e.g., on a Saturday, but continues to receive some items by mail or over the counter if, for example, it opens Saturday evening for the limited purpose of receiving deposits and cashing checks.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

##### *Prior Codifications*

1981 Ed., § 28:4-108.

1973 Ed., § 28:4-107.

##### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-109. DELAYS.**

(a) Unless otherwise instructed, a collecting bank in a good faith effort to secure payment of a specific item drawn on a payor other than a bank, and with or without the approval of any person involved, may waive, modify, or extend time limits imposed or permitted by this article for a period not exceeding 2 additional banking days without discharge of drawers or indorsers or liability to its transferor or a prior party.

(b) Delay by a collecting bank or payor bank beyond time limits prescribed or permitted by this article or

by instructions is excused if (i) the delay is caused by interruption of communication or computer facilities, suspension of payments by another bank, war, emergency conditions, failure of equipment, or other circumstances beyond the control of the bank, and (ii) the bank exercises such diligence as the circumstances require.

(Dec. 30, 1963, 77 Stat. 697, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

##### *UNIFORM COMMERCIAL CODE COMMENT*

1. Sections 4-202(b), 4-214, 4-301, and 4-302 prescribe various time limits for the handling of items. These are the limits of time within which a bank, in fulfillment of its obligation to exercise ordinary care, must handle items entrusted to it for collection or payment. Under Section 4-103 they may be varied by agreement or by Federal Reserve regulations or operating circular, clearing-house rules, or the like. Subsection (a) permits a very limited extension of these time limits. It authorizes a collecting bank to take additional time in attempting to collect drafts drawn on nonbank payors with or without the approval of any interested party. The right of a collecting bank to waive time limits under subsection (a) does not apply to checks. The two-day extension can only be granted in a good faith effort to secure payment and only with respect to specific items. It cannot be exercised if the customer instructs otherwise. Thus limited the escape provision should afford a limited degree of flexibility in special cases but should not interfere with the overall requirement and objective of speedy collections.

2. An extension granted under subsection (a) is without discharge of drawers or indorsers. It therefore extends the times for presentment or payment as specified in Article 3.

3. Subsection (b) is another escape clause from time limits. This clause operates not only with respect to time limits imposed by the Article itself but also time limits imposed by special instructions, by agreement or by Federal regulations or operating circulars, clearing-house rules or the like. The latter time limits are "permitted" by the Code. For example, a payor bank that fails to make timely return of a dishonored item may be accountable for the amount of the item. Subsection (b) excuses a bank from this liability when its failure to meet its midnight deadline resulted from, for example, a computer breakdown that was beyond the control of the bank, so long as the bank exercised the degree of diligence that the circumstances required. In *Port City State Bank v. American National Bank*, 486 F.2d 196 (10th Cir. 1973), the court held that a bank exercised sufficient diligence to be excused under this subsection. If delay is sought to be excused under this subsection, the bank has the burden of proof on the issue of whether it exercised "such diligence as the circumstances require." The subsection is consistent with Regulation CC, Section 229.38(e).

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (a) is amended to exclude checks and other items drawn on banks from its application so that the provision will not impede the speedy collection of these items. The amended subsection authorizes a collecting bank to take additional time, not in excess of two days, in a good faith effort to collect drafts drawn on nonbank payors with or without the approval of any interested party. The term "secondary parties" is deleted because it is no longer used in Articles 3 and 4. Subsection (b) is amended to make clear that the delay is excused for one of the reasons stated only if the bank exercises such diligence as the circumstances require. With the addition of references to the interruption of computer facilities and the failure of equipment, the permissible reasons for delay enumerated are made to conform to those stated in Regulation CC Section 229.38(e). The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-109.

1973 Ed., § 28:4-108.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-110. ELECTRONIC PRESENTMENT.**

(a) "Agreement for electronic presentment" means an agreement, clearing-house rule, or Federal Reserve regulation or operating circular, providing that presentment of an item may be made by transmission of an image of an item or information describing the item ("presentment notice") rather than delivery of the item itself. The agreement may provide for procedures governing retention, presentment, payment, dishonor, and other matters concerning items subject to the agreement.

(b) Presentment of an item pursuant to an agreement for presentment is made when the presentment notice is received.

(c) If presentment is made by presentment notice, a reference to "item" or "check" in this article means the presentment notice unless the context otherwise indicates.

(Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. "An agreement for electronic presentment" refers to an agreement under which presentment may be made to a payor bank by a presentment notice rather than by presentment of the item. Under imaging technology now under development, the presentment notice might be an image of the item. The electronic presentment agreement may provide that the item may be retained by a depository bank, other collecting bank, or even a customer of the depository bank, or it may provide that the item will follow the presentment notice. The identifying characteristic of an electronic presentment agreement is that presentment occurs when the presentment notice is received. "An agreement for electronic presentment" does not refer to the common case of retention of items by payor banks because the item itself is presented to the payor bank in these cases. Payor bank check retention is a matter of agreement between payor banks and their customers. Provisions on payor bank check retention are found in Section 4-406(b).

2. The assumptions under which the electronic presentment amendments are based are as follows: No bank will participate in an electronic presentment program without an agreement. These agreements may be either bilateral (Section 4- 103(a)), under which two banks that frequently do business with each other may agree to depository bank check retention, or multilateral (Section 4- 103(b)), in which large segments of the banking industry may participate in such a program. In the latter case, federal or other uniform regulatory standards would likely supply the substance of the electronic presentment agreement, the application of which could be triggered by the use of some form of identifier on the item. Regulation CC, Section 229.36(c) authorizes truncation agreements but forbids them from extending return times or otherwise varying requirements of the part of Regulation CC governing check collection without the agreement of all parties interested in the check. For instance, an extension of return time could damage a depository bank which must make funds available to its customers under mandatory availability schedules. The Expedited Funds Availability Act, 12 U.S.C. Section 4008(b)(2), directs the Federal Reserve Board to consider requiring that banks provide for check truncation.

3. The parties affected by an agreement for electronic presentment, with the exception of the customer, can be expected to protect themselves. For example, the payor bank can probably be expected to limit its risk of loss from drawer forgery by limiting the dollar amount of eligible items (Federal Reserve program), by reconciliation agreements (ABA Safekeeping program), by insurance (credit union share draft program), or by other means. Because agreements will exist, only minimal amendments are needed to make clear that the UCC does not prohibit electronic presentment.

*Prior Codifications*

1981 Ed., § 28:4-110.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-111. STATUTE OF LIMITATIONS.**

An action to enforce an obligation, duty, or right arising under this article must be commenced within 3 years after the cause of action accrues.

(Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

This section conforms to the period of limitations set by Section 3-118(g) for actions for breach of warranty and to enforce other obligations, duties or rights arising under Article 3. Bracketing "cause of action" recognizes that some states use a different term, such as "claim for relief."

*Prior Codifications*

1981 Ed., § 28:4-111.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **PART 2. COLLECTION OF ITEMS: DEPOSITORY AND COLLECTING BANKS.**



**§ 28:4-201. STATUS OF COLLECTING BANK AS AGENT AND PROVISIONAL STATUS OF CREDITS; APPLICABILITY OF ARTICLE; ITEM INDORSED "PAY ANY BANK".**

(a) Unless a contrary intent clearly appears and before the time that a settlement given by a collecting bank for an item is or becomes final, the bank, with respect to the item, is an agent or subagent of the owner of the item and any settlement given for the item is provisional. This provision applies regardless of the form of indorsement or lack of indorsement and even though credit given for the item is subject to immediate withdrawal as of right or is in fact withdrawn; but the continuance of ownership of an item by its owner and any rights of the owner to proceeds of the item are subject to rights of a collecting bank, such as those resulting from outstanding advances on the item and rights of recoupment or setoff. If an item is handled by banks for purposes of presentment, payment, collection, or return, the relevant provisions of this article apply even though action of the parties clearly establishes that a particular bank has purchased the item and is the owner of it.

(b) After an item has been indorsed with the words "pay any bank" or the like, only a bank may acquire the rights of a holder until the item has been:

- (1) Returned to the customer initiating collection; or
- (2) Specially indorsed by a bank to a person who is not a bank.

(Dec. 30, 1963, 77 Stat. 698, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. This section states certain basic rules of the bank collection process. One basic rule, appearing in the last sentence of subsection (a), is that, to the extent applicable, the provisions of the Article govern without regard to whether a bank handling an item owns the item or is an agent for collection. Historically, much time has been spent and effort expended in determining or attempting to determine whether a bank was a purchaser of an item or merely an agent for collection. See discussion of this subject and cases cited in 11 A.L.R. 1043, 16 A.L.R. 1084, 42 A.L.R. 492, 68 A.L.R. 725, 99 A.L.R. 486. See also Section 4 of the American Bankers Association Bank Collection Code. The general approach of Article 4, similar to that of other articles, is to provide, within reasonable limits, rules or answers to major problems known to exist in the bank collection process without regard to questions of status and ownership but to keep general principles such as status and ownership available to cover residual areas not covered by specific rules. In line with this approach, the last sentence of subsection (a) says in effect that Article 4 applies to practically every item moving through banks for the purpose of presentment, payment or collection.

2. Within this general rule of broad coverage, the first two sentences of subsection (a) state a rule of agency status. "Unless a contrary intent clearly appears" the status of a collecting bank is that of an agent or sub-agent for the owner of the item. Although as indicated in Comment 1 it is much less important under Article 4 to determine status than has been the case heretofore, status may have importance in some residual areas not covered by specific rules. Further, since status has been considered so important in the past, to omit all reference to it might cause confusion. The status of agency "applies regardless of the form of indorsement or lack of indorsement and even though credit given for the item is subject to immediate withdrawal as of right or is in fact withdrawn." Thus questions heretofore litigated as to whether ordinary indorsements "for deposit," "for collection" or in blank have the effect of creating an agency status or a purchase, no longer have significance in varying the prima facie rule of agency. Similarly, the nature of the credit given for an item or whether it is subject to immediate withdrawal as of right or is in fact withdrawn, does not alter the agency status. See A.L.R. references *supra* in Comment 1.

A contrary intent can change agency status but this must be clear. An example of a clear contrary intent would be if collateral papers established or the item bore a legend stating that the item was sold absolutely to the depository bank.

3. The prima facie agency status of collecting banks is consistent with prevailing law and practice today. Section 2 of the American Bankers Association Bank Collection Code so provided. Legends on deposit tickets, collection letters and acknowledgments of items and Federal Reserve operating circulars consistently so provide. The status is consistent with rights of charge-back (Section 4-214 and Section 11 of the ABA Code) and risk of loss in the event of insolvency (Section 4-216 and Section 13 of the ABA Code). The right of charge-back with respect to checks is limited by Regulation CC, Section 226.36(d).

4. Affirmative statement of a prima facie agency status for collecting banks requires certain limitations and qualifications. Under current practices substantially all bank collections sooner or later merge into bank credits, at least if collection is effected. Usually, this takes place within a few days of the initiation of collection. An intermediary bank receives final collection and evidences the result of its collection by a "credit" on its books to the depository bank. The depository bank evidences the results of its collection by a "credit" in the account of its customer. As used in these instances the term "credit" clearly indicates a debtor-creditor relationship. At some stage in the bank collection process the agency status of a collecting bank changes to that of debtor, a debtor of its customer. Usually at about the same time it also becomes a creditor for the

amount of the item, a creditor of some intermediary, payor or other bank. Thus the collection is completed, all agency aspects are terminated and the identity of the item has become completely merged in bank accounts, that of the customer with the depository bank and that of one bank with another.

Although Section 4-215(a) provides that an item is finally paid when the payor bank takes or fails to take certain action with respect to the item, the final payment of the item may or may not result in the simultaneous final settlement for the item in the case of all prior parties. If a series of provisional debits and credits for the item have been entered in accounts between banks, the final payment of the item by the payor bank may result in the automatic firming up of all these provisional debits and credits under Section 4-215(c), and the consequent receipt of final settlement for the item by each collecting bank and the customer of the depository bank simultaneously with such action of the payor bank. However, if the payor bank or some intermediary bank accounts for the item with a remittance draft, the next prior bank usually does not receive final settlement for the item until the remittance draft finally clears. See Section 4-213(c). The first sentence of subsection (a) provides that the agency status of a collecting bank (whether intermediary or depository) continues until the settlement given by it for the item is or becomes final. In the case of the series of provisional credits covered by Section 4-215(c), this could be simultaneously with the final payment of the item by the payor bank. In cases in which remittance drafts are used or in straight noncash collections, this would not be until the times specified in Sections 4-213(c) and 4-215(d). With respect to checks Regulation CC Sections 229.31(c), 229.32(b) and 229.36(d) provide that all settlements between banks are final in both the forward collection and return of checks.

Under Section 4-213(a) settlements for items may be made by any means agreed to by the parties. Since it is impossible to contemplate all the kinds of settlements that will be utilized, no attempt is made in Article 4 to provide when settlement is final in all cases. The guiding principle is that settlements should be final when the presenting person has received usable funds. Section 4-213(c) and (d) and Section 4-215(c) provide when final settlement occurs with respect to certain kinds of settlement, but these provisions are not intended to be exclusive.

A number of practical results flow from the rule continuing the agency status of a collecting bank until its settlement for the item is or becomes final, some of which are specifically set forth in this Article. One is that risk of loss continues in the owner of the item rather than the agent bank. See Section 4-214. Offsetting rights favorable to the owner are that pending such final settlement, the owner has the preference rights of Section 4-216 and the direct rights of Section 4-302 against the payor bank. It also follows from this rule that the dollar limitations of Federal Deposit Insurance are measured by the claim of the owner of the item rather than that of the collecting bank. With respect to checks, rights of the parties in insolvency are determined by Regulation CC Section 229.39 and the liability of a bank handling a check to a subsequent bank that does not receive payment because of suspension of payments by another bank is stated in Regulation CC Section 229.35(b).

5. In those cases in which some period of time elapses between the final payment of the item by the payor bank and the time that the settlement of the collecting bank is or becomes final, e.g., if the payor bank or an intermediary bank accounts for the item with a remittance draft or in straight noncash collections, the continuance of the agency status of the collecting bank necessarily carries with it the continuance of the owner's status as principal. The second sentence of subsection (a) provides that whatever rights the owner has to proceeds of the item are subject to the rights of collecting banks for outstanding advances on the item and other valid rights, if any. The rule provides a sound rule to govern cases of attempted attachment of proceeds of a noncash item in the hands of the payor bank as property of the absent owner. If a collecting bank has made an advance on an item which is still outstanding, its right to obtain reimbursement for this advance should be superior to the rights of the owner to the proceeds or to the rights of a creditor of the owner. An intentional crediting of proceeds of an item to the account of a prior bank known to be insolvent, for the purpose of acquiring a right of setoff, would not produce a valid setoff. See 8 Zollman, Banks and Banking (1936) Sec. 5443.

6. This section and Article 4 as a whole represent an intentional abandonment of the approach to bank collection problems appearing in Section 4 of the American Bankers Association Bank Collection Code. Because the tremendous volume of items handled makes impossible the examination by all banks of all indorsements on all items and thus in fact this examination is not made, except perhaps by depository banks, it is unrealistic to base the rights and duties of all banks in the collection chain on variations in the form of indorsements. It is anomalous to provide throughout the ABA Code that the prima facie status of collecting banks is that of agent or sub-agent but in Section 4 to provide that subsequent holders (sub-agents) shall have the right to rely on the presumption that the bank of deposit (the primary agent) is the owner of the item. It is unrealistic, particularly in this background, to base rights and duties on status of agent or owner. Thus Section 4-201 makes the pertinent provisions of Article 4 applicable to substantially all items handled by banks for presentment, payment or collection, recognizes the prima facie status of most banks as agents, and then seeks to state appropriate limits and some attributes to the general rules so expressed.

7. Subsection (b) protects the ownership rights with respect to an item indorsed "pay any bank or banker" or in similar terms of a customer initiating collection or of any bank acquiring a security interest under Section 4-210, in the event the item is subsequently acquired under improper circumstances by a person who is not a bank and transferred by that person to another person, whether or not a bank. Upon return to the customer initiating collection of an item so indorsed, the indorsement may be cancelled (Section 3-207). A bank holding an item so indorsed may transfer the item out of banking channels by special indorsement; however, under

Section 4-103(e), the bank would be liable to the owner of the item for any loss resulting therefrom if the transfer had been made in bad faith or with lack of ordinary care. If briefer and more simple forms of bank indorsements are developed under Section 4- 206 (e.g., the use of bank transit numbers in lieu of present lengthy forms of bank indorsements), a depository bank having the transit number "X100" could make subsection (b) operative by indorsements such as "Pay any bank--X100." Regulation CC Section 229.35(c) states the effect of an indorsement on a check by a bank.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (a) is amended to delete the cross references to former Sections 4- 211, 4-212 and 4-213. The reason for the deletion is to remove any implication that final settlement is determined only by these provisions. Sections 4- 213(c) and (d) and 4-215(c) provide when final settlement occurs with respect to certain kinds of settlements, but these provisions are not intended to be exclusive. Since it is impossible to contemplate all the kinds of settlements that will be utilized, no attempt is made in Article 4 to provide when settlement is final in all cases. "Recoupment" is added to the second sentence to clarify the collecting bank's rights against the item or its proceeds. Terms like "valid" or "binding" have been deleted entirely from Article 4 as superfluous. "Or return" is added to the third sentence to make clear that the effect of the provision is not restricted to the forward collection activities of banks but also extends to their acts in returning items. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-201.

1973 Ed., § 28:4-201.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-202. RESPONSIBILITY FOR COLLECTION OR RETURN; WHEN ACTION TIMELY.**

(a) A collecting bank must exercise ordinary care in:

- (1) Presenting an item or sending it for presentment;
- (2) Sending notice of dishonor or nonpayment, or returning an item other than a documentary draft to the bank's transferor after learning that the item has not been paid or accepted, as the case may be;
- (3) Settling for an item when the bank receives final settlement; and
- (4) Notifying its transferor of any loss or delay in transit within a reasonable time after discovery thereof.

(b) A collecting bank exercises ordinary care under subsection (a) of this section by taking proper action before its midnight deadline following receipt of an item, notice, or settlement. Taking proper action within a reasonably longer time may constitute the exercise of ordinary care, but the bank has the burden of establishing timeliness.

(c) Subject to subsection (a)(1) of this section, a bank is not liable for the insolvency, neglect, misconduct, mistake, or default of another bank or person or for loss or destruction of an item in the possession of others or in transit.

(Dec. 30, 1963, 77 Stat. 698, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Subsection (a) states the basic responsibilities of a collecting bank. Of course, under Section 1-203 a collecting bank is subject to the standard requirement of good faith. By subsection (a) it must also use ordinary care in the exercise of its basic collection tasks. By Section 4-103(a) neither requirement may be disclaimed.

2. If the bank makes presentment itself, subsection (a)(1) requires ordinary care with respect both to the time and manner of presentment. (Sections 3- 501 and 4-212.) If it forwards the item to be presented the subsection requires ordinary care with respect to routing (Section 4-204), and also in the selection of intermediary banks or other agents.

3. Subsection (a) describes types of basic action with respect to which a collecting bank must use ordinary care. Subsection (b) deals with the time for taking action. It first prescribes the general standard for timely action, namely, for items received on Monday, proper action (such as forwarding or presenting) on Monday or Tuesday is timely. Although under current "production line" operations banks customarily move items along on regular schedules substantially briefer than two days, the subsection states an outside time within which a bank may know it has taken timely action. To provide flexibility from this standard norm, the subsection further

states that action within a reasonably longer time may be timely but the bank has the burden of proof. In the case of time items, action after the midnight deadline, but sufficiently in advance of maturity for proper presentation, is a clear example of a "reasonably longer time" that is timely. The standard of requiring action not later than Tuesday in the case of Monday items is also subject to possibilities of variation under the general provisions of Section 4-103, or under the special provisions regarding time of receipt of items (Section 4-108), and regarding delays (Section 4-109). This subsection (b) deals only with collecting banks. The time limits applicable to payor banks appear in Sections 4-301 and 4-302.

4. At common law the so-called New York collection rule subjected the initial collecting bank to liability for the actions of subsequent banks in the collection chain; the so-called Massachusetts rule was that each bank, subject to the duty of selecting proper intermediaries, was liable only for its own negligence. Subsection (c) adopts the Massachusetts rule. But since this is stated to be subject to subsection (a)(1) a collecting bank remains responsible for using ordinary care in selecting properly qualified intermediary banks and agents and in giving proper instructions to them. Regulation CC Section 229.36(d) states the liability of a bank during the forward collection of checks.

#### **Reason for 1990 Change [D.C. Law 10-249]**

The term "timely" is substituted for "seasonable" throughout the section. The bracketed material in paragraph (2) of subsection (a) is deleted because the provision to which it refers in former Section 4-212 is deleted. Paragraph (d) of former subsection (1) is deleted because Article 4 has no requirement of protest. Subsection (b) is a restatement of former subsection (2). The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-202.

1973 Ed., § 28:4-202.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-203. EFFECT OF INSTRUCTIONS.**

Subject to Article 3 concerning conversion of instruments (section 28:3-420) and restrictive indorsements (section 28:3-206), only a collecting bank's transferor can give instructions that affect the bank or constitute notice to it, and a collecting bank is not liable to prior parties for any action taken pursuant to the instructions or in accordance with any agreement with its transferor.

(Dec. 30, 1963, 77 Stat. 699, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

This section adopts a "chain of command" theory which renders it unnecessary for an intermediary or collecting bank to determine whether its transferor is "authorized" to give the instructions. Equally the bank is not put on notice of any "revocation of authority" or "lack of authority" by notice received from any other person. The desirability of speed in the collection process and the fact that, by reason of advances made, the transferor may have the paramount interest in the item requires the rule.

The section is made subject to the provisions of Article 3 concerning conversion of instruments (Section 3-420) and restrictive indorsements (Section 3-206). Of course instructions from or an agreement with its transferor does not relieve a collecting bank of its general obligation to exercise good faith and ordinary care. See Section 4-103(a). If in any particular case a bank has exercised good faith and ordinary care and is relieved of responsibility by reason of instructions of or an agreement with its transferor, the owner of the item may still have a remedy for loss against the transferor (another bank) if such transferor has given wrongful instructions.

The rules of the section are applied only to collecting banks. Payor banks always have the problem of making proper payment of an item; whether such payment is proper should be based upon all of the rules of Articles 3 and 4 and all of the facts of any particular case, and should not be dependent exclusively upon instructions from or an agreement with a person presenting the item.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Article 4 no longer has provisions on restrictive indorsements; hence, the reference to "this Article" is deleted. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-203.

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-204. METHODS OF SENDING AND PRESENTING; SENDING DIRECTLY TO PAYOR BANK.**

(a) A collecting bank shall send items by a reasonably prompt method, taking into consideration relevant instructions, the nature of the item, the number of those items on hand, the cost of collection involved, and the method generally used by it or others to present those items.

(b) A collecting bank may send:

- (1) An item directly to the payor bank;
- (2) An item to a nonbank payor if authorized by its transferor; and
- (3) An item other than documentary drafts to a nonbank payor, if authorized by Federal Reserve regulation or operating circular, clearing-house rule, or the like.

(c) Presentment may be made by a presenting bank at a place where the payor bank or other payor has requested that presentment be made.

(Dec. 30, 1963, 77 Stat. 699, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Subsection (a) prescribes the general standards applicable to proper sending or forwarding of items. Because of the many types of methods available and the desirability of preserving flexibility any attempt to prescribe limited or precise methods is avoided.

2. Subsection (b)(1) codifies the practice of direct mail, express, messenger or like presentment to payor banks. The practice is now country-wide and is justified by the need for speed, the general responsibility of banks, Federal Deposit Insurance protection and other reasons.

3. Full approval of the practice of direct sending is limited to cases in which a bank is a payor. Since nonbank drawees or payors may be of unknown responsibility, substantial risks may be attached to placing in their hands the instruments calling for payments from them. This is obviously so in the case of documentary drafts. However, in some cities practices have long existed under clearing-house procedures to forward certain types of items to certain nonbank payors. Examples include insurance loss drafts drawn by field agents on home offices. For the purpose of leaving the door open to legitimate practices of this kind, subsection (b)(3) affirmatively approves direct sending of any item other than documentary drafts to any nonbank payor, if authorized by Federal Reserve regulation or operating circular, clearing-house rule or the like.

On the other hand subsection (b)(2) approves sending any item directly to a nonbank payor if authorized by a collecting bank's transferor. This permits special instructions or agreements out of the norm and is consistent with the "chain of command" theory of Section 4-203. However, if a transferor other than the owner of the item, e.g., a prior collecting bank, authorizes a direct sending to a nonbank payor, such transferor assumes responsibility for the propriety or impropriety of such authorization.

4. Section 3-501(b) provides where presentment may be made. This provision is expressly subject to Article 4. Section 4-204(c) specifically approves presentment by a presenting bank at any place requested by the payor bank or other payor. The time when a check is received by a payor bank for presentment is governed by Regulation CC Section 229.36(b).

### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (c) is amended to allow nonbank payors to request a place of payment. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-204.

1973 Ed., § 28:4-204.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-205. DEPOSITARY BANK HOLDER OF UNINDORSED ITEM.**

If a customer delivers an item to a depository bank for collection:

(1) The depositary bank becomes a holder of the item at the time it receives the item for collection if the customer at the time of delivery was a holder of the item, whether or not the customer indorses the item, and, if the bank satisfies the other requirements of section 28:3-302, it is a holder in due course; and

(2) The depositary bank warrants to collecting banks, the payor bank or other payor, and the drawer that the amount of the item was paid to the customer or deposited to the customer's account.

(Dec. 30, 1963, 77 Stat. 699, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

Section 3-201(b) provides that negotiation of an instrument payable to order requires indorsement by the holder. The rule of former Section 4-205(1) was that the depositary bank may supply a missing indorsement of its customer unless the item contains the words "payee's indorsement required" or the like. The cases have differed on the status of the depositary bank as a holder if it fails to supply its customer's indorsement. *Marine Midland Bank, N.A. v. Price, Miller, Evans & Flowers*, 446 N.Y.S.2d 797 (N.Y.App.Div.4th Dept. 1981), *rev'd*, 455 N.Y.S.2d 565 (N.Y.1982). It is common practice for depositary banks to receive unindorsed checks under so-called "lock-box" agreements from customers who receive a high volume of checks. No function would be served by requiring a depositary bank to run these items through a machine that would supply the customer's indorsement except to afford the drawer and the subsequent banks evidence that the proceeds of the item reached the customer's account. Paragraph (1) provides that the depositary bank becomes a holder when it takes the item for deposit if the depositor is a holder. Whether it supplies the customer's indorsement is immaterial. Paragraph (2) satisfies the need for a receipt of funds by the depositary bank by imposing on that bank a warranty that it paid the customer or deposited the item to the customer's account. This warranty runs not only to collecting banks and to the payor bank or nonbank drawee but also to the drawer, affording protection to these parties that the depositary bank received the item and applied it to the benefit of the holder.

*Prior Codifications*

1981 Ed., § 28:4-205.

1973 Ed., § 28:4-205.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-206. TRANSFER BETWEEN BANKS.**

Any agreed method that identifies the transferor bank is sufficient for the item's further transfer to another bank.

(Dec. 30, 1963, 77 Stat. 699, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

This section is designed to permit the simplest possible form of transfer from one bank to another, once an item gets in the bank collection chain, provided only identity of the transferor bank is preserved. This is important for tracing purposes and if recourse is necessary. However, since the responsibilities of the various banks appear in the Article it becomes unnecessary to have liability or responsibility depend on more formal indorsements. Simplicity in the form of transfer is conducive to speed. If the transfer is between banks, this section takes the place of the more formal requirements of Section 3-201.

### **Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

*Prior Codifications*

1981 Ed., § 28:4-206.

1973 Ed., § 28:4-206.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-207. TRANSFER WARRANTIES.**

(a) A customer or collecting bank that transfers an item and receives a settlement or other consideration warrants to the transferee and to any subsequent collecting bank that:

- (1) The warrantor is a person entitled to enforce the item;
- (2) All signatures on the item are authentic and authorized;
- (3) The item has not been altered;
- (4) The item is not subject to a defense or claim in recoupment (section 28:3-305(a)) of any party that can be asserted against the warrantor; and
- (5) The warrantor has no knowledge of any insolvency proceeding commenced with respect to the maker or acceptor or, in the case of an unaccepted draft, the drawer.

(b) If an item is dishonored, a customer or collecting bank transferring the item and receiving settlement or other consideration is obliged to pay the amount due on the item (i) according to the terms of the item at the time it was transferred, or (ii) if the transfer was of an incomplete item, according to its terms when completed as stated in sections 28:3-115 and 28:3-407. The obligation of a transferor is owed to the transferee and to any subsequent collecting bank that takes the item in good faith. A transferor cannot disclaim its obligation under this subsection by an indorsement stating that it is made "without recourse" or otherwise disclaiming liability.

(c) A person to whom the warranties under subsection (a) of this section are made and who took the item in good faith may recover from the warrantor as damages for breach of warranty an amount equal to the loss suffered as a result of the breach, but not more than the amount of the item plus expenses and loss of interest incurred as a result of the breach.

(d) The warranties stated in subsection (a) of this section cannot be disclaimed with respect to checks. Unless notice of a claim for breach of warranty is given to the warrantor within 30 days after the claimant has reason to know of the breach and the identity of the warrantor, the warrantor is discharged to the extent of any loss caused by the delay in giving notice of the claim.

(e) A cause of action for breach of warranty under this section accrues when the claimant has reason to know of the breach.

(Dec. 30, 1963, 77 Stat. 699, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

Except for subsection (b), this section conforms to Section 3-416 and extends its coverage to items. The substance of this section is discussed in the Comment to Section 3-416. Subsection (b) provides that customers or collecting banks that transfer items, whether by indorsement or not, undertake to pay the item if the item is dishonored. This obligation cannot be disclaimed by a "without recourse" indorsement or otherwise. With respect to checks, Regulation CC Section 229.34 states the warranties made by paying and returning banks.

#### *Prior Codifications*

1981 Ed., § 28:4-207.

1973 Ed., § 28:4-207.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-208. PRESENTMENT WARRANTIES.**

(a) If an unaccepted draft is presented to the drawee for payment or acceptance and the drawee pays or accepts the draft, (i) the person obtaining payment or acceptance, at the time of presentment, and (ii) a previous transferor of the draft, at the time of transfer, warrant to the drawee that pays or accepts the draft in good faith that:

- (1) The warrantor is, or was, at the time the warrantor transferred the draft, a person entitled to enforce the draft or authorized to obtain payment or acceptance of the draft on behalf of a person entitled to enforce the draft;
- (2) The draft has not been altered; and
- (3) The warrantor has no knowledge that the signature of the purported drawer of the draft is unauthorized.

(b) A drawee making payment may recover from a warrantor damages for breach of warranty equal to the amount paid by the drawee less the amount the drawee received or is entitled to receive from the drawer because of the payment. In addition, the drawee is entitled to compensation for expenses and loss of

interest resulting from the breach. The right of the drawee to recover damages under this subsection is not affected by any failure of the drawee to exercise ordinary care in making payment. If the drawee accepts the draft (i) breach of warranty is a defense to the obligation of the acceptor, and (ii) if the acceptor makes payment with respect to the draft, the acceptor is entitled to recover from a warrantor for breach of warranty the amounts stated in this subsection.

(c) If a drawee asserts a claim for breach of warranty under subsection (a) of this section based on an unauthorized indorsement of the draft or an alteration of the draft, the warrantor may defend by proving that the indorsement is effective under section 28:3-404 or 28:3-405 or the drawer is precluded under section 28:3-406 or 28:4-406 from asserting against the drawee the unauthorized indorsement or alteration.

(d) If (i) a dishonored draft is presented for payment to the drawer or an indorser or (ii) any other item is presented for payment to a party obliged to pay the item, and the item is paid, the person obtaining payment and a prior transferor of the item warrant to the person making payment in good faith that the warrantor is, or was, at the time the warrantor transferred the item, a person entitled to enforce the item or authorized to obtain payment on behalf of a person entitled to enforce the item. The person making payment may recover from any warrantor for breach of warranty an amount equal to the amount paid plus expenses and loss of interest resulting from the breach.

(e) The warranties stated in subsections (a) and (d) of this section cannot be disclaimed with respect to checks. Unless notice of a claim for breach of warranty is given to the warrantor within 30 days after the claimant has reason to know of the breach and the identity of the warrantor, the warrantor is discharged to the extent of any loss caused by the delay in giving notice of the claim.

(f) A cause of action for breach of warranty under this section accrues when the claimant has reason to know of the breach.

(Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

This section conforms to Section 3-417 and extends its coverage to items. The substance of this section is discussed in the Comment to Section 3-417. "Draft" is defined in Section 4-104 as including an item that is an order to pay so as to make clear that the term "draft" in Article 4 may include items that are not instruments within Section 3-104.

#### *Prior Codifications*

1981 Ed., § 28:4-208.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-209. ENCODING AND RETENTION WARRANTIES.**

(a) A person who encodes information on or with respect to an item after issue warrants to any subsequent collecting bank and to the payor bank or other payor that the information is correctly encoded. If the customer of a depository bank encodes, that bank also makes the warranty.

(b) A person who undertakes to retain an item pursuant to an agreement for electronic presentment warrants to any subsequent collecting bank and to the payor bank or other payor that retention and presentment of the item comply with the agreement. If a customer of a depository bank undertakes to retain an item, that bank also makes this warranty.

(c) A person to whom warranties are made under this section and who took the item in good faith may recover from the warrantor as damages for breach of warranty an amount equal to the loss suffered as a result of the breach, plus expenses and loss of interest incurred as a result of the breach.

(Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Encoding and retention warranties are included in Article 4 because they are unique to the bank collection process. These warranties are breached only by the person doing the encoding or retaining the item and not by subsequent banks handling the item. Encoding and check retention may be done by customers who are payees of a large volume of checks; hence, this section imposes warranties on customers as well as banks. If a customer encodes or retains, the depository bank is also liable for any breach of this warranty.

2. A misencoding of the amount on the MICR line is not an alteration under Section 3-407(a) which defines alteration as changing the contract of the parties. If a drawer wrote a check for \$2,500 and the depository bank encoded \$25,000 on the MICR line, the payor bank could debit the drawer's account for only \$2,500.



This subsection would allow the payor bank to hold the depository bank liable for the amount paid out over \$2,500 without first pursuing the person who received payment. Intervening collecting banks would not be liable to the payor bank for the depository bank's error. If a drawer wrote a check for \$25,000 and the depository bank encoded \$2,500, the payor bank becomes liable for the full amount of the check. The payor bank's rights against the depository bank depend on whether the payor bank has suffered a loss. Since the payor bank can debit the drawer's account for \$25,000, the payor bank has a loss only to the extent that the drawer's account is less than the full amount of the check. There is no requirement that the payor bank pursue collection against the drawer beyond the amount in the drawer's account as a condition to the payor bank's action against the depository bank for breach of warranty. See *Georgia Railroad Bank & Trust Co. v. First National Bank & Trust*, 229 S.E.2d 482 (Ga.App.1976), *aff'd*, 235 S.E.2d 1 (Ga.1977), and *First National Bank of Boston v. Fidelity Bank, National Association*, 724 F.Supp. 1168 (E.D.Pa.1989).

3. A person retaining items under an electronic presentment agreement (Section 4-110) warrants that it has complied with the terms of the agreement regarding its possession of the item and its sending a proper presentment notice. If the keeper is a customer, its depository bank also makes this warranty.

#### *Prior Codifications*

1981 Ed., § 28:4-209.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-210. SECURITY INTEREST OF COLLECTING BANK IN ITEMS, ACCOMPANYING DOCUMENTS, AND PROCEEDS.**

(a) A collecting bank has a security interest in an item and any accompanying documents or the proceeds of either:

- (1) In case of an item deposited in an account, to the extent to which credit given for the item has been withdrawn or applied;
- (2) In case of an item for which it has given credit available for withdrawal as of right, to the extent of the credit given, whether or not the credit is drawn upon or there is a right of charge-back; or
- (3) If it makes an advance on or against the item.

(b) If credit given for several items received at one time or pursuant to a single agreement is withdrawn or applied in part, the security interest remains upon all the items, any accompanying documents or the proceeds of either. For the purpose of this section, credits first given are first withdrawn.

(c) Receipt by a collecting bank of a final settlement for an item is a realization on its security interest in the item, accompanying documents, and proceeds. So long as the bank does not receive final settlement for the item or give up possession of the item or accompanying documents for purposes other than collection, the security interest continues to that extent and is subject to Article 9, but:

- (1) No security agreement is necessary to make the security interest enforceable (section 28:9-203(b)(e)(A));
- (2) No filing is required to perfect the security interest; and
- (3) The security interest has priority over conflicting perfected security interests in the item, accompanying documents, or proceeds.

(Dec. 30, 1963, 77 Stat. 700, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467; Oct. 26, 2000, D.C. Law 13-201, § 201(e), 47 DCR 7576.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Subsection (a) states a rational rule for the interest of a bank in an item. The customer of the depository bank is normally the owner of the item and the several collecting banks are agents of the customer (Section 4-201). A collecting agent may properly make advances on the security of paper held for collection, and acquires at common law a possessory lien for these advances. Subsection (a) applies an analogous principle to a bank in the collection chain which extends credit on items in the course of collection. The bank has a security interest to the extent stated in this section. To the extent of its security interest it is a holder for value (Sections 3-303, 4-211) and a holder in due course if it satisfies the other requirements for that status (Section 3-302). Subsection (a) does not derogate from the banker's general common law lien or right of setoff against indebtedness owing in deposit accounts. See Section 1-103. Rather subsection (a) specifically implements and extends the principle as a part of the bank collection process.

2. Subsection (b) spreads the security interest of the bank over all items in a single deposit or received under a single agreement and a single giving of credit. It also adopts the "first-in, first-out" rule.

3. Collection statistics establish that the vast majority of items handled for collection are in fact collected. The first sentence of subsection (c) reflects the fact that in the normal case the bank's security interest is self-liquidating. The remainder of the subsection correlates the security interest with the provisions of Article 9, particularly for use in the cases of noncollection in which the security interest may be important.

#### **Reason for 1990 Change [D.C. Law 10-249]**

The addition of "collecting" in subsection (a) is a clarification. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

##### *Prior Codifications*

1981 Ed., § 28:4-210.

1973 Ed., § 28:4-208.

##### *Effect of Amendments*

D.C. Law 13-201, enacting a new Article 9 of the Uniform Commercial Code applicable July 1, 2001, made conforming amendments to this section applicable upon the same date.

##### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

Law 13-201, the "Uniform Commercial Code Secured Transactions Revision Act of 2000," was introduced in Council and assigned Bill No. 13-370, which was referred to the Committee on Finance and Revenue. The Bill was adopted on first and second readings on June 6, 2000, and July 11, 2000, respectively. Signed by the Mayor on August 11, 2000, it was assigned Act No. 13-434 and transmitted to both Houses of Congress for its review. D.C. Law 13-201 became effective on October 26, 2000.

### **§ 28:4-211. WHEN BANK GIVES VALUE FOR PURPOSES OF HOLDER IN DUE COURSE.**

For purposes of determining its status as a holder in due course, a bank has given value to the extent it has a security interest in an item, if the bank otherwise complies with the requirements of section 28:3-302 on what constitutes a holder in due course.

(Dec. 30, 1963, 77 Stat. 700, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

##### *HISTORICAL AND STATUTORY NOTES*

##### *UNIFORM COMMERCIAL CODE COMMENT*

The section completes the thought of the previous section and makes clear that a security interest in an item is "value" for the purpose of determining the holder's status as a holder in due course. The provision is in accord with the prior law (N.I.L. Section 27) and with Article 3 (Section 3-303). The section does not prescribe a security interest under Section 4-210 as a test of "value" generally because the meaning of "value" under other Articles is adequately defined in Section 1-201.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

##### *Prior Codifications*

1981 Ed., § 28:4-211.

1973 Ed., § 28:4-209.

##### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-212. PRESENTMENT BY NOTICE OF ITEM NOT PAYABLE BY, THROUGH, OR AT BANK; LIABILITY OF DRAWER OR INDORSER.**

(a) Unless otherwise instructed, a collecting bank may present an item not payable by, through, or at a bank by sending to the party to accept or pay a written notice that the bank holds the item for acceptance or payment. The notice must be sent in time to be received on or before the day when presentment is due and the bank must meet any requirement of the party to accept or pay under section 28:3-501 by the close of the bank's next banking day after it knows of the requirement.

(b) If presentment is made by notice and payment, acceptance, or request for compliance with a requirement under section 28:3-501 is not received by the close of business on the day after maturity or, in the case of demand items, by the close of business on the third banking day after notice was sent, the

presenting bank may treat the item as dishonored and charge any drawer or indorser by sending it notice of the facts.

(Dec. 30, 1963, 77 Stat. 701, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. This section codifies a practice extensively followed in presentation of trade acceptances and documentary and other drafts drawn on nonbank payors. It imposes a duty on the payor to respond to the notice of the item if the item is not to be considered dishonored. Notice of such a dishonor charges drawers and indorsers. Presentment under this section is good presentment under Article 3. See Section 3-501.

2. A drawee not receiving notice is not, of course, liable to the drawer for wrongful dishonor.

3. A bank so presenting an instrument must be sufficiently close to the drawee to be able to exhibit the instrument on the day it is requested to do so or the next business day at the latest.

**Reason for 1990 Change [D.C. Law 10-249]**

The term "secondary party" is no longer used in Articles 3 and 4. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

*Prior Codifications*

1981 Ed., § 28:4-212.

1973 Ed., § 28:4-210.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

**§ 28:4-213. MEDIUM AND TIME OF SETTLEMENT BY BANK.**

(a) With respect to settlement by a bank, the medium and time of settlement may be prescribed by Federal Reserve regulations or circulars, clearing-house rules, and the like, or agreement. In the absence of such prescription:

(1) The medium of settlement is cash or credit to an account in a Federal Reserve bank of or specified by the person to receive settlement; and

(2) The time of settlement, is:

(A) With respect to tender of settlement by cash, a cashier's check, or teller's check, when the cash or check is sent or delivered;

(B) With respect to tender of settlement by credit in an account in a Federal Reserve Bank, when the credit is made;

(C) With respect to tender of settlement by a credit or debit to an account in a bank, when the credit or debit is made or, in the case of tender of settlement by authority to charge an account, when the authority is sent or delivered; or

(D) With respect to tender of settlement by a funds transfer, when payment is made pursuant to section 28:4A-406(a) to the person receiving settlement.

(b) If the tender of settlement is not by a medium authorized by subsection (a) of this section or the time of settlement is not fixed by subsection (a) of this section, no settlement occurs until the tender of settlement is accepted by the person receiving settlement.

(c) If settlement for an item is made by cashier's check or teller's check and the person receiving settlement, before its midnight deadline:

(1) Presents or forwards the check for collection, settlement is final when the check is finally paid; or

(2) Fails to present or forward the check for collection, settlement is final at the midnight deadline of the person receiving settlement.

(d) If settlement for an item is made by giving authority to charge the account of the bank giving settlement in the bank receiving settlement, settlement is final when the charge is made by the bank receiving settlement if there are funds available in the account for the amount of the item.

(Dec. 30, 1963, 77 Stat. 701, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. Subsection (a) sets forth the medium of settlement that the person receiving settlement must accept. In

nearly all cases the medium of settlement will be determined by agreement or by Federal Reserve regulations and circulars, clearing-house rules, and the like. In the absence of regulations, rules or agreement, the person receiving settlement may demand cash or credit in a Federal Reserve bank. If the person receiving settlement does not have an account in a Federal Reserve bank, it may specify the account of another bank in a Federal Reserve bank. In the unusual case in which there is no agreement on the medium of settlement and the bank making settlement tenders settlement other than cash or Federal Reserve bank credit, no settlement has occurred under subsection (b) unless the person receiving settlement accepts the settlement tendered. For example, if a payor bank, without agreement, tenders a teller's check, the bank receiving the settlement may reject the check and return it to the payor bank or it may accept the check as settlement.

2. In several provisions of Article 4 the time that a settlement occurs is relevant. Subsection (a) sets out a general rule that the time of settlement, like the means of settlement, may be prescribed by agreement. In the absence of agreement, the time of settlement for tender of the common agreed media of settlement is that set out in subsection (a)(2). The time of settlement by cash, cashier's or teller's check or authority to charge an account is the time the cash, check or authority is sent, unless presentment is over the counter in which case settlement occurs upon delivery to the presenter. If there is no agreement on the time of settlement and the tender of settlement is not made by one of the media set out in subsection (a), under subsection (b) the time of settlement is the time the settlement is accepted by the person receiving settlement.

3. Subsections (c) and (d) are special provisions for settlement by remittance drafts and authority to charge an account in the bank receiving settlement. The relationship between final settlement and final payment under Section 4-215 is addressed in subsection (b) of Section 4-215. With respect to settlement by cashier's checks or teller's checks, other than in response to over-the-counter presentment, the bank receiving settlement can keep the risk that the check will not be paid on the bank tendering the check in settlement by acting to initiate collection of the check within the midnight deadline of the bank receiving settlement. If the bank fails to initiate settlement before its midnight deadline, final settlement occurs at the midnight deadline, and the bank receiving settlement assumes the risk that the check will not be paid. If there is no agreement that permits the bank tendering settlement to tender a cashier's or teller's check, subsection (b) allows the bank receiving the check to reject it, and, if it does, no settlement occurs. However, if the bank accepts the check, settlement occurs and the time of final settlement is governed by subsection (c).

With respect to settlement by tender of authority to charge the account of the bank making settlement in the bank receiving settlement, subsection (d) provides that final settlement does not take place until the account charged has available funds to cover the amount of the item. If there is no agreement that permits the bank tendering settlement to tender an authority to charge an account as settlement, subsection (b) allows the bank receiving the tender to reject it. However, if the bank accepts the authority, settlement occurs and the time of final settlement is governed by subsection (d).

#### **Reason for 1990 Change [D.C. Law 10-249]**

New section. See the Official Comment. Former Section 4-211 applied only to settlements by remittance instruments and authorities to charge which could be received in settlement by a collecting bank without the collecting bank's being responsible if the remittance wasn't paid. The new section is much broader in stating general rules for all types of settlements with respect to the time settlement is made and the medium which the person receiving settlement must accept. Subsections (c) and (d) apply to the issues treated in former Section 4-211.

#### *Prior Codifications*

1981 Ed., § 28:4-213.

1973 Ed., § 28:4-211.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-214. RIGHT OF CHARGE-BACK OR REFUND; LIABILITY OF COLLECTING BANK; RETURN OF ITEM.**

(a) If a collecting bank has made provisional settlement with its customer for an item and fails by reason of dishonor, suspension of payments by a bank, or otherwise to receive settlement for the item which is or becomes final, the bank may revoke the settlement given by it, charge back the amount of any credit given for the item to its customer's account, or obtain refund from its customer, whether or not it is able to return the item, if by its midnight deadline or within a longer reasonable time after it learns the facts it returns the item or sends notification of the facts. If the return or notice is delayed beyond the bank's midnight deadline or a longer reasonable time after it learns the facts, the bank may revoke the settlement, charge back the credit, or obtain refund from its customer, but it is liable for any loss resulting from the delay. These rights to revoke, charge back, and obtain refund terminate if and when a settlement for the item received by the bank is or becomes final.

(b) A collecting bank returns an item when it is sent or delivered to the bank's customer or transferor or

pursuant to its instructions.

(c) A depository bank that is also the payor may charge back the amount of an item to its customer's account or obtain refund in accordance with the section governing return of an item received by a payor bank for credit on its books (section 28:4-301).

(d) The right to charge back is not affected by:

(1) Previous use of a credit given for the item; or

(2) Failure by any bank to exercise ordinary care with respect to the item, but a bank so failing remains liable.

(e) A failure to charge back or claim refund does not affect other rights of the bank against the customer or any other party.

(f) If credit is given in dollars as the equivalent of the value of an item payable in foreign money, the dollar amount of any charge-back or refund must be calculated on the basis of the bank-offered spot rate for the foreign money prevailing on the day when the person entitled to the charge-back or refund learns that it will not receive payment in ordinary course.

(Dec. 30, 1963, 77 Stat. 702, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Under current bank practice, in a major portion of cases banks make provisional settlement for items when they are first received and then await subsequent determination of whether the item will be finally paid. This is the principal characteristic of what are referred to in banking parlance as "cash items." Statistically, this practice of settling provisionally first and then awaiting final payment is justified because the vast majority of such cash items are finally paid, with the result that in this great preponderance of cases it becomes unnecessary for the banks making the provisional settlements to make any further entries. In due course the provisional settlements become final simply with the lapse of time. However, in those cases in which the item being collected is not finally paid or if for various reasons the bank making the provisional settlement does not itself receive final payment, provision is made in subsection (a) for the reversal of the provisional settlements, charge-back of provisional credits and the right to obtain refund.

2. Various causes of a bank's not receiving final payment, with the resulting right of charge-back or refund, are stated or suggested in subsection (a). These include dishonor of the original item; dishonor of a remittance instrument given for it; reversal of a provisional credit for the item; suspension of payments by another bank. The causes stated are illustrative; the right of charge-back or refund is stated to exist whether the failure to receive final payment in ordinary course arises through one of them "or otherwise."

3. The right of charge-back or refund exists if a collecting bank has made a provisional settlement for an item with its customer but terminates if and when a settlement received by the bank for the item is or becomes final. If the bank fails to receive such a final settlement the right of charge-back or refund must be exercised promptly after the bank learns the facts. The right exists (if so promptly exercised) whether or not the bank is able to return the item. The second sentence of subsection (a) adopts the view of *Appliance Buyers Credit Corp. v. Prospect National Bank*, 708 F.2d 290 (7th Cir.1983), that if the midnight deadline for returning an item or giving notice is not met, a collecting bank loses its rights only to the extent of damages for any loss resulting from the delay.

4. Subsection (b) states when an item is returned by a collecting bank. Regulation CC, Section 229.31 preempts this subsection with respect to checks by allowing direct return to the depository bank. Because a returned check may follow a different path than in forward collection, settlement given for the check is final and not provisional except as between the depository bank and its customer. Regulation CC Section 229.36(d). See also Regulations CC Sections 229.31(c) and 229.32(b). Thus owing to the federal preemption, this subsection applies only to noncheck items.

5. The rule of subsection (d) relating to charge-back (as distinguished from claim for refund) applies irrespective of the cause of the nonpayment, and of the person ultimately liable for nonpayment. Thus charge-back is permitted even if nonpayment results from the depository bank's own negligence. Any other rule would result in litigation based upon a claim for wrongful dishonor of other checks of the customer, with potential damages far in excess of the amount of the item. Any other rule would require a bank to determine difficult questions of fact. The customer's protection is found in the general obligation of good faith (Sections 1-203 and 4-103). If bad faith is established the customer's recovery "includes other damages, if any, suffered by the party as a proximate consequence" (Section 4-103(e); see also Section 4-402).

6. It is clear that the charge-back does not relieve the bank from any liability for failure to exercise ordinary care in handling the item. The measure of damages for such failure is stated in Section 4-103(e).

7. Subsection (f) states a rule fixing the time for determining the rate of exchange if there is a charge-back or refund of a credit given in dollars for an item payable in a foreign currency. Compare Section 3-107. Fixing such a rule is desirable to avoid disputes. If in any case the parties wish to fix a different time for determining the rate of exchange, they may do so by agreement.

## Reason for 1990 Change [D.C. Law 10-249]

Subsection (a) is amended by the addition of the second sentence which adopts the view of *Appliance Buyers Credit Corp. v. Prospect National Bank*, 708 F.2d 290 (7th Cir.1983), that if the midnight deadline for returning an item or giving notice is not met, a collecting bank loses its rights only to the extent of damages for any loss resulting from the delay. The cross references to former Sections 4-211 and 4-213 are deleted. The reason for the deletion is to remove any implication that final settlement is determined by only these provisions. See Reasons for 1990 Change for Section 4-201.

Former subsection (2) is replaced by subsection (b). Former subsection (2) broadly allowed for direct return of all types of unpaid items. The purpose of the amendment is to limit the right of direct return with respect to noncheck items. This purpose is accomplished by subsection (b) when read against the background of Regulation CC Section 229.31 which allows for the direct return of checks but does not apply to noncheck items. Since Regulation CC preempts subsection (b) with respect to checks, the result is that the limitation on direct return found in subsection (b) applies only to noncheck items.

Subsection (f) is amended to conform to the terminology ("bank-offered spot rate") used in Section 3-107.

The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

### *Prior Codifications*

1981 Ed., § 28:4-214.

1973 Ed., § 28:4-212.

### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-215. FINAL PAYMENT OF ITEM BY PAYOR BANK; WHEN PROVISIONAL DEBITS AND CREDITS BECOME FINAL; WHEN CERTAIN CREDITS BECOME AVAILABLE FOR WITHDRAWAL.**

(a) An item is finally paid by a payor bank when the bank has first done any of the following:

- (1) Paid the item in cash;
- (2) Settled for the item without having a right to revoke the settlement under statute, clearing-house rule, or agreement; or
- (3) Made a provisional settlement for the item and failed to revoke the settlement in the time and manner permitted by statute, clearing-house rule, or agreement.

(b) If provisional settlement for an item does not become final, the item is not finally paid.

(c) If provisional settlement for an item between the presenting and payor banks is made through a clearing house or by debits or credits in an account between them, then to the extent that provisional debits or credits for the item are entered in accounts between the presenting and payor banks or between the presenting and successive prior collecting banks seriatim, they become final upon final payment of the items by the payor bank.

(d) If a collecting bank receives a settlement for an item which is or becomes final, the bank is accountable to its customer for the amount of the item and any provisional credit given for the item in an account with its customer becomes final.

(e) Subject to (i) applicable law stating a time for availability of funds and (ii) any right of the bank to apply the credit to an obligation of the customer, credit given by a bank for an item in a customer's account becomes available for withdrawal as of right:

- (1) If the bank has received a provisional settlement for the item, when the settlement becomes final and the bank has had a reasonable time to receive return of the item and the item has not been received within that time; or
- (2) If the bank is both the depository bank and the payor bank, and the item is finally paid, at the opening of the bank's second banking day following receipt of the item.

(f) Subject to applicable law stating a time for availability of funds and any right of a bank to apply a deposit to an obligation of the depositor, a deposit of money becomes available for withdrawal as of right at the opening of the bank's next banking day after receipt of the deposit.

(Dec. 30, 1963, 77 Stat. 703, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

### *HISTORICAL AND STATUTORY NOTES*

### *UNIFORM COMMERCIAL CODE COMMENT*

1. By the definition and use of the term "settle" (Section 4-104(a)(11)) this Article recognizes that various debits or credits, remittances, settlements or payments given for an item may be either provisional or final, that settlements sometimes are provisional and sometimes are final and sometimes are provisional for awhile but later become final. Subsection (a) defines when settlement for an item constitutes final payment.

Final payment of an item is important for a number of reasons. It is one of several factors determining the relative priorities between items and notices, stop-payment orders, legal process and setoffs (Section 4-303). It is the "end of the line" in the collection process and the "turn around" point commencing the return flow of proceeds. It is the point at which many provisional settlements become final. See Section 4-215(c). Final payment of an item by the payor bank fixes preferential rights under Section 4-216.

2. If an item being collected moves through several states, e.g., is deposited for collection in California, moves through two or three California banks to the Federal Reserve Bank of San Francisco, to the Federal Reserve Bank of Boston, to a payor bank in Maine, the collection process involves the eastward journey of the item from California to Maine and the westward journey of the proceeds from Maine to California. Subsection (a) recognizes that final payment does not take place, in this hypothetical case, on the journey of the item eastward. It also adopts the view that neither does final payment occur on the journey westward because what in fact is journeying westward are *proceeds* of the item.

3. Traditionally and under various decisions payment in cash of an item by a payor bank has been considered final payment. Subsection (a)(1) recognizes and provides that payment of an item in cash by a payor bank is final payment.

4. Section 4-104(a)(11) defines "settle" as meaning "to pay in cash, by clearing-house settlement, in a charge or credit or by remittance, or otherwise as agreed. A settlement may be either provisional or final." Subsection (a)(2) of Section 4-215 provides that an item is finally paid by a payor bank when the bank has "settled for the item without having a right to revoke the settlement under statute, clearing-house rule or agreement." Former subsection (1)(b) is modified by subsection (a)(2) to make clear that a payor bank cannot make settlement provisional by unilaterally reserving a right to revoke the settlement. The right must come from a statute (e.g., Section 4-301), clearing-house rule or other agreement. Subsection (a)(2) provides in effect that if the payor bank finally settles for an item this constitutes final payment of the item. The subsection operates if nothing has occurred and no situation exists making the settlement provisional. If under statute, clearing-house rule or agreement, a right of revocation of the settlement exists, the settlement is provisional. Conversely, if there is an absence of a right to revoke under statute, clearing-house rule or agreement, the settlement is final and such final settlement constitutes final payment of the item.

A primary example of a statutory right on the part of the payor bank to revoke a settlement is the right to revoke conferred by Section 4-301. The underlying theory and reason for deferred posting statutes (Section 4-301) is to require a settlement on the date of receipt of an item but to keep that settlement provisional with the right to revoke prior to the midnight deadline. In any case in which Section 4-301 is applicable, any settlement by the payor bank is provisional solely by virtue of the statute, subsection (a)(2) of Section 4-215 does not operate, and such provisional settlement does not constitute final payment of the item. With respect to checks, Regulation CC Section 229.36(d) provides that settlement between banks for the forward collection of checks is final. The relationship of this provision to Article 4 is discussed in the Commentary to that section.

A second important example of a right to revoke a settlement is that arising under clearing-house rules. It is very common for clearing-house rules to provide that items exchanged and settled for in a clearing (e.g., before 10:00 a.m. on Monday) may be returned and the settlements revoked up to but not later than 2:00 p.m. on the same day (Monday) or under deferred posting at some hour on the next business day (e.g., 2:00 p.m. Tuesday). Under this type of rule the Monday morning settlement is provisional and being provisional does not constitute a final payment of the item.

An example of an agreement allowing the payor bank to revoke a settlement is a case in which the payor bank is also the depository bank and has signed a receipt or duplicate deposit ticket or has made an entry in a passbook acknowledging receipt, for credit to the account of A, of a check drawn on it by B. If the receipt, deposit ticket, passbook or other agreement with A is to the effect that any credit so entered is provisional and may be revoked pending the time required by the payor bank to process the item to determine if it is in good form and there are funds to cover it, the agreement keeps the receipt or credit provisional and avoids its being either final settlement or final payment.

The most important application of subsection (a)(2) is that in which presentment of an item has been made over the counter for immediate payment. In this case Section 4-301(a) does not apply to make the settlement provisional, and final payment has occurred unless a rule or agreement provides otherwise.

5. Former Section 4-213(1)(c) provided that final payment occurred when the payor bank completed the "process of posting." The term was defined in former Section 4-109. In the present Article, Section 4-109 has been deleted and the process-of-posting test has been abandoned in Section 4-215(a) for determining when final payment is made. Difficulties in determining when the events described in former Section 4-109 take place make the process-of-posting test unsuitable for a system of automated check collection or electronic presentment.

6. The last sentence of former Section 4-213(1) is deleted as an unnecessary source of confusion. Initially the view that payor bank may be accountable for, that is, liable for the amount of, an item that it has already paid

seems incongruous. This is particularly true in the light of the language formerly found in Section 4-302 stating that the payor bank can defend against liability for accountability by showing that it has already settled for the item. But, at least with respect to former Section 4-213(1)(c), such a provision was needed because under the process-of-posting test a payor bank may have paid an item without settling for it. Now that Article 4 has abandoned the process-of-posting test, the sentence is no longer needed. If the payor bank has neither paid the item nor returned it within its midnight deadline, the payor bank is accountable under Section 4-302.

7. Subsection (a)(3) covers the situation in which the payor bank makes a provisional settlement for an item, and this settlement becomes final at a later time by reason of the failure of the payor bank to revoke it in the time and manner permitted by statute, clearing-house rule or agreement. An example of this type of situation is the clearing-house settlement referred to in Comment 4. In the illustration there given if the time limit for the return of items received in the Monday morning clearing is 2:00 p.m. on Tuesday and the provisional settlement has not been revoked at that time in a manner permitted by the clearing-house rules, the provisional settlement made on Monday morning becomes final at 2:00 p.m. on Tuesday. Subsection (a)(3) provides specifically that in this situation the item is finally paid at 2:00 p.m. Tuesday. If on the other hand a payor bank receives an item in the mail on Monday and makes some provisional settlement for the item on Monday, it has until midnight on Tuesday to return the item or give notice and revoke any settlement under Section 4-301. In this situation subsection (a)(3) of Section 4-215 provides that if the provisional settlement made on Monday is not revoked before midnight on Tuesday as permitted by Section 4-301, the item is finally paid at midnight on Tuesday. With respect to checks, Regulation CC Section 229.30(c) allows an extension of the midnight deadline under certain circumstances. If a bank does not expeditiously return a check liability may accrue under Regulation CC Section 229.38. For the relationship of that liability to responsibility under this Article, see Regulation CC Sections 229.30 and 229.38.

8. Subsection (b) relates final settlement to final payment under Section 4-215. For example, if a payor bank makes provisional settlement for an item by sending a cashier's or teller's check and that settlement fails to become final under Section 4-213(c), subsection (b) provides that final payment has not occurred. If the item is not paid, the drawer remains liable, and under Section 4-302(a) the payor bank is accountable unless it has returned the item before its midnight deadline. In this regard, subsection (b) is an exception to subsection (a)(3). Even if the payor bank has not returned an item by its midnight deadline there is still no final payment if provisional settlement had been made and settlement failed to become final. However, if presentment of the item was over the counter for immediate payment, final payment has occurred under Section 4-215(a)(2). Subsection (b) does not apply because the settlement was not provisional. Section 4-301(a). In this case the presenting person, often the payee of the item, has the right to demand cash or the cash equivalent of federal reserve credit. If the presenting person accepts another medium of settlement such as a cashier's or teller's check, the presenting person takes the risk that the payor bank may fail to pay a cashier's check because of insolvency or that the drawee of a teller's check may dishonor it.

9. Subsection (c) states the country-wide usage that when the item is finally paid by the payor bank under subsection (a) this final payment automatically without further action "firms up" other provisional settlements made for it. However, the subsection makes clear that this "firming up" occurs only if the settlement between the presenting and payor banks was made either through a clearing house or by debits and credits in accounts between them. It does not take place if the payor bank remits for the item by sending some form of remittance instrument. Further, the "firming up" continues only to the extent that provisional debits and credits are entered seriatim in accounts between banks which are successive to the presenting bank. The automatic "firming up" is broken at any time that any collecting bank remits for the item by sending a remittance draft, because final payment to the remittee then usually depends upon final payment of the remittance draft.

10. Subsection (d) states the general rule that if a collecting bank receives settlement for an item which is or becomes final, the bank is accountable to its customer for the amount of the item. One means of accounting is to remit to its customer the amount it has received on the item. If previously it gave to its customer a provisional credit for the item in an account its receipt of final settlement for the item "firms up" this provisional credit and makes it final. When this credit given by it so becomes final, in the usual case its agency status terminates and it becomes a debtor to its customer for the amount of the item. See Section 4-201(a). If the accounting is by a remittance instrument or authorization to charge further time will usually be required to complete its accounting (Section 4-213).

11. Subsection (e) states when certain credits given by a bank to its customer become available for withdrawal as of right. Subsection (e)(1) deals with the situation in which a bank has given a credit (usually provisional) for an item to its customer and in turn has received a provisional settlement for the item from an intermediary or payor bank to which it has forwarded the item. In this situation before the provisional credit entered by the collecting bank in the account of its customer becomes available for withdrawal as of right, it is not only necessary that the provisional settlement received by the bank for the item becomes final but also that the collecting bank has a reasonable time to receive return of the item and the item has not been received within that time. How much time is "reasonable" for these purposes will of course depend on the distance the item has to travel and the number of banks through which it must pass (having in mind not only travel time by regular lines of transmission but also the successive midnight deadlines of the several banks) and other pertinent facts. Also, if the provisional settlement received is some form of a remittance instrument or authorization to charge, the "reasonable" time depends on the identity and location of the payor of the remittance instrument, the means for clearing such instrument, and other pertinent facts. With respect to checks Regulation CC Sections 229.10-229.13 or similar applicable state law (Section 229.20) control. This



is also time for the situation described in Comment 12.

12. Subsection (e)(2) deals with the situation of a bank that is both a depositary bank and a payor bank. The subsection recognizes that if A and B are both customers of a depositary-payor bank and A deposits B's check on the depositary-payor in A's account on Monday, time must be allowed to permit the check under the deferred posting rules of Section 4-301 to reach the bookkeeper for B's account at some time on Tuesday, and, if there are insufficient funds in B's account, to reverse or charge back the provisional credit in A's account. Consequently this provisional credit in A's account does not become available for withdrawal as of right until the opening of business on Wednesday. If it is determined on Tuesday that there are insufficient funds in B's account to pay the check, the credit to A's account can be reversed on Tuesday. On the other hand if the item is in fact paid on Tuesday, the rule of subsection (e)(2) is desirable to avoid uncertainty and possible disputes between the bank and its customer as to exactly what hour within the day the credit is available.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (a)(2) is amended to provide that a payor bank cannot make settlement provisional by unilaterally reserving a right to revoke the settlement. The right to revoke must come from a statute (e.g., Section 4-301), clearing-house rule or other agreement. Former subsection (1)(c) is deleted for the reason stated in the Reason for 1990 Change for former Section 4-109. Subsection (a)(3) is amended to remove the final sentence as an unnecessary source of confusion. Initially the view that payor bank may be accountable for, that is, liable for the amount of, an item that it has already paid seems incongruous. This is particularly true in the light of the language formerly found in former Section 4-302 stating that the payor bank can defend against liability for accountability by showing that it has already settled for the item. But, at least with respect to former Section 4-213(1)(c), such a provision was needed because under the process-of-posting test a payor bank may have paid an item without settling for it. Now that Article 4 has abandoned the process-of-posting test, the sentence is no longer needed. If the payor bank has neither paid the item nor returned it within its midnight deadline, the payor bank is accountable under Section 4-302.

Subsection (b) was added to clarify the relationship of final settlement to final payment under Section 4-215. For example, if a payor bank makes provisional settlement for an item by sending a cashier's or teller's check and that settlement fails to become final under Section 4-213(c), subsection (b) provides that final payment has not occurred. Under Section 4-302(a) the payor bank is accountable unless it has returned the item before its midnight deadline. In this regard, subsection (b) is an exception to subsection (a)(3). Even if the payor bank has not returned an item by its midnight deadline there is still no final payment if provisional settlement had been made and settlement failed to become final. However, if presentment of the item was over the counter for immediate payment, final payment has occurred under Section 4-215(a)(2). Subsection (b) does not apply because the settlement was not provisional. Section 4-301(a). In this case the presenting person, often the payee of the item, has the right to demand cash or the cash equivalent of federal reserve credit. If the presenting person accepts another medium of settlement such as a cashier's or teller's check, the presenting person takes the risk that the payor bank may fail to pay a cashier's check because of insolvency or that the drawee of a teller's check may dishonor it.

Subsection (d) is amended to delete the cross references to former Sections 4-211 and 4-213. The reason for the deletion is to remove any implication that final settlement is determined by only those provisions. See Reasons for 1990 Change for Section 4-201.

The preamble to subsection (e), as well as subsection (f), is amended to recognize that Regulation CC Sections 229.10-229.13 and the laws of several states (Regulation CC Section 229.20) prescribe times for availability of a depositor's funds. Subsections (e) and (f) are expressly made subject to these funds availability laws. Paragraph (1) of subsection (e) is amended to delete the test that a customer may withdraw funds after the bank has had a reasonable time to "learn that the settlement is final." The depositary bank may never affirmatively learn that a settlement is final. The substituted test is that the bank may delay making funds available to a customer until it has had a reasonable time to receive return of the item and the item has not been returned. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-215.

1973 Ed., § 28:4-213.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-216. INSOLVENCY AND PREFERENCE.**

(a) If an item is in or comes into the possession of a payor or collecting bank that suspends payment and the item has not been finally paid, the item must be returned by the receiver, trustee, or agent in charge of the closed bank to the presenting bank or the closed bank's customer.

(b) If a payor bank finally pays an item and suspends payments without making a settlement for the item with its customer or the presenting bank which settlement is or becomes final, the owner of the item has a preferred claim against the payor bank.

(c) If a payor bank gives or a collecting bank gives or receives a provisional settlement for an item and thereafter suspends payments, the suspension does not prevent or interfere with the settlement's becoming final if the finality occurs automatically upon the lapse of certain time or the happening of certain events.

(d) If a collecting bank receives from subsequent parties settlement for an item, which settlement is or becomes final and the bank suspends payments without making a settlement for the item with its customer which settlement is or becomes final, the owner of the item has a preferred claim against the collecting bank.

(Dec. 30, 1963, 77 Stat. 703, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. The underlying purpose of the provisions of this section is not to confer upon banks, holders of items or anyone else preferential positions in the event of bank failures over general depositors or any other creditors of the failed banks. The purpose is to fix as definitely as possible the cut-off point of time for the completion or cessation of the collection process in the case of items that happen to be in the process at the time a particular bank suspends payments. It must be remembered that in bank collections as a whole and in the handling of items by an individual bank, items go through a whole series of processes. It must also be remembered that at any particular point of time a particular bank (at least one of any size) is functioning as a depository bank for some items, as an intermediary bank for others, as a presenting bank for still others and as a payor bank for still others, and that when it suspends payments it will have close to its normal load of items working through its various processes. For the convenience of receivers, owners of items, banks, and in fact substantially everyone concerned, it is recognized that at the particular moment of time that a bank suspends payment, a certain portion of the items being handled by it have progressed far enough in the bank collection process that it is preferable to permit them to continue the remaining distance, rather than to send them back and reverse the many entries that have been made or the steps that have been taken with respect to them. Therefore, having this background and these purposes in mind, the section states what items must be turned backward at the moment suspension intervenes and what items have progressed far enough that the collection process with respect to them continues, with the resulting necessary statement of rights of various parties flowing from this prescription of the cut-off time.

2. The rules stated are similar to those stated in the American Bankers Association Bank Collection Code, but with the abandonment of any theory of trust. On the other hand, some law previous to this Act may be relevant. See Note, Uniform Commercial Code: Stopping Payment of an Item Deposited with an Insolvent Depository Bank, 40 Okla.L.Rev. 689 (1987). Although for practical purposes Federal Deposit Insurance affects materially the result of bank failures on holders of items and banks, no attempt is made to vary the rules of the section by reason of such insurance.

3. It is recognized that in view of *Jennings v. United States Fidelity & Guaranty Co.*, 294 U.S. 216, 55 S.Ct. 394, 79 L.Ed. 869, 99 A.L.R. 1248 (1935), amendment of the National Bank Act would be necessary to have this section apply to national banks. But there is no reason why it should not apply to others. See Section 1-108.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (c) is amended to delete the cross references to former Sections 4-211 and 4-213. The reason for the deletion is to remove any implication that final settlement is determined by only those provisions. See Reasons for 1990 Change for Section 4-201. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-216.

1973 Ed., § 28:4-214.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **PART 3. COLLECTION OF ITEMS: PAYOR BANKS.**

### **§ 28:4-301. DEFERRED POSTING; RECOVERY OF PAYMENT BY RETURN OF ITEMS; TIME OF DISHONOR; RETURN OF ITEMS BY PAYOR BANK.**

(a) If a payor bank settles for a demand item other than a documentary draft presented otherwise than for immediate payment over the counter before midnight of the banking day of receipt, the payor bank may revoke the settlement and recover the settlement if, before it has made final payment and before its midnight deadline, it

(1) Returns the item; or

(2) Sends written notice of dishonor or nonpayment if the item is unavailable for return.

(b) If a demand item is received by a payor bank for credit on its books, it may return the item or send notice of dishonor and may revoke any credit given or recover the amount thereof withdrawn by its customer, if it acts within the time limit and in the manner specified in subsection (a) of this section.

(c) Unless previous notice of dishonor has been sent, an item is dishonored at the time when, for purposes of dishonor, it is returned or notice sent in accordance with this section.

(d) An item is returned:

(1) As to an item presented through a clearing house, when it is delivered to the presenting or last collecting bank or to the clearing house or is sent or delivered in accordance with clearing-house rules; or

(2) In all other cases, when it is sent or delivered to the bank's customer or transferor or pursuant to instructions.

(Dec. 30, 1963, 77 Stat. 704, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. The term "deferred posting" appears in the caption of Section 4-301. This refers to the practice permitted by statute in most of the states before the UCC under which a payor bank receives items on one day but does not post the items to the customer's account until the next day. Items dishonored were then returned after the posting on the day after receipt. Under Section 4-301 the concept of "deferred posting" merely allows a payor bank that has settled for an item on the day of receipt to return a dishonored item on the next day before its midnight deadline, without regard to when the item was actually posted. With respect to checks Regulation CC Section 229.30(c) extends the midnight deadline under the UCC under certain circumstances. See the Commentary to Regulation CC Section 229.38(d) on the relationship between the UCC and Regulation CC on settlement.

2. The function of this section is to provide the circumstances under which a payor bank that has made timely settlement for an item may return the item and revoke the settlement so that it may recover any settlement made. These circumstances are: (1) the item must be a demand item other than a documentary draft; (2) the item must be presented otherwise than for immediate payment over the counter; and (3) the payor bank must return the item (or give notice if the item is unavailable for return) before its midnight deadline and before it has paid the item. With respect to checks, see Regulation CC Section 229.31(f) on notice in lieu of return and Regulation CC Section 229.33 as to the different requirement of notice of nonpayment. An instance of when an item may be unavailable for return arises under a collecting bank check retention plan under which presentment is made by a presentment notice and the item is retained by the collecting bank. Section 4-215(a)(2) provides that final payment occurs if the payor bank has settled for an item without a right to revoke the settlement under statute, clearing-house rule or agreement. In any case in which Section 4-301(a) is applicable, the payor bank has a right to revoke the settlement by statute; therefore, Section 4-215(a)(2) is inoperable, and the settlement is provisional. Hence, if the settlement is not over the counter and the payor bank settles in a manner that does not constitute final payment, the payor bank can revoke the settlement by returning the item before its midnight deadline.

3. The relationship of Section 4-301(a) to final settlement and final payment under Section 4-215 is illustrated by the following case. Depository Bank sends by mail an item to Payor Bank with instructions to settle by remitting a teller's check drawn on a bank in the city where Depository Bank is located. Payor Bank sends the teller's check on the day the item was presented. Having made timely settlement, under the deferred posting provisions of Section 4-301(a), Payor Bank may revoke that settlement by returning the item before its midnight deadline. If it fails to return the item before its midnight deadline, it has finally paid the item if the bank on which the teller's check was drawn honors the check. But if the teller's check is dishonored there has been no final settlement under Section 4-213(c) and no final payment under Section 4-215(b). Since the Payor Bank has neither paid the item nor made timely return, it is accountable for the item under Section 4-302(a).

4. The time limits for action imposed by subsection (a) are adopted by subsection (b) for cases in which the payor bank is also the depository bank, but in this case the requirement of a settlement on the day of receipt is omitted.

5. Subsection (c) fixes a base point from which to measure the time within which notice of dishonor must be given. See Section 3-503.

6. Subsection (d) leaves banks free to agree upon the manner of returning items but establishes a precise time when an item is "returned." For definition of "sent" as used in paragraphs (1) and (2) see Section 1-

201(38). Obviously the subsection assumes that the item has not been "finally paid" under Section 4-215(a). If it has been, this provision has no operation.

7. The fact that an item has been paid under proposed Section 4-215 does not preclude the payor bank from asserting rights of restitution or revocation under Section 3-418. *National Savings and Trust Co. v. Park Corp.*, 722 F.2d 1303 (6th Cir. 1983), cert. denied, 466 U.S. 939 (1984), is the correct interpretation of the present law on this issue.

#### **Reason for 1990 Change [D.C. Law 10-249]**

The term "authorized settlement" is deleted in subsection (a) because Section 4-213 makes the term superfluous. That section prescribes the medium of settlement that a bank must accept. References to settlement throughout Article 4 assume that settlement was made by tender of the proper medium; hence, the word "settles" in subsection (a) means an authorized settlement. Substitution of "settlement" for "payment" in subsection (a) is consistent with the usage throughout Article 4 in distinguishing the act of settlement from the issue of whether the settlement constitutes final payment. The cross reference to former Section 4-213 is deleted. The reason for the deletion is to remove any implication that final settlement is determined only by that provision. See Reason for 1990 Change for Section 4-201. The reference to protest is deleted in paragraph (2) of subsection (a) because Article 4 no longer deals with protest. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-301.

1973 Ed., § 28:4-301.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-302. PAYOR BANK'S RESPONSIBILITY FOR LATE RETURN OF ITEM.**

(a) If an item is presented to and received by a payor bank, the bank is accountable for the amount of:

(1) A demand item, other than a documentary draft, whether properly payable or not, if the bank, in any case in which it is not also the depository bank, retains the item beyond midnight of the banking day of receipt without settling for it or, whether or not it is also the depository bank, does not pay or return the item or send notice of dishonor until after its midnight deadline; or

(2) Any other properly payable item unless, within the time allowed for acceptance or payment of that item, the bank either accepts or pays the item or returns it and accompanying documents.

(b) The liability of a payor bank to pay an item pursuant to subsection (a) of this section is subject to defenses based on breach of a presentment warranty (section 28:4-208) or proof that the person seeking enforcement of the liability presented or transferred the item for the purpose of defrauding the payor bank.

(Dec. 30, 1963, 77 Stat. 704, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Subsection (a)(1) continues the former law distinguishing between cases in which the payor bank is not also the depository bank and those in which the payor bank is also the depository bank ("on us" items). For "on us" items the payor bank is accountable if it retains the item beyond its midnight deadline without settling for it. If the payor bank is not the depository bank it is accountable if it retains the item beyond midnight of the banking day of receipt without settling for it. It may avoid accountability either by settling for the item on the day of receipt and returning the item before its midnight deadline under Section 4-301 or by returning the item on the day of receipt. This rule is consistent with the deferred posting practice authorized by Section 4-301 which allows the payor bank to make provisional settlement for an item on the day of receipt and to revoke that settlement by returning the item on the next day. With respect to checks, Regulation CC Section 229.36(d) provides that settlements between banks for forward collection of checks are final when made. See the Commentary on that provision for its effect on the UCC.

2. If the settlement given by the payor bank does not become final, there has been no payment under Section 4-215(b), and the payor bank giving the failed settlement is accountable under subsection (a)(1) of Section 4-302. For instance, the payor bank makes provisional settlement by sending a teller's check that is dishonored. In such a case settlement is not final under Section 4-213(c) and no payment occurs under Section 4-215(b). Payor bank is accountable on the item. The general principle is that unless settlement provides the presenting bank with usable funds, settlement has failed and the payor bank is accountable for the amount of the item.

3. Subsection (b) is an elaboration of the deleted introductory language of former Section 4-302: "In the absence of a valid defense such as breach of a presentment warranty (subsection (1) of Section 4-207), settlement effected or the like...." A payor bank can defend an action against it based on accountability by

showing that the item contained a forged indorsement or a fraudulent alteration. Subsection (b) drops the ambiguous "or the like" language and provides that the payor bank may also raise the defense of fraud. Decisions that hold an accountable bank's liability to be "absolute" are rejected. A payor bank that makes a late return of an item should not be liable to a defrauder operating a check kiting scheme. In *Bank of Leumi Trust Co. v. Bally's Park Place Inc.*, 528 F.Supp. 349 (S.D.N.Y. 1981), and *American National Bank v. Foodbasket*, 497 P.2d 546 (Wyo. 1972), banks that were accountable under Section 4-302 for missing their midnight deadline were successful in defending against parties who initiated collection knowing that the check would not be paid. The "settlement effected" language is deleted as unnecessary. If a payor bank is accountable for an item it is liable to pay it. If it has made final payment for an item, it is no longer accountable for the item.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (b) is added to clarify the deleted introductory language of former Section 4-302: "In the absence of a valid defense such as breach of a presentment warranty (subsection (1) of Section 4-207), settlement effected or the like ...." A payor bank can defend an action against it based on accountability by showing that the item contained a forged indorsement or a fraudulent alteration. Section 4-208. Proposed subsection (b) drops the ambiguous "or the like" language and provides that the payor bank may also raise the defense of fraud. Decisions that hold an accountable bank's liability to be "absolute" are rejected. A payor bank that makes a late return of an item should not be liable to a defrauder operating a check kiting scheme. In *Bank Leumi Trust Co. v. Bailey's Park Place Inc.*, 528 F.Supp. 349 (S.D.N.Y.1981), and *American National Bank v. Foodbasket*, 497 P.2d 546 (Wyo.1972), banks that were accountable under Section 4-302 for missing their midnight deadline were successful in defending against parties who initiated collection knowing that the check would not be paid. The "settlement effected" language is deleted as unnecessary. If a payor bank is accountable for an item it is liable to pay it. If it has made final payment for an item, it is no longer accountable for the item. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-302.

1973 Ed., § 28:4-302.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-303. WHEN ITEMS SUBJECT TO NOTICE, STOP-PAYMENT ORDER, LEGAL PROCESS, OR SETOFF; ORDER IN WHICH ITEMS MAY BE CHARGED OR CERTIFIED.**

(a) Any knowledge, notice, or stop-payment order received by, legal process served upon, or setoff exercised by a payor bank comes too late to terminate, suspend, or modify the bank's right or duty to pay an item or to charge its customer's account for the item if the knowledge, notice, stop-payment order, or legal process is received or served and a reasonable time for the bank to act thereon expires or the setoff is exercised after the earliest of the following:

- (1) The bank accepts or certifies the item;
- (2) The bank pays the item in cash;
- (3) The bank settles for the item without having a right to revoke the settlement under statute, clearing-house rule, or agreement;
- (4) The bank becomes accountable for the amount of the item under section 28:4-302 dealing with the payor bank's responsibility for late return of items; or
- (5) With respect to checks, a cutoff hour no earlier than one hour after the opening of the next banking day after the banking day on which the bank received the check and no later than the close of that next banking day or, if no cutoff hour is fixed, the close of the next banking day after the banking day on which the bank received the check.

(b) Subject to subsection (a) of this section, items may be accepted, paid, certified, or charged to the indicated account of its customer in any order.

(Dec. 30, 1963, 77 Stat. 705, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. While a payor bank is processing an item presented for payment, it may receive knowledge or a legal notice affecting the item, such as knowledge or a notice that the drawer has filed a petition in bankruptcy or made an assignment for the benefit of creditors; may receive an order of the drawer stopping payment on the

item; may have served on it an attachment of the account of the drawer; or the bank itself may exercise a right of setoff against the drawer's account. Each of these events affects the account of the drawer and may eliminate or freeze all or part of whatever balance is available to pay the item. Subsection (a) states the rule for determining the relative priorities between these various legal events and the item.

2. The rule is that if any one of several things has been done to the item or if it has reached any one of several stages in its processing at the time the knowledge, notice, stop-payment order or legal process is received or served and a reasonable time for the bank to act thereon expires or the setoff is exercised, the knowledge, notice, stop-payment order, legal process or setoff comes too late, the item has priority and a charge to the customer's account may be made and is effective. With respect to the effect of the customer's bankruptcy, the bank's rights are governed by Bankruptcy Code Section 542(c) which codifies the result of *Bank of Marin v. England*, 385 U.S. 99 (1966). Section 4-405 applies to the death or incompetence of the customer.

3. Once a payor bank has accepted or certified an item or has paid the item in cash, the event has occurred that determines priorities between the item and the various legal events usually described as the "four legals." Paragraphs (1) and (2) of subsection (a) so provide. If a payor bank settles for an item presented over the counter for immediate payment by a cashier's check or teller's check which the presenting person agrees to accept, paragraph (3) of subsection (a) would control and the event determining priority has occurred. Because presentment was over the counter, Section 4-301(a) does not apply to give the payor bank the statutory right to revoke the settlement. Thus the requirements of paragraph (3) have been met unless a clearing-house rule or agreement of the parties provides otherwise.

4. In the usual case settlement for checks is by entries in bank accounts. Since the process-of-posting test has been abandoned as inappropriate for automated check collection, the determining event for priorities is a given hour on the day after the item is received. (Paragraph (5) of subsection (a).) The hour may be fixed by the bank no earlier than one hour after the opening on the next banking day after the bank received the check and no later than the close of that banking day. If an item is received after the payor bank's regular Section 4-108 cutoff hour, it is treated as received the next banking day. If a bank receives an item after its regular cutoff hour on Monday and an attachment is levied at noon on Tuesday, the attachment is prior to the item if the bank had not before that hour taken the action described in paragraphs (1), (2), and (3) of subsection (a). The Commentary to Regulation CC Section 229.36(d) explains that even though settlement by a paying bank for a check is final for Regulation CC purposes, the paying bank's right to return the check before its midnight deadline under the UCC is not affected.

5. Another event conferring priority for an item and a charge to the customer's account based upon the item is stated by the language "become accountable for the amount of the item under Section 4-302 dealing with the payor bank's responsibility for late return of items." Expiration of the deadline under Section 4-302 with resulting accountability by the payor bank for the amount of the item, establishes priority of the item over notices, stop-payment orders, legal process or setoff.

6. In the case of knowledge, notice, stop-payment orders and legal process the effective time for determining whether they were received too late to affect the payment of an item and a charge to the customer's account by reason of such payment, is receipt plus a reasonable time for the bank to act on any of these communications. Usually a relatively short time is required to communicate to the accounting department advice of one of these events but certainly some time is necessary. Compare Sections 1-201(27) and 4-403. In the case of setoff the effective time is when the setoff is actually made.

7. As between one item and another no priority rule is stated. This is justified because of the impossibility of stating a rule that would be fair in all cases, having in mind the almost infinite number of combinations of large and small checks in relation to the available balance on hand in the drawer's account; the possible methods of receipt; and other variables. Further, the drawer has drawn all the checks, the drawer should have funds available to meet all of them and has no basis for urging one should be paid before another; and the holders have no direct right against the payor bank in any event, unless of course, the bank has accepted, certified or finally paid a particular item, or has become liable for it under Section 4-302. Under subsection (b) the bank has the right to pay items for which it is itself liable ahead of those for which it is not.

#### **Reason for 1990 Change [D.C. Law 10-249]**

The preamble of subsection (a) is restated in order to improve comprehension. Paragraphs (1)-(4) of subsection (a) are restated to accommodate the addition of paragraph (5) which is stated in terms of the reaching of a cutoff hour rather than the doing of an act. Subsection (a)(3) is amended to conform to Section 4-215(a)(2) which provides that a payor bank cannot make settlement provisional by unilaterally reserving a right to revoke the settlement. The right to revoke must come from a statute (e.g. Section 4-301), a clearing-house rule or other agreement. Former subsection (1)(d) is deleted for the reason stated in the Reason for 1990 Change for former Section 4-109. The reference to former Section 4-213 is deleted from subsection (a)(4) because the reference to accountability in former Section 4-213 is deleted from what is now Section 4-215.

Subsection (a)(5) is added to allow payor banks, under time pressure to return checks to meet Regulation CC deadlines, to fix a cutoff hour earlier than the close of the next banking day after the banking day on which the checks are received. Banks must have time after receiving an attachment or effecting a setoff to return a check if the attachment or setoff renders the customer's account insufficient to pay the check. Since banks are now returning checks earlier during the next banking day after the banking day of receipt owing to Regulation

CC, they need a cutoff hour earlier than the close of the banking day after that of receipt because they may be returning their checks before the close of that banking day.

Subsection (b) is amended to delete "convenient to the bank" as being superfluous. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

*Prior Codifications*

1981 Ed., § 28:4-303.

1973 Ed., § 28:4-303.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **PART 4. RELATIONSHIP BETWEEN PAYOR BANK AND ITS CUSTOMERS.**

### **§ 28:4-401. WHEN BANK MAY CHARGE CUSTOMER'S ACCOUNT.**

(a) A bank may charge against the account of a customer an item that is properly payable from that account even though the charge creates an overdraft. An item is properly payable if it is authorized by the customer and is in accordance with any agreement between the customer and bank.

(b) A customer is not liable for the amount of an overdraft if the customer neither signed the item nor benefited from the proceeds of the item.

(c) A bank may charge against the account of a customer a check that is otherwise properly payable from the account, even though payment was made before the date of the check, unless the customer has given notice to the bank of the postdating describing the check with reasonable certainty. The notice is effective for the period stated in section 28:4-403(b) for stop-payment orders, and must be received at such time and in such manner as to afford the bank a reasonable opportunity to act on it before the bank takes any action with respect to the check described in section 28:4-303. If a bank charges against the account of a customer a check before the date stated in the notice of postdating, the bank is liable for damages for the loss resulting from its act. The loss may include damages for dishonor of subsequent items under section 28:4-402.

(d) A bank that in good faith makes payment to a holder may charge the indicated account of its customer according to:

(1) The original terms of the altered item; or

(2) The terms of the completed item, even though the bank knows the item has been completed unless the bank has notice that the completion was improper.

(Dec. 30, 1963, 77 Stat. 705, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. An item is properly payable from a customer's account if the customer has authorized the payment and the payment does not violate any agreement that may exist between the bank and its customer. For an example of a payment held to violate an agreement with a customer, see *Torrance National Bank v. Enesco Federal Credit Union*, 285 P.2d 737 (Cal.App.1955). An item drawn for more than the amount of a customer's account may be properly payable. Thus under subsection (a) a bank may charge the customer's account for an item even though payment results in an overdraft. An item containing a forged drawer's signature or forged indorsement is not properly payable. Concern has arisen whether a bank may require a customer to execute a stop-payment order when the customer notifies the bank of the loss of an undorsed or specially indorsed check. Since such a check cannot be properly payable from the customer's account, it is inappropriate for a bank to require stop-payment order in such a case.

2. Subsection (b) adopts the view of case authority holding that if there is more than one customer who can draw on an account, the nonsigning customer is not liable for an overdraft unless that person benefits from the proceeds of the item.

3. Subsection (c) is added because the automated check collection system cannot accommodate postdated checks. A check is usually paid upon presentment without respect to the date of the check. Under the former law, if a payor bank paid a postdated check before its stated date, it could not charge the customer's account because the check was not "properly payable." Hence, the bank might have been liable for wrongfully dishonoring subsequent checks of the drawer that would have been paid had the postdated check not been prematurely paid. Under subsection (c) a customer wishing to postdate a check must notify the payor bank of its postdating in time to allow the bank to act on the customer's notice before the bank has to commit itself to

pay the check. If the bank fails to act on the customer's timely notice, it may be liable for damages for the resulting loss which may include damages for dishonor of subsequent items. This Act does not regulate fees that banks charge their customers for a notice of postdating or other services covered by the Act, but under principles of law such as unconscionability or good faith and fair dealing, courts have reviewed fees and the bank's exercise of a discretion to set fees. *Perdue v. Crocker National Bank*, 38 Cal.3d 913 (1985) (unconscionability); *Best v. United Bank of Oregon*, 739 P.2d 554, 562-566 (1987) (good faith and fair dealing). In addition, Section 1-203 provides that every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.

4. Section 3-407(c) states that a payor bank or drawee which pays a fraudulently altered instrument in good faith and without notice of the alteration may enforce rights with respect to the instrument according to its original terms or, in the case of an incomplete instrument altered by unauthorized completion, according to its terms as completed. Section 4- 401(d) follows the rule stated in Section 3-407(c) by applying it to an altered item and allows the bank to enforce rights with respect to the altered item by charging the customer's account.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (a) is amended by the addition of the second sentence which provides a more general definition of "properly payable" than the narrow definition that was contained in former Section 4-104(1)(i). An item is properly payable from a customer's account if the customer has authorized the payment and the payment does not violate the customer-bank agreement concerning the account. An item drawn for more than the balance of the customer's account may be properly payable.

Subsection (b) is added to adopt the view of case authority holding that if there is more than one customer who can draw on an account, the nonsigning customer is not liable for an overdraft unless that person benefits from the proceeds of the item.

Subsection (c) is added because the automated check collection system cannot accommodate postdated checks. A check is usually paid upon presentment without respect to the date of the check. Under the former law, if a payor bank paid a postdated check before its stated date, it could not charge the customer's account because the check was not "properly payable." Hence, the bank might have been liable for wrongfully dishonoring subsequent checks of the drawer that would have been paid had the postdated check not been prematurely paid. Under subsection (c) a customer wishing to postdate a check must notify the payor bank of its postdating in time to allow the bank to act on the customer's notice before the bank has to commit itself to pay the check. If the bank fails to act on the customer's timely notice, it may be liable for damages for the resulting loss which may include damages for dishonor of subsequent items.

The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-401.

1973 Ed., § 28:4-401.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-402. BANK'S LIABILITY TO CUSTOMER FOR WRONGFUL DISHONOR; TIME OF DETERMINING INSUFFICIENCY OF ACCOUNT.**

(a) Except as otherwise provided in this article, a payor bank wrongfully dishonors an item if it dishonors an item that is properly payable, but a bank may dishonor an item that would create an overdraft unless it has agreed to pay the overdraft.

(b) A payor bank is liable to its customer for damages proximately caused by the wrongful dishonor of an item. Liability is limited to actual damages proved and may include damages for an arrest or prosecution of the customer or other consequential damages. Whether any consequential damages are proximately caused by the wrongful dishonor is a question of fact to be determined in each case.

(c) A payor bank's determination of the customer's account balance on which a decision to dishonor for insufficiency of available funds is based may be made at any time between the time the item is received by the payor bank and the time that the payor bank returns the item or gives notice in lieu of return, and no more than one determination need be made. If, at the election of the payor bank, a subsequent balance determination is made for the purpose of reevaluating the bank's decision to dishonor the item, the account balance at that time is determinative of whether a dishonor for insufficiency of available funds is wrongful.

(Dec. 30, 1963, 77 Stat. 705, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)



1. Subsection (a) states positively what has been assumed under the original Article: that if a bank fails to honor a properly payable item it may be liable to its customer for wrongful dishonor. Under subsection (b) the payor bank's wrongful dishonor of an item gives rise to a statutory cause of action. Damages may include consequential damages. Confusion has resulted from the attempts of courts to reconcile the first and second sentences of former Section 4-402. The second sentence implied that the bank was liable for some form of damages other than those proximately caused by the dishonor if the dishonor was other than by mistake. But nothing in the section described what these noncompensatory damages might be. Some courts have held that in distinguishing between mistaken dishonors and nonmistaken dishonors, the so-called "trader" rule has been retained that allowed a "merchant or trader" to recover substantial damages for wrongful dishonor without proof of damages actually suffered. Comment 3 to former Section 4-402 indicated that this was not the intent of the drafters. White & Summers, Uniform Commercial Code, Section 18-4 (1988), states: "The negative implication is that when wrongful dishonors occur not 'through mistake' but willfully, the court may impose damages greater than 'actual damages'..... Certainly the reference to 'mistake' in the second sentence of 4-402 invites a court to adopt the relevant pre-Code distinction." Subsection (b) by deleting the reference to mistake in the second sentence precludes any inference that Section 4-402 retains the "trader" rule. Whether a bank is liable for noncompensatory damages, such as punitive damages, must be decided by Section 1-103 and Section 1-106 ("by other rule of law").

2. Wrongful dishonor is different from "failure to exercise ordinary care in handling an item," and the measure of damages is that stated in this section, not that stated in Section 4-103(e). By the same token, if a dishonor comes within this section, the measure of damages of this section applies and not another measure of damages. If the wrongful refusal of the beneficiary's bank to make funds available from a funds transfer causes the beneficiary's check to be dishonored, no specific guidance is given as to whether recovery is under this section or Article 4A. In each case this issue must be viewed in its factual context, and it was thought unwise to seek to establish certainty at the cost of fairness.

3. The second and third sentences of the subsection (b) reject decisions holding that as a matter of law the dishonor of a check is not the "proximate cause" of the arrest and prosecution of the customer and leave to determination in each case as a question of fact whether the dishonor is or may be the "proximate cause."

4. Banks commonly determine whether there are sufficient funds in an account to pay an item after the close of banking hours on the day of presentment when they post debit and credit items to the account. The determination is made on the basis of credits available for withdrawal as of right or made available for withdrawal by the bank as an accommodation to its customer. When it is determined that payment of the item would overdraw the account, the item may be returned at any time before the bank's midnight deadline the following day. Before the item is returned new credits that are withdrawable as of right may have been added to the account. Subsection (c) eliminates uncertainty under Article 4 as to whether the failure to make a second determination before the item is returned on the day following presentment is a wrongful dishonor if new credits were added to the account on that day that would have covered the amount of the check.

5. Section 4-402 has been construed to preclude an action for wrongful dishonor by a plaintiff other than the bank's customer. *Loucks v. Albuquerque National Bank*, 418 P.2d 191 (N.Mex. 1966). Some courts have allowed a plaintiff other than the customer to sue when the customer is a business entity that is one and the same with the individual or individuals operating it. *Murdaugh Volkswagen, Inc. v. First National Bank*, 801 F.2d 719 (4th Cir. 1986) and *Karsh v. American City Bank*, 113 Cal.App.3d 419, 169 Cal.Rptr. 851 (1980). However, where the wrongful dishonor impugns the reputation of an operator of the business, the issue is not merely, as the court in *Koger v. East First National Bank*, 443 So.2d 141 (Fla.App. 1983), put it, one of a literal versus a liberal interpretation of Section 4-402. Rather the issue is whether the statutory cause of action in Section 4-402 displaces, in accordance with Section 1-103, any cause of action that existed at common law in a person who is not the customer whose reputation was damaged. See *Marcum v. Security Trust and Savings Co.*, 221 Ala. 419, 129 So. 74 (1930). While Section 4-402 should not be interpreted to displace the latter cause of action, the section itself gives no cause of action to other than a "customer," however that definition is construed, and thus confers no cause of action on the holder of a dishonored item. *First American National Bank v. Commerce Union Bank*, 692 S.W.2d 642 (Tenn.App. 1985).

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (a) is added for the purpose of stating positively what has been assumed under the original Article: that if a bank fails to honor a properly payable item it may be liable to its customer for wrongful dishonor. Subsection (b) is amended for clarification. Under this subsection the payor bank's wrongful dishonor of an item gives rise to a statutory cause of action. Damages may include consequential damages. Confusion has resulted from the attempts of courts to reconcile the first and second sentences of former Section 4-402. The second sentence implied that the bank was liable for some form of damages other than those proximately caused by the dishonor if the dishonor was other than by mistake. But nothing in the section described what these noncompensatory damages might be. Some courts have held that in distinguishing between mistaken dishonors and nonmistaken dishonors, the so-called "trader" rule has been retained that allowed a "merchant or trader" to recover substantial damages for wrongful dishonor without proof of damages actually suffered. Comment 3 to former Section 4-402 indicated that this was not the intent of the drafters. White & Summers, Uniform Commercial Code, Section 18-4 (1988), states: "The negative implication is that when wrongful dishonors occur not 'through mistake' but willfully, the court may impose

damages greater than 'actual damages' .... Certainly the reference to 'mistake' in the second sentence of 4-402 invites a court to adopt the relevant pre-Code distinction." Subsection (b) by deleting the reference to mistake in the second sentence precludes any inference that Section 4-402 retains the "trader" rule. Whether a bank is liable for noncompensatory damages, such as punitive damages, must be decided by Section 1-103 and Section 1-106 ("by other rule of law").

Subsection (c) is added for clarification. Banks commonly determine whether there are sufficient funds in an account to pay an item after the close of banking hours on the day of presentment when they post debit and credit items to the account. The determination is made on the basis of credits available for withdrawal as of right or made available for withdrawal by the bank as an accommodation to its customer. When it is determined that payment of the item would overdraw the account, the item may be returned at any time before the bank's midnight deadline the following day. Before the item is returned new credits that are withdrawable as of right may have been added to the account. Subsection (c) eliminates uncertainty under Article 4 as to whether the failure to make a second determination before the item is returned on the day following presentment is a wrongful dishonor if new credits were added to the account on that day that would have covered the amount of the check.

#### *Prior Codifications*

1981 Ed., § 28:4-402.

1973 Ed., § 28:4-402.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-403. CUSTOMER'S RIGHT TO STOP PAYMENT; BURDEN OF PROOF OF LOSS.**

(a) A customer, or any person authorized to draw on the account if there is more than one person, may stop payment of any item drawn on the customer's account or close the account by an order to the bank describing the item or account with reasonable certainty received at a time and in a manner that affords the bank a reasonable opportunity to act on it before any action by the bank with respect to the item described in section 28:4-303. If the signature of more than one person is required to draw on an account, any of these persons may stop payment or close the account.

(b) A stop-payment order is effective for 6 months, but it lapses after 14 calendar days if the original order was oral and was not confirmed in writing within that period. A stop-payment order may be renewed for additional 6-month periods by a writing given to the bank within a period during which the stop-payment order is effective.

(c) The burden of establishing the fact and amount of loss resulting from the payment of an item contrary to a stop-payment order or order to close an account is on the customer. The loss from payment of an item contrary to a stop-payment order may include damages for dishonor of subsequent items under section 28:4-402.

(Dec. 30, 1963, 77 Stat. 705, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

##### *UNIFORM COMMERCIAL CODE COMMENT*

1. The position taken by this section is that stopping payment or closing an account is a service which depositors expect and are entitled to receive from banks notwithstanding its difficulty, inconvenience and expense. The inevitable occasional losses through failure to stop or close should be borne by the banks as a cost of the business of banking.

2. Subsection (a) follows the decisions holding that a payee or indorsee has no right to stop payment. This is consistent with the provision governing payment or satisfaction. See Section 3-602. The sole exception to this rule is found in Section 4-405 on payment after notice of death, by which any person claiming an interest in the account can stop payment.

3. Payment is commonly stopped only on checks; but the right to stop payment is not limited to checks, and extends to any item payable by any bank. If the maker of a note payable at a bank is in a position analogous to that of a drawer (Section 4-106) the maker may stop payment of the note. By analogy the rule extends to drawees other than banks.

4. A cashier's check or teller's check purchased by a customer whose account is debited in payment for the check is not a check drawn on the customer's account within the meaning of subsection (a); hence, a customer purchasing a cashier's check or teller's check has no right to stop payment of such a check under subsection (a). If a bank issuing a cashier's check or teller's check refuses to pay the check as an accommodation to its customer or for other reasons, its liability on the check is governed by Section 3-411. There is no right to stop payment after certification of a check or other acceptance of a draft, and this is true

no matter who procures the certification. See Sections 3-411 and 4-303. The acceptance is the drawee's own engagement to pay, and it is not required to impair its credit by refusing payment for the convenience of the drawer.

5. Subsection (a) makes clear that if there is more than one person authorized to draw on a customer's account any one of them can stop payment of any check drawn on the account or can order the account closed. Moreover, if there is a customer, such as a corporation, that requires its checks to bear the signatures of more than one person, any of these persons may stop payment on a check. In describing the item, the customer, in the absence of a contrary agreement, must meet the standard of what information allows the bank under the technology then existing to identify the item with reasonable certainty.

6. Under subsection (b), a stop-payment order is effective after the order, whether written or oral, is received by the bank and the bank has a reasonable opportunity to act on it. If the order is written it remains in effect for six months from that time. If the order is oral it lapses after 14 days unless there is written confirmation. If there is written confirmation within the 14-day period, the six-month period dates from the giving of the oral order. A stop-payment order may be renewed any number of times by written notice given during a six-month period while a stop order is in effect. A new stop-payment order may be given after a six-month period expires, but such a notice takes effect from the date given. When a stop-payment order expires it is as though the order had never been given, and the payor bank may pay the item in good faith under Section 4-404 even though a stop-payment order had once been given.

7. A payment in violation of an effective direction to stop payment is an improper payment, even though it is made by mistake or inadvertence. Any agreement to the contrary is invalid under Section 4-103(a) if in paying the item over the stop-payment order the bank has failed to exercise ordinary care. An agreement to the contrary which is imposed upon a customer as part of a standard form contract would have to be evaluated in the light of the general obligation of good faith. Sections 1-203 and 4-104(c). The drawee is, however, entitled to subrogation to prevent unjust enrichment (Section 4-407); retains common law defenses, e.g., that by conduct in recognizing the payment the customer has ratified the bank's action in paying over a stop-payment order (Section 1-103); and retains common law rights, e.g., to recover money paid under a mistake under Section 3-418. It has sometimes been said that payment cannot be stopped against a holder in due course, but the statement is inaccurate. The payment can be stopped but the drawer remains liable on the instrument to the holder in due course (Sections 3-305, 3-414) and the drawee, if it pays, becomes subrogated to the rights of the holder in due course against the drawer. Section 4-407. The relationship between Sections 4-403 and 4-407 is discussed in the comments to Section 4-407. Any defenses available against a holder in due course remain available to the drawer, but other defenses are cut off to the same extent as if the holder were bringing the action.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (a) removes any ambiguity that may have been present under former subsection (1) by making clear that if there is more than one person authorized to draw on a customer's account any one of them can stop payment of any check drawn on the account or can order the account closed. Moreover, if there is a customer, such as a corporation, that requires its checks to bear the signatures of more than one person, any of these persons may stop payment on a check. In describing the item, the customer, in the absence of a contrary agreement, must meet the standard of what information allows the bank under the technology then existing to identify the item with reasonable certainty. An order to close an account is assimilated to an order to stop payment in this section and in Section 4-407.

Subsection (b) restates and clarifies former subsection (2). Subsection (c) is amended by the addition of the last sentence to provide expressly for what was only assumed under the former section: that a customer's damages for payment contrary to a stop-payment order may include damages for wrongful dishonor of subsequent items. The word "binding" is deleted as superfluous.

The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-403.

1973 Ed., § 28:4-403.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-404. BANK NOT OBLIGED TO PAY CHECK MORE THAN 6 MONTHS OLD.**

A bank is under no obligation to a customer having a checking account to pay a check, other than a certified check, which is presented more than 6 months after its date, but it may charge its customer's account for a payment made thereafter in good faith.

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

This section incorporates a type of statute that had been adopted in 26 jurisdictions before the Code. The time limit is set at six months because banking and commercial practice regards a check outstanding for longer than that period as stale, and a bank will normally not pay such a check without consulting the depositor. It is therefore not required to do so, but is given the option to pay because it may be in a position to know, as in the case of dividend checks, that the drawer wants payment made.

Certified checks are excluded from the section because they are the primary obligation of the certifying bank (Sections 3-409 and 3-413). The obligation runs directly to the holder of the check. The customer's account was presumably charged when the check was certified.

*Prior Codifications*

1981 Ed., § 28:4-404.

1973 Ed., § 28:4-404.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **§ 28:4-405. DEATH OR INCOMPETENCE OF CUSTOMER.**

(a) A payor or collecting bank's authority to accept, pay, or collect an item or to account for proceeds of its collection, if otherwise effective, is not rendered ineffective by incompetence of a customer of either bank existing at the time the item is issued or its collection is undertaken if the bank does not know of an adjudication of incompetence. Neither death nor incompetence of a customer revokes the authority to accept, pay, collect, or account until the bank knows of the fact of death or of an adjudication of incompetence and has reasonable opportunity to act on it.

(b) Even with knowledge, a bank may for 10 days after the date of death pay or certify checks drawn on or before that date unless ordered to stop payment by a person claiming an interest in the account.

(Dec. 30, 1963, 77 Stat. 706, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. Subsection (a) follows existing decisions holding that a drawee (payor) bank is not liable for the payment of a check before it has notice of the death or incompetence of the drawer. The justice and necessity of the rule are obvious. A check is an order to pay which the bank must obey under penalty of possible liability for dishonor. Further, with the tremendous volume of items handled any rule that required banks to verify the continued life and competency of drawers would be completely unworkable.

One or both of these same reasons apply to other phases of the bank collection and payment process and the rule is made wide enough to apply to these other phases. It applies to all kinds of "items"; to "customers" who own items as well as "customers" who draw or make them; to the function of collecting items as well as the function of accepting or paying them; to the carrying out of instructions to account for proceeds even though these may involve transfers to third parties; to depositary and intermediary banks as well as payor banks; and to incompetency existing at the time of the issuance of an item or the commencement of the collection or payment process as well as to incompetency occurring thereafter. Further, the requirement of actual knowledge makes inapplicable the rule of some cases that an adjudication of incompetency is constructive notice to all the world because obviously it is as impossible for banks to keep posted on such adjudications (in the absence of actual knowledge) as it is to keep posted as to death of immediate or remote customers.

2. Subsection (b) provides a limited period after death during which a bank may continue to pay checks (as distinguished from other items) even though it has notice. The purpose of the provision, as of the existing statutes, is to permit holders of checks drawn and issued shortly before death to cash them without the necessity of filing a claim in probate. The justification is that these checks normally are given in immediate payment of an obligation, that there is almost never any reason why they should not be paid, and that filing in probate is a useless formality, burdensome to the holder, the executor, the court and the bank.

This section does not prevent an executor or administrator from recovering the payment from the holder of the check. It is not intended to affect the validity of any gift causa mortis or other transfer in contemplation of death, but merely to relieve the bank of liability for the payment.

3. Any surviving relative, creditor or other person who claims an interest in the account may give a direction to the bank not to pay checks, or not to pay a particular check. Such notice has the same effect as a direction to stop payment. The bank has no responsibility to determine the validity of the claim or even whether it is

"colorable." But obviously anyone who has an interest in the estate, including the person named as executor in a will, even if the will has not yet been admitted to probate, is entitled to claim an interest in the account.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-405.

1973 Ed., § 28:4-405.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-406. CUSTOMER'S DUTY TO DISCOVER AND REPORT UNAUTHORIZED SIGNATURE OR ALTERATION.**

(a) A bank that sends or makes available to a customer a statement of account showing payment of items for the account shall either return or make available to the customer the items paid or provide information in the statement of account sufficient to allow the customer reasonably to identify the items paid. The statement of account provides sufficient information if the item is described by item number, amount, and date of payment.

(b) If the items are not returned to the customer, the person retaining the items shall either retain the items or, if the items are destroyed, maintain the capacity to furnish legible copies of the items until the expiration of 7 years after receipt of the items. A customer may request an item from the bank that paid the item, and that bank must provide in a reasonable time either the item or, if the item has been destroyed or is not otherwise obtainable, a legible copy of the item.

(c) If a bank sends or makes available a statement of account or items pursuant to subsection (a) of this section, the customer must exercise reasonable promptness in examining the statement or the items to determine whether any payment was not authorized because of an alteration of an item or because a purported signature by or on behalf of the customer was not authorized. If, based on the statement or items provided, the customer should reasonably have discovered the unauthorized payment, the customer must promptly notify the bank of the relevant facts.

(d) If the bank proves that the customer failed, with respect to an item, to comply with the duties imposed on the customer by subsection (c) of this section, the customer is precluded from asserting against the bank:

(1) The customer's unauthorized signature or any alteration on the item, if the bank also proves that it suffered a loss by reason of the failure; and

(2) The customer's unauthorized signature or alteration by the same wrongdoer on any other item paid in good faith by the bank if the payment was made before the bank received notice from the customer of the unauthorized signature or alteration and after the customer had been afforded a reasonable period of time, not exceeding 30 days, in which to examine the item or statement of account and notify the bank.

(e) If subsection (d) of this section applies and the customer proves that the bank failed to exercise ordinary care in paying the item and that the failure substantially contributed to loss, the loss is allocated between the customer precluded and the bank asserting the preclusion according to the extent to which the failure of the customer to comply with subsection (c) of this section and the failure of the bank to exercise ordinary care contributed to the loss. If the customer proves that the bank did not pay the item in good faith, the preclusion under subsection (d) of this section does not apply.

(f) Without regard to care or lack of care of either the customer or the bank, a customer who does not within one year after the statement or items are made available to the customer (subsection (a) of this section) discover and report the customer's unauthorized signature on or any alteration on the item is precluded from asserting against the bank the unauthorized signature or alteration. If there is a preclusion under this subsection, the payor bank may not recover for breach of warranty under section 28:4-208 with respect to the unauthorized signature or alteration to which the preclusion applies.

(Dec. 30, 1963, 77 Stat. 706, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

1. Under subsection (a), if a bank that has paid a check or other item for the account of a customer makes available to the customer a statement of account showing payment of the item, the bank must either return the item to the customer or provide a description of the item sufficient to allow the customer to identify it. Under subsection (c), the customer has a duty to exercise reasonable promptness in examining the statement or the

returned item to discover any unauthorized signature of the customer or any alteration and to promptly notify the bank if the customer should reasonably have discovered the unauthorized signature or alteration.

The duty stated in subsection (c) becomes operative only if the "bank sends or makes available a statement of account or items pursuant to subsection (a)." A bank is not under a duty to send a statement of account or the paid items to the customer; but, if it does not do so, the customer does not have any duties under subsection (c).

Under subsection (a), a statement of account must provide information "sufficient to allow the customer reasonably to identify the items paid." If the bank supplies its customer with an image of the paid item, it complies with this standard. But a safe harbor rule is provided. The bank complies with the standard of providing "sufficient information" if "the item is described by item number, amount, and date of payment." This means that the customer's duties under subsection (c) are triggered if the bank sends a statement of account complying with the safe harbor rule without returning the paid items. A bank does not have to return the paid items unless it has agreed with the customer to do so. Whether there is such an agreement depends upon the particular circumstances. See Section 1-201(3). If the bank elects to provide the minimum information that is "sufficient" under subsection (a) and, as a consequence, the customer could not "reasonably have discovered the unauthorized payment," there is no preclusion under subsection (d). If the customer made a record of the issued checks on the check stub or carbonized copies furnished by the bank in the checkbook, the customer should usually be able to verify the paid items shown on the statement of account and discover any unauthorized or altered checks. But there could be exceptional circumstances. For example, if a check is altered by changing the name of the payee, the customer could not normally detect the fraud unless the customer is given the paid check or the statement of account discloses the name of the payee of the altered check. If the customer could not "reasonably have discovered the unauthorized payment" under subsection (c) there would not be a preclusion under subsection (d).

The safe harbor provided by subsection (a) serves to permit a bank, based on the state of existing technology, to trigger the customer's duties under subsection (c) by providing a "statement of account showing payment of items" without having to return the paid items, in any case in which the bank has not agreed with the customer to return the paid items. The safe harbor does not, however, preclude a customer under subsection (d) from asserting its unauthorized signature or an alteration against a bank in those circumstances in which under subsection (c) the customer should not "reasonably have discovered the unauthorized payment." Whether the customer has failed to comply with its duties under subsection (c) is determined on a case-by-case basis.

The provision in subsection (a) that a statement of account contains "sufficient information if the item is described by item number, amount, and date of payment" is based upon the existing state of technology. This information was chosen because it can be obtained by the bank's computer from the check's MICR line without examination of the items involved. The other two items of information that the customer would normally want to know--the name of the payee and the date of the item--cannot currently be obtained from the MICR line. The safe harbor rule is important in determining the feasibility of payor or collecting bank check retention plans. A customer who keeps a record of checks written, e.g., on the check stubs or carbonized copies of the checks supplied by the bank in the checkbook, will usually have sufficient information to identify the items on the basis of item number, amount, and date of payment. But customers who do not utilize these record-keeping methods may not. The policy decision is that accommodating customers who do not keep adequate records is not as desirable as accommodating customers who keep more careful records. This policy results in less cost to the check collection system and thus to all customers of the system. It is expected that technological advances such as image processing may make it possible for banks to give customers more information in the future in a manner that is fully compatible with automation or truncation systems. At that time the Permanent Editorial Board may wish to make recommendations for an amendment revising the safe harbor requirements in the light of those advances.

2. Subsection (d) states the consequences of a failure by the customer to perform its duty under subsection (c) to report an alteration or the customer's unauthorized signature. Subsection (d)(1) applies to the unauthorized payment of the item to which the duty to report under subsection (c) applies. If the bank proves that the customer "should reasonably have discovered the unauthorized payment" (See Comment 1) and did not notify the bank, the customer is precluded from asserting against the bank the alteration or the customer's unauthorized signature if the bank proves that it suffered a loss as a result of the failure of the customer to perform its subsection (c) duty. Subsection (d)(2) applies to cases in which the customer fails to report an unauthorized signature or alteration with respect to an item in breach of the subsection (c) duty (See Comment 1) and the bank subsequently pays other items of the customer with respect to which there is an alteration or unauthorized signature of the customer and the same wrongdoer is involved. If the payment of the subsequent items occurred after the customer has had a reasonable time (not exceeding 30 days) to report with respect to the first item and before the bank received notice of the unauthorized signature or alteration of the first item, the customer is precluded from asserting the alteration or unauthorized signature with respect to the subsequent items.

If the customer is precluded in a single or multiple item unauthorized payment situation under subsection (d), but the customer proves that the bank failed to exercise ordinary care in paying the item or items and that the failure substantially contributed to the loss, subsection (e) provides a comparative negligence test for allocating loss between the customer and the bank. Subsection (e) also states that, if the customer proves that the bank did not pay the item in good faith, the preclusion under subsection (d) does not apply.

Subsection (d)(2) changes former subsection (2)(b) by adopting a 30-day period in place of a 14-day period. Although the 14-day period may have been sufficient when the original version of Article 4 was drafted in the 1950s, given the much greater volume of checks at the time of the revision, a longer period was viewed as more appropriate. The rule of subsection (d)(2) follows pre-Code case law that payment of an additional item or items bearing an unauthorized signature or alteration by the same wrongdoer is a loss suffered by the bank traceable to the customer's failure to exercise reasonable care (See Comment 1) in examining the statement and notifying the bank of objections to it. One of the most serious consequences of failure of the customer to comply with the requirements of subsection (c) is the opportunity presented to the wrongdoer to repeat the misdeeds. Conversely, one of the best ways to keep down losses in this type of situation is for the customer to promptly examine the statement and notify the bank of an unauthorized signature or alteration so that the bank will be alerted to stop paying further items. Hence, the rule of subsection (d)(2) is prescribed, and to avoid dispute a specific time limit, 30 days, is designated for cases to which the subsection applies. These considerations are not present if there are no losses resulting from the payment of additional items. In these circumstances, a reasonable period for the customer to comply with its duties under subsection (c) would depend on the circumstances (Section 1-204(2)) and the subsection (d)(2) time limit should not be imported by analogy into subsection (c).

3. Subsection (b) applies if the items are not returned to the customer. Check retention plans may include a simple payor bank check retention plan or the kind of check retention plan that would be authorized by a truncation agreement in which a collecting bank or the payee may retain the items. Even after agreeing to a check retention plan, a customer may need to see one or more checks for litigation or other purposes. The customer's request for the check may always be made to the payor bank. Under subsection (b) retaining banks may destroy items but must maintain the capacity to furnish legible copies for seven years. A legible copy may include an image of an item. This Act does not define the length of the reasonable period of time for a bank to provide the check or copy of the check. What is reasonable depends on the capacity of the bank and the needs of the customer. This Act does not specify sanctions for failure to retain or furnish the items or legible copies; this is left to other laws regulating banks. See Comment 3 to Section 4-101. Moreover, this Act does not regulate fees that banks charge their customers for furnishing items or copies or other services covered by the Act, but under principles of law such as unconscionability or good faith and fair dealing, courts have reviewed fees and the bank's exercise of a discretion to set fees. *Perdue v. Crocker National Bank*, 38 Cal.3d 913 (1985) (unconscionability); *Best v. United Bank of Oregon*, 739 P.2d 554, 562-566 (1987) (good faith and fair dealing). In addition, Section 1-203 provides that every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.

4. Subsection (e) replaces former subsection (3) and poses a modified comparative negligence test for determining liability. See the discussion on this point in the Comments to Sections 3-404, 3-405, and 3-406. The term "good faith" is defined in Section 3-103(a)(4) as including "observance of reasonable commercial standards of fair dealing." The connotation of this standard is fairness and not absence of negligence.

The term "ordinary care" used in subsection (e) is defined in Section 3-103(a)(7), made applicable to Article 4 by Section 4-104(c), to provide that sight examination by a payor bank is not required if its procedure is reasonable and is commonly followed by other comparable banks in the area. The case law is divided on this issue. The definition of "ordinary care" in Section 3-103 rejects those authorities that hold, in effect, that failure to use sight examination is negligence as a matter of law. The effect of the definition of "ordinary care" on Section 4-406 is only to provide that in the small percentage of cases in which a customer's failure to examine its statement or returned items has led to loss under subsection (d) a bank should not have to share that loss solely because it has adopted an automated collection or payment procedure in order to deal with the great volume of items at a lower cost to all customers.

5. Several changes are made in former Section 4-406(5). First, former subsection (5) is deleted and its substance is made applicable only to the one-year notice preclusion in former subsection (4) (subsection (f)). Thus if a drawer has not notified the payor bank of an unauthorized check or material alteration within the one-year period, the payor bank may not choose to recredit the drawer's account and pass the loss to the collecting banks on the theory of breach of warranty. Second, the reference in former subsection (4) to unauthorized indorsements is deleted. Section 4-406 imposes no duties on the drawer to look for unauthorized indorsements. Section 4-111 sets out a statute of limitations allowing a customer a three-year period to seek a credit to an account improperly charged by payment of an item bearing an unauthorized indorsement. Third, subsection (c) is added to Section 4-208 to assure that if a depository bank is sued for breach of a presentment warranty, it can defend by showing that the drawer is precluded by Section 3-406 or Section 4-406(c) and (d). Revisions approved by the Permanent Editorial Board for the Uniform Commercial Code, March 16, 1991.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Subsection (a), (b) and (c) restate and enlarge on former subsection (1). Subsection (a) recognizes that the parties may agree that the payor, a collecting bank or other person may retain the items drawn on the customer's account. In these cases the payor bank must provide sufficient information in a statement of account to allow the customer to reasonably identify the items paid. A safe harbor rule is stated that provides that the payor bank has satisfied its obligation if the item is described by item number, amount and the date of payment. This information is selected because it can be captured by the payor bank by automation without manual processing of the item.

Subsection (b) allows the bank retaining the item to destroy the item so long as it maintains the capacity to furnish legible copies for seven years. During this period the customer is entitled to demand from its payor bank the item or a copy of it. If the item is being retained by a collecting bank or other person, the payor bank must obtain the item or copy from that bank for its customer.

Subsection (c) continues the rule of former subsection (1) of requiring the customer to exercise reasonable promptness in examining the statement or items for an unauthorized signature of the customer or an alteration and to notify the bank promptly.

Subsection (d)(2) restates the conditions of the customer's preclusion and extends the 14-day period under former subsection (2) to a 30-day period. Although the 14-day period may have been sufficient when the original version of Article 4 was drafted, given the huge increase in the volume of checks, a longer period is viewed as more appropriate today.

Subsection (e) replaces former subsection (3) and poses a modified comparative negligence test for determining liability. See the discussion on this point in the Official Comments to Sections 3-404, 3-405 and 3-406. The term "good faith" is defined in Section 3-103(a)(4) as including "observance of reasonable commercial standards of fair dealing." The connotation of this standard is fairness and not absence of negligence. The term "ordinary care" used in subsection (e) is defined in Section 3-103(a)(7) to provide that sight examination by a payor bank is not required if its procedure is reasonable and is commonly followed by other comparable banks in the area. The case law is divided on this issue. The definition of "ordinary care" in Section 3-103 rejects those authorities that hold, in effect, that failure to use sight examination is negligence as a matter of law.

Subsection (f) amends former subsection (4) to delete the reference to a three-year period to discover an unauthorized indorsement. Section 4-406 imposes no duty on a customer to discover a forged indorsement. Section 4-111 sets out a statute of limitations allowing a customer a three-year period to seek a credit to an account improperly charged by payment of an item bearing an unauthorized indorsement. The final sentence added to subsection (f) incorporates the substance of former subsection (5).

The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-406.

1973 Ed., § 28:4-406.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-407. PAYOR BANK'S RIGHT TO SUBROGATION ON IMPROPER PAYMENT.**

If a payor bank has paid an item over the order of the drawer or maker to stop payment, or after an account has been closed, or otherwise under circumstances giving a basis for objection by the drawer or maker, to prevent unjust enrichment and only to the extent necessary to prevent loss to the bank by reason of its payment of the item, the payor bank is subrogated to the rights:

- (1) Of any holder in due course on the item against the drawer or maker;
- (2) Of the payee or any other holder of the item against the drawer or maker either on the item or under the transaction out of which the item arose; and
- (3) Of the drawer or maker against the payee or any other holder of the item with respect to the transaction out of which the item arose.

(Dec. 30, 1963, 77 Stat. 707, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

##### *UNIFORM COMMERCIAL CODE COMMENT*

1. Section 4-403 states that a stop-payment order or an order to close an account is binding on a bank. If a bank pays an item over such an order it is prima facie liable, but under subsection (c) of Section 4-403 the burden of establishing the fact and amount of loss from such payment is on the customer. A defense frequently interposed by a bank in an action against it for wrongful payment over a stop-payment order is that the drawer or maker suffered no loss because it would have been liable to a holder in due course in any event. On this argument some cases have held that payment cannot be stopped against a holder in due course. Payment can be stopped, but if it is, the drawer or maker is liable and the sound rule is that the bank is subrogated to the rights of the holder in due course. The preamble and paragraph (1) of this section state this rule.

2. Paragraph (2) also subrogates the bank to the rights of the payee or other holder against the drawer or maker either on the item or under the transaction out of which it arose. It may well be that the payee is not a



holder in due course but still has good rights against the drawer. These may be on the check but also may not be as, for example, where the drawer buys goods from the payee and the goods are partially defective so that the payee is not entitled to the full price, but the goods are still worth a portion of the contract price. If the drawer retains the goods it is obligated to pay a part of the agreed price. If the bank has paid the check it should be subrogated to this claim of the payee against the drawer.

3. Paragraph (3) subrogates the bank to the rights of the drawer or maker against the payee or other holder with respect to the transaction out of which the item arose. If, for example, the payee was a fraudulent salesman inducing the drawer to issue a check for defective securities, and the bank pays the check over a stop-payment order but reimburses the drawer for such payment, the bank should have a basis for getting the money back from the fraudulent salesman.

4. The limitations of the preamble prevent the bank itself from getting any double recovery or benefits out of its subrogation rights conferred by the section.

5. The spelling out of the affirmative rights of the bank in this section does not destroy other existing rights (Section 1-103). Among others these may include the defense of a payor bank that by conduct in recognizing the payment a customer has ratified the bank's action in paying in disregard of a stop-payment order or right to recover money paid under a mistake.

#### **Reason for 1990 Change [D.C. Law 10-249]**

An order to close an account is assimilated to an order to stop payment in this section and in Section 4-403. The other modifications are made to conform with current legislative drafting practices, with no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-407.

1973 Ed., § 28:4-407.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

## **PART 5. COLLECTION OF DOCUMENTARY DRAFTS.**

### **§ 28:4-501. HANDLING OF DOCUMENTARY DRAFTS; DUTY TO SEND FOR PRESENTMENT AND TO NOTIFY CUSTOMER OF DISHONOR.**

A bank that takes a documentary draft for collection shall present or send the draft and accompanying documents for presentment and, upon learning that the draft has not been paid or accepted in due course, shall seasonably notify its customer of the fact even though it may have discounted or bought the draft or extended credit available for withdrawal as of right.

(Dec. 30, 1963, 77 Stat. 707, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

#### *HISTORICAL AND STATUTORY NOTES*

#### *UNIFORM COMMERCIAL CODE COMMENT*

This section states the duty of a bank handling a documentary draft for a customer. "Documentary draft" is defined in Section 4-104. The duty stated exists even if the bank has bought the draft. This is because to the customer the draft normally represents an underlying commercial transaction, and if that is not going through as planned the customer should know it promptly.

#### **Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

#### *Prior Codifications*

1981 Ed., § 28:4-501.

1973 Ed., § 28:4-501.

#### *Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

### **§ 28:4-502. PRESENTMENT OF "ON ARRIVAL" DRAFTS.**

If a draft or the relevant instructions require presentment "on arrival", "when goods arrive", or the like, the collecting bank need not present until in its judgment a reasonable time for arrival of the goods has

expired. Refusal to pay or accept because the goods have not arrived is not dishonor; the bank must notify its transferor of the refusal but need not present the draft again until it is instructed to do so or it learns of the arrival of the goods.

(Dec. 30, 1963, 77 Stat. 707, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

The section is designed to establish a definite rule for "on arrival" drafts. The term includes not only drafts drawn payable "on arrival" but also drafts forwarded with instructions to present "on arrival." The term refers to the arrival of the relevant goods. Unless a bank has actual knowledge of the arrival of the goods, as for example, when it is the "notify" party on the bill of lading, the section only requires the exercise of such judgment in estimating time as a bank may be expected to have. Commonly the buyer-drawee will want the goods and will therefore call for the documents and take up the draft when they do arrive.

**Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

*Prior Codifications*

1981 Ed., § 28:4-502.

1973 Ed., § 28:4-502.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

**§ 28:4-503. RESPONSIBILITY OF PRESENTING BANK FOR DOCUMENTS AND GOODS; REPORT OF REASONS FOR DISHONOR; REFEREE IN CASE OF NEED.**

Unless otherwise instructed and except as provided in Article 5, a bank presenting a documentary draft:

- (1) Must deliver the documents to the drawee on acceptance of the draft if it is payable more than 3 days after presentment; otherwise, only on payment; and
- (2) Upon dishonor, either in the case of presentment for acceptance or presentment for payment, may seek and follow instructions from any referee in case of need designated in the draft or, if the presenting bank does not choose to utilize the referee's services, it must use diligence and good faith to ascertain the reason for dishonor, must notify its transferor of the dishonor and of the results of its effort to ascertain the reasons therefor, and must request instructions. However, the presenting bank is under no obligation with respect to goods represented by the documents except to follow any reasonable instructions seasonably received; it has a right to reimbursement for any expense incurred in following instructions and to prepayment of or indemnity for those expenses.

(Dec. 30, 1963, 77 Stat. 707, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

1. This section states the rules governing, in the absence of instructions, the duty of the presenting bank in case either of honor or of dishonor of a documentary draft. The section should be read in connection with Section 2-514 on when documents are deliverable on acceptance, when on payment.

2. If the draft is drawn under a letter of credit, Article 5 controls. See Sections 5-109 through 5-114.

**Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

*Prior Codifications*

1981 Ed., § 28:4-503.

1973 Ed., § 28:4-503.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.

**§ 28:4-504. PRIVILEGE OF PRESENTING BANK TO DEAL WITH GOODS; SECURITY INTEREST FOR EXPENSES.**

(a) A presenting bank that, following the dishonor of a documentary draft, has seasonably requested instructions but does not receive them within a reasonable time may store, sell, or otherwise deal with the goods in any reasonable manner.

(b) For its reasonable expenses incurred by action under subsection (a) of this section, the presenting bank has a lien upon the goods or their proceeds, which may be foreclosed in the same manner as an unpaid seller's lien.

(Dec. 30, 1963, 77 Stat. 708, Pub. L. 88-243, § 1; Mar. 23, 1995, D.C. Law 10-249, § 2(e), 42 DCR 467.)

*HISTORICAL AND STATUTORY NOTES*

*UNIFORM COMMERCIAL CODE COMMENT*

The section gives the presenting bank, after dishonor, a privilege to deal with the goods in any commercially reasonable manner pending instructions from its transferor and, if still unable to communicate with its principal after a reasonable time, a right to realize its expenditures as if foreclosing on an unpaid seller's lien (Section 2-706). The provision includes situations in which storage of goods or other action becomes commercially necessary pending receipt of any requested instructions, even if the requested instructions are later received.

The "reasonable manner" referred to means one reasonable in the light of business factors and the judgment of a business man.

**Reason for 1990 Change [D.C. Law 10-249]**

Modified to conform with current drafting practices; no intent to change substance.

*Prior Codifications*

1981 Ed., § 28:4-504.

1973 Ed., § 28:4-504.

*Legislative History of Laws*

For legislative history of D.C. Law 10-249, see Historical and Statutory Notes following § 28:4-101.