New Mexico's Uniform Commercial Code: Who is the Beneficiary of the Stop Payment Provisions of Article 4

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WHO IS THE BENEFICIARY OF THE STOP PAYMENT PROVISIONS OF ARTICLE 4?

Customer's Right to Stop Payment; Burden of Proof of Loss.¹

(1) A customer may by order to his bank stop payment of any item payable for his account but the order must be received at such time and in such manner as to afford the bank a reasonable opportunity to act on it prior to any action by the bank with respect to the item described in Section 4-303.

(2) An oral order is binding upon the bank only for fourteen calendar days unless confirmed in writing within that period. A written order is effective for only six months unless renewed in writing.

(3) The burden of establishing the fact and amount of loss resulting from the payment of an item contrary to a binding stop order is effective for only six months unless renewed in writing.

A close analysis of each Code provision relating to stop payment orders is necessary to answer the question posed in the title to this paper. Part I examines the mechanics of stopping payment, and Part II deals with proof of loss and standard of care.

I

THE MECHANICS OF STOPPING PAYMENT

A. “Customer’s Right to Stop Payment”

Any discussion of an Article 4 section must be prefaced by a reminder that the effect of any provision of Article 4 may be varied by


All references to New Mexico’s version of the Code, often designated UCC both in footnotes and text, will omit the full statutory citation. Citations to “Comments” are those accompanying the 1958 Official Text.

References to the Uniform Negotiable Instruments Law, N.M. Laws 1907, ch. 83, §§ 1-197, repealed by N.M. Laws 1961, ch. 96, § 10-102, will be to “NIL.”
The scope of this “right” to vary seems to overcome any thought of absolute rights under the remaining provisions of the Article.

The right of a customer to countermand his prior order to pay has generally been recognized since early common law. A few cases treated a check as an assignment of funds in the hands of the bank and denied the right to stop payment, but adoption of the NIL forced an abandonment of this theory.

2. UCC § 4-103(1) provides:
   The effect of the provisions of this Article may be varied by agreement except that no agreement can disclaim a bank’s responsibility for its own lack of good faith or failure to exercise ordinary care or can limit the measure of damages for such lack or failure; but the parties may by agreement determine the standards by which such responsibility is to be measured if such standards are not manifestly unreasonable.
   See text at 81-84, infra, for a discussion of this section.

3. E.g., “I presume no one at this day questions the right of the drawer of a check to stop payment thereof. This is usually done by notice to the bank upon which the check is drawn. If the bank pays after such notice it does so at its peril.” German Nat’l Bank v. Farmers’ Deposit Bank, 118 Pa. 294, 313, 12 Atl. 303, 305 (1888); See also Florence Mining Co. v. Brown, 124 U.S. 385 (1888); Taylor v. First Nat’l Bank, 119 Minn. 525, 138 N.W. 783 (1912).

4. In Raesser v. National Exch. Bank, 112 Wis. 591, 88 N.W. 618 (1912), the court stated that the issuance of the check to a payee for consideration was an assignment of the funds in the hands of the bank; the drawer had died before his checks were presented, but the bank paid them. The court held that the force of prior decisions would require that a drawer could not arbitrarily, without good cause, stop payment and avoid the assignment; that such an act would be a fraud. In Unaka Nat’l Bank v. Butler, 113 Tenn. 574, 83 S.W. 655 (1904), the drawer and a holder in due course requested the bank to stop payment on a lost check, but the bank paid the item to a subsequent holder in due course. The court denied the drawer’s right to recover from the bank, on the grounds that there had been an assignment of the funds.

5. NIL § 189 provides: “A check of itself does not operate as an assignment of any part of the funds to the credit of the drawer with the bank, and the bank is not liable to the holder, unless and until it accepts or certifies the check.”

The court in Boswell v. Citizens’ Sav. Bank, 123 Ky. 485, 96 S.W. 797 (1906), stated that prior to the NIL, Kentucky had held the issuance of a check to be an assignment of funds but that since the NIL, it was no longer the rule. Accord, Kaesemeyer v. Smith, 22 Idaho 1, 123 Pac. 943 (1912); In re Thornton’s Guardianship, 243 Wis. 397, 10 N.W.2d 193 (1943). In Thornton, the court referred to its earlier opinion Raesser v. National Exch. Bank, supra note 4, and stated: “The section of the Negotiable Instruments Act referred to [§ 189] was enacted for the express purpose of changing the law as theretofore declared in this state.” Id. at 403, 10 N.W.2d at 196. Cf. Hiroshima v. Bank of Italy, 78 Cal. App. 362, 248 Pac. 947 (3d Dist. Ct. App. 1926).

A few cases have held that a drawer’s right to stop payment ceases upon positive action by the parties to a check showing a clear intent that the check operate as an assignment of the funds in the hands of a drawer. This was permissible under NIL § 189 which states that a check shall not “of itself” operate as an assignment of the funds. Green v. Brown, 22 S.W.2d 701 (Tex. Civ. App. 1929); Fourth Street Bank v. Yardley, 165 U.S. 634 (1897). See also Moravek v. First Nat’l Bank, 119 Kan. 84, 237 Pac. 921
In 1929, the American Banker's Association recommended legislation to govern stop payment orders:

No revocation, countermand or stop-payment order relating to the payment of any check or draft against an account of a depositor in any bank or trust company doing business in this state shall remain in effect for more than six months after the service thereof on the bank, unless the same be renewed, which renewals shall be in writing and which renewals shall be in effect for not more than six months from the date of service thereof on the bank or trust company, but such renewals may be made from time to time.  

New Mexico adopted this draft, as did eighteen other states. The recommended legislation did not specifically state that the drawer of a check had the right to stop payment. Perhaps such a right could be inferred from the statutory language which limits the duration of a stop order. Be that as it may, the common law's recognition of the right to stop payment seems to have been carried forward in the Banker's Association draft.

The Code does little to establish a specific "right" in the customer to issue a stop order. Like the earlier legislation, section 4-403 is stated in terms of permissiveness rather than as an absolute right in the drawer. If the bank secures an agreement from its customer varying the provisions of section 4-403, the courts probably will enforce the agreement, as long as it does not disclaim the "bank's responsibility for its own lack of good faith or failure to exercise ordinary care . . . ." Query if the bank, in its deposit contract, can force a customer to waive his "right" to order a stop payment? A discussion of the permissible extent of disclaimer appears below.

B. "(1) A customer may be order to his bank stop payment of any item payable for his account . . . ."

1. The Customer

(1925). Section 3-409 of the Code is substantially the same as NIL § 189; hence the same result is possible under the Code.
6. 3 Paton's Digest 3443, 3462 (2d ed. 1944).
8. Paton, op. cit. supra note 6, at 3462. The intent of this recommended draft is stated to be to avoid the continued and indefinite effect of a stop payment order. Ten additional states adopted some modification of the recommended draft. Ibid.
9. UCC § 4-103(1).
10. See text at 81-84, infra.
Although the section refers only to a "customer" issuing a stop order, it seems probable that an agent properly may exercise the "right" in behalf of the customer. And upon the death of the customer, any person claiming an interest in the account, e.g., a prospective heir or creditor, may stop the payment of any check.

2. Other Parties

Other parties to an instrument have no right to stop payment under section 4-403; presumably, they would request the drawer to issue a stop order. If the drawer refuses to order stop payment, and the instrument has been stolen, lost, or destroyed, the "owner" of the instrument may recover its face value from "any party liable thereon upon due proof of his [the owner's] ownership, the facts which prevent his production of the instrument and its terms." As applied to checks, the provision is of no use to such an owner. He is given a right only against parties liable on the instrument. The draw-

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11. A "customer" of a bank includes any "person" having an account with a bank. UCC § 4-104(1) (c). A "person" is defined by § 1-201(30) as including an "organization." An "organization" is defined by § 1-201(28) as including "two or more persons having a joint or common interest." It would seem that a "customer" would include two persons having a joint bank account. If H and W have a joint account and H issues a check to X, then H or W may issue a stop payment order, and the bank would be liable if it paid the check. On these facts, prior to the Code, the court in Brown v. Eastman Nat'l Bank, 291 P.2d 828 (Okla. 1955), held to the contrary and said the bank was not liable when it paid the check over the otherwise valid stop payment order of the wife. But see Commercial Bank v. Hall, 77 Ala. 168, 94 So. 2d 198 (1957) (partner stopped payment of co-partner's check on partnership joint account); Harlan Nat'l Bank v. Carbon Glow Coal Co., 289 S.W.2d 200 (Ky. Ct. App. 1956) (purchaser of corporation gave notice to stop payment to avoid dissipation of assets).

12. Section 1-103 of the Code provides that the law relative to principal and agent, unless displaced by the Code, supplements the Code. Prior to the Code, the right of one acting for the customer to stop payment in accordance with the customer's wishes was upheld in Third Nat'l Bank v. Carver, 31 Tenn. App. 520, 218 S.W.2d 66 (1948). See also Commercial Bank v. Hall, 77 Ala. 168, 94 So. 2d 198 (1957); Carroll v. South Carolina Nat'l Bank, 211 S.C. 406, 45 S.E.2d 729 (1947).

13. UCC § 4-405(2), quoted in note 26 infra.


15. [T]he owner of such an instrument is not a holder as that term is defined in this Act, since he is not in possession of the paper, and he does not have the holder's prima facie right to recover under the section on the burden of establishing signatures. He must prove his case. He must establish the terms of the instrument and his ownership, and must account for its absence.

16. UCC § 3-804.

The section further provides: "The Court may require security indemnifying the defendant against loss by reason of further claims on the instrument." Ibid. (Emphasis added.) Prior to the Code, an indemnity bond was mandatory for double the face amount of the item. N.M. Laws 1897, ch. 73, § 127, repealed by N.M. Laws 1961, ch. 96, § 10-102.
er and indorsers are not liable on a check until it has been presented and dishonored.17 An instrument which is stolen, lost, or destroyed cannot be presented by the owner. The bank is never liable on a check until acceptance,18 and acceptance must be accomplished by a writing on the instrument itself.19 Thus, it is difficult to find any party who would be liable on the check. The provision seems aimed at the two-party instrument, i.e., the note, rather than the three-party check.

Hence, if an owner wishes to stop payment, his proper course of action is not made clear by the Code. One means of stopping payment may be to request the drawee that it refuse to pay while simultaneously providing security deemed adequate by the drawee for its protection.20 As the drawee's dishonor of the item would make the drawer primarily liable,21 the owner would also have to furnish the drawer security deemed adequate by the drawer. These multiple financial burdens seem to preclude any practical consideration of this alternative.22

In addition to the owner of a lost instrument, a transferor of an instrument for consideration, in a transaction involving fraud, defective goods, or the like, may have need of stop payment rights. This raises the question of whether the Code should extend the "right" to stop payment to the owner and transferor.

Suppose for a moment that a new provision were enacted under the Code which allowed such parties the right to stop payment, upon presentation of the order to the payor bank, together with a reasonable fee for the bank's services, plus a deposit for the face amount of the check. Suppose, too, that the provision discharged the drawer from all liability upon subsequent dishonor by the bank, substituting the transferor as the party primarily liable.

As the funds would be certain, the negotiability of checks should not suffer, nor would reliance on the credit of the drawer be misplaced. Subsequent transferees, including a holder in due course,

17. UCC §§ 3-413(2), -414(1).
18. UCC § 3-409(1).
19. UCC § 3-410(1).
20. UCC § 3-603(1) provides in part: "The liability of any party is discharged to the extent of his payment . . . to the holder . . . unless prior to such payment . . . [a claimant] . . . supplies indemnity deemed adequate by the party seeking the discharge . . . ."
21. UCC § 3-413(2).
22. It seems that "adequate" security might include costs and attorney fees for anticipated litigation, particularly for protection against a slander of credit suit by the drawer.
would have the same rights against the "new drawer" as against the old. The bank would be compensated for any administrative burden by the fee charged the "new drawer"; if the bank paid the item in error over the stop order, it would be entitled to be subrogated to the rights of the holder against the "new drawer." All but the most necessary use of the new provision might be discouraged by a penalty provision, perhaps an arbitrary percentage of the face amount of the check.

The need for extending the right to stop payment must be balanced against (1) the possibility of forcing a holder in due course to sue to collect and (2) the administrative burden on the bank. Perhaps the number of transactions in which this need arises are too few to justify the burden imposed on these parties.

3. Death of a Customer

Prior to the Code, the death of the customer revoked the authority of the bank to pay an item issued by the customer before his death, however, the bank was not held liable until after it had notice or knowledge of the death. Notwithstanding the language of section 189 of the NIL, that a "check of itself does not operate as an assignment," New Mexico as a minority of one used the assignment theory to hold that a bank with knowledge of its customer's death had authority to pay a check drawn by him.

The Code continues to protect the bank. The bank may pay an


23. In Elgin v. Gross-Kelly & Co., 20 N.M. 450, 150 Pac. 922 (1915), the court found that the payee, as assignee of the funds in the bank, had an authority coupled with an interest which death never revoked.

24. UCC § 4-405:

(1) 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 such 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.
item until notified of the death (or incompetence) of the customer. Even with knowledge of the death, the bank may pay an item within ten days of death unless a stop order is issued by a person claiming an interest in the account. Thus, the holder of an outstanding check may be able to avoid the expense and delay of probate proceedings. The estate and its creditors are protected from undue dissipation of cash from the customer’s account by the broad stop payment provisions. The net effect of the Code treatment seems good. It permits payment which will avoid needless expense and delay, while protecting the estate and creditors.

4. Cashier’s Checks

Prior to the Code, a cashier’s check, an instrument drawn by a bank on itself, was not subject to revocation. Payment of a banker’s draft, drawn by one bank on another, could be stopped. Under the Code, the only party who can stop payment is a bank’s “customer,” who is defined as “any person having an account with a bank . . . and includes a bank carrying an account with another bank.” Hence, the right to stop payment would be afforded a bank issuing a banker’s draft. The Code, however, makes no specific provision for the stopping of cashier’s checks.

An argument could be made that the term any person includes banks by definition, and—even though the cashier’s check is drawn on itself—it is drawn on an “account with a bank.” This would make a bank a “customer” with the corresponding right to stop payment on its own checks. However, it seems that if the drafters of the Code had intended this result, they would not have included the words “carrying an account with another bank.” Further, acceptance is one of the procedures which cuts off the right to stop payment, and is-

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


29. UCC § 4-104(1) (e). (Emphasis added.)

30. Ibid.

31. UCC § 4-303(1) (a).
suance of a check by the bank would seem to constitute acceptance in advance.\footnote{32} Unless the term "customer" is extended to include a bank drawing on itself, which, in effect, makes the bank its own customer, the issuance of a cashier's check will be final, just as if certified.\footnote{33} A bank paying its own bills by checks drawn on itself will be denied the right to stop payment.

C. "but the order must be received at such time and in such manner as to afford the bank a reasonable opportunity to act on it prior to any action by the bank with respect to the item described in Section 4-303."\footnote{34}

In explaining the rationale of the "reasonable opportunity" rule of section 4-403, the Comments state:

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. . . . The acceptance is the drawee's own engagement to pay, and he is not required to impair his credit by refusing payment for the convenience of the drawer.

The rule goes well beyond protecting the drawee's credit. Posting or mere sight posting cuts off the customer's right to stop payment.\footnote{35} Neither act can obligate the bank to pay.

Finality—the need to end a transaction—may have been the goal sought by the drafters. But was it necessary to draw the line before

\footnote{32. UCC § 3-410(1) defines acceptance as "the drawee's signed engagement to honor the draft . . . . [A]nd [it] may consist of . . . [the] signature alone."}

\footnote{33. See UCC § 3-411 for certification provisions.}

\footnote{34. UCC § 4-303 provides:}

\footnote{(1) Any . . . stop-order received by . . . a payor bank . . . comes too late . . . if the . . . stop-order . . . is received or served and a reasonable time for the bank to act thereon expires . . . after the bank has done any of the following:}

\footnote{(a) accepted or certified an item;}

\footnote{(b) paid the item in cash;}

\footnote{(c) settled for the item without reserving a right to revoke the settlement and without having such right under statute, clearing house rule or agreement;}

\footnote{(d) completed the process of posting the item to the indicated account of the drawer, maker or other person to be charged therewith or otherwise has evidenced by examination of such indicated account and by action its decision to pay the item; or}

\footnote{(e) become accountable for the amount of the item under subsection (1) (d) of Section 4-213 and Section 4-302 dealing with the payor bank's responsibility for late return of items.}

\footnote{35. UCC § 4-303(1) (d).}
the bank had taken action which would obligate it to pay? If finality was the goal, and the justification was protection of the credit of the drawee, then acceptance, certification, or payment as at common law, and "final settlement," or "late return," as added by the Code, are the only actions by the bank which should operate to preclude the drawer from stopping payment. The posting provisions appear to be purely for the convenience of the bank, at the expense of the customer.

Although the bank may not have taken any "4-303 action" on the instrument, the customer must still allow the bank a "reasonable opportunity" to act, as well as time for the notice to become effective. According to section 1-201(27), notice received by an "organization" is not effective until notice is brought to the attention of the person within the organization handling stop orders. The organization, of course, must act diligently in bringing the order to the attention of the person handling the transaction. If the notice is given to the cashier, and the tellers are the persons engaged in cashing checks, the notice does not become effective until it is "brought to the attention" of the tellers. This would seem to mean that the stop order would become effective only when the cashier, acting with due diligence, had a reasonable opportunity to notify the teller. The order becomes effective at this time whether or not the cashier actually informed the teller.

D. "(2) An oral order is binding upon the bank only for fourteen calendar days unless confirmed in writing within that period."

The Code allows the customer fourteen days to renew his oral

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37. Settlements under the Code may be provisional or final. See §4-104(1)(j). Settlement under §4-303(1) forecloses the right of the drawer to stop payment only when there remains no right to revoke, "under statute, clearing house rule or agreement." Until the settlement becomes final under §4-211(3), presumably it may be revoked by the payor bank under statutory right regardless of whether the right to revoke was retained. For example, if the remitting bank issues a banker's draft in settlement of an item, the remitting bank, as a customer of the payor bank on whom the draft is drawn, has the right to stop payment until the payor bank takes some action as described in §4-303. So long as the remitting bank can revoke, its customer has the right to issue a binding stop order. Hence, the type of remittance instrument and the authorization of the person receiving the remittance will determine finality in each instance. See §4-211. Compare Bohlig v. First Nat'l Bank, 233 Minn. 523, 48 N.W.2d 445 (1951).

38. The payor bank's responsibility for payment of an item in all events, arises not later than midnight of the banking day of receipt of the item. UCC §4-302(a). Hence, a return after that is a late return.
order by a written order. This appears more than a reasonable time for the customer to provide the bank with written notice, even if the customer is out of the country. A question arises whether the bank will follow the Code provision or shorten the period by agreement. Section 4-103 permits agreements which vary the provisions of Article 4—so long as the agreement does not disclaim the bank's responsibility for failure to exercise ordinary care or good faith. It seems unlikely that the bank could eliminate the oral order entirely, but shortening the effective period would not seem to violate the limitations of section 4-103.

The oral order may present administrative and customer relation problems for banks, but the Code places the risk of use of the oral order on the customer. He has the burden of proof under section 4-403 (3). With the burden of proof, the customer will have to convince the jury that the bank received the oral order. The customer who is aware of his burden will probably avoid the difficulty with corroborating evidence; others may find they are unable to recall the exact date and time, much less offer proof of such facts.

E. "A written order is effective for six months unless renewed in writing."

Prior to the Code, under similar statutory language requiring a six months written order, several courts held the writing requirement was intended to protect the banks. However, it could be waived by the bank's acceptance of an oral order. According to the Official Comment, section 4-403 (2) is intended to eliminate the possibility of waiver. The language, however, does not seem to require such

39. UCC § 4-103 (1), quoted in note 2 supra.
40. See notes 60 and 61 infra and accompanying text for a discussion of "4-103 agreements."
41. See note 51 infra and accompanying text for a discussion of UCC § 4-403 (3).
42. In Pankey v. First Nat'l Bank, 40 N.M. 270, 58 P.2d 1186 (1936), the bank was sued for slander of credit. The defense was receipt of an oral stop order. The court said that it was a matter for the jury to decide whether or not such order was given.
43. In Dinger v. Market Street Trust Co., 7 Pa. D. & C.2d 674 (Pa.C.P. 1956), the plaintiff alleged violation of oral stop payment orders. The bank filed an objection that the complaint did not sufficiently identify the persons within the bank to whom such orders were given. The court sustained the objection, on the grounds that the customer had the burden of proof under § 4-403 (3), and that identity was a necessary element of his claim.
45. Ibid.
46. See UCC § 4-403, Comment 6.
an interpretation. On the fourteenth day of an oral order, a customer might request, orally, that the stop order be renewed. If the bank agrees to honor the request, the pre-Code decisions might be used as authority for the application of estoppel, the bank having waived the statute's protection.47

The common law exacted accuracy in describing the instrument in the stop payment order. Failure to describe correctly a material part of the item was held fatal.48

While the Code contains no detailed specification of the contents of a stop order, section 4-403(1) does require that the order be “received at such time and in such manner as to afford the bank a reasonable opportunity to act . . . .” Surely, under this broad language, mere lack of formality will not affect the order's validity. Any accurate description should be sustained if it is sufficient to identify the instrument.49

Once the stop order has expired, no construction of the Code appears which would require inquiry by the bank before payment following expiration.50

II

PROOF OF LOSS

“(3) The burden of establishing the fact and amount of loss resulting from payment of an item contrary to a binding stop order is on the customer.”

When the bank has received a stop payment order within the time

47. See cases cited in note 44 supra.
49. Similarly, a description of personal property in a security agreement is sufficient if it “identifies what is described.” UCC § 9-110.
50. For a minority pre-Code decision, holding a bank liable for payment three years after date of instrument for failure to inquire after expiration of stop order, see Goldberg v. Manufacturer's Trust Co., 199 Misc. 167, 102 N.Y.S.2d 144, (Sup. Ct. 1951). The Comments to § 4-403 say that Goldberg is rejected by the Code.
limits and in proper form, and it pays a check by mistake, what are its rights and duties, and what action should it take?51

1. Normal procedure

At first blush the burden of proof rule seems to give the bank the "right" to charge the customer's account although the check was paid in violation of a stop payment order. And it seems to give the bank the "right" to refrain from reversing the charge until the customer establishes the fact and amount of his loss. The Code's definition of "the burden of establishing," however, would seem to confine the application of the rule to court actions:

'Burden of Establishing' a fact means the burden of persuading the triers of fact that the existence of the fact is more probable than its non-existence.52

A bank may charge its customer's account only with an item which is "properly payable"53 from the account.54 A stop order is a revocation of authority by the customer;55 if a bank has no authority to pay, it seems unlikely that the item could be said to be "properly payable."

Despite its lack of authority to charge the account, a bank would seem to have the "power" to do so. Certainly it is a matter completely within its control subject only to such deterrents as the Code may provide. There are two deterrents which may encourage reversal of the charge. First, in order to qualify for the right of subrogation to the rights of the holder, payee and drawer, the bank must have suf-

51. The bank's mistake will probably be discovered by the customer when he receives the bank's statement of his account. Must he notify the bank of its mistake? No provision of the Code requires it, but it might be successfully argued by the bank that the customer ratified their payment by failing to make a timely objection. See American Defense Soc'y v. Sherman Nat'l Bank, 225 N.Y. 506, 122 N.E. 695 (1919) (ratification by customer evidenced by acknowledgment of payment of debt); Woodmere Cedarhurst Corp. v. National City Bank, 157 Misc. 660, 284 N.Y. Supp. 238 (Sup. Ct. 1935) (ratification by customer evidenced by retention of benefit of payment); see also UCC § 4-403, Comment 8.

The customer, however, must bring his action for the improper charge within five years of the date of rendition of the account. N.M. Stat. Ann. § 48-10-10 (1953). Thereafter, the customer is precluded from questioning the account for any cause.

52. UCC § 1-201(8). (Emphasis added.)

53. UCC § 4-104(1)(i): "'Properly payable' includes the availability of funds for payment at the time of decision to pay or dishonor."

54. UCC § 4-401(1): "As against its customer, a bank may charge against his account any item which is otherwise properly payable from that account even though the charge creates an overdraft."

55. See cases cited in note 3 supra.
fered a "loss." If the bank refuses to re-credit the account, it has suffered no "loss" and can only await an action by the customer. Second, if the bank refuses to honor subsequent checks due to insufficient funds caused by the payment contrary to the stop order, it may be liable for damages for wrongful dishonor. Once the bank becomes entitled to subrogation rights, it may institute a single action against all parties to the check, thereby avoiding multiplicity of suits and the chance of inconsistent verdicts.

2. Procedure under a "4-103 agreement"

If the bank and customer have entered an agreement which includes an exculpatory clause, it seems unlikely that the bank will re-credit the unauthorized charge. Suppose the stop order agreement includes the following clause:

In the event of payment by the bank after receipt of a valid stop order, this bank shall be liable only for such loss as is the proximate result of its failure to exercise ordinary care or good faith.

56. UCC §4-407:
If a payor bank has paid an item over the stop payment order of the drawee or maker . . . [then] 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 shall be subrogated to the rights
(a) of any holder in due course on the item against the drawee or maker;
and
(b) of the payee or any other holder of the item against the drawee or maker either on the item or under the transaction out of which the item arose;
and
(c) of the drawee or maker against the payee or any other holder of the item with respect to the transaction out of which the item arose.

57. As the bank's conduct is unauthorized, after notice, refusal of subsequent checks may be characterized as "wrongful dishonor." Under § 4-402, the bank may be liable for actual damages, wrongful arrest and prosecution of the customer, and "other consequential damages."

Where two [2] or more persons are bound by contract, . . . including the parties to negotiable paper . . . and checks, . . . the action thereon may, at the option of the plaintiff, be brought against any or all of them . . .

59. Prior to the Code, the American Banker's Association recommended the following clause for stop orders:
In requesting you to stop payment of this item, the undersigned agrees to hold you harmless for all expenses and costs incurred by you on account of refusing payment thereof; and further agrees not to hold you liable on account of payment contrary to this request if same occur through inadvertence, accident, or oversight, or if by reason of such payment other items drawn by the undersigned are returned insufficient.

3 Paton's Digest 3474 (2d ed. 1944).
Such a clause appears proper in that agreements which vary the provisions of the Code are recognized so long as they do not disclaim the bank's responsibility for lack of good faith or ordinary care. Hence, whenever a bank decides it has exercised ordinary care in handling a stop order, it will retain the charge on the customer's account. The bank now has added assurance—lacking when no exculpatory clause protects them—of non-liability when it exercises ordinary care. Further, in order to establish ordinary care, the bank need only show that its conduct in handling the stop order was consistent with that of ordinary banks in the area. Proof of action or non-action consistent with "general banking usage" prima facie constitutes ordinary care.

Although the customer will have to institute the action for return of his funds, it is unlikely that he would have the burden of showing negligence of the bank. Of course, the customer will have the bur-

60. UCC § 4-103(1):

The effect of the provisions of this Article may be varied by agreement except that no agreement can disclaim a bank's responsibility for its own lack of good faith or failure to exercise ordinary care or can limit the measure of damages for such lack or failure; but the parties may by agreement determine the standards by which such responsibility is to be measured if such standards are not manifestly unreasonable.

Note that the pre-Code American Banker's Association draft would not meet the requirements of § 4-103(1).

61. UCC § 4-103(3):

Action or non-action approved by this Article or pursuant to Federal Reserve regulations or operating letters constitutes the exercise of ordinary care and, in the absence of special instructions, action or non-action consistent with clearing house rules and the like or with a general banking usage not disapproved by this Article, prima facie constitutes the exercise of ordinary care.


In Carroll, the customer sued the bank for its alleged negligence in paying a check against which a valid stop order had been issued. The bank denied negligence and, as a further defense, asserted a negligence disclaimer agreement. At trial, the customer introduced a letter from the bank in which it was stated that the bank had received the order two days before the check was paid by mistake. The trial court upheld the disclaimer agreement and entered judgment for the bank. On appeal, the court did not consider the disclaimer agreement, and reversed on the grounds that the bank had failed to sustain the burden of proof of its own due care:

[W]e think the admitted facts show a prima facie case of liability and the burden of producing evidence to overcome appellant's prima facie case by showing that it acted in good faith and used all reasonable efforts to comply with the instructions given rested on . . . [the bank]. It is not unreasonable to require the bank to explain the circumstances under which the check was paid. Appellant would not be expected to know these facts. She intrusted the bank with her funds and gave it exclusive possession and it has the exclusive means of knowing why it paid out appellant's funds contrary to her instructions. To require an explanation imposes no hardship. It is not necessary to resort to the
den of proof of the fact and the amount of his loss. But the ease of establishing a prima facie defense through banking custom, and the sole knowledge of the bank as to its internal procedure in handling the stop order, should lead the courts to impose the burden of coming forward on the bank. The customer may overcome the bank's prima facie case by showing that the custom is manifestly unreasonable or that the practice constitutes bad faith. As the customer's attack will be on the unreasonableness of custom involving internal procedures of banks, expert testimony probably will be needed to overcome the bank's prima facie case. But it is questionable whether expert testimony will be readily available to the customer.

Presumably, banks will take advantage of the Code's provisions allowing exculpatory clauses. If such clauses are sustained and become common, much of the customer protection accorded by section 4-403 will be dissipated. The section might just as well omit the restrictions and provide that the bank would be responsible for losses occurring only when the action of the bank failed to meet ordinary banking procedures. It should be noted that before the Code, only a minority of jurisdictions upheld "negligence disclaimer agreements"; certainly banking custom did not prima facie constitute ordinary care such as would release a bank from liability.

The doctrine of res ipsa loquitur . . . to sustain this view as to the burden of proof.

45 S.E.2d at 731.

The court cited a prior case involving a bailment and stated:

The plaintiff in that case brought an action to recover damages to a dinner coat which had been delivered to defendant to be cleaned and pressed. The Court held that when the plaintiff proved the delivery of the coat to the defendant in good condition and its return in a damaged condition, he made out a prima facie case and the burden then rested upon the defendant to offer evidence that it exercised ordinary care. The Court reached this conclusion upon the theory that the defendant had exclusive possession of the property and the facts attending the injury or damage to coat were peculiarly within its knowledge, and that the plaintiff could not be expected to know the details of defendant's business or the cause of the loss or damage. Of course, the relation there was that of bailor and bailee which does not exist in the instant case but there does exist substantially the same reason and necessity for imposing upon respondent the burden of explaining the transaction.

45 S.E.2d at 731-32.

See also McCormick, Evidence § 308 (1954).

63. UCC §4-103(1).


65. Due to the disclaimer agreements, the cases turn on the validity of such agreements rather than what might constitute ordinary care. See cases cited in note 64 supra and notes 66 and 67 infra.
The majority of states ruling on the matter held the negligence disclaimer agreements invalid as against public policy or as lacking consideration for the agreement.

The above discussion concerns court actions; when the amount involved does not make litigation feasible, the customer's position seems even more hazardous for obvious reasons.

CONCLUSION

Three things stand out as encroachments on the customer's rights as compared to pre-Code stop payment procedures and statutes: (1) the "sight-posting" limitation on timely presentation; (2) the power of the bank to avoid liability except for negligence; and (3) the custom of banks establishing a prima facie case of ordinary care in stop payment procedures. These changes may present such burdens as to justify their abolishment in favor of absolute liability for payment over a valid stop order. Surely, if the banks realized their liability for mistake was certain, their procedures would be more efficient. The corresponding increased administrative costs could be passed on as costs to those wishing to use the procedure. This seems more desirable than indirectly abolishing the right which well might be the result of the present Code provisions. Subrogation rights seem sufficient to protect the bank when it pays by error; perhaps imposition of costs and attorney fees on the customer in a successful subrogation action by the bank would be a further deterrent to abuse.

One might accept the sight posting limitation in return for recognition of an oral order; but section 4-103 and possible interpretations thereof makes the stop payment right conditional on the efficiency of the bank. This is the real objection to the Code handling of the customer's right to stop payment. If section 4-103 did not apply to section 4-403, the position of the bank and customer would generally be the same as at common law.

E. Richard Tanner, Jr.
