

Supreme Court No. 92483-0

(E.D. Washington Case No. CV-13-0409-JQL)

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IN THE SUPREME COURT  
OF THE STATE OF WASHINGTON

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TRAVELERS CASUALTY AND SURETY COMPANY OF AMERICA,  
as Assignee and Subrogee of Skils' Kin,

Plaintiff,

v.

WASHINGTON TRUST BANK,

Defendant

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***AMICUS CURIAE* BRIEF OF  
NORTHWEST CONSUMER LAW CENTER**

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## **I. INTEREST OF *AMICUS CURIAE***

Northwest Consumer Law Center (“NWCLC”) is a nonprofit law firm that represents low and moderate-income consumers in Washington State. The certified questions ask this Court to determine the respective rights and obligations of bank customers and banks with regard to frauds perpetrated on customer accounts. NWCLC has an interest in the Court’s resolution of the certified questions because it represents consumers, many of whom have bank accounts and are susceptible to frauds perpetrated against them. Also, NWCLC represents consumers with disabilities who would benefit from services provided by organizations like Skills’Kin as well as consumers who have been scammed by those targeting vulnerable populations.

## **II. CERTIFIED QUESTIONS**

Certified Question One: When a check (i) is presented for payment, (ii) bears no signature in the name of the payee on the back, and (iii) the drawee/payor bank pays the check over the counter, in cash, to an individual who is not the payee but who is an authorized signer on the account and who signs the back of the check in her own name, is the signature on the back of the check an “unauthorized signature,” “alteration,” or “unauthorized indorsement” as a matter of law imposing on the customer the notice requirements of RCW 62A.4-406(f)?

Certified Question Two: If the Answer to Question #1 is “Yes,” does providing a bank customer with a listing of the front of the checks and electronic access to images of the front and back of the checks via on-line banking make the “statement of account” and “items” reasonably available as required by 4-406(a)?

Certified Question Three: Does a bank fail to exercise ordinary care as a matter of law if it pays a check to a person other than the payee when the check contains no indorsement in the name of the payee?

### **III. ARGUMENT**

#### **A. The Court Should Construe the Provisions of the Uniform Commercial Code at Issue in Light of the Code’s Policies and Purposes**

By its text, the Uniform Commercial Code (“UCC” or “Code”) must be “liberally construed and applied to promote its underlying purposes and policies,” which include simplifying and clarifying the law governing commercial transactions and to promote the uniformity of commercial law. RCW 62A.1-103(a).

Construing and applying the Code to achieve simplicity, clarity, and uniformity in light of the statutory text is particularly important for financially disadvantaged members of society, including consumers and the nonprofit organizations who assist them. These consumers typically have limited or no access to sophisticated legal representation to guide

them through the intricacies of complex statutory texts like the UCC. At the same time, the UCC can have an enormous effect on these disadvantaged groups. Most individuals never have to deal with the rules surrounding the discovery and reporting of fraud on their bank accounts, yet when a fraud occurs, the effect can be devastating. The legal rules governing such situations should be clear and fixed to allow the victims to address such circumstances swiftly and accurately.

**B. To Assure Clarity, Simplicity, and Uniformity in the Commercial Law, the Court Should Answer the First Certified Question “No.”**

The first certified question turns on the text of RCW 62A.4-406(f). The text directs a customer to discover and report to its bank an alteration, unauthorized indorsement, or unauthorized customer signature on a check within certain time periods, and details the consequences if the customer does not make such a report. *Id.* Specifically, if the customer does not make a timely report, it is “precluded from asserting against the bank” the alteration, the unauthorized indorsement, or the customer’s unauthorized signature. *Id.*

Logically, RCW 62A.4-406(f) does not apply if the customer’s claim against the bank does not depend on an alteration, an unauthorized indorsement, or the customer’s unauthorized signature. The customer may theoretically be “precluded” from making such an assertion against the

bank, but the preclusion makes no difference if the customer's claim does not depend on the customer's ability to make the precluded assertion.

Travelers explains in its briefs why its claim against Washington Trust Bank ("WTB") for wrongful payment does not depend on any of the three statutory preclusions under RCW 62A.4-406(f). In deference to the statutory text and to promote clarity, simplicity, and uniformity in the law, the Court should apply the statute as written and hold that RCW 62A.4-406(f) does not apply in this case.

WTB does not accept Travelers' description of its own claim. As WTB summarizes its argument: "Travelers is precluded – whether it plans to or not – from asserting against WTB that Patterson's indorsement and signature was [sic] unauthorized." (WTB Brf., p. 29). The Court should not permit a bank to recast a customer's claim as WTB attempts to do here.

WTB's position raises more questions than it answers. What are the ramifications for a customer who is "precluded" from asserting an unauthorized indorsement against its bank when the customer does not intend to assert the alleged unauthorized indorsement when pursuing its claim? What is the purpose of precluding a customer from asserting an unauthorized indorsement if its claim does not depend on such an assertion? In this case, does Travelers have to prove an unauthorized

indorsement to prevail against WTB? If so, why? WTB's brief does not answer these questions, and its arguments certainly do not fulfill the statutory goals of clarity, simplicity, and uniformity in the law.

In its decision, for the benefit of bank customers and the banking industry alike, this Court should clarify certain fundamental principles of negotiable instrument law, including the following:

- A bank may only charge its customer's account for a check if the check is properly payable. If the bank charges its customer's account for a check that is not properly payable, the customer has a claim against the bank to recredit its account.

- A check is properly payable if the customer authorized the bank to pay the person whom the bank paid. In the case of a check, a customer authorizes the bank to pay the holder of the check. For a check payable to a specified payee (as opposed to cash), a payee or indorsee in possession of the check is the holder entitled to payment. A check is not properly payable to a person who is neither the payee nor indorsee.

- When a bank pays a check that is not properly payable, a bank sometimes has a defense to the customer's claim to recredit its account. Pertinent to this case, if the customer's claim that a check was not properly payable depends on an indorsement being unauthorized, then the

customer must timely discover and report that unauthorized indorsement to the bank under RCW 62A.4-406(f) to preserve its claim.

- A customer's claim depends on an indorsement being unauthorized when the bank (i) pays a presenter; (ii) who purports to be a holder because of the indorsement of a prior holder; but (iii) who is not actually a holder because the prior indorsement is unauthorized.

- A customer's claim to recredit does not depend on an indorsement being unauthorized when the drawee bank pays someone under the wrong assumption that the person receiving payment was the payee's agent. In such situations, either the bank properly paid a holder (i.e., the payee, who possessed the check through his agent) or the bank paid someone who was not a holder. This has nothing to do with indorsements.

Some examples in the consumer context illustrate these principles.

**Scenario 1.** Imagine a situation where Jane Doe hires John Smith, a plumber, to perform plumbing services at her home. Jane pays John by writing a check payable to "John Smith" and delivering the check to him. A few weeks later, Jane sees from her bank statement that her bank had paid the check and charged her account. The bank included a copy of the back of the check with her statement, which shows that the check had been indorsed in the name "John Smith" and deposited to a depository bank.

The depository bank had transferred the check to the Federal Reserve Bank, which in turn presented it for payment to Jane's bank. Upon receiving the check, Jane's bank debited Jane's account and paid the Federal Reserve Bank, which then paid the depository bank, which then credited the depositor's account.

If the depositor was a fraudster who had stolen the check from John and had fraudulently indorsed John's name on the back of the check, the check was not properly payable to the fraudster, and therefore not properly payable to the depository bank or to the Federal Reserve Bank. If Jane had to write a second check to John to pay her plumbing bill, she could seek recredit of her account from her bank for its payment of the first check.

In this scenario, Jane's claim depended on the fact that John's indorsement was unauthorized because her bank had paid the Federal Reserve Bank, which could only be a holder entitled to payment if all prior indorsements were authorized. To perfect her claim, therefore, she had to timely report the unauthorized indorsement to her bank under RCW 62A.4-406(f).

**Scenario 2.** Now imagine a different scenario where the fraudster simply went in person to a branch of Jane's bank and convinced the teller to cash John's check for him without any signature on the back, in

currency over the counter, without depositing the check. There are no intermediary collecting banks. Jane's bank paid the fraudster directly when he was not entitled to payment. Jane has a claim against her bank to recredit her account in this scenario too, but the claim has nothing to do with any unauthorized indorsement. Rather, the payment was wrongful simply because the bank paid someone who was not a holder of the check when there were no negotiations to intermediary holders by indorsement.

The result in Scenario 2 is the same even if the fraudster had signed his own name on the back of the check. Whether or not one characterizes his signature as an "indorsement," Jane's claim does not depend on the signature being unauthorized. The fraudster was not a holder of the check entitled to payment, whether or not his signature was authorized.

These principles appropriately respect the common understanding of the checking system held by average Americans. In Scenario 1, the fraudster only got Jane's money because he had forged John's indorsement. Between Jane's bank and Jane, Jane had the better opportunity to discover the forgery because Jane had the relationship with John—John was Jane's plumber but had no dealings with Jane's bank. If Jane did not timely tell her own bank about the forgery after learning the facts, she should bear the loss.

In Scenario 2, on the other hand, Jane's bank already knew, when it cashed the check, that it was handing John's money over to someone other than John. If the fraudster had insisted to the teller that John had authorized him to cash the check, reasonable people would expect that the teller would ask for a power of attorney or some other definitive proof that he was John's agent rather than a crook. Reasonable people expect a bank to refuse to cash a check, over the counter in currency, for someone other than the payee named on the check. The law should not require the customer to take the pointless step of formally notifying the bank that it had paid someone other than the payee when the bank knew that fact already from participating in the transaction itself.

As the court stated in *Ford Motor Credit Co. v. United Services Automobile Ass'n*, 1972 WL 20865, 11 UCC Rep. Sev. 361 (N.Y. Civ. Ct. 1972), "there is no 'notice' [that the customer] could have given at any time that would have been superior to that derived from even a cursory examination of the instrument by Chase's [the drawee bank's] employees." *Id.* Applying this principle to the present facts would promote clarity, simplicity, and uniformity of the law as directed by RCW 62A.1-103(a).

**C. Providing a Bank Customer with Electronic Images of the Front and Back of Checks Via Online Banking Does Not Make the Statement of Account Reasonably Available**

Certified Question Two asks whether sending a bank customer a statement with the listing of checks and separately providing electronic access to the images of the front and back of checks via online banking make the “statement of account” and “items” reasonably available as required by RCW 62A.4-406(a).

RCW 62A.4-406(a) only applies if the bank made both the statement and items available to the customer. Making items available through online access only was found to be not reasonably available by a New York court. *Elden v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, No. 08 Civ. 8738 (RJS), 2011 WL 1236141 (S.D.N.Y. Mar. 30, 2011). In *Elden*, the bank sent monthly paper statements to the customer that did not include any images of cancelled checks. *Id.* at \*1. While the bank offered online banking to its customers, the court held that online access did not make the items reasonably available to trigger the notice requirements of RCW 62A.4-406. *Id.* at \*6-7. It found that the online service was voluntary for customers, made “as an accommodation,” and “superfluous to the account statement.” *Id.* Similarly, holding statements for the customer at the bank does not satisfy the requirements of § 4-406(a). *See*

*First Citizens Bank of Clayton County v. All-Life of Georgia, Inc.*, 251 Ga. App. 484, 555 S.E.2d 1 (2001).

If the Court reaches the second certified question, it should hold that online access is not sufficient to trigger § 4-406 if the customer did not agree to receive the statement and items via online banking. While online banking has become more popular in certain segments of society, many individuals do not have access to online banking. The notice requirements in § 4-406 apply to ordinary consumers in addition to large businesses. Many consumers do not have computers, access to the Internet, or requisite computer skills to conduct online banking. Moreover, for those consumers who do have such abilities, online banking is still relatively new and viewed as an optional convenience rather than as a trigger of statutory duties that would preclude the customer from seeking recredit of his account in the event of a fraud.

By insisting that access to online images of cancelled checks automatically makes items “available” under the statute, regardless of the particular circumstances and capabilities of the customer and regardless of whether the customer even agreed to take advantage of the service to review cancelled items, WTB seeks to impose by judicial fiat an excessive burden on consumers that the legislature never contemplated when enacting § 4-406, long before the modern computer age.

In the present case, Skils'Kin had access to electronic banking but did not affirmatively agree to utilize the service for reviewing images of checks. As such, it should not be barred from pursuing its claims. The Court should hold that online access without such agreement by the customer does not meet the requirements of RCW 62A.4-406(a).

**D. WTB Failed to Exercise Ordinary Care as a Matter of Law when it Paid Checks to a Person Other than the Payee when the Check Contains No Indorsement In The Name of the Payee**

Certified Question Three asks whether a bank fails to exercise ordinary care as a matter of law when it pays a check with no payee indorsement to a person other than the payee.

RCW 62A.3-103(a)(7) defines ordinary care as “reasonable commercial standards, prevailing in the area in which the person is located, with respect to the business in which the person is engaged.” Paying checks to a person other than the payee is unreasonable as a matter of law.

While Patterson and Skils'Kin had limited authority to manage Skils'Kin client funds under the Representative Payee Program, Washington law has long been crystal clear that this did not imply that Skils'Kin or Patterson had authority to cash the checks. *See Coleman v. Seattle Nat'l Bank*, 109 Wash. 80, 81-85, 186 P. 275 (1919) (finding that an agent who had written authority to “transact any and all business” for

the principal did not have authority to indorse and transfer negotiable instruments of the principal); *California Stucco Co. of Wash. v. Marine Nat'l Bank*, 148 Wash. 341, 341-45, 268 P. 891 (1928) (finding that an employee's role as bookkeeper and cashier did not imply authority to indorse and cash checks; "If mere employment furnishes apparent authority to indorse checks, then no business would be safe"); *Toadvine v. Northwest Trust & State Bank*, 122 Wash. 609, 211 P. 286 (1922) (finding that a financial secretary who had express, written authority to "collect all moneys and pay the same to the treasurer" did not have implied authority to indorse and transfer checks payable to the treasurer).

Several courts have found conduct in similar factual situations to this case to be unreasonable as a matter of law. For example, courts have found payment of a check to a third party without inquiry by the bank to be commercially unreasonable as a matter of law. *See, e.g., Govoni & Sons v. Mechanics Bank*, 51 Mass. App. Ct. 35, 50-51, 742 N.E.2d 1094 (2001) ("This failure [to conduct a basic inquiry] invites fraud against both the [payee] and the bank's depositors, and is commercially unreasonable as a matter of law."); *Bank of S. Md. v. Robertson's Crab House*, 39 Md. App. 707, 389 A.2d 388 (1978) (finding the bank negligent as a matter of law when it disbursed depositor's funds to employee based only on the appearance of authority, without making any inquiry to depositor); *Master*

*Chemical Corp. v. Inkrott*, 55 Ohio St. 3d 23, 563 N.E.2d 26 (1990)  
(finding bank's policy of treating all transfers from one corporate account to another corporate account as presumptively correct, without inquiry with depositor, permitted theft from depositor's account and is more than negligent); *Olean Area Camp Fire Council, Inc. v. Olean Dresser Clark Fed. Credit Union*, 538 N.Y.S.2d 905, 142 Misc.2d 1049 (1989)  
(reasoning that accepting oral instructions of presenter, without inquiry to depositor, for disbursement of proceeds for checks payable to bank is negligence of the grossest kind).

Courts have also found that depositing checks into a personal account by an employee, when the check is payable to a corporation, to be commercially unreasonable as a matter of law. *See, e.g., Govoni & Sons v. Mechanics Bank*, 51 Mass. App. Ct. 35, 50-51, 742 N.E.2d 1094 (2001); *National Bank of Georgia v. Refrigerated Transport Co.*, 147 Ga. App. 240, 248 S.E.2d. 496 (1978) (finding the bank acted commercially unreasonable as a matter of law where the checks were not presented by the payee named thereon); *Aetna Casualty & Surety Co. v. Hepler State Bank*, 6 Kan. App. 2d. 543, 630 P.2d 721 (1981) (accepting deposits into a personal account for checks payable to corporate payee is commercially unreasonable); *O'Petro Energy Corp. v. Canadian State Bank*, 1992 OK

126, 837 P.2d 1391 (1992); *Pargas, Inc. v. Estate of Taylor*, 416 So.2d 1358, 34 UCC Rep.Serv. 1238 (1982).

Here, similar to the defendant bank in *Govoni*, WTB paid the checks to Patterson who was not the payee when the payees had not indorsed the checks. *See Govoni & Sons v. Mechanics Bank*, 51 Mass. App. Ct. 35, 742 N.E.2d 1094 (2001). Allowing Patterson to cash checks payable to others is similar to allowing an employee to deposit to his personal account a check payable to his corporate employer. Indeed, the present facts are much more egregious because the tellers delivered currency to Patterson, thus precluding any possibility of the check bouncing later during the collection process.

Moreover, in Washington, financial institutions have a role to play in preventing financial exploitation of the disabled, as evidenced by the permissive reporting statutes which enable bank employees to report suspected financial abuse. *See* RCW 74.34.035. Skils'Kin's clients are disabled adults who require assistance in managing their finances. The services Skils'Kin provides are essential as many vulnerable adults are unable to effectively manage their finances. Unfortunately, many scams target the disabled for this particular reason. Financial institutions should be particularly zealous in protecting the funds of the disadvantaged, such as those of Skils'Kin's clients. WTB undeniably breached this standard of

care by cashing Skills'Kin checks for Patterson without any documentation of her authority to conduct the transactions.

#### IV. CONCLUSION

For the foregoing reasons, NWCLC respectfully requests that this Court clarify that: (1) RCW 62A.4-406(f) does not preclude a claim where a non-payee signed her own name on the back of a check to document receipt of cash; (2) online banking does not make reasonably available the statement and items under RCW 62A.4-406(a) if the customer did not agree to receive statements and items via this method; and (3) a bank fails to exercise ordinary care as a matter of law when it pays a check that bears no indorsement of the payee to a third party.

DATED this 10th day of August, 2016.

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**DECLARATION OF SERVICE**

I, Olena Trofymchuk, certify under penalty of perjury under the laws of the State of Washington that on this day I caused a copy of the foregoing *Amicus Curiae* Memorandum of Northwest Consumer Law Center to be served by first-class mail, postage prepaid, upon the following counsel of record:

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