

## ARTICLE 4: BANK DEPOSITS AND COLLECTIONS

### SECTION 4-406. Customer's Duty to Discover and Report Unauthorized Signature or Alteration

HUBER GLASS CO. v. FIRST NAT'L BANK  
138 N.W.2d 157 (Wis. 1965)

Plaintiff maintained a checking account with the defendant. Plaintiff's president, R. C. Huber, and his wife were the only persons authorized to sign checks on the corporation's behalf. Plaintiff's bookkeeper, Miller, had forged thirty-eight checks drawn on the plaintiff's account over a three-year period. Miller alone had reconciled the account each month. Before the forgeries were discovered, Miller committed suicide. After their discovery, plaintiff commenced an action to recover the amount defendant had paid out on the forged checks. The trial court entered judgment for the plaintiff, finding as a matter of fact that the defendant had been "negligent in not detecting the forgeries" and that the plaintiff "was not negligent." The supreme court reversed.

Since the defendant had established that it had processed all checks in a prescribed manner, the court held that it had sustained its burden of showing that it had acted reasonably and diligently. In a footnote, the court noted that Section 4-406(3) of the Code now places the burden of proving a bank's negligence on a depositor.

The court also found that, even if the defendant had been negligent, plaintiff could recover only in the absence of negligence on its own part. The court held, moreover, that since plaintiff had never attempted to reconcile the bank account but had left this task solely to Miller, it had not acted reasonably. The court concluded that, as a minimum, plaintiff's duty included "(1) a comparison of the cancelled checks with the check stubs; (2) a comparison of the statement balance with the checkbook balance; and (3) a comparison of the returned checks with the checks listed on the statement."

### COMMENT

Basically, the liability of a bank under the Code for payment of a forged check is not dependent upon its or a customer's negligence; a bank which pays a forged check is absolutely liable for the amount of the check. Sections 4-401, -406(2), -406, Comment 4. Under Section 4-406(1), however, a customer is obliged to examine each bank statement when made available and to notify the bank promptly of any unauthorized items. If the bank establishes that the customer has failed to "comply with the duties imposed by" Section 4-406(1), the customer is generally *precluded* from asserting any unauthorized signature against the bank, Section 4-406(2), and thus from recovering the amount of any forged checks. Under Section 4-406(3), on the other hand, the preclusion of Section 4-406(2) will not apply if the customer establishes "lack of ordinary care on the part of the bank . . . ." This is in contrast with the instant case which held that, even if the

defendant bank had acted without due care, the plaintiff could not recover since he had been negligent.

Under this view, Section 4-406(4) becomes operative. That section provides: "Without regard to care or lack of care of either the customer or the bank," a customer who does not discover and report an unauthorized signature within one year "from the time of the statement" (three years for an unauthorized indorsement), "is precluded from asserting against the bank such unauthorized signature . . . ." This is to say that, assuming a customer does not comply with Section 4-406(1), but he does establish lack of ordinary care on the part of the bank, Section 4-406(3), the customer can recover only the amount of those forged checks which were returned to him during the year prior to discovery and report of the forgeries.

R.R.B.

## ARTICLE 5: LETTERS OF CREDIT

### SECTION 5-109. Issuer's Obligations to Its Customer

FAIR PAVILIONS, INC. v. FIRST NAT'L CITY BANK  
264 N.Y.S.2d 255 (App. Div. 1965)

Plaintiff Pavilions contracted to construct a building for Exhibitions at the World's Fair. The contract contained a provision for termination should specified occurrences come to pass. Exhibitions then contracted with Willard, pursuant to which Willard had the defendant bank issue an irrevocable letter of credit in favor of plaintiff. The letter provided that the credit could be cancelled after a certain date on receipt by defendant of an affidavit issued by an officer of Willard "to the effect that one or more of the events described in . . . [the termination provision of the contract between plaintiff and Exhibitions] has occurred." Before the final payment had been made to plaintiff, defendant received an affidavit stating that "one or more of the events . . . have occurred," and notified plaintiff that the credit had been terminated. None of the specified occurrences had in fact come to pass. Plaintiff then commenced an action for damages resulting from the cancellation of the credit. Defendant, in turn, moved for summary judgment, which the lower court denied.

The Appellate Division granted defendant's motion on the ground that, under the terms of the letter of credit, defendant could cancel the credit merely on receipt of the affidavit without making an investigation as to its accuracy. The court, citing Sections 5-109 and -115, determined that, although the letter of credit was by its terms irrevocable, with the result plaintiff's consent to any modification of its terms would have been required, defendant could be held only to its engagement and was therefore empowered to terminate the credit upon receipt of the affidavit from Willard.

### COMMENT

Although the court cited certain Code sections as applicable to the case, the result of the case could not be dependent upon these sections, since