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COMMERCIAL LAW--CONVERSION LIABILITY OF COLLECTING BANK TO PAYEE OF A NEGOTIABLE INSTRUMENT AND THE DEFENSE OF UNIFORM COMMERCIAL CODE SECTION 3-419(3)

*Cooper v. Union Bank*¹

Bernice Ruff had financial difficulties as a result of gambling debts. In 1963 she retained the services of an attorney, Joseph Stell, to represent her in litigation brought by her creditors. Not long thereafter Mr. Stell employed Miss Ruff as his secretary and bookkeeper. Between December 14, 1965, and February 20, 1967, Miss Ruff took 29 checks intended for her employer and forged the necessary endorsements. She cashed some of the checks and deposited the others in her own account. She withdrew all funds prior to the discovery of the forgeries.² Stell and his partners brought an action for conversion against the collecting and the payor banks.³ The California Court of Appeals affirmed a judgment for defendants,⁴ concluding that *Uniform Commercial Code* section 3-419(3)⁵ provides a complete defense for both collecting and payor banks so long as they act reasonably and in good faith.⁶ The Supreme Court of California affirmed the nonliability of the payor banks⁷ and

1. 9 Cal. 3d 371, 507 P.2d 609, 107 Cal. Rptr. 1 (1973).

2. Miss Ruff pleaded guilty to two counts of forgery.

3. A drawee/payor bank is the bank upon which the check is written. A collecting bank is any bank that handles the instrument prior to its receipt by the payor bank. UNIFORM COMMERCIAL CODE § 4-105.

4. *Cooper v. Union Bank*, 27 Cal. App. 3d 351, 103 Cal. Rptr. 610 (1972).

5. UNIFORM COMMERCIAL CODE § 3-419(3) provides:

Subject to the provisions of this Act concerning restrictive indorsements a representative, including a depository or collecting bank, who has in good faith and in accordance with the reasonable commercial standards applicable to the business of such representative dealt with an instrument or its proceeds on behalf of one who was not the true owner is not liable in conversion or otherwise to the true owner beyond the amount of any proceeds remaining in his hands.

The word "Code" is substituted for the word "Act" in the California statute.

6. Transferees of instruments with forged indorsements cannot claim to be holders in due course. Whaley, *Forgery and the Holder in Due Course: The Commercial Paper Puzzle*, 78 COM. L.J. 277 (1973).

7. The court disagreed with the lower court on the applicability of the defense of section 3-419(3) to payor banks. The supreme court found that the payor banks were not liable because the suit against the collecting banks operated as a ratification of the payment by the payor banks. In the three instances where there was no ratification the payor bank was allowed to utilize the defense of section 3-406, which provides:

Any person who by his negligence substantially contributes . . . to the making of an unauthorized signature is precluded from asserting the alteration or lack of authority . . . against a drawee or other payor who pays the instrument in good faith and in accordance with the reasonable commercial standards of the drawee's or payor's business (emphasis added).

the collecting banks for all instruments received after April 1, 1966;⁸ however, the court reversed the lower courts and held the collecting banks liable for checks handled before that date. The reversal rested upon an interpretation of *Uniform Commercial Code* section 3-419(3).

Two reasons were given for holding that section 3-419(3) does not limit the liability of collecting and depository banks. First, the banks had the proceeds. Under bank collection theory, when the payor bank transmits funds to the collecting bank in return for the forged instrument, it is transmitting its own funds. A suit for conversion against the collecting bank ratifies this transfer, so that the collecting bank holds the proceeds in a constructive trust for the payee. Because the payee has not ratified the transfer of funds to the forger, the money given to the forger is the bank's. The second reason for avoiding the defense was that the legislature did not intend to change pre-Code law holding collecting and depository banks liable to the payee.

Prior to the enactment of the *Uniform Commercial Code*, a majority of jurisdictions, including California and Missouri, held a collecting bank liable to the payee if the bank took a check upon an unauthorized endorsement.⁹ Sometimes this liability was for conversion,¹⁰ sometimes assumpsit.¹¹ A recent case said collecting banks are liable, but the theory behind the liability is unimportant.¹²

The *Uniform Commercial Code* followed pre-Code law in holding a collecting and depository bank liable to the payee for conversion if it pays a check which has not been validly endorsed.¹³ However, section 3-419(3)

8. The court relied on section 3-404 and the accompanying official comments. Section 3-404(1). Any unauthorized signature is wholly inoperative as that of the person whose name is signed unless he ratifies it or is *precluded from denying* it . . . (emphasis added).

Comment 4. The words "or is precluded from denying it" are . . . to recognize the negligence which precludes a denial of the signature.

This is a novel use of this section, and is discussed in 5 *RUTGERS CAMDEN L.J.* 319, 333-35 (1974). *But cf.* *Federal Deposit Ins. Corp. v. Marine Bank*, 431 F.2d 341, 344 (5th Cir. 1970) (applying Florida law) (defense of contributory negligence is not available in an action for conversion).

9. See cases collected in Annot., 100 A.L.R.2d 670 (1965).

10. *Kansas City Cas. Co. v. Westport Ave. Bank*, 191 Mo. App. 287, 177 S.W. 1092 (K.C. Ct. App. 1915).

11. *Universal Carloading & Distributing Co. v. South Side Bank*, 224 Mo. App. 876, 27 S.W.2d 768 (K.C. Ct. App. 1930); *Strong v. Missouri-Lincoln Tr. Co.*, 263 S.W. 1038 (St. L. Mo. App. 1924).

12. *Chemical Workers Basic Union v. Arnold Sav. Bank*, 411 S.W.2d 159 (Mo. En Banc 1966) (dictum).

13. *UNIFORM COMMERCIAL CODE* § 3-419(1)(c). An instrument is converted when it is paid on a forged indorsement. *Stone & Webster Eng. Corp. v. First Nat. Bank*, 345 Mass. 1, 6, 184 N.E.2d 358, 361 (1962); *Belmar Trucking Corp. v. American Trust Co.*, 65 Misc. 2d 31, 34, 316 N.Y.S.2d 247, 251 (Civ. Ct. 1970). See Annot., 23 A.L.R.3d 932, § 34 (c).

Although subsection (1)(c) says "forged indorsements," courts have interpreted this to include unauthorized indorsements. R. ANDERSON, 2 *ANDERSON ON THE UNIFORM COMMERCIAL CODE* 1034 (2d ed. 1971). An unauthorized signature includes a forgery. *UNIFORM COMMERCIAL CODE* § 1-201(43).

seemingly limits this liability¹⁴ to the remaining funds if the bank acts in good faith and in accordance with reasonable commercial standards.¹⁵ The prevailing rule prior to *Cooper* was that a collecting bank's liability to the true owner¹⁶ was reduced by whatever amounts were paid out.¹⁷ However, only one reported case¹⁸ has used section 3-419 (3) to deny relief to a payee. One well-known work attributes this paucity to deliberate manipulation by the courts.¹⁹ The most common method is to find that the bank did not act in a reasonable commercial manner,²⁰ although sometimes courts simply ignore the section.²¹ One court found that the bank was not a representative²² in the ordinary check handling situation. The state of the law prior to *Cooper* was that a collecting bank's liability could be limited if the requirements of section 3-419 (3) were met—but the courts rarely found that they were.

The defendant collecting and depository banks in *Cooper* asserted nonliability to the payee under section 3-419 (3)—i.e., no proceeds remaining in their hands. The lower courts sustained this defense, but the California Supreme Court, after redefining proceeds,²³ found that they retained the proceeds and thus were liable to the plaintiff. *Cooper* is a reversal of prior understanding, but not case law,²⁴ of the meaning of “pro-

14. A collecting bank may be liable to other banks under sections 3-417 and 4-207 even if no proceeds remain; but the payee cannot recover directly against the collecting bank under these warranty sections. See text accompanying notes 53-61 *infra*.

15. *Forman v. First Nat. Bank*, 320 N.Y.S.2d 648 (Sup. Ct. 1971) (dictum).

16. Section 3-419 speaks of the “true owner” of an instrument, rather than the payee, but for the purposes of this note, the terms are assumed to be synonymous.

17. “To the extent it pays cash over the counter to the thief it has no proceeds.” J. WHITE & R. SUMMERS, *UNIFORM COMMERCIAL CODE* 502 (1972) (hereinafter cited as WHITE & SUMMERS).

“Hence, a collecting bank which has remitted the proceeds of a check which has a forged indorsement would not be liable to the owner. . . .” Murray, *Negotiable Instruments*, 20 U. MIAMI L.R. 225, 237 (1965).

18. *Messeroff v. Kantor*, 261 So. 2d 553 (Fla. App. 1972).

19. So much for the work of the Code draftsmen. Thereafter, the courts have taken up section 3-419 (3), and what they have done to it shouldn't happen to a dog. The courts have ingeniously evaded the restrictions in 3-419 (3). . . .

WHITE & SUMMERS, *supra* note 17, at 504.

20. *Hermetic Refrig. Co. v. Central Valley Nat. Bank*, 493 F.2d 476 (1974); *Federal Deposit Ins. Corp. v. Marine Nat. Bank*, 431 F.2d 341 (5th Cir. 1970); *Belmar Trucking Corp. v. American Trust Co.*, 65 Misc. 2d 31, 316 N.Y.S.2d 247 (Civ. Ct. 1970); *Salsman v. National Community Bank*, 102 N.J. Super. 482, 246 A.2d 162 (1968), *aff'd*, 105 N.J. Super. 164, 251 A.2d 460 (1969).

21. *Harry H. White Lumber Co. v. Crocker-Citizens Nat. Bank*, 253 Cal. App. 2d 368, 61 Cal. Rptr. 381 (1967).

22. *Ervin v. Dauphin Deposit Trust Co.*, 38 Pa. D. & C.2d 473, 84 Dauph. 280 (C.P. 1965). *Cooper* also came to this conclusion.

23. The *Cooper* definition of proceeds is criticized in Note, 74 COLUM. L. REV. 104 (1974); Note, 5 RUTGERS-CAMDEN L.J. 319 (1974).

24. The only other case that has discussed the nature of “proceeds”, *Ervin v. Dauphin Deposit Trust Co.*, 38 Pa. D. & C.2d 473, 84 Dauph. 280 (C.P. 1965), came to the same conclusion as *Cooper*, namely, when a depository bank releases

ceeds" as used in section 3-419 (3). The effect of its definition of "proceeds" is that no matter how much the depository bank gives to the forger, the bank will still have all of the proceeds remaining in its hands.

The *Cooper* court began its analysis by asking two questions: "first, did [the depository banks] receive any proceeds and second, have they parted with any proceeds they may have received?"²⁵ In answer to the first, the suit brought by the payee against the depository bank ratified the collection of the proceeds from the payor bank; therefore, the defendant collecting banks did receive the proceeds. This answer is not controversial and is well-supported in case law. But the answer to the second question, the finding that the bank retained the proceeds even after releasing to the forger amounts equal to the proceeds, was not so obvious.

In support of its holding that the depository bank gave its own funds to the forger while retaining the proceeds, *Cooper* makes several points. There is the general point that ratification of the collection is not a ratification of delivery to the wrong person. And in the case of an instrument cashed over the counter,²⁶ the bank must be giving its own money because it has not yet collected the proceeds. As for an instrument deposited, the court relies on the doctrine of constructive trusts. The court said that agency ceases after the collection process is completed and the bank becomes a debtor to the true owner. The money collected is mingled with the bank's funds and thus the money received by the forger is the bank's money, while the bank holds the proceeds of the collected instrument in a constructive trust for the true owner.²⁷

The court's reasoning is open to criticism in several respects. First, the court assumes that "proceeds" is a word of art, with a highly technical meaning. The absence of any Code definition²⁸ would seem to negate this inference and suggest an ordinary meaning for the word. An ordinary understanding would be that once the depository bank gives value for the instrument and is in turn given value for the instrument by the payor bank, it has parted with the proceeds. Second, even assuming that "proceeds" has a technical meaning in the bank collection situation,

funds to a forger, it is giving away its own money, while the proceeds collected from the payor bank are held for the true owner. See also *United States v. Collins*, 464 F.2d 1163 (9th Cir. 1972) (no conversion since the bank paid its own money on a draft with a forged indorsement).

25. 9 Cal. 3d at 376, 507 P.2d at 609, 107 Cal. Rptr. at 5.

26. Some commentators have suggested that a bank is not a representative when it cashes a check (and therefore purchases the instrument with its own funds), but is when it accepts it for deposit. Farnsworth and Leary, *UGC Brief No. 10: Forgery and Alteration of Checks*, 14 PRAC. LAW. 75, 79 (March, 1968). *Ervin* rejected such a distinction. 38 D. & C.2d at 478, 84 Dauph. at 283, as did *Cooper*. 9 Cal. 3d at 380, 507 P.2d at 616, 107 Cal. Rptr. at 8. This rejection is criticized in Note, 74 COLUM. L. REV. 104 (1974).

27. 9 Cal. 3d at 379, 507 P.2d at 615, 107 Cal. Rptr. at 7.

28. "Proceeds" are not defined in Articles 3 or 4. The definition given in section 9-306 (1) does not apply.

the court's definition is questionable statutory construction because it is apparently irreconcilable with the language of section 3-419 (3). That subsection says liability for conversion is limited to the amount of proceeds remaining in the bank's hands; a clear implication that it is possible for no proceeds to remain in the bank's hands. Yet, under the *Cooper* definition, it is practically impossible for the depository bank not to have the proceeds remaining in its hands.²⁹ A final criticism of the court's "proceeds" argument is the lack of authority for its application of the constructive trust theory to the Code and to the forged endorsement situation.³⁰

On balance, whether *Cooper's* definition of proceeds is correct is a close question. On the one hand, it is supported by the only other court to face the issue³¹ and by the many pre-Code cases saying the proceeds are held in trust for the true owner.³² On the other hand, the *Cooper* definition makes section 3-419 (3) a nullity, which violates one of the first principles of statutory construction, namely, that a statute should be construed so as to give meaning to every part. The answer would seem to lie with the intent of the drafters and the legislators.

The California Supreme Court found no intent on the part of either draftsmen or the legislature to change the pre-Code law that collecting and depository banks are liable to the true owner for conversion if they take an instrument with a forged endorsement.³³ The court placed significance on the fact that section 3-419 (3) uses the ambiguous word "proceeds" instead of expressly absolving collecting and depository banks if they gave "value" for the instrument. The court went on to say that neither the draftsmen nor the legislature had any reason for making direct suits against the collecting and depository banks more difficult, because these banks will ultimately be liable anyway,³⁴ and that requiring uneconomical circuitry of action violates the purposes of the Code and creates "a significant potential for injustice."³⁵ Furthermore, the court pointed

29. The only time the bank will not have the full proceeds is when cash on hand goes below the face amount of the instrument.

30. The court relied on 5 R. SCOTT ON TRUSTS § 540 (3d ed. 1967) and *Jennings v. United States Fidelity and Guar. Co.*, 294 U.S. 216 (1935). An examination of *Scott* reveals that the treatise is concerned with the claims of depositors, creditors, etc., against a bank that has failed, not instruments collected upon a forged indorsement. Likewise, *Jennings* involved a bank failure and not a forged indorsement situation.

31. *Ervin v. Dauphin Deposit Trust Co.*, 38 Pa. D. & C. 2d 473, 84 Dauph. 280 (C.P. 1965).

32. Some pre-Code Missouri cases used the word "proceeds" in a similar way as used in *Cooper*. See *Strong v. Missouri-Lincoln Tr. Co.*, 263 S.W. 1038 (St. L. Mo. App. 1924); *Aetna Cas. & Surety Co. v. Lindell Tract Co.*, 348 S.W.2d 558 (St. L. Mo. App. 1961); *Chemical Workers Basic Union v. Arnold Sav. Bank*, 411 S.W.2d 159 (Mo. En Banc 1966). See also *United States Fidelity & Guar. Co. v. Fidelity Nat. Bank & Tr. Co.*, 232 Mo. App. 412, 109 S.W.2d 47 (K.C. Ct. App. 1937).

33. This is criticized in Note, 23 CATHOLIC U.L.REV. 163 (1973).

34. UNIFORM COMMERCIAL CODE §§ 4-207, 3-417.

35. 9 Cal. 3d at 382, 506 P.2d at 617, 107 Cal. Rptr. at 9.

out that the comments to section 3-419 (3) do not indicate any change in the law.³⁶ And finally, the court found that section 3-419 (3) was not meant to apply to the ordinary bank collection transaction,³⁷ because all of the illustrations and cases cited in the comments deal with the situation where an innocent broker sells stolen securities for his principal.

Criticism of the *Cooper* divination of legislative intent can focus on two areas; the weakness of the evidence supporting the "no-change" contention, and other evidence strongly suggesting that a change was meant.

To begin with, the court said the Code should and could have said "for value" instead of the ambiguous word "proceeds" if collecting and depositary banks are to be exonerated when they release funds to the forger. This assumes that "proceeds" is an ambiguous term. Prior to *Cooper*, however, there was no difficulty in understanding what "proceeds" meant. Even if "proceeds" is an ambiguous term, no special significance should be placed on bad draftsmanship.

The court also said there is no reason why the Code should present impediments to direct suit by the payee against collecting and depositary banks; therefore, there are no impediments. This argument overlooks the background against which the Code was drafted. Although most states allowed a payee to sue any bank which handled the instrument, a substantial number of states did not allow the payee to sue the drawee bank³⁸ and a few other states did not allow him to recover from collecting banks.³⁹ The Code does not explain why it was drafted in this way, but possibly there was a compromise on the issue. The draftsmen might have been influenced by the civil law.⁴⁰ At a more basic level, the interests of the banks might have influenced the draftsmen.⁴¹ The point is, there might have been many reasons why the Code modified the pre-Code rule.

Evidence of the function of section 3-419 (3) as a defense is found in Official Comment 6,⁴² which explicitly foresees that a collecting bank will

36. The court characterizes Official Comment 5 as saying that section 3-419 (3) is a codification of prior case law and California Comment 5 as saying the section is consistent with prior California law.

37. *Accord*, Comment, 45 U. COLO. L. REV. 281 (1974); Note, 25 HASTINGS L.J. 715 (1974).

38. California Code Comment 3 to § 3-419.

39. *Soderlin v. Marquette Nat. Bank*, 214 Minn. 408, 8 N.W.2d 331 (1943). This is still true in Louisiana. *Smith v. Louisiana Bank & Trust Co.*, 255 So.2d 816 (La. App. 1971).

40. For a comparison of Anglo-American and Continental law, see Kessler, *Forged Indorsements*, 47 YALE L.J. 863 (1938).

41. Beutel, *The Proposed Uniform [?] Commercial Code Should Not Be Adopted*, 61 YALE L.J. 334 (1954); *Allocation of Losses from Check Forgeries Under the Law of Negotiable Instruments and the Uniform Commercial Code*, 62 YALE L.J. 417, 469 (1953); WHITE & SUMMERS, *supra* note 17, at 505 n.18.

42. Official Comment 6 reads:

Thus a collecting bank might be liable to a drawee bank which had been subject to liability under this section, even though the collecting bank might not be liable directly to the owner of the instrument.

not always be liable to the payee, even though it will be liable to the drawee bank. This comment seems inconsistent with the *Cooper* definition of proceeds under which the collecting bank will *always* be liable to the true owner.

The court saw another indication that no change was intended in California Code Comment 5, which says section 3-419 (3) is consistent with prior California law.⁴³ But a reading of the full text of the comment erodes the comment's credibility, because it incorrectly summarizes the Code and prior California law as allowing good faith as a complete defense to conversion.⁴⁴ The court went on to find support in Official Comment 5⁴⁵ by characterizing it as saying that section 3-419 (3) is "merely a codification of prior decisions,"⁴⁶ and since the prior decisions referred to are cases of an investment broker selling stolen securities, section 3-419 (3) does not refer to the bank collection situation. But the comment does not say the section is a codification of prior case law. Rather, it says subsection (3) adopts the rule of decisions which limit a good faith representative's liability to the proceeds remaining in his hands. If the "decisions" referred to are investment broker cases which held an agent not liable after he turned the proceeds over to his principal, then it may be significant that the comment says "adopt the rule," rather than "adopt the decisions." Apparently, the draftsmen intended to extend the rule to the bank collection situation, because section 3-419 (3) defines a representative as including depository and collecting banks. An even more compelling argument that *Cooper* is wrong in limiting section 3-419 (3) to the investment broker situation is that investment securities⁴⁷ and the liability of brokers⁴⁸ thereon are covered by Article 8 of the Code and not Article 3.⁴⁹

The intent of the draftsmen to provide a defense to collecting and

43. California Code Comment 5 reads:

Subdivision (3) is new statutory law. Its basic premise that a person dealing in good faith with the property of another is not liable for conversion is consistent with prior California law on the tort of conversion.

The Missouri Code Comment reads: "Subsection (3) is new and is self-explanatory."

44. For example, *Cooper* held the collecting banks liable for conversion, even though the lower court "concluded that all defendants . . . had acted in good faith. . ." 9 Cal. 3d at 375-76, 507 P.2d at 613, 107 Cal. Rptr. at 5.

45. Official Comment 5 reads:

Subsection (3), which is new, is intended to adopt the rule of decisions which has held that a representative, such as a broker or depository bank, who deals with a negotiable instrument for his principal in good faith is not liable to the true owner for conversion of the instrument or otherwise, except that he may be compelled to turn over to the true owner the instrument itself or any proceeds of the instrument remaining in his hands. . . .

46. 9 Cal. 3d at 382, 507 P.2d at 617-18, 107 Cal. Rptr. at 10.

47. For a technical definition, see section 8-102.

48. UNIFORM COMMERCIAL CODE § 8-318 provides in part:

An agent . . . who in good faith . . . has received securities and sold, pledged, or delivered them according to the instructions of his principal is not liable for conversion . . . although the principal has no right to dispose of them.

49. UNIFORM COMMERCIAL CODE § 8-102 (b) provides in part: "A writing which

depository banks is clear. Official Comment 5⁵⁰ says section 3-419(3) adopts the rule of those cases which limit a representative's liability. Official Comment 6⁵¹ foresees that collecting banks will not be liable to the payee in some situations, even though the drawee bank will be. The very inclusion of the subdivision in the section on conversion and forged indorsements raises the natural inference that the limitation of liability applies to collecting and depository banks which handle instruments containing a forged indorsement.

Once it becomes evident that the draftsmen intended section 3-419(3) as a limitation on conversion liability, the proper definition of "proceeds" is obvious—the amount forwarded from the payor bank in exchange for the instrument less the amounts paid out to the forger. The *Cooper* definition cannot withstand close scrutiny, because it violates the intent of the draftsmen and the purpose of subdivision (3).

The bases for the *Cooper* interpretation of section 3-419(3) are unsound. The court did not, however, decide the case solely on the basis of statutory construction; it made a policy choice in favor of payees and against collecting banks.⁵² As a matter of policy, the court may well have been right. No commentator or court has praised the process whereby the payee sues the drawer,⁵³ who sues the drawee bank,⁵⁴ who sues the intermediary bank who sues the depository bank,⁵⁵ whereas several have condemned it.⁵⁶ Defenders of this circuitous method say it is necessary because the defenses which may not be available in a direct suit by the payee against the depository bank are available in the longer route.⁵⁷ The weakness of this argument is that most of the defenses spoken of are either

is a security is governed by this article and not by Uniform Commercial Code-Commercial Paper. . . ." UNIFORM COMMERCIAL CODE § 3-103(1): "This Article does not apply to . . . investment securities."

50. See note 45 *supra*.

51. See note 42 *supra*.

52. Apparently the interpretation of the Code as given in *Cooper* was entirely the court's own and was made without benefit of arguments and briefs of the opposing counsels. 5 RUTGERS CAMDEN L.J. 319, 321 n.15 (1974).

53. UNIFORM COMMERCIAL CODE § 3-804. The payee can also sue the drawee. UNIFORM COMMERCIAL CODE § 3-419(1).

54. See UNIFORM COMMERCIAL CODE § 4-401.

55. See UNIFORM COMMERCIAL CODE §§ 4-207, 3-417, describing the warranty of good title.

56. "[T]he Code unreasonably promotes circuity of action. . . ." "[N]eedless circuity of action." O'Malley, *Common Check Frauds and the Uniform Commercial Code*, 23 RUTGERS L. REV. 189, 267 (1969). Comment, *Allocation of Losses from Check Forgeries Under the Law of Negotiable Instruments and the Uniform Commercial Code*, 62 YALE L.J. 417, 471 (1953). Cf. Sales Promotion Executives Ass'n. v. Schlinger & Weiss, Inc., 234 N.Y.S.2d 785 (Civ. Ct. 1962) (pre-Code): "There's no need to cross the Mississippi by way of Siberia." *Id.* at 787.

57. O'Malley, *Common Check Frauds and the Uniform Commercial Code*, 23 RUTGERS L. REV. 189, 234 (1969). Cf. Dawson Textile Corp. v. Flatbush Check Cashing Serv., Inc., 69 Misc. 2d 293, 329 N.Y.S.2d 246 (Civ. Ct. 1972); Stone & Webster Eng. Corp. v. First Nat. Bank, 345 Mass. 1, 184 N.E.2d 358 (1962). However, in *Stone* the court said: "Cases where the payee has acquired rights in an instrument may stand on a different footing." *Id.* at 8, 184 N.E.2d at 363 n.4.

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available only when the drawer is the plaintiff⁵⁸ or are as readily available as a defense⁵⁹ by collecting and depositary banks as by any other defendant.⁶⁰ As a practical matter, the drawee banks might be located all across the nation and the expense of bringing suit in a distant forum might be so great, that the payee would have to bear the loss. The court felt this to be unjust, and more than one commentator has agreed that the better rule would be to allow direct suit.⁶¹

The *Cooper* definition of proceeds may be correct under bank collection theory, but it is obvious that the draftsmen of section 3-419 (3) had a broader definition in mind. The draftsmen intended to limit the conversion liability of collecting and depositary banks, a goal that cannot be achieved under *Cooper*. On the other hand, the Code is so complex that the court may have been correct in asserting that the legislature neither knew nor intended such a result. And as a matter of fairness and economy, the *Cooper* solution is superior to the Code.

Other courts will have to face this same problem and should consider two other relevant factors: uniformity and the true rule. Uniformity is the reason for the existence of the *Uniform Commercial Code*.⁶² Although it would be desirable for all courts to interpret the Code correctly, this will not happen; California is a precedent setter. Perhaps it would be better if all jurisdictions uniformly interpreted section 3-419 (3) incorrectly than to have a "majority rule" and a "minority rule." A second factor to consider is what could be called a "true rule." Although courts have said collecting and depositary banks can limit their conversion liability, the courts almost never allow them to do so. Perhaps it would be better to emasculate section 3-419 (3) openly than to do so by setting an impossible standard of reasonableness for banks. These two factors, plus sympathy for the payee, would lead a court to adopt the *Cooper* definition of proceeds.

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The banks prefer the circuitous route because it increases the likelihood of someone else shouldering the loss. On occasion the collecting bank will escape liability because the payor bank asserts a successful defense against the drawer under section 4-406. Other times the collecting bank will be able to defend successfully against the payor bank under sections 4-207 (4) and 4-406 (5). And often the payor bank will be in such a distant forum that the payee cannot afford to sue.

58. UNIFORM COMMERCIAL CODE § 4-406.

59. See, e.g., UNIFORM COMMERCIAL CODE § 1-201 (43) (an unauthorized indorsement means one without actual, implied, or apparent authority); § 3-404 (an unauthorized signature can be ratified).

60. WHITE & SUMMERS, *supra* note 17, at 503. For example in *Cooper* the collecting banks were in as good a position as anyone to show that the payee had been negligent, and were able to do so successfully.

61. 9 Cal. 3d at 382, 507 P.2d at 617, 107 Cal. Rptr. at 9. Funk, *The Fate of the Instrument in the Hands of the U.C.C.*, 87 BANKING L.J. 502, 507 (1970); WHITE & SUMMERS, *supra* note 17, at 505. Cf. Comment, 45 TEMP. L.Q. 102 (1971).

62. Schnader, *Looking Ahead at the Uniform Commercial Code*, 19 BUS. LAW. 771, 772 (1964); Schnader, *The New Movement Toward Uniformity in Commercial Law—The Uniform Commercial Code Marches On*, 13 BUS. LAW. 646, 655 (1958).