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Bills and Notes: Fictitious Payees: Negligence of Banks in Honoring Checks

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Wisconsin statute [WIS. STAT. (1937) § 85.01] is substantially like the Minnesota statute [MINN. STAT. (Mason, 1927) § 2677] and since the orthodox rules of bailments will very likely be applied in cases like this, it seems plausible to predict that the Wisconsin court will dispose of the case as the Minnesota court has done. Perhaps the registration statute could be amended to require that the certificate of title contain a specification of any bailor's title.

BILLS AND NOTES—FICTITIOUS PAYEES—NEGLIGENCE OF BANKS IN HONORING CHECKS.—The plaintiff board of education brought suit against the defendant bank for money paid out by the defendant and charged against the plaintiff's account on the ground that the payments were unlawful. The evidence disclosed that the plaintiff's clerk prepared the checks on which the money was paid out, and that he inserted the names of fictitious payees. He then procured the signature of the president of the board through the misrepresentation that they were to be used in payment of bills due the payees named. Thereupon for a period of a year and a half after indorsing on the back of each check the name of the fictitious payee, with the knowledge or consent of such person, he added his own name below that of the payee, proceeded to the bank and deposited the checks with the exception of three or four, to his individual account. The bank contended, that since the checks had been made to the order of fictitious payees, under Article 1, § 9(3) of the Negotiable Instruments Act they must be regarded as payable to bearer and that delivery to the bank by the clerk passed valid title. The lower court found for the plaintiff. On appeal by the bank, *held,* judgment affrmed, the court holding that in order for the statute to operate the fact that the payee was fictitious must be known to the person making the checks so payable. *Board of Education* v. *Nat'l. Union Bank,* (N.J. Sup. 1938) 196 Atl. 352.

The rule of the Negotiable Instruments Act that an instrument is payable to bearer "when it is payable to the order of a fictitious or non-existing person, and such fact was known to the person making it so payable," [WIS. STAT. (1937) § 116.13(3)], is intended partly for the protection of the drawee, partly for the protection of the holder, and partly for the protection of the person presenting the check to the drawee. 6 ZOLLMANN, BANKS AND BANKING (1936) § 3661; *McCormack* v. *Central State Bank,* 203 Iowa 833, 211 N.W. 542, 52 A.L.R. 1297 (1926). The cases all agree that it is the business of a bank to see to it that its depositor's moneys are expended according to his direction, and that every expenditure is at the bank's risk of the direction's being valid. *Citizen's Nat. Bank* v. *Importers' & Traders' Nat. Bank,* 119 N.Y. 195, 23 N.E. 540 (1890); *Bank of Hatfield* v. *Chatham,* 160 Ark. 564, 255 S.W. 31 (1923). Where a clerk of a city padded the payroll by issuing time slips in the names of fictitious persons, and he indorsed the name of the payee on each of the fraudulent checks, the city was held entitled to recover the amount of such checks from the drawee bank, on the ground that the fictitious nature of the payees was not known to the officials signing the checks so that the indorsements must be considered forged. *City of St. Paul* v. *Merchants Nat. Bank,* 151 Minn. 485, 187 N.W. 516 (1922). On behalf of the bank the strongest argument is that the payee is estopped to assert his right to recover in cases like the instant one. Where the dishonest agent has authority to draw checks and signs the principal's name the New York and Pennsylvania courts have held that the principal is to be charged with the knowledge of the agent in selecting a fictitious payee. *Phillips* v. *Mercantile Nat. Bank,* 140 N.Y. 556, 35 N.E. 982 (1894); *Snyder* v. *Corn Exchange*

Bank, 221 Pa. 599, 70 Atl. 876 (1908). A different rule prevails where the wrongful agent is a government official having authority under the treasury rules to draw instruments payable to the order of real persons only because if he draws it payable to a fictitious person and indorses the payee's name the depository bank will be charged with notice that the agent's authority is limited. *Nat. Bank of Commerce* v. *United State,* 224 Fed. 679 (C.C.A. 9th, 1915). Banks have also been allowed to recover in cases where the payee has himself been negligent. *Critten* v. *Chemical Nat. Bank,* 171 N.Y. 220, 63 N.E. 969 (1902); *California Vegetable U. Co.* v. *Crocker Nat. Bank,* 37 Cal. App. 743, 174 Pac. 920 (1918). Where monthly statements were furnished by the bank, together with the original checks, and no errors were reported therein for three years, the evidence is held sufficient to show neglignce on the part of the bank and to preclude a recovery by the drawee. *C. E. Erickson Company* v. *Iowa Nat. Bank,* 211 Iowa 495, 230 N.W. 342 (1930); *General Cigar Co.* v. *First Nat. Bank,* 290 Fed. 143 (C.C.A. 9th, 1923). The rule is not the same if the bank was itself negligent. *Wussow* v. *Badger State Bank,* 204 Wis. 467, 234 N.W. 720 (1930). In the cases holding the bank exempt from liability because of the plaintiff's negligence, it affirmatively appears that the bank was not negligent or the question of its negligence was not raised. In the instant case although the issue of negligence on the part of the drawer was raised, the court brushed it aside because there was no evidence that the board had any knowledge that the payees named were fictitious and therefore they could not have been put upon notice.

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BANKRUPTCY—PROCEEDINGS UNDER SECTION 74—PROPERTY OF DEBTOR IN CUSTODY OF AN OFFICER OF THE COURT.—In 1932 the debtor executed a bond and mortgage for $2700. After default judgment by confession was entered on the bond as prescribed by the local statutes. Thereafter a writ of execution was issued. The property was seized and advertised for sale. Prior to the sale the debtor filed a petition for an extension under Section 74 of the Bankruptcy Act. The mortgagee-creditor claimed under the seizure and contended that the court had no power to interfere with the seizure on behalf of the debtor because the property was not in the constructive possession of the debtor and bacause a final decree had been entered in the creditor's action. The court, in dismissing a petition for review of a report of the special master recommending that an order restraining the mortgagee from selling be made permanent, *held* that a state court's custody of the *res* cannot affect the bankruptcy court's jurisdiction and that since no sale had been confirmed no final decree had been entered within the meaning of Section 74. The court directed that the order to show cause why an injunction against the mortgagee should not issue be made absolute. *In re Krull,* 21 F. Supp. 377 (M.D. Pa. 1937).

Under the older provisions of the Bankruptcy Act, where the debtor is adjudged a bankrupt and his estate is to be liquidated, the bankruptcy court cannot interfere with foreclosure process begun by secured creditors outside the bankruptcy court and before the filing of any petition in bankruptcy by or against the debtor. *Straton* v. *New,* 283 U.S. 318, 51 Sup. Ct. 465, 75 L.ed. 1060 (1930). After a petition is filed by or against a debtor to have him adjudged a bankrupt then the bankruptcy court only has jurisdiction and no foreclosure suits may be started unless with the consent of the bankruptcy court. *Isaacs* v. *Hobbs T. & T. Co.,* 282 U.S. 738, 51 Sup. Ct. 270, 75 L.ed. 645 (1930). Section 74 was drawn apparently to afford jurisdiction to the bankruptcy court over the