The Case to Be Made for Proposed Article 4A of the Uniform Commercial Code: What's a Trillion Dollars between Friends?!

Michael I. Spak
Chicago-Kent College of Law
The Case to Be Made for Proposed Article 4A of the Uniform Commercial Code: What’s a Trillion Dollars between Friends?!

BY MICHAEL I. SPAK*

INTRODUCTION

As the title of this article indicates, over a trillion dollars is transferred electronically between business and financial institutions by means of what are referred to in the banking industry as "wholesale wire transfers.1" While many other types of financial transactions are extensively governed by existing state and federal law, there is no comprehensive body of law governing the rights and obligations of parties arising from these wire transfer transactions.2 Payments by check are covered under Articles 3 and 4 of the Uniform Commercial Code (U.C.C.), while many aspects of credit card transactions are covered by various state and federal laws, most notably the Electronic Funds Transfer Act of 1978 (EFTA),3 which addresses itself to a broad spectrum of consumer financial transactions, and the federal Truth in Lending laws.4

The only uniform legal rules that pertain to wholesale wire transfers are to be culled from four sources: (1) the regulations governing the two principal wire transfer systems in the United States, the Federal Reserve wire transfer network (Fedwire) and

---

* Professor of Law, IIT Chicago-Kent College of Law. B.S. 1958, J.D. 1961, DePaul University; LL.M. 1962, Northwestern University. The author acknowledges the highly original contributions of Jeffrey Eric Margulis, Esq., a member of the Illinois Bar. Funding for this article was provided by the Marshall Ewell Research Fund at IIT Chicago-Kent College of Law.


the New York Clearing House Interbank Payments Systems (CHIPS); (2) the uniform rules of various regional bank associations throughout the United States; (3) the rules of the National Automated Clearing House Association on credit transfers; and (4) Federal Reserve Bank rules and operating circulars. These uniform rules, however, only cover the limited technical aspects of these transactions and do not resolve broader issues which depend on such variables as the contract between the parties and the extent to which courts are willing to make an analogy to the law which governs similar types of payment mechanisms. There is, however, no consensus as to the rights and obligations created by the various wholesale wire transfer systems; Article 4A of the U.C.C. is designed to address the uncertainty in this area of the law.

Article 4A is precisely what is needed in this era of upheaval in the banking system. With the advent of proposed wholesale revisions to the federal banking laws, which would aim to increase interstate banking and open up investment banking opportunities to the nation's commercial banks heretofore barred under the Glass-Steagall Act, the frequency and volume of wire transfer activity can only increase. In order to handle this inevitable growth in wire transfer transactions, it is crucial to have a uniform set of rules in place to protect the justifiable expectations of the parties involved. There must be a predictable scheme of rules to enable parties to foresee and insure against risks, adjust operational and security procedures, and price funds transfers appropriately. This need for predictability is especially crucial when viewed in light of the increasing volume of money being moved through wire transfers. Article 4A is a coherent and effective response to the currently intractable legal issues that wire transfer activity creates. It strikes the appropriate balance among the competing interests of the banks providing funds transfer services, the commercial and institutional users of those services, and the public interest.

This Article first addresses the scope of Article 4A. Then a brief introduction to the fundamentals of Article 4A is presented.

\* \* \* 

5 See Prefatory Note, supra note 2, at iii; see also Miller & Davenport, Introduction to the Special Issue on the Uniform Commercial Code, 45 Bus. Law. 1389, 1391 (1990).
6 See Prefatory Note, supra note 2, at iii.
7 Id.
9 U.C.C. § 4A-102 comment.
10 See id.
11 See infra notes 15-37 and accompanying text.
to familiarize the reader with its operation. This Article concludes by arguing that Article 4A offers precisely the sort of guidance that courts are grappling for in dealing with the currently uncharted legal territory of wire transfer transactions.

I. SCOPE OF ARTICLE 4A

Article 4A defines its scope of operation by first stating that it generally applies to "funds transfers," which are defined as the series of transactions that begin with an "originator" making a "payment order" for the purpose of making a payment to a "beneficiary" of the order.

This seemingly broad scope is subsequently winnowed down to focus Article 4A's operation on a particular arena of funds transfer activity involving large amounts of money, highly sophisticated parties, and rapid transaction speed. First, Article 4A explicitly includes "credit transfer" transactions and explicitly excludes "debit transfer" transactions. The identity of the party giving instructions distinguishes these two transactions. In a credit transaction, the person making payment gives the instruction to pay, while in a debit transaction, the person receiving payment gives the instruction to pay. Thus, in a debit transaction the person receiving payment has been given authority by the debtor to draw on the debtor's bank account. Because of the different mechanisms employed in credit and debit transactions, the drafters were in accord that these two types of funds transfers should not be governed by the same statute.

Second, Article 4A is limited in its operation to funds transfer activity carried out by banking institutions, since a "funds transfer system," as defined by Article 4A, is a "wire transfer network,

---

12 See infra notes 38-411 and accompanying text.
13 See infra note 412 and accompanying text.
15 See U.C.C. § 4A-102.
16 See U.C.C. § 4A-104. For definitions of those terms, see infra notes 39-54 and accompanying text.
17 See Prefatory Note, supra note 2, at iii.
18 See U.C.C. § 4A-103(a)(1)(ii)-(iii); see also id. § 4A-104 comment 4; Prefatory Note, supra note 2, at iii.
19 U.C.C. § 4A-104 comment 4.
20 Id.
automated clearing house, or other communication system of a clearing house or other association of banks through which a payment order by a bank may be transmitted to the bank to which the order is addressed. Moreover, the fact that a payment order is defined in terms of "bank" payments indicates the restriction of Article 4A's scope to transactions within the banking system.

Also explicitly excluded from the scope of Article 4A are consumer transactions that contain any element governed by the EFTA. However, the drafters did envision resort to Article 4A by analogy, to resolve issues relating to parts of consumer transactions not covered by EFTA, where no other law governs the non-EFTA components of the transaction.

Additionally, transactions involving checks and credit cards are excised from Article 4A's reach. An Article 4A "payment order" must involve a payment instruction that is transmitted directly by the sender to the receiving bank. In check and credit card transactions, the payment instruction is transmitted from the sender to the beneficiary, who then presents the instruction for payment to the sender's bank, either directly or indirectly through the bank collection process. These transactions are already addressed in Articles 3 and 4 of the U.C.C. as well as federal law.

A final category of excluded transactions are those in which the payment instruction states a condition of payment other than the time of payment. Often, the presentation of documents is a payment condition, such as when the beneficiary of a letter of credit is entitled to payment only upon presentation of documents proving that goods have been shipped. Conditional payment instructions are not characteristic of the sort of high speed, low cost transactions that Article 4A was meant to embrace. This type of conditional payment instruction entails necessary delay in procuring

22 See U.C.C. § 4A-105(a)(5).
23 See id. § 4A-104 comment 2. Article 4A defines the term "bank" to include savings and loan institutions, credit unions, trust companies, and also Federal Reserve and foreign banks. See id. § 4A-105(a)(2) & comment 1.
24 See id. § 4A-108.
25 See id. § 4A-108 comment.
26 See id. § 4A-104 comment 5.
27 See id. § 4A-103(a)(1)(iii).
28 See id. § 4A-104 comment 5.
29 See id.
30 See id. § 4A-103(a)(1)(i).
31 See id. § 4A-104 comment 3.
32 See id.
documentation and imposes additional costs on the banks involved in authenticating such documentation.\(^3\) These slower, more expensive transactions are more appropriately treated under other applicable law, such as Article 5 of the U.C.C., which governs letters of credit.\(^4\)

One additional aspect of the scope of Article 4A concerns the importance (or rather non-importance) of the "medium" by which a funds transfer is effected.\(^5\) While most of the funds transfer activity contemplated by Article 4A is done electronically by means of wire transmission, the employment of electronic means of transfer is not a predicate to the applicability of Article 4A.\(^6\) Article 4A recognizes transmission of a payment instruction from the sender to the receiving bank by oral or written communication.\(^7\)

II. THE FUNDAMENTALS OF ARTICLE 4A

A. The Payment Order

Article 4A's\(^8\) central theme is the "payment order," which begins the funds transfer process. A payment order must possess a number of essential elements to be subject to Article 4A. First, it must be an instruction given by the sender to the receiving bank to pay, or cause another bank to pay, a "fixed or determinable amount of money to a beneficiary."\(^9\) Since the drafters did not comment regarding any special treatment to be given the requirement of "fixed or determinable," it should be interpreted along the same lines as it is construed under Article 3 of the U.C.C.\(^10\) Thus, so long as the amount to be paid is calculable by some formula (i.e., foreign currency conversion or interest rate specified) then the amount is "fixed and determinable" within the meaning of Article 4A.

---

\(^3\) See id.
\(^4\) See id. §§ 5-101 to 5-117 (comprising Article 5).
\(^5\) See id. § 4A-104 comment 6.
\(^6\) See id.
\(^7\) See id.
\(^9\) See id. § 4A-103(a)(1).
\(^10\) See Fry, supra note 21, at 1408 n.38 (commenting on the meaning to be given Article 4A's "fixed or determinable" requirement for payment order amounts by referring to U.C.C. § 3-104(a)'s requirement of "a fixed or readily ascertainable amount of money," and U.C.C. § 3-104(b)'s requirement of a promise or order to pay "a sum certain in money").
An Article 4A payment order must meet several additional requirements: (1) the order must state no condition for payment other than the time at which it is to be made;\(^{41}\) (2) the transaction involved must be a credit transfer and not a debit transfer;\(^{42}\) and (3) it must entail an instruction transmitted by the sender directly to the receiving bank or to an agent or funds transfer system for transmittal to the receiving bank.\(^ {43}\) The reader should note that the elements of the payment order are directly tied in to the scope of Article 4A.\(^ {44}\) Thus, the careful practitioner must be certain to meet each and every one of these requisites to ensure the application of Article 4A's provisions.

B. *The Cast of Characters*

The funds transfer process begins with the "sender," the person that sets the wheels in motion by instructing the receiving bank with a payment order.\(^ {45}\) On some occasions, the sender may be the same person as the beneficiary of the payment. For example, a corporation that ordered a bank to transfer funds from one of its accounts to another at that or another bank would be both a sender and a beneficiary.\(^ {46}\)

The "receiving bank" is defined as the bank to which the sender's payment order is addressed.\(^ {47}\) A receiving bank may also become a sender when it carries out a sender's payment order by transmitting a second payment order to another bank requesting a payment to be made to the person specified in the original sender's payment order.\(^ {48}\) The process can continue in a chain of transactions, where a number of banks receive and in turn send payment orders to other banks to execute the original payment order. Each bank that receives a payment order and then issues its own payment order to effectuate the first one acts as both a receiving bank and a sender within the meaning of Article 4A.

Also involved in this process is the "originator." The originator is defined in Article 4A as "the sender of the first payment order

\(^{41}\) See U.C.C. § 4A-103(a)(1)(i).
\(^{42}\) See id. § 4A-103(a)(1)(ii); id. § 4A-104 comment 4.
\(^{43}\) See id. § 4A-103(a)(1)(iii); id. § 4A-104 comment 5.
\(^{44}\) See supra notes 15-37 and accompanying text.
\(^{45}\) See U.C.C. § 4A-103(a)(2).
\(^{46}\) See id. § 4A-104 comment 1.
\(^{47}\) See id. § 4A-103(a)(4).
\(^{48}\) See id. § 4A-104 comment 1 (providing illustrative cases).
in a funds transfer.\textsuperscript{49} In the payment order chain scenario discussed above, there can be any number of senders involved, but only the sender of the first payment order in the chain can be the originator.

Along with the originator, Article 4A also defines the role of the "originator's bank." The originator's bank is "(i) the receiving bank to which the payment order of the originator is issued if the originator is not a bank, or (ii) the originator if the originator is a bank."\textsuperscript{50}

Another definitional distinction drawn by Article 4A is found in the term "intermediary bank." The intermediary bank is any bank in the chain of the transaction other than the originator's bank or the beneficiary's bank.\textsuperscript{51} Thus, in any transaction where either the originator's bank is the same bank as the beneficiary's bank or the originator's bank sends a payment order directly to the beneficiary's bank, there are no intermediary banks involved.\textsuperscript{52}

At the end of the chain of banks involved in the funds transfer transaction is the "beneficiary's bank." Article 4A defines this bank as the "bank identified in a payment order in which an account of the beneficiary is to be credited pursuant to the order or which otherwise is to make payment to the beneficiary if the order does not provide for payment to an account."\textsuperscript{53} In other words, the beneficiary's bank is the bank that is directed to or in fact does give the beneficiary the money due from the payment order.

Another important actor in this transactional drama is the "beneficiary." Article 4A defines the beneficiary as "the person to be paid by the beneficiary's bank."\textsuperscript{54} This seems a bit of a circular way to refer to this most crucial character in the transaction. Perhaps a more helpful definition would characterize the beneficiary as the person whom the originator intends to pay when he transmits the payment order to the receiving bank.

Article 4A mentions the "customer" as another character in its schematic. A customer is "a person, including a bank, having an account with a bank or from whom a bank has agreed to

\textsuperscript{49} See id. § 4A-104(c).
\textsuperscript{50} Id. § 4A-104(d).
\textsuperscript{51} See id. § 4A-104(b).
\textsuperscript{52} See Fry, supra note 21, at 1413.
\textsuperscript{53} U.C.C. § 4A-103(a)(3).
\textsuperscript{54} Id. § 4A-103(a)(2).
receive payment orders. Thus a customer can be a person that has a standing agreement with a bank for the execution of the customer's payment orders or, simply, any other person without such a standing agreement that approaches a bank and requests that his payment order be executed.

Tied in with the role of the customer is the "authorized account," also provided for in Article 4A. The authorized account is a deposit account of the customer that is designated by the customer as the source of funds for his payment order(s). If the customer does not designate an authorized account, any account of the customer at the bank will be an authorized account for the purposes of Article 4A, so long as such usage would be consonant with any restrictions previously agreed to by the customer and the bank regarding use of that account. The drafters of Article 4A were persuaded by wire transfer users that the customer should be able to specify the account to be used for payment order funding since specification would be instrumental in guarding against any unauthorized use of payment orders by means of accessing other customer accounts at a bank.

One caveat to this description of the funds transfer process must be made regarding requests by an originator to make more than one payment to a beneficiary. Where, for example, an originator instructs a bank to make payments to X at regular intervals for a continuing service or regular shipments of goods, the blanket payment instruction to the bank is treated by Article 4A as a separate payment order with respect to each payment made to the named beneficiary.

The funds transfer user that sends payment orders (or any cancellation/amendments thereto) to a receiving bank by means of a funds transfer system or other third party communications network should also be aware that such intermediaries are not liable, under Article 4A, for mistransmission of the sender's payment order. The funds transfer system or third party communications system is deemed to be an agent of the sender under Article 4A.

55 Id. § 4A-105(a)(3).
56 See Fry, supra note 21, at 1422 & n.112.
57 See U.C.C. § 4A-105(a)(1).
58 See id.
59 See Fry, supra note 21, at 1421.
60 See U.C.C. § 4A-103(b).
Thus, liability for mistransmission, if any, must be determined by resort to agency law.\textsuperscript{61}

Now that the reader has been familiarized with the parties to the funds transfer transaction, an analysis of the process itself is in order.

C. The Funds Transfer Process

The process begins when the sender gives the payment order to the receiving bank. At this point, the sender has made what Article 4A refers to as a "request" to the bank to execute the payment order.\textsuperscript{62} The request can either be accepted or rejected, unless the bank has agreed to accept such payment orders or a funds transfer system rule requires acceptance.\textsuperscript{63} The duties and obligations incumbent upon a receiving bank do not begin until the bank chooses to accept the payment order.\textsuperscript{64} During the pre-acceptance period, however, the receiving bank may be liable for lost interest to the sender for delay in giving notice of rejection of the payment order past the requested payment date.\textsuperscript{65}

The acceptance of a payment order by a receiving bank can occur in a variety of ways under Article 4A, as the discussion below explains.

1. Acceptance by the Receiving Bank When the Receiving Bank is Not the Beneficiary's Bank

When the receiving bank is not the same bank as the beneficiary's bank, the receiving bank manifests acceptance under Article 4A when it executes the payment order.\textsuperscript{66} An understanding of such acceptance depends on a proper explanation of payment order execution.

Execution occurs when the receiving bank issues a payment order to carry out the payment order given to it by the sender.\textsuperscript{67} When a bank executes a payment order it incurs the following

\textsuperscript{61} See id. § 4A-206; see also Baxter & Bhala, The Interrelationship of Article 4A With Other Law, 45 Bus. Law. 1485, 1500-01 (1990) (discussing the application of agency law to this problem).

\textsuperscript{62} See U.C.C. § 4A-209 comment 1.

\textsuperscript{63} See id., comment 3.

\textsuperscript{64} See id. § 4A-212.

\textsuperscript{65} See id. § 4A-209(b)(3), § 4A-212 comment.

\textsuperscript{66} See id. § 4A-209(a).

\textsuperscript{67} See id. § 4A-301(a).
obligations under Article 4A: (1) it must issue a payment order that complies with the sender's order and follows the sender's instructions regarding (i) the medium to be used for carrying out the funds transfer or (ii) the means by which funds are to be transmitted; (2) it must advise any intermediary bank involved in the funds transfer about the instructions of the original sender; (3) in cases where the sender indicates a desire for the transaction to be carried out by telephone or wire transfer, or otherwise asks for the most expeditious means of transfer, the receiving bank must employ such means and instruct any intermediary banks to do the same; and (4) the receiving bank must transmit its payment order in sufficient time to allow payment to the beneficiary on the sender's requested payment date, if any, or as soon thereafter as is feasible.68

If the receiving bank executes the payment order before the sender's requested payment date, resulting in payment to the beneficiary before the requested payment date, acceptance will not occur until the requested payment date.69 Thus, the sender will not be required to pay the receiving bank until the requested payment date, even though the receiving bank may be required to pay before that date for the payment order it issued in executing the sender's payment order.70 Such an occurrence would result in a loss of interest to the receiving bank. Moreover, if the bank executes early, it risks cancellation of or amendment to the payment order by the sender; in the event of a cancellation by the sender, the sender will not be obliged to pay the receiving bank, but the receiving bank will have to resort to the law of mistake and restitution to recover its money from the beneficiary it paid prematurely.71 Thus a prime concern for banks' counsel under Article 4A will be avoidance of this early execution trap since Article 4A places the risk of loss on the banks.72

2. Acceptance by the Receiving Bank When the Receiving Bank is Also the Beneficiary's Bank

When the receiving bank is also the beneficiary's bank, acceptance of the sender's payment order does not occur through exe-
cution. This can be explained by reference to the differing functions of the receiving bank and the beneficiary bank in the funds transfer process. The receiving bank accepts by issuing a payment order of its own complying with the sender’s payment order. The beneficiary bank, however, generally accepts by crediting the beneficiary’s account with the proceeds of the incoming payment order and notifying the beneficiary. This difference explains the separate treatment of acceptance by beneficiary banks and non-beneficiary banks in the funds transfer process.

Article 4A provides three means by which the beneficiary bank can be said to have accepted the payment order it has received from either the receiving bank or an intermediary bank, with acceptance occurring at the earliest of the three.

First, acceptance by the beneficiary bank can occur upon the beneficiary bank either (a) making payment to the beneficiary’s account or (b) notifying the beneficiary of either (1) the receipt of the payment order or (2) of the account being credited as a result of the order’s receipt. Notice of receipt of the order, however, will not operate as acceptance if the notice specifies that the order has been rejected or that funds may not be withdrawn until the sender’s payment has been received.

Second, acceptance by the beneficiary bank can occur when the beneficiary bank receives payment of the entire amount of the sender’s order. This provision of Article 4A is applicable when the beneficiary bank mistakenly credits the account of the wrong person with the payment from the sender. In such a case, the bank will be deemed to have accepted by virtue of having received payment. Thus, the beneficiary bank will have to pay the correct beneficiary and resort to the law of mistake and restitution to recover any losses sustained.

Third, and finally, the beneficiary bank may also accept by its inaction. The beneficiary bank will be deemed to have accepted

---

73 See id. § 4A-301 comment 1.
74 See id. § 4A-209 comment 4.
75 See supra notes 66-72 and accompanying text.
76 See U.C.C. § 4A-209 comment 4.
77 See id. § 4A-209(b).
78 See id. § 4A-209(b)(1) & comment 5.
79 See id. § 4A-209(b)(1).
80 See id. § 4A-209(b)(2).
81 See id. § 4A-209 comment 6.
82 See id. § 4A-209 comment 7.
if, at the opening of business on the next funds-transfer business
day following the payment date of the sender's payment order, either (a) the amount of the sender's payment order is covered by
a withdrawable sum in an authorized account of the sender or
(b) the beneficiary bank has received full payment from the sender. Acceptance is created by inaction, provided that the order was not rejected by the beneficiary bank within the allowable time limits for rejection under Article 4A.

Thus, for receiving banks and beneficiary banks to accept a payment order and thereby incur the rights and obligations that result under Article 4A, there are two distinct means of acceptance. For receiving banks, acceptance is generally accomplished by execution of the sender's payment order through issuing its own payment order in compliance. For beneficiary banks, acceptance is accomplished either by (i) payment or notice of receipt to the

---

83 Article 4A defines “funds-transfer business day” as that part of the day during which the receiving bank is open for the receipt, processing, and transmittal of payment orders and cancellations and amendments of payment orders. See id. § 4A-105(a)(4). While a bank's computer can be programmed to receive payment orders and payment order instructions 24 hours a day year-round, the bank may not necessarily be open at the time the computer receives an order or instruction. See id. § 4A-105 comment 2. In that case, the computer will be programmed to store the order or instruction until the beginning of the next funds-transfer business day when it will be retrieved from the computer and acted upon. Id. Moreover, the receiving bank also has the discretion to fix cut-off times during its designated funds-transfer business day, after which orders or instructions may be treated as having been received at the opening of business on the next funds-transfer business day. See id. § 4A-106(a). The receiving bank may establish different cut-off times for payment orders as opposed to payment order instructions as well as different times for different senders and categories of payment orders. See id.

Although there was some concern among members of the drafting committee that worked on Article 4A as to potential delay in payment order action resulting from the discretion vested in the receiving banks to fix their designated funds-transfer business day and cut-off times, this discretion was left unfettered. See Fry, supra note 21, at 1423 n.123. The sentiment of the consensus was that the competitive pressures to keep and retain funds-transfer business, plus the industry practice of accommodating time-sensitive funds transfer requests, would prevent any excessive delay for funds transfer users. See id.

84 See supra notes 51-59 and accompanying text (explaining authorized accounts under Article 4A).

85 See U.C.C. § 4A-209(b)(3) & comment 7. As the comments explain, this provision was written bearing in mind that banks often cannot know how much money will be left in a customer's bank account after numerous transactions pertaining to that account have taken place during a business day. Thus, the verifiable balance will be determined as of the opening of business on the first funds-transfer business day following the payment date of the sender's order.

86 See id. Article 4A provides that the beneficiary bank has the power to prevent this automatic acceptance by means of rejecting the order. See infra notes 88-112 and accompanying text (discussing rejection).
beneficiary; (ii) receipt of the full amount of the payment order; or (iii) inaction if the sender’s account is sufficient to cover the balance of his payment order.\(^{87}\)

3. Rejection of the Payment Order

Article 4A also provides receiving banks that are also beneficiary banks an effective means by which to avoid acceptance and its resulting obligations. The provided means is a “rejection” of the payment order. Rejection is not necessary for the prevention of acceptance by a receiving bank that is not also the beneficiary bank to a transaction. Such a bank can only accept by execution through issuance of its own payment order in compliance with the sender’s payment order.\(^{88}\) A receiving bank that is also the beneficiary bank, however, can be deemed to have accepted by inaction,\(^{89}\) so rejection offers these banks a means by which they can affirmatively act to defeat this automatic acceptance.\(^{90}\) Also, even though it is not required of them, receiving banks that are not also beneficiary banks routinely will give notice of rejection for a variety of reasons (e.g., ambiguity in the payment order, technical problems at the receiving bank, or insufficient funds in the sender’s account).\(^{91}\)

Rejection can be accomplished by a notice of rejection, transmitted to the sender orally, electronically, or in writing.\(^{92}\) There is no requirement that the notice of rejection use any magic words. It is effective if it communicates to the sender that the order will not be executed or paid.\(^{93}\) Transmission of the notice of rejection must be by a means that is reasonable under the circumstances, otherwise it will not be effective until it is received.\(^{94}\) If the method of transmitting rejection notices is specified by agreement of the parties, it will be considered reasonable. Any noncomplying mode will be deemed unreasonable, unless no significant delay results from its use.\(^{95}\)

\(^{87}\) See U.C.C. § 4A-209(b).
\(^{88}\) See id. § 4A-210 comment 1.
\(^{89}\) See supra notes 82-86 and accompanying text.
\(^{90}\) See U.C.C. § 4A-210 comment 2.
\(^{91}\) See id. § 4A-210 comment 1.
\(^{92}\) See id. § 4A-210(a).
\(^{93}\) See id.
\(^{94}\) See id.
\(^{95}\) See id.
Thus for the beneficiary bank wishing to reject an incoming payment order, a notice of rejection will be necessary to prevent the automatic acceptance envisioned by Article 4A. Such rejection to prevent automatic acceptance must occur either before or within one hour of the time that automatic acceptance occurs under the rules. This means that a beneficiary bank's deadline for an effective rejection will be fixed at one hour from the opening of the first funds-transfer business day following the payment date of the payment order. In cases where such notice is not feasible, there is the alternative deadline of one hour from the opening of the business day of the sender. For example, if the sender is in California and the beneficiary bank is in New York, and the sender would not be open for business to receive a rejection notice until several hours had elapsed from the opening of the New York bank's funds-transfer business day, the latter deadline could be used to protect the New York bank.

Despite this alternative deadline, if the sender receives the notice of rejection after the requested payment date, the bank must pay interest to the sender if the sender's account is non-interest bearing. The interest is to be paid for each day that receipt of the rejection notice is delayed beyond the payment date, and its rate is calculated on the basis of either (i) the agreement of the parties or (ii) any applicable funds transfer system rules. In the event that there is neither a contract nor an applicable funds transfer system rule, a further provision of Article 4A details a somewhat complex formula, based on the Federal Funds rate and the number of days the notice of rejection arrives beyond the requested payment date.

While, as noted above, receiving banks that are not also the beneficiary bank need not issue a notice of rejection to prevent

---

96 See id. § 4A-209 comment 8.
97 See id.; see also supra notes 82-86 and accompanying text (discussing the definition of the "funds-transfer business day").
98 See U.C.C. § 4A-209 comment 8; see also id. § 4A-209(b)(3).
99 See id. § 4A-209 comment 8.
100 See id.
101 See id. § 4A-506(a).
102 See id. § 4A-506(b) & comment 1. The comment provides a helpful illustration of how this formula would be used to calculate the interest that would be paid for a typical delay in receipt of the notice of rejection.
103 U.C.C. § 4A-506 governs all six instances under which Article 4A calls for a party to pay interest as a consequence of some action or inaction taken with respect to a funds transfer transaction. Id. § 4A-506 comment 1.
acceptance, they may be subject to interest liability for failure to execute a payment order when the sender has a withdrawable credit balance sufficient to cover the order.\footnote{104} The rationale for awarding interest, even without wrongdoing by the bank, is that the sender is denied the use of his own money by the bank when he reasonably expected that it would be used as a source of payment for the desired transaction.\footnote{105} In such a case, that is, when the sender does not receive notice of the rejection on the execution date and the sender's account does not bear interest, the bank will be required to pay interest to the sender for the days that pass between the execution date and either (i) the date the order is cancelled or (ii) the date the sender learns of the rejection or receives notice of rejection, whichever date comes first.\footnote{106} If the withdrawable credit balance falls below the order amount, interest is accordingly reduced.\footnote{107}

Two final points should be made with respect to rejection of payment orders. First, when a bank "suspends payments" by virtue of (a) being closed by supervisory authorities, or (b) having a public officer appointed to take it over, or (c) ceasing or refusing to make payments in the ordinary course of business, then all payment orders subsequently issued to that bank will be deemed to have been rejected as of the time suspension of payments began.\footnote{108} In these times of current weakness and uncertainty in the United States banking system, this provision will be of increasing importance to funds transfer users nervous about the health of the banks performing this vital service for them.

Second, rejection and acceptance are cast by Article 4A as mutually exclusive payment order actions.\footnote{109} Once a bank rejects a payment order, it may not later accept it without the consent of the sender.\footnote{110} This consent would be accomplished by issuance of a second payment order by the sender to replace the first, rejected, payment order.\footnote{111} Once a payment order has been accepted, however, rejection becomes impossible.\footnote{112}
4. Cancellation and Amendment of the Payment Order

Occasionally, a sender may want to cancel or amend his payment order. The sender may have changed his mind about the transaction, erroneously requested payment, transmitted multiple requests for payment orders for the same obligation, or simply requested the wrong amount in the payment order. Whatever the case, the sender can rectify the problem by either amending his order or simply cancelling it and issuing a new one to achieve the desired result.

A cancellation or amendment instruction may be transmitted to the bank orally, electronically, or in writing, but if a "security procedure" is in effect between the sender and the receiving bank, the cancellation or amendment must be verified accordingly, unless the bank agrees otherwise. (For now it suffices to say that a security procedure is an agreement between the sender and the receiving bank by which payment orders and instructions can be (i) authenticated as originating from the sender or (ii) checked for errors.)

Cancellation or amendment instructions must be received by the bank within a reasonable time before acceptance in order for the bank to have sufficient time to act, otherwise the instruction will not be effective. Instructions received after acceptance by the receiving bank will only be effective if the bank agrees or the applicable funds transfer system rules allow cancellation or amendment without agreement by the bank.

There are two further requirements for cancellation or amendment instructions to be effective after acceptance, one of which applies to a receiving bank that is not the beneficiary’s bank and the other of which applies to a receiving bank that is also the beneficiary’s bank. For a receiving bank other than the benefi-
ciary's bank, the cancellation or amendment instruction will not be effective unless a conforming cancellation or acceptance of the payment order issued by the receiving bank is made. This provision insulates the receiving bank from liability to an intermediary or beneficiary bank in the event that the intermediary or beneficiary bank to whom the receiving bank issued its payment order refuses to consent to the cancellation or amendment, and the receiving bank cannot rely on a funds transfer system rule to effect a unilateral cancellation or amendment.121

For a receiving bank that is also the beneficiary's bank, cancellation or amendment instructions will not be effective unless all parties to the transaction agree that they will be effective,122 or unless one of the following events has occurred: (i) the sender's order was not authorized by the sender; (ii) the sender mistakenly requested a duplicate of a previously issued payment order; (iii) the payment order requests payment to a beneficiary not entitled to payment from the originator; or (iv) the payment order requests payment in excess of the amount that the beneficiary is entitled to receive from the originator.123

Cancellation of an unaccepted payment order may well occur by operation of law, at the close of the fifth funds-transfer business day after the execution date or payment date of the payment order.124 Such provision is intended to deal with the rare occasion when a payment order was inadvertently not cancelled by the sender.125 To prevent the sender from unexpectedly having the payment order accepted, after he assumed that it was cancelled, the cancellation is made automatically under Article 4A after five funds-transfer business days from the payment or execution date.126

Cancelled payment orders cannot thereafter be accepted.127 An amendment is treated, at the time of amendment, as a simultaneous

---

120 See id. § 4A-211(c)(1).
121 See id. § 4A-211 comment 3.
122 See id. § 4A-211 comment 4.
123 See id. § 4A-211(c)(2) & comment 4 (providing four illustrative hypotheticals concerning the cancellation or amendment of a payment order accepted by a beneficiary bank).
124 See id. § 4A-211(d).
125 See id. § 4A-211 comment 7.
126 See id. This situation can arise when the sender initially lacked sufficient funds or credit to cover his payment order or there were some problems with the terms of the order. Delayed acceptance of this type of payment order would be unanticipated by the sender. Thus, Article 4A makes cancellation a matter of operation of law. See id.
127 See id. § 4A-211(e).
cancellation of the original payment order and issuance of a new payment order.\textsuperscript{128}

The questions regarding losses, expenses, and attorneys' fees are also addressed in Article 4A's treatment of the subject of cancellation.\textsuperscript{129} Unless a funds transfer system rule or the agreement of the parties provides to the contrary, if the receiving bank agrees to a post-acceptance cancellation or amendment or is bound to allow post-acceptance cancellation or amendment by a funds transfer system rule, the sender will be liable to the bank for losses or expenses it incurs, including attorney's fees arising out of the cancellation or amendment.\textsuperscript{130} The sender will be liable regardless of whether the cancellation or amendment is ultimately effective or not.\textsuperscript{131}

The death or legal incapacity of a sender will not operate as a revocation of the payment order unless the bank has notice and a reasonable opportunity to act before acceptance of the order.\textsuperscript{132} Although the acceptance by a bank of a sender's payment order is comparable to the acceptance of an offer in contract law, this provision reverses the portion of the law of contracts that provides that death or incapacity terminates an offer, even without an offeree having notice.\textsuperscript{133} The rule of Article 4A follows the rule for checks found in Article 4 of the Uniform Commercial Code.\textsuperscript{134}

Article 4A is not explicit in its treatment of the effect that the sender's bankruptcy has on a payment order not yet accepted. The Supreme Court previously has held that the mere filing of involuntary bankruptcy by the customer of a bank is not sufficient to operate as revocation of the bank's authority to honor the customer's checks.\textsuperscript{135} Additionally, the federal Bankruptcy Code seems to contemplate that a receiving bank that accepts a sender's payment order in ignorance of the bankruptcy filing of the sender is

\textsuperscript{128} See id.
\textsuperscript{129} See id. § 4A-211(f).
\textsuperscript{130} See id.
\textsuperscript{131} See id.
\textsuperscript{132} See id. § 4A-211(g).
\textsuperscript{133} See id. § 4A-211 comment 6; see also Restatement (Second) of Contracts § 48 (1979).
\textsuperscript{134} See U.C.C. § 4A-211(g) comment 6; id. § 4-405(1).
\textsuperscript{135} See Bank of Marin v. England, 385 U.S. 99, 101-02 (1966). In England, the bank honored checks drawn before, but presented for payment after, the voluntary bankruptcy filing of the depositor. The Court held that without more, a mere filing of voluntary bankruptcy by a depositor did not operate as a revocation of the bank’s authority to honor the checks of the depositor. Bankruptcy filing would not be construed as a per se notice to the bank of revocation of authority to honor previously drawn checks.
free to charge the sender's account for the amount of the payment order.\textsuperscript{136}

Finally, to underscore the drafters' intended supremacy of Article 4A over inconsistent private agreements on payment order cancellation, the Article provides that any funds transfer system rule shall not be effective to the extent that it is in conflict with Article 4A's provisions that allow cancellation after the beneficiary bank has accepted, if certain criteria are met.\textsuperscript{137} The rationale for this provision is that while a funds transfer system rule is intended to govern the rights and obligations between banks, reaching the opposite result contemplated by Article 4A, such a rule may also affect the rights of third parties in an unacceptable way.\textsuperscript{138} To prevent such a funds transfer system rule from foreclosing a third party sender's limited rights to cancellation after acceptance by the beneficiary bank, the rule will be given no effect to the extent that the sender's right to cancellation is abridged.\textsuperscript{139}

5. The Payment Obligation and Process

A discussion of the funds transfer process would not be complete without an examination of Article 4A's treatment of the issues of actual payment as they relate to a transaction's parties. Conceptually, Article 4A discusses the issues of payment in two distinct units: 1) the payment at the beginning of the process—by the sender to the receiving bank;\textsuperscript{140} and 2) the payment at the end of the process—by the beneficiary bank to the beneficiary.\textsuperscript{141}

a. Payment by the Sender to the Receiving Bank

i. Creation of the Obligation to Pay

The sender's obligation to pay the receiving bank is discussed in two contexts. The first case is when the receiving bank is also

\textsuperscript{136} See U.C.C. § 4A-211 comment 6. The relevant provision of the Bankruptcy Code is 11 U.S.C. § 542(c) (1988), which provides:

\[\text{[A]}\text{a entity that has neither actual notice nor actual knowledge of the commencement of the case concerning the debtor may transfer property of the estate, or pay a debt owing to the debtor, in good faith . . . to an entity other than the trustee, with the same effect as to the entity making such transfer or payment as if the case under this title . . . concerning the debtor had not been commenced.}\]

\textsuperscript{137} See U.C.C. § 4A-211(h); supra notes 122-23 and accompanying text (explaining the sender's right to cancellation after acceptance by the beneficiary bank).

\textsuperscript{138} See U.C.C. § 4A-211 comment 8.

\textsuperscript{139} See id.

\textsuperscript{140} See id. §§ 4A-402 to 4A-403.

\textsuperscript{141} See id. §§ 4A-404 to 4A-405.
the beneficiary’s bank and the second case is when the receiving bank is one other than the beneficiary’s bank.

When the sender is sending the payment order to the beneficiary’s bank, the sender is obliged to pay at the point at which the beneficiary’s bank accepts the order. However, the payment will not be due until the payment date of the order. This provision was drafted to cover cases when a beneficiary bank accepts a payment order before the payment date (i.e., the beneficiary bank notifies the beneficiary of receipt of the payment order and, by doing so, accepts it before the payment date). Thus, while the obligation to pay is created at the moment of acceptance, the payment is not due until the payment date.

If the sender issues a payment order to a bank other than the beneficiary’s bank, acceptance by the receiving bank will obligate the sender to pay the full amount of the order to the receiving bank. Payment is not due, however, until the execution date of the sender’s order. The sender’s obligation will be excused if the funds transfer process is not completed by the beneficiary bank’s acceptance of a payment order that instructs payment to the beneficiary. In this case, the funds transfer is said to have miscarried and the sender, if he has already paid the receiving bank, will be entitled to a refund of his payment with interest as provided under Article 4A.

In the case of an intermediary bank suspending payments, Article 4A creates protection for the parties involved. Since the funds transfer would not be accepted by the beneficiary bank in such a case, the funds transfer would not be completed. The originator, therefore, would not be obliged to pay the receiving bank. While the receiving bank would be entitled to a refund if it paid the intermediary bank before the intermediary bank sus-

---

142 See id. § 4A-402(b).
143 See id.
144 See id. § 4A-402 comment 1. This problem often arises in the case of automated clearing house transfers. See also supra notes 73-87 and accompanying text.
145 See U.C.C. § 4A-402 comment 1.
146 See id. § 4A-402(c).
147 See id.
148 See id.
149 See id. § 4A-402 comment 2; see also U.C.C. § 4A-506 (explaining Article 4A interest calculation); infra notes 150-54 and accompanying text (discussing Article 4A’s refund feature).
150 See U.C.C. § 4A-402 comment 2.
151 See id.
pended payments, the intermediary could be insolvent and unable to give the receiving bank its refund. Article 4A provides, therefore, that if the originator instructed the receiving bank that the intermediary bank was to be used, then the originator will be required to reimburse the receiving bank for the amount paid to the intermediary bank. By giving an explicit instruction to the receiving bank that a specific intermediary is to be employed, the originator takes the risk of that intermediary's insolvency.\textsuperscript{152} The originator will then have a subrogated claim against the insolvent intermediary.\textsuperscript{153} Neither the originator's right to have the payment obligation excused in the event of nonacceptance by the beneficiary bank nor the right to subrogation in the cases where his designated intermediary bank suspends payments may be varied by agreement.\textsuperscript{154}

ii. *Time and Means of Payment by the Sender to the Receiving Bank*

If the sender of a payment order is a bank, payment occurs when the receiving bank receives final settlement of the obligation through the Federal Reserve Bank or through a funds transfer system.\textsuperscript{155} Payment orders between banks are settled in one of two general ways. First, if the payment order is sent out on a network other than that maintained by the Federal Reserve (Fedwire), the amounts of various payment orders are credited and debited to accounts of one bank at another or credited and debited through a clearing house account.\textsuperscript{156} Subsequent settlement is then achieved through a Federal Reserve bank, which charges the accounts of all net debtor banks and credits the accounts of all net creditor banks.\textsuperscript{157} Second, if the payment order is sent out over Fedwire, a Federal Reserve bank will debit and credit the appropriate banks at the time the payment order is received by the receiving bank.\textsuperscript{158} Under both mechanisms, when the Federal Reserve settlement is finalized, the sender's obligation is paid.


\textsuperscript{153} See U.C.C. § 4A-402(e).

\textsuperscript{154} See id. § 4A-402(f).

\textsuperscript{155} See id. § 4A-403(a)(1).

\textsuperscript{156} See id. § 4A-403 comment 1.

\textsuperscript{157} See id.

\textsuperscript{158} See id.
Some bank to bank payment obligations, however, are settled outside the Federal Reserve System. This is often the case with foreign banks, which have no access to the Federal Reserve payment system. Payments must be made through accounts the banks have with each other or with third banks. Under this type of payment regime, payment is effectuated (1) by the sender crediting an account of the receiving bank and the credit subsequently being withdrawn by the receiving bank or (2) at midnight on the day the credit becomes withdrawable and the receiving bank learns of it. This midnight provision is designed to allow the bank being credited sufficient time to reject the payment order if it chooses, thus avoiding acceptance and the resultant liability to the beneficiary.

Payment can also be effectuated in other ways. The sender, either a bank or non-bank, may have an account with the receiving bank, allowing the receiving bank to effect payment by debiting that account thereby discharging the sender's payment obligation. Payment by this means, however, is only possible to the extent a withdrawable credit balance exists in the account being debited.

A further means of achieving payment under Article 4A involves those banks that are members of a funds transfer system such as CHIPS. Such a system allows member banks to transmit payment orders over the system, with settlement of all obligations being made at the end of the day. At that time, the aggregate credits and debits of member banks are tabulated; Article 4A payment results when each bank is given its net credit or debit after all transactions have been processed. Article 4A makes it clear that this netting settlement under the applicable funds transfer system rules is valid and not subject to common law attack based on the theory that no mutuality of obligation exists.

---

159 See id. § 4A-403 comment 2.
160 See id.
161 See id.
162 See id. § 4A-403(a)(2).
163 See id. § 4A-403 comment 2.
164 See id. § 4A-403(a)(3) & comment 3.
165 See id.
166 CHIPS is the acronym for the New York Clearing House Interbank Payment Systems.
167 See U.C.C. § 4A-403(b) & comment 4.
168 See id.
169 See id.
A final apparatus for the payment of receiving banks under Article 4A is the system whereby two banks have a mutual agreement to settle their respective payment order obligations either daily or periodically by setting off the amount owed by each bank against the amount owed to it by the other.\textsuperscript{170} Payment occurs when this setoff is made.\textsuperscript{171} It must be noted that the obligations created by this scheme, and by the previously discussed CHIPS type scheme, are obligations between the banks that do not involve their respective customers. Thus, in case of a bank's insolvency, any outstanding liability of the insolvent bank is measured in terms of its net setoff position with the other bank or banks.\textsuperscript{172}

In the unlikely case that the sender does not have an account relationship with the receiving bank or does not settle with the Federal Reserve bank (e.g., a customer that pays for the payment order by cash, check, or bank obligation), Article 4A does not provide for when payment is effected. Payment time must then be determined by reference to extrinsic law.\textsuperscript{173}

\textbf{b. Payment by the Beneficiary's Bank to the Beneficiary}

\textit{i. Creation of the Obligation to Pay}

In general, when the beneficiary's bank accepts the payment order under Article 4A, it has an obligation to pay the beneficiary of that order.\textsuperscript{174} The payment is due on the payment date of the order, but if acceptance occurs after the close of the beneficiary bank's funds-transfer business day, payment is due on the next funds-transfer business day.\textsuperscript{175} Most importantly, Article 4A provides that if the beneficiary bank refuses to pay after demand is made by the beneficiary, and if the bank receives notice of particular facts that may give rise to consequential damages arising out of nonpayment, the beneficiary will be able to recover those consequential damages to the extent of the beneficiary's notice.\textsuperscript{176} The

\textsuperscript{170} See id. § 4A-403(c).
\textsuperscript{171} See id.
\textsuperscript{172} See id. § 4A-403 comment 4.
\textsuperscript{173} See id. § 4A-403(d) & comment 5.
\textsuperscript{174} See id. § 4A-404(a).
\textsuperscript{175} See id.
\textsuperscript{176} See id.
beneficiary bank may escape liability with proof that it had reasonable doubt as to beneficiary’s right to payment.  

It is crucial to understand that the beneficiary bank need not have notice of the exact or even approximate amount of potential consequential damages. It is sufficient that the bank have notice of the general type or nature of the potential damages that the beneficiary may suffer from nonpayment. A case illustrating this principle is Evra Corp. v. Swiss Bank Corp. In Evra, the charterer of a ship sued a bank for failure to make timely payment, which resulted in the cancellation of a charter. From a failure to transmit $27,000 in a timely manner, the charter was claiming consequential damages exceeding $2,000,000. The court held that the bank had not been given notice of the special circumstances of the funds transfer—that failure to consummate the $27,000 transfer would result in this large sum of consequential damages. Had there been actual notice to the bank that consequential damages of over $1,000,000 would result, the bank would have been put on notice and been liable for the consequential damages.

Also important is the concept of reasonable doubt as to the beneficiary’s right to payment. The presence of reasonable doubt is the beneficiary bank’s defense to a consequential damage claim by the beneficiary based on nonpayment. In the ordinary case, this right of payment issue should be fairly clear since the bank should know if it has accepted and thus obliged itself to pay. In some

---

177 See id. The drafters of the rule have recognized that the Expedited Funds Availability Act, codified at 12 U.S.C.A. §§ 4001-4010 (West 1989 & Supp. 1991), also governs the issue of funds availability in a funds transfer such that this portion of Article 4A may be subject to federal preemption. See U.C.C. § 4A-404 comment 1. The Expedited Funds Availability Act (EFA Act) is federal consumer protection legislation intended to provide bank customers with expedited access to their bank deposits. See Baxter & Bhala, supra note 61, at 1488. The two statutes appear to be in conflict in some respects as a result of their different orientation and purpose. In some cases, the EFA Act may not require a beneficiary bank to pay the beneficiary until later than required under Article 4A, while in others, the EFA Act would require payment earlier. The preemption issue, however, might be averted by resort to the conflict of laws provision of the EFA Act. See id. at 1489-90. The case law is not sufficiently developed on this point since only a handful of states have adopted Article 4A as of this writing. Consequently final resolution of this issue will be made at some point in the future.

178 See U.C.C. § 4A-404 comment 2.

179 673 F.2d 951 (7th Cir. 1982).

180 See Evra Corp. v. Swiss Bank Corp., 673 F.2d 951, 956 (7th Cir. 1982). The Evra court made reference to the time honored rule of Hadley v. Baxendale, 156 Eng. Rep. 145 (Ex. Ch. 1854), in articulating its holding that liability for consequential damages is predicated on the defendant being put on notice of the special circumstances giving rise to them.

181 U.C.C. § 4A-404 comment 2.

182 See id. § 4A-404 comment 3.
cases, however, it may not be entirely clear that acceptance has occurred. When, for example, acceptance occurs by receipt of payment by the beneficiary bank, some doubt may exist as to whether payment was in fact received. Also, a doubtful case may arise when there is uncertainty that the person demanding payment is in fact the beneficiary.

No reasonable doubt defense can be raised, however, when a funds transfer is being used to pay an obligation and a dispute subsequently arises between the originator and the beneficiary concerning whether the obligation is in fact owed. In this situation, the grounds alleged by the originator as a defense to his payment obligations to the beneficiary do not have any effect on the beneficiary bank’s duty to pay the beneficiary upon acceptance. The originator has no right to cancel a payment order to the beneficiary’s bank (except in those cases involving a “book transfer,” which involves the originator and the beneficiary having the same bank) because the originator is not the sender of that payment order. Instead, the receiving or intermediary bank is the sender, and it alone retains the right of cancellation. Article 4A further emphasizes the centrality of the beneficiary’s right to payment by providing that it may not be varied by either agreement or by a funds transfer system rule.

The beneficiary’s bank’s duty to notify the beneficiary of the receipt of the payment order is also demarcated by Article 4A. Ordinarily, when acceptance occurs by giving notice, notice and acceptance occur simultaneously; when acceptance occurs under any other means provided for under Article 4A, the beneficiary’s bank still must discharge its duty of notice to the beneficiary. If the payment order instructs payment to the beneficiary’s account, the beneficiary’s bank must notify the beneficiary of receipt before midnight of the next funds-transfer business day after receipt.

183 See id.
184 See id.
185 See id. An example is the case in which the originator is attempting to halt payment to the beneficiary on the grounds of fraud or breach of contract.
186 Id.
187 See id.
188 See id.
189 See id. § 4A-404(c).
190 See id. § 4A-209(b)(1).
191 See id. § 4A-404 comment 4.
192 See id.
193 See id. § 4A-404(b).
the payment order does not instruct payment to an account of the beneficiary, notice to the beneficiary is only required if the order so stipulates. Notice can be given by first-class mail or any other reasonable means under the circumstances.

Failure of the beneficiary's bank to give notice will oblige the beneficiary's bank to pay interest on the payment order. Interest accrues from the period when notice should have been given until the beneficiary learns of the beneficiary's bank's receipt of the payment order. While damages other than interest are not recoverable, attorney's fees may be recovered if a demand for interest is made and refused before legal action is commenced to recover the interest.

The beneficiary's right to notice, unlike the beneficiary's right to payment, is subject to variation by agreement or by funds transfer system rules, provided the beneficiary has notice of the rule before the beginning of the funds transfer. In automatic clearing house transactions, it is customary not to give the beneficiary notice unless it is requested. This practice obviously can be continued by the adoption of a funds transfer system rule.

ii. *Time and Means of Payment by the Beneficiary's Bank to the Beneficiary*

If the beneficiary's bank credits the beneficiary's account with the proceeds of the payment order, payment of the bank's obligation occurs when and to the extent that (i) the beneficiary is notified of his right to withdraw the credit, (ii) the bank lawfully applies the credit to a debt of the beneficiary, or (iii) the proceeds of the payment order are otherwise made available to the beneficiary. On the other hand, if the beneficiary's bank does not credit an account of the beneficiary, the time when payment occurs is governed by principles of law outside Article 4A.

---

194 See id.
195 See id.
196 See id.
197 See id.
198 See id. § 4A-404(c) & comment 4.
199 See id. § 4A-404 comment 4.
200 See id. § 4A-405(a). The principal cases in which a bank applies the payment order proceeds to a beneficiary's debt are instances of setoff by the beneficiary's bank or garnishment by a creditor of the beneficiary. See id. § 4A-405 comment 1; see also id. § 4A-502 comment 2.
201 See id. § 4A-405(b). In almost all cases the bank credits the account of the beneficiary, so resort to extrinsic law to decide issues of payment should not be a common occurrence. See id. § 4A-405 comment 1.
In general, the beneficiary's bank cannot pay the beneficiary and reserve a right to recover from the beneficiary should the beneficiary bank not receive payment for the payment order. Such a condition is unenforceable. By paying the beneficiary before it receives payment for the order, the beneficiary's bank assumes the risk of nonpayment. Thus, when the beneficiary's bank has paid within the meaning of Article 4A by informing the beneficiary that it may withdraw the credit, the beneficiary bank generally cannot revoke the withdrawal right in the event that the bank is not paid.

This general rule, prohibiting the beneficiary bank's recovery after payment is made, is subject to two exceptions under Article 4A. The first exception involves the case of a funds transfer system rule providing that a payment made to a beneficiary through the system is "provisional" until the beneficiary's bank is paid. In such a case, the beneficiary's bank is entitled to a refund from the beneficiary if (i) the rule requires both the beneficiary and originator to be given notice of the provisional nature of system payments before the transfer is initiated, (ii) the beneficiary, the beneficiary's bank, and the originator's bank agree to abide by the rule, and (iii) payment is not received by the beneficiary's bank. Thus, if the beneficiary is required to effect a refund to the beneficiary's bank, the bank's acceptance will be nullified and no payment to the beneficiary will have occurred. Essentially, the drafters designed this rule to cope with automated clearing house transfers that handle transfers made in batches of payment orders from different originators' banks. In this scenario, funds are customarily released to beneficiaries earlier than the payment date, with the understanding that all payments are provisional until the beneficiary's bank receives payment.

The second exception to the general rule concerns funds transfer system rules on loss-sharing. In any funds transfer system

---

202 See id. § 4A-405(c).
203 See id. § 4A-405 comment 2. This rule also applies when the funds are released to the beneficiary as a "loan." See id.
204 See id.
205 See id. § 4A-405(d).
206 See id.
207 See id.
208 See id. § 4A-405 comment 3; see also id. § 4A-206 comment 2.
209 See id. § 4A-405 comment 3. The comment provides an in-depth, explanatory treatment of the intricacies of automated clearing house rules on provisional payments to beneficiaries.
210 See id. § 4A-405(e).
that (i) nets obligations multilaterally among participants and (ii) has a loss-sharing rule that provides funds necessary to complete the settlement of obligations of participants that do not otherwise meet their settlement obligations, a beneficiary bank may recover after it has paid its beneficiary. Such a rule is in effect on the CHIPS system.

In the unlikely event that CHIPS or any other system would fail to settle according to its rule, Article 4A provides an alternative route of recovery. Article 4A provides that should this event occur with respect to any payment order, the bank's acceptance will be nullified, and the beneficiary bank will be entitled to recover from the beneficiary. In addition, no payment by the originator to the beneficiary will have occurred, and each sender in the funds transfer of that payment order will be excused from its payment obligations and entitled to a refund if it has already paid.

c. Discharge of Underlying Obligations From Payment by Originator to Beneficiary

Under Article 4A, payment by the originator to the beneficiary is accomplished by providing to the beneficiary the obligation of the beneficiary's bank to pay. When the beneficiary's bank accepts the payment order for the benefit of the beneficiary, the obligation thus created in the beneficiary bank substitutes for the obligation of the originator to the beneficiary. Discharge of the originator's obligation will not result, however, where (i) such mode of payment is prohibited by the contract between the beneficiary and originator, (ii) the beneficiary notifies the originator of the refusal of payment within a reasonable time after receiving notice from his bank of receipt of the order, (iii) funds from the order were not withdrawn or applied to a debt of the beneficiary, and (iv) the beneficiary would suffer a loss reasonably avoided by a

---

211 See id.
212 See id.
213 See id. According to CHIPS rules, if the system failed to settle, no bank would receive settlement at all.
214 See id. § 4A-405 comment 4.
215 See id. § 4A-406 comment 1.
216 See id. § 4A-406 comment 2. This effect is similar to that of the beneficiary receiving a cashier's check payable to him under Article 3 of the Uniform Commercial Code. Once a holder procures a certified check, the drawer and all prior endorsers are discharged. See id.; see also id. § 3-411(1).
means of payment complying with the contract.\textsuperscript{217} The rationale for this rule of no discharge is to prevent the originator from imposing the risk of any bank insolvency upon the beneficiary when the beneficiary had requested other means of payment not encompassing such a risk.\textsuperscript{218} Where no discharge of the obligation results under this rule, the originator is subrogated to the rights of the beneficiary to receive payment from the beneficiary’s bank.\textsuperscript{219}

In the ordinary wire transfer transaction, charges are nominal in relation to the amount of money being transferred.\textsuperscript{220} Generally, the parties to a wire transfer transaction agree in advance on how the charges for the transfer service will be divided among themselves.\textsuperscript{221} When the parties fail to agree on this point, however, Article 4A provides a resolution. Article 4A allows the bank issuing a payment order to deduct the charges for transmission from the amount of the issued payment order. The beneficiary then receives an amount from the payment order that reflects the amount owed to him by the originator less the charges for transmission.\textsuperscript{222} This amount is deemed to be payment in the amount of the originator’s order and discharges the originator’s underlying obligation to the beneficiary, unless the beneficiary subsequently demands reimbursement for the transmission costs and the originator refuses.\textsuperscript{223}

III. Why Article 4A is the Solution to Many Unanswered Questions Under the Current Law of Funds Transfers

The reader is now familiar with the scope of Article 4A, the cast of Article 4A characters, and the inner workings of the Article 4A transfer process from start to finish.\textsuperscript{224} But these matters are simply the preliminaries in terms of appreciating the real import of Article 4A.\textsuperscript{225} These matters address themselves to the bulk of funds transfer activity, which is executed without a hitch. However, Article 4A’s ultimate value must be assessed in terms of how it

\textsuperscript{217} See id. § 4A-406(b). Comments 3 and 4 to this section discuss some of the permutations of this rule of no discharge and how it would work in practice.

\textsuperscript{218} See id. § 4A-406 comment 3.

\textsuperscript{219} See id. § 4A-406(b) & comment 3.

\textsuperscript{220} See id. § 4A-406 comment 5.

\textsuperscript{221} See id.

\textsuperscript{222} See id.

\textsuperscript{223} See id. § 4A-406(c) & comment 5.

\textsuperscript{224} For a discussion, see supra Parts I & II of this Article.

handles those funds transfer transactions in which something goes wrong, leaving uncertainty about all phases of liability.

Article 4A is precisely the sort of statutory scheme needed to address these liability and liability-related issues. In the discussion below, the reader will be introduced to potential liability issues that can and do arise in the funds transfer arena and how Article 4A presents a cogent and effective response to those issues.

A. Choice of Law

Often, a threshold inquiry in the resolution of any liability problem involves the applicable law by which the issue is to be decided. The drafters of Article 4A were not content to leave this potentially nettlesome issue to the courts without explicit statutory guidance.\(^\text{226}\) Since funds transfers are typically interstate or even international in character, uncertainty in choice of law would make predictability of legal outcomes extremely difficult.\(^\text{227}\) Therefore, the drafters chose the following choice of law rule scheme to create some order in what would otherwise be a chaos of conflicting and overlapping law.

In the absence of a funds transfer system rule or contractual agreement that operates as a choice of law provision, the rights and obligations between the sender and the receiving bank are governed by the law of the jurisdiction where the receiving bank is located; the rights and obligations between the beneficiary’s bank and the beneficiary are governed by the law of the jurisdiction where the beneficiary’s bank is located; and, the issue of when payment is made pursuant to a funds transfer is governed by the law of the jurisdiction where the beneficiary’s bank is located.\(^\text{228}\) The issues of when payment occurs are governed by the law of the beneficiary’s bank’s jurisdiction since it is often difficult to ascertain where the beneficiary is located.\(^\text{229}\) It must be noted here, however, that Article 4A has binding effect only on a jurisdiction that has adopted it; its effect outside Article 4A jurisdictions is limited to any court’s willingness to apply it by analogy.\(^\text{230}\)

\(^{226}\) See Baxter & Bhala, supra note 61, at 1502.

\(^{227}\) See U.C.C. § 4A-507 comment 1.

\(^{228}\) See id. § 4A-507(a)(1)-(3).

\(^{229}\) See id. § 4A-507 comment 2.

\(^{230}\) See id.; Shawmut Worcester County Bank v. First American Bank & Trust, 731 F. Supp. 57 (D. Mass. 1990). In this case, the United States District Court for the District of Massachusetts was deciding a case that it had determined would be governed by Florida
If, however, the parties to a funds transfer have made an agreement selecting the applicable choice of law, that election will govern the rights and liabilities of the parties despite the absence of a reasonable relation between the transaction and the jurisdiction whose law is stipulated.\(^{231}\) This provision increases the respect for freedom of contract to a higher level than is apparent from the position of the Restatement (Second) of Conflicts of Laws.\(^{232}\) The Restatement view requires either a "substantial relationship" between the jurisdiction whose law is selected and the transaction involved, or, at least, some other reasonable basis for the choice of the parties before a court will be bound to honor the choice of law election.\(^{233}\) Moreover, the Restatement view allows a court to disregard the choice of law election if it would result in a policy outcome offensive to a jurisdiction other than the jurisdiction selected by the parties.\(^{234}\) The Article 4A choice of law framework is more akin to the view expressed by the California and New York state legislatures. That view accords more deference to the choice of law preferences expressed in the parties' contract.\(^{235}\)

Article 4A also recognizes that a funds transfer system rule may serve as a choice of law provision.\(^{236}\) A funds-transfer system rule may be fashioned to govern either (i) the rights and obligations between participating banks with respect to payment orders in the system, or (ii) the rights and obligations of some or all parties to a funds transfer effected by the system.\(^{237}\) The choice of law provision that purports to bind all participating banks is indeed binding upon them. The binding effect of the second type of funds transfer system choice of law rule, however, depends upon notice.\(^{238}\) While this second type of clause is binding upon the originator or other sender, it will only be binding upon a receiving bank where

---

\(^{231}\) See U.C.C. § 4A-507 comment 3.

\(^{232}\) See id.; see also RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)(a) (1971).

\(^{233}\) See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)(a).

\(^{234}\) See id. § 187(2)(b).

\(^{235}\) See U.C.C. § 4A-507 comment 3; CAL. CIV. CODE § 1646.5 (West Supp. 1991) (stating that transactions over $250,000 are to be governed by California law if parties so elect even if California bears no relation to the transaction); N.Y. GEN. OBLIG. LAW § 5-1401 (McKinney Supp. 1989) (parties may elect to have N.Y. law govern any transaction over $250,000 whether or not N.Y. bears a relation to the transaction).

\(^{236}\) See U.C.C. § 4A-507(c).

\(^{237}\) See id.

\(^{238}\) See id.
it has notice (a) that the particular funds transfer system may be used in the transaction and (b) of the choice of law of the system, at the time when the originator, other sender, or receiving bank issued or accepted a payment order.\textsuperscript{239} The beneficiary will be bound by the choice of law election of the funds transfer system only if, at the time the transfer is initiated, the beneficiary has notice of the possible use of the funds transfer system in the transaction. In addition, the beneficiary must have notice of that system's choice of law election.\textsuperscript{240} As with the contractually chosen choice of law discussed above, the funds transfer system's choice of law applies notwithstanding the lack of reasonable relation between the jurisdiction and the transaction.\textsuperscript{241}

Deference to the funds transfer system's choice of law rule is important because it allows the uniformity of law required to operate an efficient system.\textsuperscript{242} Such a rule enables the system to dispense with the myriad individual agreements on choice of law and cover those cases in which private choice of law agreements are not feasible.\textsuperscript{243} The drafters of Article 4A recognized the probability that funds transfer systems would exercise their right to establish a unitary choice of law regime, increasing the certainty of the transactions that they process.\textsuperscript{244}

The drafters foresaw, as well, possible conflicts between the unitary regime and the parties' freedom to contract. In cases containing a private contractual agreement on choice of law and a funds transfer system choice of law rule that conflict, the private contractual choice of law provision will prevail.\textsuperscript{245}

Finally, when a funds transfer is carried out over more than one funds transfer system, and an inconsistency exists between the systems' choice of law rules, the governing law will be that of the jurisdiction with the most significant relationship to the matter in issue.\textsuperscript{246} Under this fact pattern, courts will have their greatest discretion in selecting the choice of law based on usual choice of law analysis.

\textsuperscript{239} See id.
\textsuperscript{240} See id.
\textsuperscript{241} See id.
\textsuperscript{242} See id. § 4A-507 comment 4.
\textsuperscript{243} See id.
\textsuperscript{244} See id.
\textsuperscript{245} See id. § 4A-507(d).
\textsuperscript{246} See id. § 4A-507(e).
In considering choice of law under Article 4A, the point to remember is that choice of law outcomes under Article 4A are to a large extent malleable. The parties themselves can choose, by their action or by design, whether they want Article 4A to apply to their transaction.247

B. Injunctive Relief Under Article 4A

Another threshold issue in any liability problem is the scope of relief offered to the parties. In addition to the damage remedies previously mentioned in this commentary under Article 4A, the question of available injunctive relief may arise.

Article 4A addresses this issue, recognizing that in the proper circumstances, injunctive relief may be sought and granted without offense to the purposes for which Article 4A was enacted.248 Article 4A provides that for proper cause and in compliance with applicable law a court may restrain (i) a person from issuing a payment order to initiate a funds transfer, (ii) an originator’s bank from executing the payment order of the originator, and (iii) the beneficiary’s bank from releasing funds to the beneficiary or the beneficiary from withdrawing the funds credited to his account.249 An injunctive scheme such as this gives courts the power to halt a funds transfer even after it is set in motion.250

This injunctive power is limited, however. No injunction may be obtained respecting any funds transfer other than those mentioned.251 Furthermore, intermediary banks are immune from injunctive relief, and injunctive relief against the originator and the originator’s bank is limited to the issuance of the payment order.252 No one except the beneficiary’s bank may be enjoined from paying a payment order, and no receiving bank can be enjoined from receiving the payment it is due from the sender of an order it has accepted.253

In light of these limitations, it may be inferred from the text of Article 4A that although the drafters did not see injunctive relief as wholly incompatible with the operation of the statute, they saw

247 See Baxter & Bhala, supra note 61, at 1504.
248 See U.C.C. § 4A-503.
249 See id.
250 See id. § 4A-503 comment.
251 See id.
252 See id.
253 See id.
such application as appropriately confined to a limited number of cases.

C. Unauthorized Payment Orders

Given the enormous amount of money moved around the country and internationally each day by funds transfer activity, it is no surprise that all parties involved have justifiable anxieties about the potential for fraudulent and criminal activity. Article 4A specifically addresses the question of what is to be done both to (a) prevent unauthorized use of customer accounts, which could cost funds transfer parties millions of dollars before discovery of such use, and (b) place legal responsibility for unauthorized use on the appropriate parties.

1. Prevention of Unauthorized Use

To guard against the unauthorized use of payment orders, Article 4A first introduces the concept of a "security procedure." Article 4A defines a security procedure as a means agreed upon by the customer and the receiving bank for the purposes of (i) verifying that a payment order or instruction is that of the customer or (ii) detecting error in the transmission or content of the payment order or instruction. Security procedures may entail the use of algorithms or other codes, identifying words or numbers, encryption, callback procedures, or other similar security devices. Notably, Article 4A states that comparison of a signature with an authorized signature specimen is not by itself a security procedure. Also not a security procedure within the meaning of Article 4A is any procedure unilaterally adopted by the receiving bank.

Use of security procedures is not mandated by Article 4A. The liability rules for unauthorized funds transfers were drafted with built-in incentives for banks and their customers to enter into security procedure agreements.

---

254 See U.C.C. § 4A-201.
255 See id.
256 See id.
257 See id. § 4A-201 comment.
2. Liability Rules for Unauthorized Payment Orders

a. No Security Procedure

In the absence of a security procedure agreement in effect between the sender and the receiving bank, any payment order received by a receiving bank will be deemed the authorized order of the person identified by the order as the sender if that person authorized it or that person is otherwise bound by agency law. Therefore, if, for example, a receiving bank executed a payment order and the sender refuses to pay, alleging that the payment order was unauthorized, and no security procedure was in effect, the receiving bank must resort to agency law principles of actual or apparent authority or the equitable principles of subrogation or restitution to establish its right to recover.

In most cases, however, these legal principles offer the receiving banks little protection against losses. Prudent banks simply are not willing to gamble that they can recover in this manner. With the large amounts of money being transferred, the potential for loss makes banks seek the assurance and protection that Article 4A affords to them through a security agreement with their payment order customers.

b. Effect of a Security Procedure

When the receiving bank and the customer have entered into an agreement to establish a security procedure, the bank gains a certain level of protection under Article 4A. If a security agreement is in effect, a payment order will be effective as the order of the customer (and the bank will be entitled to enforce it) regardless of any agency law based defense of lack of authority, if two conditions are met: (i) the security procedure is a commercially reasonable method of providing security against unauthorized payment orders, and (ii) the bank proves that it accepted the payment order.

---

259 See U.C.C. § 4A-202(a).
260 See id. § 4A-203 comment 1. The comment contains a hypothetical illustration of how agency law could allow the receiving bank to recover on either an estoppel or negligence theory. For an illustration of a receiving bank’s ability to recover in subrogation, see Gatoil (U.S.A.), Inc. v. Forest Hill State Bank, 104 F.R.D. 580 (D. Md. 1986).
261 See U.C.C. § 4A-203 comment 1.
262 See id.
263 See id.
264 See id. § 4A-202(b).
order in good faith and in compliance with the security procedure as well as any written agreement or instruction of the customer that restricts the acceptance of payment orders issued under the customer’s name.265 The bank will not be required to follow any instruction from the customer that contravenes a written agreement or does not arrive with sufficient time to give the bank a reasonable opportunity to act on it.266

The above rules follow from the drafters’ assumption that a commercially reasonable security procedure is the best means of avoiding any problems of unauthorized payment orders.267 Protections are thus afforded to both the customer and the receiving bank in order to encourage the use of security procedures.268

c. Commercial Reasonableness

The customer is protected by the requirement that any security procedure adopted be commercially reasonable. This rule places on the bank the burden of making commercially reasonable security procedures available to its customers because the banks are in the better position to evaluate the efficacy of a given procedure in combating fraud.269 The customer, in contradistinction, has the burden of supervising its employees to assure compliance with the agreed to security procedure and of safeguarding both information on security procedures and access to facilities for transmitting payment orders and instructions.270

Of course, whenever the drafters of a statute use the words “commercially reasonable” as a standard for predicating liability upon a party, an inevitable definitional controversy arises. In using these words, the drafters intended a flexible definition that would be suited to the great variety that exists within the funds transfer arena in terms of (1) labor and equipment costs for verification; (2) customer needs in terms of volume of payment orders sent and dollar amounts involved; (3) the type of bank acting as a receiving bank; (4) the types of payment order involved; and (5) the particular modes of transmission.271

265 See id.
266 See id.
267 See id. § 4A-203 comment 3.
268 See id.
269 See id.
270 See id.
271 See id. § 4A-203 comment 4.
Article 4A puts the issue of commercial reasonableness in the hands of the trial judge by declaring that the issue is a question of law.272 The judge is directed, under Article 4A, to consider the following factors in assessing commercial reasonableness: (1) the wishes of the customer expressed to the bank; (2) the circumstances of the customer known to the bank, including the size, type, and frequency of payment orders normally issued by the customer to the bank; (3) alternative security procedures offered to the customer; and (4) security procedures in general use by customers and receiving banks similarly situated.273

The drafters chose to make the issue of commercial reasonableness a question of law since such questions are more susceptible to predictability than questions of fact. Thus, from an analysis of decisions, banks could reasonably anticipate whether their security procedures would pass judicial muster.274

The standard for the judge's decision should not be whether another security procedure would have been better than the one chosen; rather, the decision should focus on whether the procedure arrived at was a reasonable one given the customer and bank involved.275 However, a security procedure falling below the applicable prevailing standards of good banking practice should not be considered commercially reasonable.276

A security procedure can also be deemed commercially reasonable by operation of Article 4A. Under the statute, a security procedure will be deemed commercially reasonable where (i) it was chosen by the customer after the bank offered and the customer rejected a security procedure that was commercially reasonable for that customer, and (ii) the customer expressly agreed in writing to be bound by any payment order, authorized or not, issued in its name and accepted in compliance with the security procedure chosen by the customer.277 The customer, then, may assume the risk of his own bad decision by choosing a security procedure not

272 See id.
273 See id. § 4A-202(b). This multi-factor calculus for arriving at a determination of commercial reasonableness would seem to require at least an initial factual determination on some issues (e.g., what procedures were in fact offered to the customer?). A court conceivably might turn these fact-bound issues over to a jury while appropriately reserving for itself the ultimate legal issue of commercial reasonableness. See French, supra note 258, at 1431.
275 See id.
276 See id.
277 See id. § 4A-202(c).
recommended by the bank.\textsuperscript{278} Thus counsel for funds transfer customers should be aware of the "trap" Article 4A has created for those that wish to second-guess the advice of the bank on security procedure.\textsuperscript{279}

\textit{d. Acceptance in Good Faith and in Compliance with the Agreements}

For a receiving bank to enforce a payment order through means of an agreed-upon security procedure, not only must it demonstrate the commercial reasonableness of the procedure, the bank must also show that it accepted the disputed payment order in good faith and in compliance with both the security agreement and any other written agreement or instructions from the customer that restrict the power of the bank to accept payment order requests under the customer's name.\textsuperscript{280} The written agreement or instructions might be given to limit acceptance to (1) payment orders payable from an authorized account, (2) payment orders within an account's credit balance, or (3) payment orders to authorized beneficiaries.\textsuperscript{281}

Good faith is defined by Article 4A as "honesty in fact and the observance of reasonable commercial standards of fair dealing."\textsuperscript{282} This definition differs from the blanket definition of good faith applicable to the rest of the Uniform Commercial Code, which characterizes good faith as simply "honesty in fact in the conduct or transaction concerned."\textsuperscript{283} Thus, the drafters of Article 4A apparently wanted to stress that good faith, as it relates to funds transfers, would be construed in the light of reasonable commercial standards of fair dealing.\textsuperscript{284}

\textsuperscript{278} See id. § 4A-203 comment 4.

\textsuperscript{279} See Patrikis, Baxter & Bhala, Article 4A: The New Law of Funds Transfers and the Role of Counsel, 23 U.C.C. L.J. 219, 235-36 (1991). The authors opine that counsel for customers might be led into this trap by counsel for banks. The bank's counsel could offer a highly complex and expensive security procedure, knowing that it will be rejected. This would lead the customer to choose another one, sign the requisite written agreement, and assume all risks of its failure.

\textsuperscript{280} See U.C.C. § 4A-202(b).

\textsuperscript{281} See id. § 4A-203 comment 3. These instructions limiting acceptance might be incorporated into the security procedure itself instead of contained in a separate written agreement or instruction. In any case the duty of the bank to comply with them is the same. See id.

\textsuperscript{282} See id. § 4A-105(a)(6).

\textsuperscript{283} See id. § 1-201(19).

\textsuperscript{284} See French, supra note 258, at 1435.
e. Unenforceability of Some Verified Payment Orders

Notwithstanding the fact that a receiving bank has complied with all of the Article 4A requirements for security procedure agreements, some disputed payment orders that have been duly verified under a commercially reasonable security procedure may still be unenforceable. This unenforceability may arise in two ways. First, the receiving bank may, by express written agreement, limit the extent to which it is entitled to enforce or retain payment of the payment order. In this manner a receiving bank assumes all risk of loss with respect to unauthorized payment orders, even though its security procedure and concomitant actions were perfectly within the bounds of Article 4A.

Second, the payment order may be unenforceable, notwithstanding compliance with a commercially reasonable security procedure, if the following condition is met. The customer must prove that the order was not caused either directly or indirectly by a person that (i) was entrusted at any time with the duty to act for the customer with respect to payment orders and instructions, or (ii) obtained access to transmitting facilities of the customer, or that obtained from a source controlled by the customer and without authority of the receiving bank, information facilitating breach of the security procedure, regardless of how the information was obtained or whether the customer was at fault. Information includes any access device, computer software, or similar medium.

The customer can thus shift the risk of loss caused by unauthorized payment orders back to the receiving bank when it can “prove” that the means used by the unauthorized person were not obtained through the customer, through any of the customer’s present or former agents, or any other source controlled by the customer. “Prove,” as defined under Article 4A, means to meet the burden of establishing a fact by persuading the trier of fact that the existence of a fact is more probable than its non-existence. In any situation involving unauthorized access to payment

---

285 See U.C.C. § 4A-203.
286 See id. § 4A-203(a)(1).
287 See id. § 4A-203(a)(2).
288 See id. § 4A-203(a)(3).
289 See id. § 4A-203 comment 5.
290 See id. § 4A-203 comment 6.
291 Id.; see id. § 4A-105(a)(7). Article 4A incorporates the general Uniform Commercial Code definition of “prove.” See id. § 1-201(8).
order information or facilities, bank regulations will require a thorough criminal investigation, as an internal bank investigation, and perhaps even an investigation by bank examiners. The customer will have access to all of the evidence produced by these investigations to assist it in meeting its burden of proof.

f. Variation of Rights and Obligations by Funds Transfer System Rule

Article 4A does not prohibit a funds transfer system rule from varying the rights and obligations of banks that are participating members in the system with respect to unauthorized payment orders or instructions. A funds transfer system rule may operate to allocate losses, due to unauthorized payment orders, between participating banks in a manner inconsistent with Article 4A. However, a funds transfer system rule may not directly or indirectly affect the rights of a customer that is not a participating bank in the funds transfer system.

g. Refunds to Customer and Customer's Duty to Report with Respect to Unauthorized Payment Orders

When, in unauthorized payment situations, (i) no commercially reasonable security procedure was in effect, (ii) the bank did not comply with a commercially reasonable security procedure that was in effect, (iii) the customer can prove that the culprit did not gain confidential security information controlled by the customer, or (iv) the bank had made an agreement to take all or part of the loss of unauthorized payment orders, the bank comes under a duty to refund to the customer any amount under the payment order that it is not entitled to enforce for any of the above-stated reasons.

Moreover, the bank may also be responsible for interest on the refunded amount. This amount is calculated from the date the

---

292 See id. § 4A-203 comment 5.
293 See id.
294 See id. § 4A-202(f); id. § 4A-203 comment 7.
295 See id. § 4A-203 comment 7.
296 See id. § 4A-501(b) & comment 1. Although Article 4A would permit funds transfer system rules to affect the rights of non-participants in other contexts indirectly, such effects concerning unauthorized payment order rights and obligations would probably not be permitted. See French, supra note 258, at 1441-42.
297 See U.C.C. § 4A-204(a) & comment 1.
bank received payment to the date the refund is made. This interest obligation, however, is conditioned on the customer (1) exercising ordinary care in determining that the order was not authorized by the customer and (2) notifying the bank of the relevant facts within a reasonable time, not exceeding 90 days from the time the customer received notice from the bank of the order being accepted or of its account being debited for the order. Failure of these conditions will lead only to no interest recovery by the customer; it will not result in any recovery by the bank from the customer.

The purpose of this provision is to induce customers to notify the receiving bank promptly of any unauthorized payment order. Prompt reporting will sometimes allow the bank to recover the money from the culprit of the fraud. Thus, the interest that the customer loses for failure to report unauthorized payment orders promptly acts as an incentive to report. "Reasonable time" will depend on the facts of each case, but in no event will reasonable time be construed as beyond 90 days from the notice to the customer of acceptance or debit to its account. Within that 90 day parameter, reasonable time may be fixed by agreement of the parties. The obligation to refund, however, is not subject to variation by agreement.

D. Liability Rules for Erroneous Payment Orders and Erroneous Instructions by the Sender

Apart from the issue of liability for unauthorized payment order activity, there is a further question of liability for errors in the content or transmission of payment orders and payment order instructions from the sender to the receiving bank. Article 4A provides explicit guidance in this area.

When a payment order (i) erroneously instructs payment to an unintended beneficiary, (ii) erroneously instructs payment in a greater amount than intended, or (iii) is an unintentional duplicate

298 See id. § 4A-204(a). The interest is to be calculated pursuant to the Article 4A formula described in U.C.C. § 4A-506. See supra notes 102-03 and accompanying text.
299 See U.C.C. § 4A-204(a).
300 See id.
301 See id. § 4A-204 comment 2.
302 See id.
303 See id.
304 See id. § 4A-204(b).
305 See id. § 4A-205.
of a previously sent payment order, the sender may be able to escape liability on the order.\textsuperscript{306} This escape from payment order liability is available to only those senders that have entered into commercially reasonable security procedure agreements with the receiving bank.\textsuperscript{307} Security procedures are designed not only to prevent unauthorized payment order activity but also to prevent losses due to errors in the content or transmission of a payment order.\textsuperscript{308}

If the sender can prove that it or a person acting on its behalf\textsuperscript{309} complied with an applicable security procedure and that the error would have been detected had the receiving bank also complied, the sender will not be obligated by the payment order.\textsuperscript{310} A recent case illustrating this principle is \textit{Shawmut Worcester County Bank v. First American Bank \& Trust.}\textsuperscript{311} In \textit{Shawmut}, the sender bank filed suit against the receiving bank when the receiving bank refused to refund its money after the sender discovered that the payment order it sent to the receiving bank erroneously asked it to credit the account of a party other than the intended beneficiary. Having determined that Florida law should govern the case, but finding no applicable precedent governing wire transfers, the court decided to apply Article 4A by analogy.\textsuperscript{312} The court held that since the sending bank had not proven that the error would have been detected if the receiving bank had complied with the security procedure, the sending bank would not be allowed to shift the risk of loss flowing from the error to the receiving bank.\textsuperscript{313}

Assuming proper proof, in cases involving payment of an unintended beneficiary or duplicate payment orders, the sender is not obliged to pay anything and the receiving bank must look for recovery from the beneficiary under the law of mistake and restitution.\textsuperscript{314} In cases involving payment orders instructing payment greater than the amount intended, the sender will not be obliged

\textsuperscript{306} \textit{See id.} § 4A-205 comment 1.
\textsuperscript{307} \textit{See id.; supra} notes 254-84.
\textsuperscript{308} \textit{See U.C.C.} § 4A-205 comment 1; \textit{id.} § 4A-201. Comment 1 to U.C.C. § 4A-205 describes how security procedures may be designed to prevent each of these types of errors.\textsuperscript{309} The "person acting on behalf of the sender" refers to a fund transfer system or other third party communications system that transmits payment orders as defined in U.C.C. § 4A-206(a).
\textsuperscript{310} \textit{See id.} § 4A-205(a)(1).
\textsuperscript{312} \textit{See id.} at 62-63.
\textsuperscript{313} \textit{See id.} at 64.
\textsuperscript{314} \textit{See U.C.C.} § 4A-205(a)(2).
to pay any amount over the intended amount. The excess must be recovered by the receiving bank from the beneficiary through the law of mistake and restitution. The rationale for allowing this loss to shift from the sender to the receiving bank, despite the sender's negligence, is the common law notion of last clear chance, found in tort law. Thus, if the receiving bank had the final opportunity to act reasonably and accordingly avoid the loss, it will be the party that suffers the risk of loss.

Despite the shift of risk of loss from the sender to the receiving bank, the receiving bank may have an opportunity to recover from the sender if the sender failed to exercise reasonable care in discovering and informing the receiving bank of the error. If the sender of an erroneous payment order is not obliged to pay for an erroneous payment order by operation of the above-discussed rules, and if the sender receives notice of that order being accepted by the bank or notice of its account being debited to pay for the order, the sender comes under this duty of reasonable care to discover the error and inform the bank. This duty requires the sender to exercise ordinary care, on the basis of the information available to it, to discover the error in the order and advise the bank of the relevant facts within a reasonable time, which shall not exceed 90 days from the date of notice of acceptance or account debit. If the receiving bank can prove that the sender failed in the exercise of this duty, the receiving bank may recover any losses incurred as a result of that failure, up to the amount of the payment order. Where timely notice would not have made any difference in the resulting losses to the bank, no recovery by the bank from the sender is allowed. The same last clear chance theory that allowed the sender to shift the risk of loss to the receiving bank for its noncompliance with the security procedure will also allow the receiving bank to shift the loss back to the sender for failure to give timely notice.

315 See id. § 4A-205(a)(3).
316 See id.
317 See id. § 4A-205 comment 2.
318 See id. § 4A-205(b).
319 See id.
320 See id. The sender has a duty to act on the information available to it, so a receiving bank might trigger a higher duty of care for the sender by supplying as much relevant information as possible in its notice of acceptance or account debit. See French, supra note 258, at 1445.
321 See U.C.C. § 4A-205(b).
322 See id. § 4A-205 comment 2.
323 See id.
The rights and obligations of the parties with respect to erroneous payment orders and payment order instructions are subject to variation by agreement. These rights and obligations are not among those that Article 4A treats as inviolable by funds transfer system rule or other private agreement.

E. Liability for Losses from Misdescription of the Beneficiary

1. Types of Misdescription Covered

An additional problem area for funds transfer participants is the problem of liability for losses resulting from a payment order that either (1) directs payment to a non-existent or unidentifiable person or account or (2) identifies a beneficiary by name and account number when the name and account number refer to different entities. Article 4A provides a liability scheme for losses arising from both of these fact patterns.

2. Rights of the Parties in the Case of Misdescription

In the non-existent or unidentifiable person scenario, Article 4A provides that no person shall have any rights in that payment order and acceptance of that order cannot occur. Each sender in the funds transfer transaction will be entitled to get its money back in this case.

In contrast, in the case of a mismatched name and account number, there are payment order rights created. In such a case, when the bank is not aware that the name and account number refer to different persons, the beneficiary’s bank is free to rely on the account number as the proper identification of the beneficiary to be paid. The beneficiary’s bank is under no duty to discover the mismatch between the name and the account number. If, however, the beneficiary bank is aware of the difference between the person identified by name and the person identified by account number, no person will have rights except the person paid by the beneficiary’s bank if that person was entitled to payment from the

324 See id. § 4A-205 comment 3.
325 See id. § 4A-207.
326 See id. § 4A-207(a).
327 See id. § 4A-207 comment 1.
328 See id. § 4A-207(b)(1).
329 See id.
originator of the funds transfer.\textsuperscript{330} If no person has rights as a beneficiary, acceptance cannot occur.\textsuperscript{331}

The impetus for these rules is the automated means by which many banks process payment orders, using a machine that identifies the beneficiary by the account number indicated in the payment order.\textsuperscript{332} Such a system allows payment orders to be processed very quickly and without the attendant risk of clerical error that accompanies manual handling of such transactions.\textsuperscript{333} If banks were required to verify that the account number on every payment order corresponds to the name of the beneficiary on the payment order, the additional expense and added potential for human error would destroy the efficiency of the automated handling system.\textsuperscript{334} Thus, beneficiary banks are allowed to pay to the account number when they do not know of the discrepancy between that number and the name on the payment order. If beneficiary banks do know of the mismatch, however, only the person paid by the beneficiary's bank has rights in that payment order, and then only if he is entitled to payment from the originator of the funds transfer.

The "knowledge" of the beneficiary bank will be construed in light of general Uniform Commercial Code definition of when a person has knowledge of information received by an organization.\textsuperscript{335} Under this rule, notice of information received by an organization will be effective for a particular transaction when it is brought to the attention of the particular individual conducting the transaction "and in any event from the time when it would have been brought to his attention if the organization had exercised due diligence."\textsuperscript{336} Since Article 4A stipulates that the beneficiary bank need not discover a discrepancy between the account number and the name on the payment order, the question of due diligence should not be an issue. The beneficiary bank should be deemed to know of the discrepancy only if it is brought to the attention of the person conducting the payment order transactions.

\textsuperscript{330} See id. § 4A-207(b)(2).
\textsuperscript{331} See id.
\textsuperscript{332} See id. § 4A-207 comment 2.
\textsuperscript{333} See id.
\textsuperscript{334} See id. It should be noted, however, that U.C.C. § 4A-207 also applies to banks that use non-automated processing. Thus, even when payment orders are handled manually, the beneficiary's bank is entitled to rely on the account number as accurately identifying the beneficiary to be paid.
\textsuperscript{335} See id. § 1-201(27).
\textsuperscript{336} Id.
3. **Liability of the Originator**

When the beneficiary’s bank was unaware of a discrepancy between the name and account number on a payment order, and it pays to the account number, the originator may or may not be obligated to pay its order. If the originator is a bank, it will be liable on its order, since banks are fully aware of how payment orders are processed and should have made certain that the name and account number identified the same person. If the originator was not a bank, and it proves that the person identified by number was not entitled to receive payment from the originator, the originator will not be obliged to pay for its order unless the originator’s bank proves that the originator had notice (prior to acceptance) of the possibility that the beneficiary’s bank would pay to the account number without checking it against the name on the payment order. This proof may be accomplished by any admissible evidence. The burden of proof is satisfied by the originator’s bank if the originator, before acceptance, signs a writing stating that it has notice of the possibility of the beneficiary bank paying directly to the account number without a cross-check against the name on the payment order.

4. **Recovery by the Originator/Originator’s Bank**

If a beneficiary’s bank is unaware of the discrepancy between the name and account number on a payment order, and it pays to the account number of a person not entitled to receive payment from the originator, the originator, or its bank, may recover from that person under the law of mistake and restitution, according to the following rules: (1) if the originator (bank or non-bank) is required to pay its payment order, then it has the right to recover from the person paid by the beneficiary’s bank; (2) if the originator is not a bank and is not obliged to pay its payment order, the originator’s bank will be allowed to seek such recovery from that person.

---

337 See id. § 4A-207(c)(1) & comment 3.
338 See id. § 4A-207(c)(2).
339 See id.
340 See id. Such a writing also will act as notice for any payment order accepted by the bank thereafter. See id. § 4A-207 comment 3.
341 See id. § 4A-207(d) & comment 3. Comments 2 and 3 to this section contain an extensive hypothetical illustration of how these rules governing misdescription of the beneficiary might play themselves out in terms of liability and recovery.
5. The Need for Rules to Govern Misdescription

The pre-Article 4A case law is unclear on the issue of a beneficiary bank’s responsibility in carrying out a payment order when the name and account number do not correspond to each other. Two cases illustrating this conflict are Bradford Trust Co. v. Texas American Bank and Securities Fund Services, Inc. v. American National Bank.

In Bradford Trust, the trust company brought action against a bank for reimbursement after the trust company wired funds to the bank and the bank erroneously credited the account specified without verifying that it matched up with the name. The court held in that case that the bank would not be responsible for the losses of the trust company even though the bank may have been negligent in not verifying that the account number matched the name on the wire transfer order. The court concluded that since the trust company’s own negligence in not catching the discrepancy was the primary cause of the loss, the trust company should bear the loss.

The plaintiff in Securities Fund Services brought suit against the defendant bank to recover funds that were wired by plaintiff to defendant. In this case, as in Bradford Trust, the bank credited the relevant account number without checking to see if it matched up with the name. However, the Securities Fund Services court held that the plaintiff could recover from the bank on a negligence theory for the bank’s failure to verify that the account number and the name referred to the same person.

Article 4A has resolved this conflict in the case law. In the case of misdescription of the beneficiary by a mismatched name and account number, the beneficiary’s bank is free to rely on the account number so long as it does not “know” of the discrepancy within the meaning of the Uniform Commercial Code. Only when such knowledge is shown may the originator of the funds transfer recover from the beneficiary’s bank. It is just this type of uncertainty in the law of funds transfers that Article 4A is appropriately geared to address.

---

342 See id. § 4A-207 comment 2.
343 790 F.2d 407 (5th Cir. 1986).
344 542 F. Supp. 323 (N.D. Ill. 1982).
345 See Bradford Trust Co. v. American Texas Bank, 790 F.2d 407, 411 (5th Cir. 1986).
F. Liability for Losses from Misdescription of an Intermediary Bank or Beneficiary's Bank

Fund transfer users may also realize losses from a payment order that misdescribes an intermediary bank to be used or misdescribes the beneficiary's bank. Two types of such misdescription are contemplated by Article 4A in its liability rules: (1) the payment order identifies the intermediary bank or beneficiary's bank by number only and the number does not correspond to the intended bank or (2) the payment order contains a bank number and a bank name which refer to different banks. Since automated processing systems at the receiving banks will identify the intermediary or beneficiary's bank by means of the identifying number and not the name on the payment order they receive, problems can arise under both of these fact patterns; both are resolved by Article 4A.

If the bank is identified by number only, the receiving bank is entitled to rely on the identifying number as the proper identification of the intended bank. Moreover the receiving bank is under no duty to determine whether in fact that number identifies a bank. The sender of the payment order bearing the erroneous identifying number will be obliged to compensate the receiving bank for any loss as a result of its reliance on the number in executing or attempting to execute the order.

When the bank name and identifying number on the payment order refer to different banks, liability will depend on whether the sender is a bank or non-bank and whether the sender had notice that the receiving bank might utilize the process of numerical identification in the processing of the payment order.

If the sender is a bank, the receiving bank is entitled to rely on the number as the proper identification of the intended bank if the receiving bank does not know of the discrepancy between the number and name of the bank. The receiving bank need not determine either that such a discrepancy exists or whether the

348 See id. § 4A-208 comment 1.
349 See id. § 4A-208(a)(1).
350 See id.
351 See id. § 4A-208(a)(2) & comment 2.
352 See id. § 4A-208(b).
353 See id. § 4A-208(b)(1).
number refers to an actual bank. The sender will be obliged to compensate the receiving bank for any losses it sustains in reliance on that number in executing or attempting to execute the order.

If the sender is not a bank, and the receiving bank can prove that the sender, before the payment order was accepted, had notice that the receiving bank might rely on the number as the proper identification of the intended bank, even though the name and the number refer to different banks, the sender will be liable as though the sender were a bank. Proof of this notice may be accomplished by any admissible evidence. One way this burden can be met by the receiving bank is through proof that the sender, before acceptance of the order, signed a writing stating that it had notice of the possibility of reliance by the receiving bank on the identifying number alone.

Article 4A, in its treatment of misdescription of the beneficiary or misdescription of a bank, clearly shows the drafters' intent to accommodate the needs of banks that use automated means to process payment order transactions. A regulatory scheme that unduly impeded the swift processing by automated means, through the imposition of additional verification duties on the banks receiving payment orders, would jeopardize the quick, low cost nature of these transactions that has made them such an efficient means of moving money. Article 4A does not place such onerous additional duties on the banks, but rather rationally allocates loss liability in favor of those banks without knowledge of a mistake, and adverse to those banks or senders that caused a mistake and were aware of the potential for resulting losses from misdescription. Article 4A thus accomplishes the drafters' goals of coherent regulation, without imposing unwarranted economic hardships on funds transfer participants.

354 See id. Interestingly, however, Article 4A is silent as to whether the receiving bank must determine that the name of the bank on the payment order refers to an actual bank or not. The assumption of the drafters is that most of these transactions are handled by automated means, signifying that banks are identified by number alone. If there were a receiving bank that processed these transactions manually and identified banks by name rather than number, the question is perhaps open as to whether the receiving bank must verify that the named bank really exists.

355 See id.
356 See id. § 4A-208(b)(2).
357 See id.
358 See id. § 4A-208 comment 3.
G. Liability for Erroneous Execution of a Payment Order

1. Types of Erroneous Execution

In the previous sections, dealing with misdescription liability, the focus was on the allocation of liability for losses from errors that originated with the sender of a payment order. The focus in this and the next several sections will be on the allocation of liability for losses flowing from errors that originate with the receiving bank. The first issue to be discussed is liability for a payment order that is erroneously executed by the receiving bank.

Article 4A deals with several varieties of erroneous execution of a payment order: (1) the receiving bank executes the order by issuing a payment order in an amount greater than the amount of the sender's order; (2) the receiving bank issues a payment order in execution of a sender's order and then issues a duplicate order; (3) the receiving bank executes a sender's payment order by issuing a payment order in an amount less than the amount of the sender's order; and (4) the receiving bank executes a sender's payment order by issuing a payment order to the wrong beneficiary. In all of these cases of erroneous execution, the sender's payment obligations to the receiving bank will be defined differently from what they ordinarily would.

2. Liability for Erroneous Execution

In the first two situations, overpayment or duplicate orders, the receiving bank will be entitled to payment of the amount of the sender's order. The receiving bank will be entitled to recover from the beneficiary of the erroneous order any excess payment to the extent allowed by the law governing mistake and restitution. A recent case illustrating recovery through the law of mistake and restitution, under the laws of New York State, which recently adopted Article 4A, is Banque Worms v. BankAmerica Interna-

---

360 See id. § 4A-303.
361 See id. § 4A-303 comment 1. As the comment indicates, the sender's payment obligations to the receiving bank are defined by § 4A-303 in this situation; section 4A-303 takes precedence over § 4A-402(c) in the case of erroneous execution by the receiving bank.
362 See id. § 4A-303(a).
363 See id.
In that case, a receiving bank mistakenly issued a duplicate payment order to effect the same transaction. In the suit for recovery brought by the receiving bank against the beneficiary it mistakenly paid, the court held that the “discharge for value” doctrine of the law of restitution would allow the beneficiary to keep the money. Under the doctrine, a third party’s mistaken payment on a debtor’s behalf to an innocent creditor need not be refunded to that third party; hence the receiving bank would not be entitled to recovery. Although the newly adopted Article 4A could not be applied retroactively to the case, the court noted that Article 4A stipulates that the applicable law of mistake and restitution should govern any recovery by the receiving bank in such an instance.

When the receiving bank executes a payment order by issuing a payment order in an amount less than that of the sender’s payment order, the receiving bank will be entitled to full payment of the sender’s payment order, so long as the receiving bank corrects its mistake by issuing an additional payment order for the benefit of the beneficiary of the sender’s order. If the mistake is not corrected, however, the issuer of the erroneous order will only be entitled to receive or retain, from the sender of the order it accepted, the amount of the erroneous order. This rule does not apply when a payment order is issued in a lesser amount than the order of the sender so that charges and expenses for services to effect the transaction can be collected.

If the receiving bank executes the payment order of the sender by issuing a payment order to the wrong beneficiary, and the funds transfer is completed with a payment to that wrong beneficiary, the sender of the payment order that was erroneously executed, and all prior senders, are not obliged to pay the payment orders

---


367 See id., 568 N.Y.S.2d at 548-49; see also RESTATEMENT OF RESTITUTION § 14 (1937).

368 See Banque Worms, 570 N.E.2d at 195, 568 N.Y.S.2d at 547.


370 See U.C.C. § 4A-303(b).

371 See id.

372 See id.
they issued.\textsuperscript{373} Again, the issuer of the erroneous order may recover from the wrongly paid beneficiary to the extent allowed by the law governing mistake and restitution.\textsuperscript{374}

The question remains undecided under Article 4A as to the result if the receiving bank erroneously executes a sender’s payment order by issuing a payment order to the wrong beneficiary’s bank, resulting in no payment being made.\textsuperscript{375} Most likely, under the “money-back guarantee” provision of Article 4A,\textsuperscript{376} the sender would not be obliged to pay the receiving bank, or would be entitled to a refund with interest if it already had paid. This right to a refund exists because, in such an event, the sender’s order did not lead to acceptance by the beneficiary’s bank of an order directing that bank to pay the beneficiary.\textsuperscript{377} Under the money back-guarantee, every party to the transaction will get its money back, unless some bank in the chain of the funds transfer suspended payments.\textsuperscript{378}

3. Duty of the Sender to Notify of Erroneous Execution

If the sender of an erroneously executed payment order receives notice from the receiving bank of the execution of the order, or notice of its account being debited to pay for the order, the sender comes under a duty to (1) exercise ordinary care to determine, on the basis of the information available to it, whether the order was erroneously executed, and (2) notify the receiving bank of the relevant facts within a reasonable time, not to exceed 90 days from the date of notification of acceptance or account debit.\textsuperscript{379} If the sender fails in these duties, the bank will not be obliged to pay any interest on the amount refundable to the sender as a result of the erroneous execution of the payment order.\textsuperscript{380} The rationale for

\textsuperscript{373} See id. § 4A-303(c).
\textsuperscript{374} See id.
\textsuperscript{375} See Baxter & Bhala, Proper and Improper Execution of Payment Orders, 45 Bus. Law. 1447, 1461 (1990) [hereinafter Baxter & Bhala II].
\textsuperscript{376} See U.C.C. § 4A-402(c).
\textsuperscript{377} See Baxter & Bhala II, supra note 375, at 1461-62.
\textsuperscript{378} See id. at 1462; supra notes 150-53 and accompanying text (explaining the treatment of suspension of payments by an intermediary bank under U.C.C. § 4A-402(e)).
\textsuperscript{379} See U.C.C. § 4A-304.
\textsuperscript{380} See id. U.C.C. § 4A-402(d) provides that in general, any time a sender is not obliged to pay all or part of the amount of a payment order, the bank receiving payment is obligated to refund the sender’s money with interest as calculated under U.C.C. § 4A-506. See supra notes 102-03 and accompanying text (explaining Article 4A’s interest for-
this provision is the same as the rationale for denying interest to a sender that fails in the duty to notify of unauthorized transactions.\textsuperscript{381} Prompt notification may assist the bank in recovering its money, so the sender that delays notice is encouraged to give prompt notice on pain of losing the interest on his refund.\textsuperscript{382}

The 90 day reasonable notice provision is subject to variation by agreement, or funds transfer system rule, so that counsel for senders will want to be on the alert for such provisions in any agreement to be executed or for the rules of any funds transfer system being employed by the sender.\textsuperscript{383}

\textbf{H. Liability for Late Execution, Improper Execution, or Failure to Execute}

1. \textit{General Liability for Late and Improper Execution}

In addition to establishing liability rules for a receiving bank's erroneous execution of a payment order, Article 4A also includes a scheme of liability allocation for late execution of a payment order, improper execution of a payment order, and for the failure of a receiving bank to execute a payment order at all.\textsuperscript{384} Each of these is treated separately under Article 4A.

If a funds transfer is completed, but the execution has resulted in a delay in payment to the beneficiary, the bank whose execution caused the delay will be obligated to pay interest to either the originator or the beneficiary of the funds transfer for the period of delay.\textsuperscript{385} The expectation with most wire transfers (except automated clearing house transactions) is that they will be completed the same day as they were begun. So, delay in execution is an aberrational result for which Article 4A creates an interest penalty as an incentive for receiving banks to execute promptly if they choose to accept a payment order.\textsuperscript{386} The normal practice is to

\textsuperscript{381} See U.C.C. § 4A-204 comment.
\textsuperscript{382} See id. § 4A-204 comment 2.
\textsuperscript{383} See Patrikis, Baxter & Bhala, \textit{supra} note 279, at 240.
\textsuperscript{384} See U.C.C. § 4A-305.
\textsuperscript{385} See id. § 4A-305(a). The interest will be calculated on the basis of U.C.C. § 4A-506. \textit{See supra} notes 102-03 and accompanying text (explaining Article 4A's interest formula).
\textsuperscript{386} See U.C.C. § 4A-305 comment 1.
compensate the beneficiary's bank so it can compensate the beneficiary by back-valuing the payment by the number of days of delay, thereby putting the beneficiary in the same position he would have been in had the funds transfer been completed on time.\textsuperscript{387} No other damages, except consequential damages, are recoverable for late execution.\textsuperscript{388}

If the receiving bank did not merely delay in executing the payment order, but rather made an improper execution by (1) not completing of the funds transfer, (2) failing to use the intermediary bank designated by the originator, or (3) issuing a payment order not in compliance with the terms of the originator's payment order, the receiving bank will be liable to the originator for its expenses in the funds transfer and for additional incidental expenses and interest losses not covered by the interest penalty for delay.\textsuperscript{389} As above, no other damages, except consequential damages, may be recovered for improper execution.\textsuperscript{390}

\textbf{2. Consequential Damages Liability}

For both late execution and improper execution, consequential damages may be awarded to the extent that they are provided for in an express written agreement of the receiving bank.\textsuperscript{391} Some banks may be willing to execute such an agreement in exchange for a higher funds transfer services fee.\textsuperscript{392} While the term consequential damages is not defined in the statute, the drafters meant the term to include indirect damages, such as lost profits, lost investment opportunities, and losses attributable to price fluctuations (if the payment was a commodity).\textsuperscript{393}

This rule of no consequential damages without prior express written agreement is in contrast to Article 4A's other rule on consequential damages available to the beneficiary that is refused rightful payment by the beneficiary's bank.\textsuperscript{394} In that context,

\textsuperscript{387} See id.

\textsuperscript{388} See id. § 4A-305(a); infra notes 391-402 and accompanying text (discussing consequential damages).

\textsuperscript{389} See U.C.C. § 4A-305(b) & comment 2.

\textsuperscript{390} See id. § 4A-305(b).

\textsuperscript{391} See id. § 4A-305(c).

\textsuperscript{392} See id. § 4A-305 comment 2.

\textsuperscript{393} See Baxter & Bhala II, supra note 375, at 1463.

\textsuperscript{394} See U.C.C. § 4A-404(a) & comment 2; supra notes 176-88 and accompanying text (explaining consequential damage availability to the beneficiary in this context and the beneficiary's bank's defense of reasonable doubt as to the right to payment).
consequential damages are available so long as the beneficiary can show that the beneficiary’s bank had notice of certain “special circumstances”—namely, that refusal to pay would lead to specified consequential damages to the beneficiary. This “special circumstances” rule on consequential damages derives from the holdings in cases such as Evra Corp. v. Swiss Bank Corp. The court in Evra held that under the common law notion of consequential damages in contract law, as exemplified by the classic case of Hadley v. Baxendale, the defendant bank would not be liable for the consequential damage claims, valued in excess of $2 million, since it had no notice that such a large amount of damage could be caused by its failure to pay a mere $27,000 to the beneficiary.

In contrast, the rule on consequential damages for improper or late execution requires prior express written agreement as a predicate to liability; mere notice of “special circumstances” will not suffice. The rationale for this requirement is that personnel of the receiving bank that process payment orders are not the appropriate people to evaluate complex consequential damages risks in relation to the price being charged for wire transfer service. Even if higher level management personnel were making these evaluations, it would have to be done individually for each payment order. Such a result would not be consonant with the high speed, low price, mechanical nature of the wire transfer processing system. The argument essentially states: “Whether banks can continue to make EFT services available on a widespread basis, by charging reasonable rates, depends on whether they can do so without incurring unlimited consequential risks. Certainly no bank would handle for $3.25 a transaction entailing potential liability in the millions of dollars.” The position taken by the drafters of Article 4A is that the originator of the funds transfer is in the best position to (1) evaluate the risk of late or improper execution and (2) manage that risk by issuing a payment order in sufficient time to allow for monitoring of the transaction and correction of any error. Thus, without an express agreement to be liable for con-

395 See U.C.C. § 4A-404(a).
396 673 F.2d 951 (7th Cir. 1982). For a discussion of Evra, see supra notes 179-81 and accompanying text.
397 See Evra, 673 F.2d at 956.
398 See U.C.C. § 4A-305 comment 2.
399 See id.
400 Id. (quoting an industry amicus brief in Evra).
401 See id.
sequential damages, contrary to the rule in *Evra* and other cases, notice of special circumstances is not enough to establish liability for improper or late execution.

3. *Failure to Execute*

If a receiving bank fails to execute a payment order that it was obliged by agreement to execute, the receiving bank will be liable to the sender for its expenses in the transaction and for incidental expenses and interest losses resulting from the failure to execute. Any additional damages, including consequential damages, are recoverable only with a prior express written agreement signed by the receiving bank. Without an agreement obligating the receiving bank to accept the sender’s payment orders, the failure to execute creates no liability.

4. *Attorney’s Fees*

Reasonable attorney’s fees are recoverable by the originator or the beneficiary for late or improper execution if demand for such compensation is made of the receiving bank and refused before action is brought on the claim. If a claim for damages for failure to execute is brought and the agreement to accept payment orders does not provide for damages, reasonable attorney’s fees will be recoverable as compensation if a demand for compensation is made of the receiving bank and refused before an action is brought on the claim. There will not be any award of attorney’s fees for failure to execute if the agreement to accept contains a damage provision. This is because the parties have already agreed on a measure of damages, which may or may not have contemplated attorney’s fees.

5. *Variation by Agreement*

The liability of a receiving bank to an originator or beneficiary for late or improper execution may not be varied by agreement.

---


403 See U.C.C. § 4A-305(d). Such agreements are discussed in U.C.C. § 4A-212.

404 See id. § 4A-305(d).

405 See id. § 4A-305 comment 3.

406 See id. § 4A-305(e).

407 See id.

408 See id. § 4A-305 comment 4.

409 See id. § 4A-305(f) & comment 5.
However, banks' counsel should advise their clients that establishing early cut-off times for the processing of funds transfer business will reduce the likelihood of liability for delay in execution.\textsuperscript{410} Although, competitive pressures in the banking industry will limit the ability of banks to demand earlier than practicable cut-off times for their funds transfer users.\textsuperscript{411}

CONCLUSION

Article 4A represents the best available framework for closing the gaps in the current law applicable to funds transfer activity. Article 4A is especially needed today, given the currently unsettled nature of the United States financial sector. By answering the presently unanswered legal questions that funds transfer activity raises, Article 4A will lend precisely the sort of predictability needed for the continuation of this country's high speed, low cost, efficient mode of funds transfer processing. Given the need for uniformity in this country's banking laws, some may argue that federal rather than state adoption of Article 4A is needed for quick and uniform enactment of its provisions.\textsuperscript{412} Yet, regardless of how Article 4A is implemented, its implementation is the precise sort of remedy needed for the confusion that now confounds courts trying to resolve liability issues with no coherent statutory or common law framework to guide them. This commentator urges the adoption of Article 4A, post-haste.

\textsuperscript{410} See Patrikis, Baxter & Bhala, \textit{supra} note 279, at 241-42.
\textsuperscript{411} See \textit{id.} at 242.