The Role of Negligence in Section 3-405 of the Uniform Commercial Code: Owensboro National Bank v. Crisp

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COMMENTS

THE ROLE OF NEGLIGENCE IN SECTION 3-405 OF THE UNIFORM COMMERCIAL CODE: OWENSBORO NATIONAL BANK V. CRISP

INTRODUCTION

Section 3-405 of the Uniform Commercial Code\(^1\) (Code) adopts the common law impostor and fictitious payee doctrines as exceptions to the general rule that forged indorsements are ineffective to pass title to an instrument. Under this section, an indorsement made by one other than the named payee nevertheless will be effective where the drawer was induced to issue the instrument by the fraudulent misrepresentations of an impostor\(^2\) or where a drawer, his agent or employee issued an instrument intending the payee to have no interest therein.\(^3\) The rationale underlying the impostor and

\(^1\) U.C.C. § 3-405 states:
(1) An indorsement by any person in the name of a named payee is effective if
   (a) an impostor by use of the mails or otherwise has induced the maker or drawer to issue the instrument to him or his confederate in the name of the payee; or
   (b) a person signing as or on behalf of a maker or drawer intends the payee to have no interest in the instrument; or
   (c) an agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest.

(2) Nothing in this section shall affect the criminal or civil liability of the person so indorsing.

U.C.C. references are to the 1972 Official Text. For the sake of uniformity, references to particular state statutes equivalent to specific U.C.C. counterparts will be cited by U.C.C. section numbers only.

\(^2\) U.C.C. § 3-405(1)(a). In the interest of simplicity, the "maker or drawer" will hereinafter be referred to as the "drawer."

\(^3\) U.C.C. §§ 3-405(1)(b), (c). The traditional fictitious payee situation is that contemplated by § 3-405(1)(b), in which the drawer himself issues the check to one who is to take no interest in it. See U.C.C. § 3-405, comment 3, for examples of this situation. Section 3-405(1)(c) contemplates what is commonly referred to as a "padded payroll scheme," in which an employee supplies the fictitious name to the drawer of the payroll checks. See U.C.C. § 3-405, comment 4, quoted in part at note 31 infra for
fictitious payee rules appears to be the same as that underlying Code sections 3-406 and 4-406: that is, that the drawer, by contributing to the forgery through his own negligence, should not subsequently assert that forgery against the drawee bank. Section 3-405, however, unlike sections 3-406 and 4-406, contains no express provision permitting the drawer to show that the payor bank was negligent in failing to pay the instrument in accordance with reasonable commercial standards. Whether a negligence standard nonetheless should operate in cases decided under section 3-405 is a question which has split the courts in recent years. The Kentucky Court of Appeals considered the issue in its recent decision in Owensboro National Bank v. Crisp.

The court in Crisp took a novel approach to section 3-405. Since Crisp involved an impostor, the court refused to

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examples of this situation: Both examples normally occur within a business establishment and involve conscious wrongdoing on the part of the drawer or his agent. They therefore will be collectively referred to as “fictitious payees” throughout this comment.


U.C.C. § 3-406 provides:

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

U.C.C. § 4-406 provides in pertinent part:

(2) If the bank establishes that the customer failed... to comply with the duties imposed on the customer by subsection (1) the customer is precluded from asserting against the bank

(a) his unauthorized signature or any alteration on the item if the bank also establishes that it suffered a loss by reason of such failure;

(3) The preclusion under subsection (2) does not apply if the customer establishes lack of ordinary care on the part of the bank in paying the item(s).

5 The party who takes the instrument for payment or deposit will not always be the drawee bank, of course. For the purpose of simplicity, however, this party will be denominated throughout this comment as either the “drawee” or “payor” bank.


6a The Court of Appeals, after some discussion of the issue, concluded that the
adopt the reasoning of any case decided under the fictitious payee provisions of section 3-405,7 thus disregarding a significant number of well-reasoned cases which have held that negligence is not a factor to be considered in section 3-405 cases.8 The court then determined that one who had been defrauded by an imposter, even though negligent himself, should not be made to bear the loss where the payor bank failed to follow reasonable commercial standards.9 Although sound principles of fairness support the approach taken by the court in Crisp, these principles should be balanced against the Code's stated purpose of simplifying, clarifying, and modernizing the law of commercial transactions.10 This comment will explore the rationale for and the soundness of distinguishing impostors from fictitious payees and will suggest that the question of the role of negligence in Code section 3-405 be resolved by placing the loss on the drawer in all cases except those where the drawer exercised care and the bank exercised none.

I. IMPOSTORS AND FICTITIOUS PAYEES AS SEPARATE CLASSES

A. Historical Development of the Doctrines11

The imposter rule as it developed at common law established the nearly uniform practice of placing the loss resulting

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7 The court specifically referred to the decision in General Accident Fire & Life Assurance Corp. v. Citizens Fidelity Bank & Trust Co., 519 S.W.2d 817 (Ky. 1975), based on U.C.C. § 3-405(1)(c).
9 No. 78-CA-401-MR at 9-10.
10 "Underlying purposes and policies of this Act are (a) to simplify, clarify, and modernize the law governing commercial transactions . . . ." U.C.C. § 1-102(2).
11 Many of the concepts discussed and adopted in the following sections are analyzed at length in Abel, The Impostor Payee: or, Rhode Island Was Right: I, 1940 Wis. L. Rev. 161 [hereinafter cited as Abel I] and Abel, The Impostor Payee II, 1940 Wis. L. Rev. 362 [hereinafter cited as Abel II].
from an impersonation on the drawer, the first party to deal with the imposter. Some courts reasoned that the drawer actually intended to issue the check to the person with whom he dealt. Others focused on the negligence of the drawer in not discovering the true identity of the imposter or on the desirability of insuring the negotiability of commercial paper. Despite the wide acceptance of the rule, exceptions did emerge.

One significant exception to the strict application of the imposter rule appeared in those cases in which the drawer of the instrument exercised care in attempting to identify the person with whom he dealt, but the second deceived party (normally a bank) did not. The courts in these cases tended to place the loss on the second victim, the only truly negligent party to the transaction. Despite the development of a well-established body of law from these impostor cases, the Negotiable Instruments Law (N.I.L.), promulgated in 1896, did not address the issue. However, most courts continued to apply the common law impostor rule.

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15 Abel II, supra note 11, at 376-77.

16 Courts often distinguished between face-to-face transactions and those occurring through the mails. Others sometimes refused to apply the impostor rule where the impostor was merely claiming to be the agent of another. See Note, UCC Section 3-405; Of Impostors, Fictitious Payees, and Padded Payrolls, 47 FORDHAM L. REV. 1083, 1087-89 (1979).


18 See generally Abel I, supra note 11, at 193-98.

19 The Negotiable Instruments Law was adopted by the Committee on Uniform Laws and by the American Bar Association in 1896. It quickly found wide acceptance among American jurisdictions. F. Beutel, Beutel's Brannan Negotiable Instruments Law (7th ed. 1948). Though attempts were made to apply §§ 9(3), 23, and 61 of the Negotiable Instruments Law (hereinafter cited as N.I.L.) to impostor cases, it is generally agreed that it was not applicable to such cases. Abel I, supra note 11, at 201-17.

20 Note, supra note 16, at 1087.
The fictitious payee doctrine, unlike the impostor rule, figured prominently in the drafting of the Negotiable Instruments Law. Section 9(3) of the N.I.L. restated the common law maxim that a check issued by a drawer to the order of a fictitious payee became bearer paper.21 Courts uniformly applied this section to situations in which the drawer intended that the payee have no interest in the instrument but held it inapplicable to the "padded payroll" cases,22 since the knowledge of the employee who supplied his employer with the fictitious name was not considered a fact known to the person making the check payable.23 An amendment to N.I.L. section 9(3), however, provided that the knowledge element could be supplied by the agent or employee who furnished the name of the payee,24 indicating that no "padded payroll" exception had been intended.

The Uniform Commercial Code was designed to revise and clarify the law which had developed under the N.I.L.25 Consistent with the amended version of the N.I.L., the Code's drafters included both the traditional fictitious payee and the padded payroll cases within section 3-405.26 Despite the entirely separate development of the impostor and fictitious payee rules at common law and under the N.I.L., however, the drafters decided that the similarities between the two doctrines justified including both within the same provision.

21 "The instrument is payable to bearer . . . (3) when it is payable to the order of a fictitious or nonexisting person, and such fact was known to the person making it so payable. . . ." Uniform Negotiable Instruments Law § 9(3).
25 The amendment added to N.I.L. § 9(3) the words "or known to his employee or other agent who supplies the name of such payee." See Note, supra note 16, at 1090 nn.42 & 43.
27 The drafters rejected, however, the N.I.L. approach of treating the fraudulently issued instrument as bearer paper. Comment 1 to U.C.C. § 3-405 states that the instrument remains order paper and that indorsements are still necessary to its negotiation.
B. Policies Affecting Allocation of the Risk of Loss

The Code approach of combining impostors and fictitious payees within section 3-405 undoubtedly resulted from the common elements in the two situations. In both, there is a "discrepancy, real or nominal, between the identity of the person actually dealing with the paper and of the person to whom it purports to have been payable and by whom it purports to have been indorsed."\textsuperscript{28} Additionally, one may view the two cases as closely related in that both originate in fraud. Beyond these two similarities, however, the situations differ in areas which are crucial in determining which party should bear the risk of loss.

Fictitious payee cases are said to involve "unilateral imposture."\textsuperscript{29} The drawer, or his agent or employee, in supplying the name of one who is to take no interest in the instrument, is fully aware of the ensuing forgery. Only the payor bank is deceived as to the identity of the indorser. Impostor cases, on the other hand, involve a "dual imposture";\textsuperscript{30} that is to say, both the drawer and the payor bank have been deceived as to the identity of the payee. This dual/unilateral classification of imposture is important in determining the culpability of the drawer in each situation. In fictitious payee cases, the drawer or his agent knowingly names as payee a person who ultimately will take no interest in the check. There is thus a conscious intent on the part of the drawer or his agent to deceive the payor bank as to the identity of the indorser. In the impostor cases, however, the wrongdoing on the part of the drawer is limited to his negligence in issuing a check to one who, in many cases, has effected a quite skillful impersonation. Regardless of his degree of negligence, the drawer has no conscious intent to deceive.

Economic considerations also justify a distinction between the two classes of "wrongdoers." Unlike the drawer in a true impostor situation, the wrongdoer in a fictitious payee case can almost always be found in an internal position within

\textsuperscript{28} Abel I, supra note 11, at 170.  
\textsuperscript{29} Id. at 166.  
\textsuperscript{30} Id.
a business organization. The Code expressly recognizes this fact in the official comments to section 3-405(1)(c): "The principle followed is that the loss should fall upon the employer as a risk of his business enterprise rather than upon the subsequent holder or drawee." It is obvious that this economic justification has no merit when the drawer is an individual deceived by an impostor.

When section 3-405 is examined in light of its history and policy, it is apparent that the Code's drafters, in their effort to simplify the divergent law relating to impostors and fictitious payees, overlooked the fundamental differences between the two. Confusing and inconsistent case law has perpetuated the inequities created by the Code provision. An examination of this case law will demonstrate the ways in which courts have dealt with the question of negligence in cases involving impostors and fictitious payees.

II. THE COURTS' VIEWS OF THE ROLE OF NEGLIGENCE IN SECTION 3-405

Courts and commentators agree that section 3-405 is not an absolute guarantee of protection to a payor bank. Implicit in all provisions of the Code is the obligation on all parties to act in "good faith." Unlike article 2 of the Code, in which the good faith standard includes "the observance of reasona-

31 U.C.C. § 3-405, comment 4. This comment adds in pertinent part: The reasons are that the employer is normally in a better position to prevent such forgeries by reasonable care in the selection or supervision of his employees, or, if he is not, is at least in a better position to cover the loss by fidelity insurance, and that the cost of such insurance is properly an expense of his business rather than of the business of the holder or drawee.


34 "Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement." U.C.C. § 1-203. For a general discussion of the role of good faith in the U.C.C., see 1 R. ANDERSON, UNIFORM COMMERCIAL CODE, § 1-203 (2d ed. 1970).
ble commercial standards of fair dealing in the trade,”35 article 3, lacking a definition of its own, resorts to the Code’s general provision which defines good faith as “honesty in fact.”36 Cases decided under section 3-405 have uniformly recognized this obligation of good faith on the part of the bank.37 “Negligence,” on the other hand, is a more stringent standard than “good faith,” running specifically to the observance of the reasonable commercial standards of a bank’s business.38 It also is defined as the failure to use ordinary care.39 While banks must act in good faith, whether they also must be free from negligence is unclear. The courts are in disagreement as to whether a bank is precluded from invoking the protection of section 3-405 when it has been negligent by failing to follow reasonable commercial standards.

A. Cases Regarding Negligence as an Irrelevant Factor

The most frequently encountered argument for the position that negligence is not to be considered in a section 3-405 case is based on the absence of qualifying language in the Code provision itself. One federal district court, in Prudential Insurance Co. v. Marine National Exchange Bank,40 noted the “conspicuous absence” in section 3-405 of a requirement that the paying or collecting bank exercise ordinary care.41 It then went on to hold that where the drawer’s employee had supplied a policy holder’s name to the insurer and then forged that name on a $20,000 check, section 3-405(1)(c) applied and rendered the question of the drawee bank’s alleged negligence immaterial.42

35 U.C.C. § 2-103(1)(b). This standard is applied only to “merchants” as defined in § 2-104(1).
36 “‘Good faith’ means honesty in fact in the conduct or transaction concerned.” U.C.C. § 1-201(19).
37 See the cases cited in note 33 supra for a list of relevant source material.
38 This standard is referred to in U.C.C. § 3-406. See note 4 supra for the full text of U.C.C. § 3-406.
41 371 F. Supp. at 1003.
42 Id. The court also mentioned comment 4 to U.C.C. § 3-405 and the lack of
Applying the Code’s impostor provision, a Texas court in *Fair Park National Bank v. Southwestern Investment Co.*,\(^{43}\) emphasized the reasoning behind the impostor rule in fixing the loss resulting from an impersonation on the drawer of the draft.\(^{44}\) According to the court in *Fair Park*, this policy is to “throw the loss . . . on the person who dealt with the impostor, and, presumably, had the best opportunity to take precautions that would have detected the fraud, rather than on a subsequent holder who had no similar opportunity.”\(^{45}\)

The Kentucky Court of Appeals in *General Accident Fire & Life Assurance Corp. v. Citizens Fidelity Bank and Trust Co.*\(^{46}\) suggested yet another justification for holding that the drawer should bear the loss, notwithstanding the collecting bank’s negligence. The *General Accident* case, decided under section 3-405(1)(c), involved an employer’s attempt to recover the loss resulting from the bank’s payment of drafts bearing indorsements forged by an employee. In affirming an order of summary judgment for the bank, the Court expressed its view of the reasons behind section 3-405: “It seems that the particular statutory section with which we deal is a banker’s provision intended to narrow the liability of the banks and broaden the responsibility of their customers.”\(^{47}\)

The pre-Code case of *Dartmouth National Bank v.*...
Keene National Bank suggested a view more protective of the public interest. In Dartmouth, the Supreme Court of New Hampshire examined other impostor cases and found that the policy of free circulation of commercial paper was sufficient reason in the ordinary case for placing the loss on the drawer in an impostor situation. It placed one significant limitation upon this generalization, however, by pointing out that the loss may be properly allocated to the second victim of an imposture where the first victim exercised care and the second victim exercised none.

B. Cases Applying a Negligence Standard

The most frequently invoked rationale in cases which have allowed a negligence standard to operate in section 3-405 is that the bank lacked the requisites for holder in due course status. In Sun 'n Sand, Inc. v. United California Bank, the Supreme Court of California held that the bank had notice of an obvious irregularity when the drawer's employee attempted
to deposit into his own account checks naming the bank as payee. § 3-405, therefore, was held not to bar the plaintiff's cause of action against the bank for negligence. Similarly, in McConnico v. Third National Bank, the Supreme Court of Tennessee found that transactions involving checks made payable to a corporation which were then deposited into the president's personal account were "highly irregular" and constituted sufficient notice to deprive the defendant bank of its holder in due course status. In Dayton, Price & Co. v. First National City Bank, the collecting bank's teller was found to have violated normal banking procedures which required that he obtain authorization to cash certain checks. Here again, the court denied holder in due course status to the bank since it had notice of the irregularity of the transactions.

The negligence standard is not always articulated in terms of whether the defendant bank qualifies as a holder in due course. In Wright v. Bank of California, a California court found that if the drawer's loss could be shown to have been proximately caused by the bank's lack of due care in failing to determine the authority of the person applying for a cashier's check, section 3-405 would not bar the drawer's cause of action. The Supreme Court of Nebraska, in Travelers Indemnity Co. v. Center Bank, considered the alleged negligence of the payor bank in failing to make reasonable inquiry as to the authority of the drawer company's employee to

53 "The bank does not have to be especially vigilant; its agent need only read what appears on the face of the check to be warned that a fraud may be in progress." Id. at 937.
54 Id. In fact, the court declared that § 3-405 did not apply at all in the context of this transaction.
55 499 S.W.2d 874 (Tenn. 1973).
56 Id. at 886.
58 Id. at 456-57.
59 Id. at 457.
61 Id. at 14. Of course it is possible to argue, as the court here seems to suggest, that § 3-405 was never intended by its drafters to cover the peculiar facts of this case.
62 275 N.W.2d 73 (Neb. 1979).
deposit company checks into his own account. The court found that in this case failure to inquire was not a breach of duty to the drawer.\textsuperscript{63} The court pointed out, however, that there are cases, notwithstanding section 3-405, in which a bank may be liable to a drawer for its negligence. Before such negligence can arise, "there must be some showing that the bank was either placed on such notice as to require further investigation or acted in a manner which was commercially unreasonable."\textsuperscript{64}

The reasoning used in these cases permitting the operation of a negligence standard is largely superficial. In contrast to the "negligence as irrelevant" group of cases, which carefully consider the absence of qualifying language in the Code, the Code's policy of placing the loss on the party presumably best able to avoid the fraud, and the public's interest in the free circulation of commercial paper, the courts in this second group of cases simply express an attitude that the payor bank, having been negligent or having lost its holder in due course status, should not escape liability. While other courts and numerous commentators have agreed that banks should not be able to escape their duty to exercise ordinary care merely because the Code's impostor and fictitious payee provisions have come into play,\textsuperscript{65} the first court to articulate fully its justification for such a position was the Kentucky Court of Appeals in its recent decision in \textit{Owensboro National Bank v. Crisp}.\textsuperscript{66}

C. Owensboro National Bank v. Crisp

The victim of the imposture in \textit{Crisp} was an aging man,
Sam Crisp, who suffered from poor eyesight and arthritis. Crisp was advised by a stranger falsely representing himself as "Bill Carter" of Southern Construction Company that the lightning rod on Crisp's house needed repairs. After making the purported repairs, Carter told Crisp that the charge for the work was $12.50. Because of his failing eyesight and arthritis, Crisp permitted Carter to fill out the check. Carter willingly complied, raising the amount to $6,212.50 after Crisp had signed the instrument. Carter immediately cashed the check at Crisp's bank and disappeared. Crisp then sued the bank to have his account recredited.67

The court identified two issues in Crisp. The first involved the alteration of the check from $12.50 to $6,212.50. The court quickly held that the bank was liable for the altered amount.68 The court then turned to the second issue, the application of section 3-405's impostor provision to that portion of the check which was otherwise properly payable.69 It first observed that the decision in General Accident70 would seem to dispose of the issue, since that case held that under section 3-405(1)(c), negligence was inapplicable to the question of the allocation of loss. The court then stated, however, that "[t]he policies underlying that subsection [(1)(c)] are entirely distinct from those underlying (1)(a)," and that "the holding in [General Accident] is strictly limited to [its]

68 Id. at 6. This part of the court's opinion was based on Code §§ 3-407(2)(a), 4-401(2)(a) and 3-406.
69 The court first considered the problem of whether this was an impostor situation at all, since "Bill Carter" had merely assumed the name and character of a fictitious person, not an actual individual. It observed, however, that other courts had applied the rule to both real and fictitious persons, and then held that the impostor rule was applicable here as well. No. 78-CA-401-MR, slip op. at 7-8. The Supreme Court disagreed with the Court of Appeals and reversed as to this issue. "Bill Carter" was not an impostor, the Supreme Court reasoned, since Crisp had contracted with Carter to do the repair work. Had the work been properly completed, Carter would have been entitled to a check for $12.50. Having determined that Carter was not an impostor, the Court applied Code section 3-406, the Code's general negligence provision, rather than section 3-405. (See note 4 supra for the text of section 3-406). The Court affirmed the decision of the Court of Appeals in all other respects. No. 79-SC-684-DG, slip op. at 6 (Ky. Oct. 14, 1980).
70 519 S.W.2d 817, 819 (Ky. 1975). See the text accompanying note 46 supra for a discussion of this case.
Citing *Travelers Indemnity*,\(^\text{72}\) the court held that the negligence of the bank in failing to follow reasonable commercial standards\(^\text{73}\) barred its attempt to escape liability under section 3-405. The court recognized that Crisp was also negligent in allowing himself to be duped\(^\text{74}\) but obviously felt that as between the two deceived parties, the bank was in a better position to detect the fraud.\(^\text{75}\) Finally, the court noted that such a holding was not inconsistent with *Fair Park*,\(^\text{76}\) since the policy underlying the impostor rule as stated in that case was to place the loss on the party which presumably should have the best opportunity to detect the imposture.\(^\text{77}\) Here, the court found that presumption to have been effectively rebutted.\(^\text{78}\)

The *Crisp* court rejected a mechanical application of section 3-405, choosing instead to determine, as between two negligent parties, which was the more negligent. The court thereby placed itself in the position of weighing the equities between the two parties, considering such factors as the age and physical condition of the drawer and the degree of commercial reasonableness exercised by the bank. The fairness of this approach is unassailable, but its practicability in light of the Code's goal of simplifying the law of commercial transac-

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71 No. 78-CA-401-MR, slip op. at 9.
72 275 N.W.2d 73 (Neb. 1979). See the text accompanying note 62 supra for a discussion of this case.
73 The jury found that the bank had failed to act in accordance with reasonable commercial standards as follows: (1) the Kentucky driver's license used by "Bill Carter" to identify himself contained his place of employment (which valid Kentucky driver's licenses do not); (2) the license contained a black and white picture (which valid Kentucky driver's licenses do not); (3) the check, which had been indorsed "Southern Construction," should have required "Carter's" check-cashing authority to be established (it was not); (4) no attempt was made to discover anything about "Southern Construction"; (5) "Carter" was not asked if he had an account with the bank; and (6) no identification (needed to establish some kind of local nexus with the bank) other than the Kentucky driver's license was requested. No. 78-CA-401-MR, slip op. at 4, 9-10.
74 *Id.* at 3.
75 *Id.* at 9-10.
77 *Id.* at 269-70.
78 No. 78-CA-401-MR, slip op. at 10. The court noted that under U.C.C. § 1-201(31), Code presumptions are rebuttable.
tions\textsuperscript{79} is more difficult to accept. A more realistic solution, one which neither defeats the Code's goal of simplicity nor rejects Crisp's laudable attempt at fairness, is both desirable and feasible.

III. A SUGGESTED APPROACH TO THE ROLE OF NEGLIGENCE IN IMPOSTOR AND FICTITIOUS PAYEE CASES

Underneath Code section 3-405 lies a fundamental assumption: the drawer of the instrument in impostor and fictitious payee cases is a wrongdoer. In impostor cases, the wrongdoer is guilty of negligence in not detecting a fraudulent impersonation. In fictitious payee cases, the drawer himself has committed a fraud on the drawee bank by making his instrument payable to one whom he meant to have no interest in it.\textsuperscript{80} In failing to distinguish between the drawer in an impostor situation and the drawer in a fictitious payee situation, the Code neglected to take into account an essential fact: the drawer is not always a wrongdoer. Whereas in subsections (b) and (c) of section 3-405 the drawer is by definition "guilty,"\textsuperscript{81} subsection (a) does not require actual wrongdoing on the part of the drawer.\textsuperscript{82} In the latter case, the drawer may have asked for identification carefully and been satisfied that the impersonator was the one he purported to be. Should the impostor at that point present the check for payment and be asked for no proof of identification at all by the bank, a strict application of section 3-405 would place the loss on the only party who has exercised care, leaving the negligent party completely absolved of liability.

For those cases in which the drawer actually has been negligent, and for all fictitious payee cases, the uniform rule

\textsuperscript{79} U.C.C. § 1-102(2)(a). See note 10 \textit{supra} for the text of this subsection.

\textsuperscript{80} The "padded payroll" cases are somewhat different in that the drawer himself is innocent of fraudulent behavior. The employer nonetheless is deemed responsible for the wrongful behavior of the employee who has fraudulently supplied the fictitious name to the drawer.

\textsuperscript{81} U.C.C. §§ 3-405(1)(b), (c) provide that the drawer (or his agent or employee) must "intend" that the payee have no interest in the instrument. See note 1 \textit{supra} for the full text of § 3-405.

\textsuperscript{82} U.C.C. § 3-405(1)(a) states merely that the drawer must have been "induced" to issue the instrument.
which places liability on the drawer is well-tailored. Even though the bank may in some cases have been more negligent than the drawer, the Code policy of simplifying commercial transactions would be defeated completely if courts were required in every instance to determine which was the more culpable party. However, section 3-405's mechanical approach should not be followed in those cases in which the drawer has not acted negligently or fraudulently and in which the bank has violated reasonable commercial standards. The basic assumption of wrongdoing underlying section 3-405 has no application in these cases. Under such circumstances, a court should not hesitate to place the loss on the negligent party, the bank.

This approach is consistent with pre-Code law. Moreover, it does not defeat the Code's purpose of simplicity, since the determination to be made is not the difficult one of who was the more negligent party but merely that of whether either party exercised any care at all. When examined in light of reasons expressed by courts which have refused to apply a negligence standard in section 3-405, this approach is quite acceptable. In Fair Park, the court's concern was that the loss be borne by the party better able to control the loss. As between a drawer who has exercised care and a bank which

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83 See the text accompanying notes 12-25 supra for a discussion of pre-Code law.
84 This was the approach taken by Professor Abel in analyzing impostor cases decided before the existence of the U.C.C.: Ours is instead the easier task of reporting whether in the cases there has been any care at all exercised by the parties. This approach removes all occasion for entering upon a comparison of the care exercised by the victims where both have been careful; solution of that difficult, if not impossible, problem as to which of two persons differently circumstanced has been the more or the less diligent is pretermitted in favor of a determination as to whether either has been at all careful. Abel I, supra note 11, at 188. Professor Abel further noted that the kind of "care" contemplated by these cases was the resort to independent sources of information to establish the identity of the impostor. Id. at 189.

This comment is limited to circumstances in which one or both of the parties to the impostor transaction are negligent. However, where both parties have exercised care in their dealings with the impostor, most pre-Code courts allowed the loss to fall upon the first party to deal with the impostor: the drawer. Id. at 191-92. U.C.C. § 3-405 does not change this result and in fact provides a simple, straightforward method for resolving such cases.

85 541 S.W.2d at 269-70.
has exercised none, the bank is obviously in a better position to avoid the loss. Furthermore, such an approach would not hamper the negotiability of instruments, a fear expressed by the Dartmouth court. Since the drawer exercised care in issuing his check, it would be futile to place the loss on him as a deterrent. Placing the loss on the bank, however, would lead to an exercise of greater care on the part of bank employees. Finally, if a goal of the Code provision is, as implied in comment 4 to section 3-405, to place the risk upon the party better able to bear the loss, then this approach is certainly preferable. In most instances, an individual defrauded by an impostor will have no insurance to cover the loss. A bank, on the other hand, handles such losses as a routine matter. It is certainly in a much better position than the average individual to recover from the theft resulting from an imposture.

Applied to the facts in Crisp, this approach will allow the bank to charge Crisp’s account for the loss due to the imposture. Despite Crisp’s age and physical condition, he was admittedly negligent. Although an individual like Crisp would probably not be able to absorb such losses as well as a bank, this approach could result in a greater exercise of care on the part of individuals dealing with strangers in commercial transactions.

CONCLUSION

The conflict over the role of negligence in section 3-405 developed out of a desire to resolve the inequities which result from a mechanical application of the provision. Section 3-405, based on the assumption that the drawer of the instrument, or his agent or employee, has been negligent or fraudulent, can be validly applied in those situations in which the drawer is indeed a wrongdoer. Such a result is certainly merited in fictitious payee cases in which the drawer or his agent has drawn

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88 Dartmouth Nat'l Bank v. Keene Nat'l Bank, 115 A.2d 316, 318 (N.H. 1955). Note that Dartmouth expressly stated that the loss might properly be placed on the second victim of the imposture where the first victim exercised care and the second victim exercised none. Id. at 319. See text accompanying note 48 supra for a discussion of this case.

87 U.C.C. § 3-405, comment 4. See note 31 supra for the text of comment 4.
a check fully intending that the payee take no interest therein. Even if the bank has been negligent in the ensuing transaction, absent its actual bad faith the drawer is the guilty party and should bear the loss. Impostor cases, unlike their fictitious payee counterparts, come in two varieties: those in which the drawer was actually negligent and those in which the drawer used reasonable care to attempt to discover the identity of his transferee. Where the drawer was negligent, section 3-405's risk allocation provision can be applied straightforwardly. Although a jury might determine that the bank was actually more negligent than the drawer, such a determination could be complicated and costly. Despite the ultimate fairness of this approach, it does not outweigh the Code's objective of simplifying the law of commercial transactions.

In those cases in which the drawer was careful in attempting to ascertain the identity of the impostor, however, while the bank exercised no care at all, a system which places the loss on the innocent drawer while absolving the guilty party of liability is unjustified. The drafters of the Code obviously did not intend such a result. The approach to section 3-405 suggested here, which would place the loss on the drawer in all cases except those where the drawer exercised care and the bank exercised none, is desirable in that it continues the common law approach to impostor and fictitious payee cases. In addition, it tends to place the loss on the party better able to prevent the loss and furthers the goal of free transferability of commercial paper. Finally, and most importantly, it strikes an even balance between the Code's purpose of simplifying the law of commercial transactions and the courts' desire to insure that all parties are treated fairly.

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