

BANKING INDUSTRY STANDARDS RELEVANT TO
COVERAGE AND RECOVERIES UNDER THE REVISED
UNIFORM COMMERCIAL CODE

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I. INTRODUCTION: THE RAMPANT PROBLEM
OF CHECK AND WIRE FRAUD

Check fraud is a very large problem, and the problem is growing. In 1995 about fifty-seven percent of banks lost money as a result of check fraud.¹ The American Bankers Association (ABA) reports that there were approximately 288,546 cases of check fraud in 1997, averaging \$1,775.00 per case.² The ABA further reports that between 1995 and 1997 actual check fraud losses increased 5.2 percent from \$487.1 million to \$512.3 million.³

The United States Comptroller of the Currency suggests that technology is a principal reason for the increase in check fraud losses. "Check fraud is one of the largest challenges facing financial institutions. Technology has made it increasingly easy for criminals, either independently or in organized gangs, to create increasingly realistic counterfeit checks and false identifica-

¹ BOARD OF GOVERNORS, REPORT TO THE CONGRESS ON FUNDS AVAILABILITY, SCHEDULES AND CHECK FRAUD AT DEPOSITORY INSTITUTIONS 5 (1996).

² AMERICAN BANKERS ASSOCIATION, ABA 1998 CHECK FRAUD SURVEY REPORT (1998).

³ *Id.* at 7.

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tion that can be used to defraud banks.”⁴ The Comptroller cites the Financial Institution Fraud and Failure Report, prepared by the Federal Bureau of Investigation in 1994, stating that sixty percent of all criminal referrals relate to check fraud.⁵ Another American Bankers Association survey found that fifty-four percent of community banks, ninety-four percent of mid-size banks, and eighty-eight percent of large banks sustained losses from check fraud in 1993.⁶ Other financial institutions, as well as retail merchants, government agencies, and large corporations, also suffer from significant check fraud. “A recent survey of more than two thousand large U.S. corporations concluded that, on average, they lost approximately \$360,000 a year to check fraud losses. The FBI estimates that if commercial banks and other institutions combined their check fraud losses, the total would be \$12 billion to \$15 billion annually.”⁷ According to the Federal Reserve, the average large institution lost more than \$6 million to check fraud in 1992.⁸

Wire fraud is also a very significant problem in today’s world of high-tech commerce. While checks and credit card payments are by far the most common payment methods in the United States,⁹ “[t]he dollar volume of payments made by wire transfer far exceeds the dollar volume of payments made by other means.”¹⁰ The Federal Reserve wire transfer network¹¹ and the New York Clearing House Interbank Payments Systems,¹² which are the two principal wire transfer systems, process payments exceeding \$1 trillion per day.¹³ With so much money being transferred by wire every day, banks run a substantial risk of loss from fraudulent payment orders no less than check fraud.

There are a number of factors that have contributed to the growing problem of check and wire fraud. Low-cost computer hardware and software have made it relatively easy for criminals to fabricate checks using stolen account information of individuals and businesses. Color copiers produce high quality duplication of checks that can be visually difficult to distinguish from the originals. The high-speed processing equipment used by financial institu-

⁴ COMPTROLLER OF THE CURRENCY, CHECK FRAUD: A GUIDE TO AVOIDING LOSSES 1 (1996) (hereinafter CHECK FRAUD).

⁵ *Id.*

⁶ *Id.*

⁷ *Id.*

⁸ Philip Britt, *Fighting Check Fraud*, SAV. & COMMUNITY BANKER 26-30 (May 1994).

⁹ 9. U.C.C. Art. 4A Prefatory Note (“In terms of number of transactions, payments made by check or credit card are the most common payment methods.”).

¹⁰ *Id.*

¹¹ Hereinafter Fedwire.

¹² Hereinafter CHIPS.

¹³ *Id.*

tions has reduced the number of opportunities for human review of checks for irregularities. Furthermore, the Expedited Funds Availability Act has shortened the processing time banks have before the depositor receives fund availability, often even before the check has cleared.¹⁴ Finally, copiers and fax machines can allow crooked employees to copy authorized signatures on to unauthorized wire transfer orders and deliver them to the employer's unsuspecting bank.

The Uniform Commercial Code is the law designed to allocate the very serious losses resulting from this rampant social problem. As one court has observed, "the Uniform Commercial Code is a delicately balanced statutory scheme designed, in principle, to ultimately shift the loss occasioned by negotiation of a forged instrument to the party bearing the responsibility for the loss."¹⁵ Three articles of the current version of the Code relate to common bank fraud. Article 3 covers negotiable instruments, such as checks, drafts, and notes.¹⁶ Article 4 overlaps with Article 3 in the sense that it also covers negotiable instruments, but only in specific circumstances. Specifically, Article 4 governs bank deposits and collections,¹⁷ and Article 4 governs Article 3 to the extent of any conflict between the two.¹⁸ Finally, Article 4A governs funds transfers, which in its most common application means wire transfers.¹⁹

¹⁴ Under the Expedited Funds Availability Act, depository banks are generally required to make funds available to their depositors for withdrawal no later than (a) the second business day following the banking day on which a local check is deposited, and (b) the fifth business day following the banking day on which a non-local check is deposited. 12 C.F.R. § 229.12(b), (c) (1998). "Check fraud arguably is made easier if depository banks are required to release funds to their customers before such banks can determine whether deposited checks will be paid by the payor bank." Subcommittee on Payments, U.C.C. Comm., Bus. Law Section, ABA, *Deterring Check Fraud: The Model Positive Pay Services Agreement and Commentary*, 54 BUS. LAW. 637, 638 n.5 (1999). The Expedited Funds Availability Act appears at 12 U.S.C. §§ 4001-4010 (1996).

¹⁵ *Ed Stinn Chevrolet, Inc. v. Nat'l City Bank*, 503 N.E.2d 524, 530 (Ohio 1987).

¹⁶ R.U.C.C. § 3-102. As discussed below, Articles 3 and 4 were significantly revised in 1990. This paper refers to pre-1990 Articles 3 and 4 as the "U.C.C." and refers to the present version of these articles as "R.U.C.C."

¹⁷ R.U.C.C. § 4-101 & *id.* Official Comment 1.

¹⁸ R.U.C.C. § 4-102(a).

¹⁹ U.C.C. Art. 4A Prefatory Note ("Another type of payment, commonly referred to as a wholesale wire transfer, is the primary focus of Article 4A."). In fact, funds transfers need not go by wire. The Code defines "funds transfer" as:

the series of transactions, beginning with the originator's payment order, made for the purpose of making payment to the beneficiary of the order. The term includes any payment order issued by the originator's bank or an intermediary bank intended to carry out the originator's payment order. A funds transfer is completed by acceptance by the beneficiary's bank of a payment order for the benefit of the beneficiary of the originator's payment order.

U.C.C. § 4A-104(a). Thus, any payment order by which a bank is directed by one customer to pay funds to someone else can be covered by Article 4A. Some payment orders, such as those affected by the use of debit cards, are subject to preemptive federal law, such as the Electronic Funds Transfer Act, 15 U.S.C. §§ 1693 *et seq.* (1996). *See* U.C.C. Art. 4A Prefatory Note.

Reflecting the common-sense notion that the best way to encourage parties to act reasonably to prevent check and wire fraud losses is to reward reasonable business practices with legal protection from those losses, the drafters of the Code have saturated the Code with vague concepts such as “ordinary care,”²⁰ “reasonable commercial standards,”²¹ “general banking usage,”²² and “commercially reasonable method of providing security.”²³ While the Code provides guidelines for what these concepts mean in practice, they are nowhere defined with any particularity.²⁴ Indeed, the drafters of the Code were much better at saying what they meant to exclude by these general definitions rather than what they meant to include.²⁵ Whether a party conformed its actions to these standards is left to the judge and jury.²⁶ If a party conforms its conduct to these standards, it is generally rewarded by exculpation. A party that does not meet these standards of care runs the risk of bearing some or all of the loss.

In 1990 the National Conference of Commissioners of Uniform State Laws and the American Law Institute promulgated the most significant revisions in a generation to Articles 3 and 4. Article 4A itself was first promulgated in 1989. The general standards of reasonable commercial practices are by far the most significant aspects of these articles as they exist today, and (for Articles 3 and 4) the law relating to these standards is vastly different than the law preceding the revisions. Because of these changes to the Code, results in commercial disputes governed by Articles 3, 4, and 4A now largely turn on the facts of the cases rather than the law.

²⁰ R.U.C.C. § 3-103(a)(7).

²¹ *Id.*

²² *Id.*

²³ *Id.* § 4A-202(b). *See also id.* § 4A-202(c) (defining “commercial reasonableness”).

²⁴ *E.g., id.* § 4A-203 Official Comment 4 (“The concept of what is commercially reasonable in a given case is flexible.”).

²⁵ *E.g., id.* § 3-103(a)(7) (reasonable commercial standards do not require a bank to examine an instrument processed for payment automatically in certain circumstances); *id.* Official Comment 5 (“Nothing in Section 3-103(a)(7) is intended to prevent a customer from proving that the procedures followed by a bank are unreasonable, arbitrary, or unfair.”); *id.* § 4A-203 Official Comment 4 (“A security procedure is not commercially unreasonable simply because another procedure might have been better or because the judge deciding the question would have opted for a more stringent procedure. The standard is not whether the security procedure is the best available.”).

²⁶ “Ordinary care” and related standards of care under Articles 3 and 4 are questions of fact. Commercial reasonableness under Article 4A, however, is a question of law for the judge. U.C.C. § 4A-203 Official Comment 4. Whether a receiving bank complied with the procedure is nonetheless a question of fact for the jury. *Id.*

This article attempts to address the facts of check and wire fraud cases, which comprise such a major cause of fidelity losses. Section II of the paper summarizes, in very basic fashion, the law surrounding the standards of ordinary care and commercial reasonableness in the revised Code. Section III explains why these issues affect the bonding company. Finally, Section IV discusses actual and recommended bank practices and procedures that are or should be followed by banks in their day-to-day operations. Section IV thus conveys certain significant standards of care that can trigger bank liability or exculpation under the revised Code.

II. A SUMMARY OF THE LAW SURROUNDING BANKING STANDARDS OF CARE IN ARTICLES 3, 4, AND 4A

Before the significant revisions to Articles 3 and 4 in 1990, the Code reflected certain assumptions of the National Conference of Commissioners on Uniform State Laws and the American Law Institute as to both how losses should be allocated and how this uniform statute should regulate that allocation. First, the old Code applied the traditional common-law concepts of contributory negligence and the “last clear chance” doctrine. In a nutshell, the plaintiff’s own negligence would preclude him from recovering against one whom he claimed was negligent. Nonetheless, if the defendant had his “last clear chance” to prevent the loss, the defendant would be liable for the loss. This common-law notion was most significantly seen in Section 3-406 of the old Code:

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.²⁷

In plain English, this essentially meant that a bank customer cannot complain that a bank paid or took a check that had been altered or forged by the crook if the customer itself was negligent. However, if the bank either acted in bad faith or itself acted negligently (*i.e.*, not “in accordance with the reasonable commercial standards” of the bank’s business), the customer still had his full claim. Thus, the slightest bit of contributory negligence by the bank’s customer defeated the customer’s entire claim, unless the bank itself acted negligently. Because the bank had the last clear chance to prevent the loss, the Code allocated the loss to the bank in this latter circumstance; and the bank would pay every nickel of the loss.

²⁷ U.C.C. § 3-406.

Except for New York,²⁸ South Carolina,²⁹ and Rhode Island,³⁰ which have not yet enacted the new Code, the old Code is now largely the stuff of legal history. Revised Section 3-406 still precludes the bank's customer from prevailing on a claim against the bank if the customer acted negligently, but the loss is allocated between the parties to the extent that each acted negligently.³¹

Thus, for example, under the old Code, if a bank customer negligently kept blank check stock on a shelf rather than in a locked drawer, and thereby substantially contributed to the making of the forgery, the customer, in its claim against its bank, would have no claim at all against its bank unless it could show that the bank itself acted negligently in paying the checks, such as by failing to detect the forgeries consistently with reasonable banking standards. If the customer could meet its burden of proof on this point, it would have a claim for one-hundred percent of its loss from the forgeries. Under the revised Code, however, the loss is allocated between the customer and the bank to the extent of each party's negligence: if a jury found that the bank customer was twenty-seven percent negligent while the bank itself was seventy-three percent negligent, the customer still has a claim against the bank for seventy-three percent of its loss.³²

The comparative negligence scheme appears elsewhere in revised Article 3 as well. Section 3-404 applies to checks caused to be issued by an imposter, as well as checks made payable to fictitious payees or to payees who were never intended to have any interest in the instrument. Thus, for example, if an imposter induces someone to issue a check by impersonating the payee, any endorsement in the name of the payee is effective and cannot serve as the basis for a claim against the bank.³³

Similarly, if a crook causes his employer to issue a check payable to a fictitious entity, later steals the check, and then deposits it to his own personal account, the employer cannot assert a claim against the bank solely on the basis that the endorsement was forged or that the depository bank wrongfully took the check. Under Section 3-404(b), the endorsement was effective, and the depository bank was a holder of the instrument.

These rules applied under the old Code as well, but the new Code imposes the comparative negligence scheme: in any case involving a check

²⁸ N.Y. U.C.C. LAW §§ 3-101 & 4-101 (McKinney 1999).

²⁹ S.C. CODE ANN. §§ 3-101 & 4-101 (Law Co-op. 1999).

³⁰ R.I. GEN. LAWS §§ 3-101 & 4-101 (1999).

³¹ R.U.C.C. § 3-406(b).

³² *Id.*

³³ *Id.* § 3-406(a).

issued because of inducement by an imposter, a check payable to a fictitious payee, or a check payable to one who was never intended to have an interest in the instrument, the loss is allocated between the parties to the extent of each party's negligence.³⁴

Section 3-405 of the revised Code is new and has no direct analog in the old Code. Under this section, if an employee with responsibility for an instrument (such as a bookkeeper, one with authority to sign or endorse instruments, to process instruments for issue, etc.) fraudulently endorses an instrument either payable to the employer or issued by the employer, the fraudulent endorsement is effective and cannot form the basis of a claim against the bank that paid the instrument or took the instrument for collection.³⁵ Nonetheless, to the extent that the employer can prove at trial that the bank itself was negligent, the employer still has a negligence claim against the bank to the extent that this negligence caused the loss.³⁶

Consistent with these provisions of Article 3, the drafters of the revised Code included a comparative negligence scheme within Article 4 as well. Section 4-406 governs a bank's customer's obligation to report unauthorized signatures or alterations of an instrument to his bank. Under the "repeater" rule of former Section 4-406, a bank's customer had to "exercise reasonable care and promptness to examine the statement and items to discover his unauthorized signature or any alteration on an item and must notify the bank promptly after discovery thereof."³⁷

If the customer failed to fulfill these obligations, the customer was absolutely precluded from asserting a claim against the bank for the item at issue to the extent that the customer's failure caused the bank to suffer a loss and also was absolutely precluded from asserting a claim against the bank for any other items bearing unauthorized signatures or alterations by the same wrongdoer that the bank paid more than fourteen days after the bank statements were made available to the customer.³⁸ This absolute preclusion, however, was mollified by Section 4-406(3), which provided that the preclusion did not apply at all if the customer could prove that the bank acted negligently when paying the item. Under the revised Code, this all-or-nothing rule of contributory negligence is again replaced by comparative negligence: in the case of a repeated fraud involving alterations or unauthorized signatures by the same

³⁴ *Id.* § 3-404(d).

³⁵ *Id.* § 3-405(b).

³⁶ *Id.*

³⁷ U.C.C. § 4-406(1).

³⁸ *Id.* § 4-406(2).

wrongdoer, the bank's customer and the bank itself share the loss to the extent of each party's negligence.³⁹

In contrast to Articles 3 and 4, Article 4A does not invoke comparative negligence. In this aspect, Article 4A resembles the pre-1990 Articles 3 and 4: the bank's compliance with applicable standards of care relieve it of liability completely, while its failure to meet these standards of care imposes absolute liability. With regard to fraudulent payment orders, the Code allocates the loss typically depending on the commercial reasonableness of security procedures between the bank and its customer. Obviously, if the sender of the order authorized the order or if the sender "is otherwise bound by it under the law of agency," the sender cannot recover against the bank.⁴⁰ If an agreement between a bank and its customer includes a security procedure by which payment orders will be verified, however, even unauthorized payment orders can be deemed "effective" under the Code if (a) the procedure "is a commercially reasonable method of providing security against unauthorized payment orders," and (b) if the bank shows that it accepted the order in good faith and in compliance with the procedure and any written instructions of the sender.⁴¹

Whether any given security procedure is "commercially reasonable" depends fully on the prevailing standards of practice in the industry at the time in question that are appropriate for that customer.

Commercial reasonableness of a security procedure is a question of law to be determined by considering the wishes of the customer expressed to the bank, 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, alternative security procedures offered to the customer, and security procedures in general used by customers and receiving banks similarly situated. A security procedure is deemed to be commercially reasonable if (i) the security procedure was chosen by the customer after the bank offered, and the customer refused, 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, whether or not authorized, issued in its name and accepted by the bank in compliance with the security procedure chosen by the customer.⁴²

³⁹ R.U.C.C. § 4-406(e).

⁴⁰ U.C.C. § 4A-202(a).

⁴¹ *Id.* § 4A-202(b).

⁴² *Id.* § 4A-202(c).

Many fine sources address the numerous legal issues arising under these and other provisions of the Code in much more detail, and the reader is encouraged to examine those other sources for such a legal analysis.⁴³ This article, by contrast, seeks to address not so much the relevant law, but the facts, which have now become so important in the law of banking and commercial paper, under Articles 3, 4, and 4A.

III. THE RELEVANCE OF COMMERCIAL BANKING STANDARDS TO BONDING COMPANIES

A good understanding of the applicable standards of care in the banking industry are crucial to sureties for claim purposes as well as salvage. Under the Standard Form No. 24 Financial Institution Bond, the insured obtains fidelity coverage (Insuring Agreement (A)), “on premises” coverage (Insuring Agreement (B)), and forgery or alteration coverage (Insuring Agreement (D)), each of which can implicate banking industry standards. Each insuring agreement requires that the loss must result “directly” from the covered activity. A negligent bank may have trouble meeting its burden of proof for coverage under these insuring agreements when the loss may well have been directly caused by the bank’s own negligence rather than the covered conduct.

For example, a covered loss under Insuring Agreement (B) results directly from “theft, false pretenses, common-law or statutory larceny, committed by a person present in an office or on the premises of the Insured.” Assuming that the principal’s wrongful conduct occurred on premises, there often remains an issue as to whether the loss resulted “directly” from the wrongful conduct or, alternatively, from the financial institution’s own negligent business practices.

In one case, the insured bank negligently permitted funds to be withdrawn by a depositor without the consent of the depositor’s business associate. The depositor absconded with the funds. After being sued by and settling with the business associate, the bank claimed on its bond. The court

⁴³ See, e.g., Stephen L. Baskind, *Who Ultimately Bears the Loss—Assignment, Subrogation and Risk Allocation Pursuant to the Uniform Commercial Code* (unpublished paper presented at 1996 Mid-Winter Meeting of the Fidelity & Surety Law Committee of TIPS in San Francisco, Cal., (Jan. 26, 1996)); Thomas C. Baxer, Jr. & Raj Bhala, *The Interrelationship of Article 4A With Other Law*, 45 BUS. LAW. 1485 (1990); Patricia B. Fry, *Basic Concepts in Article 4A: Scope and Definitions*, 45 BUS. LAW. 1401 (1990); Edward Gallager, *Barriers to the Exercise of the Fidelity Insurer’s Subrogation Rights*, 1 FID. LAW ASSOC. J. 37 (1995); Fred H. Miller, *The Benefits of New U.C.C. Articles 3 and 4*, 24 U.C.C. L. J. 99 (1991); 2 BARKLEY CLARK & BARBARA CLARK, *THE LAW OF BANK DEPOSITS, COLLECTIONS AND CREDIT CARDS* ch. 17 (rev. ed. 1999) (chapter on wire transfers); Gary J. Valeriano, *A Look at Revised Articles 3 and 4 of the Uniform Commercial Code*, 1 FID. L. ASSOC. J. 53 (1995).

ruled for the carrier, holding that the bank's loss was caused by its own negligent conduct in allowing the funds to be withdrawn.⁴⁴

In another case, crooked employees took corporate checks payable to third parties, forged the endorsements of the payees, and cashed them at their own bank. One teller testified that, on one occasion, she saw one of the employees sign the name of the third party on the back of the check. Other tellers testified that, on some occasions, the endorsements were already on the instruments when the employee would bring them to the bank and that the employee refused to add her endorsement below the endorsement of the payee when so requested. A vice-president of the bank told the tellers to cash the checks without the employee's endorsement, even though it was against bank policy to cash third-party checks without adding an endorsement of the presenter. Finally, one of the employees took third-party checks payable to the employer, endorsed them, and exchanged them for cash or cashier's checks at the bank. The bank's policies and procedures prohibited such conduct.⁴⁵ The court held that the bank's failure to follow its own procedures caused the loss rather than covered conduct under Insuring Agreement (B).

A bonding company issuing a banker's blanket bond must do so under the assumption that the bonded bank will follow the procedures set forth in its own operations manual and operate in a commercially reasonable manner, conforming its conduct to reasonable commercial banking practices in compliance with the Articles of the Uniform Commercial Code covering banking practices Empire's losses in this case were all caused by the intentional acts of an officer of Empire instructing employees to violate its prescribed procedures and reasonable commercial banking practices in order to accommodate [the wrongdoer].⁴⁶

The bonding company also must be cognizant of banking standards of care, given its option to defend claims against insured banks. Under General Agreement (F) of Standard Form No. 24, the financial institution bond carrier has an option to defend or not to defend in its sole discretion. If the carrier defends, it is responsible for defense costs up to the limit of liability. If it elects not to defend, it is not responsible for defense costs at all. Because

⁴⁴ White Rock Nat'l Bank v. United States Fire Ins. Co., 562 S.W.2d 268, 274 (Tex. Ct. App. 1978).

⁴⁵ Empire Bank v. Fidelity & Dep. Co., 828 F. Supp. 675, 676-77 (W.D. Mo. 1993), *aff'd*, 27 F.3d 333 (8th Cir. 1994).

⁴⁶ 828 F. Supp. at 678-79. *See also* Columbia Union Nat'l Bank v. Hartford Accident & Indem. Co., 496 F. Supp. 1263 (W.D. Mo. 1980) (holding that bank's loss resulted from bank's own business decision rather than false pretenses of a wrongdoer), *aff'd*, 669 F.2d 1210 (8th Cir. 1982). *Cf.* First Nat'l Bank v. Insurance Co., 424 F.2d 312 (7th Cir. 1970) (coverage under Insuring Agreement (B) for kiting losses, but strongly suggesting that no coverage would exist if the bonding company had proven that the bank had acted in bad faith).

it would have to pay defense costs out of its own pocket, the carrier often will elect not to defend a third-party proceeding against the insured.

There is a significant exception to this general rule, however: the carrier will elect to defend if it is confident that (1) the third-party claim, if proven, will result in a collectible loss under the bond, and (2) the insured's control of its own defense will not adequately protect the carrier's rights. If the third-party asserts a claim that would be a collectible loss for the insured, the insured's exposure on the third-party claim is well below its limit of liability, and the insured does not have a significant deductible, then the insured does not have much incentive to put up a strong defense to the third-party claim. Why would the insured defend the third-party claim vigorously when it is responsible for legal fees and, if it loses, it will have a collectible claim on the bond anyway?⁴⁷ When a carrier elects to defend under General Agreement F, it steps into the shoes of the bank and therefore must grapple with applicable banking standards relating to the third-party claim.

Finally, banking standards of care are also obviously relevant to recovery actions by the bonding company. Three typical situations recur. First, the insured may be a bank or other financial institution under a financial institution bond. If the insured bank paid a check bearing an unauthorized signature or an alteration, it may have a claim against other banks, such as the depository bank, that might have acted negligently in taking the instrument for deposit in the first instance. The comparative negligence provisions of revised Sections 3-404, 3-405, and 3-406 apply equally to actions by one bank against another bank as to claims between the bank's customer and the bank itself.⁴⁸

⁴⁷ Gilbert J. Schroeder, *Court Costs and Attorneys' Fees*, in FINANCIAL INSTITUTION BONDS 237 (Duncan L. Clore ed. 1995). This discussion obviously ignores the very real coverage question of when claims asserted by third-parties can result in collectible losses. Recent significant cases have rejected coverage claims premised on losses to third-parties. *See, e.g.*, *Aetna Cas. & Sur. Co. v. Kidder, Peabody & Co., Inc.*, 676 N.Y.S.2d 559 (N.Y. App. Div. 1998) (no coverage for losses resulting from third-party claims under commercial crime policy language); *Drexel Burnham Lambert Group, Inc. v. Vigilant Ins. Co.*, 595 N.Y.S.2d 999 (Sup. Ct. N.Y. County (1993) (same); *Peoples Bank & Trust Co. v. Aetna Cas. & Sur. Co.*, 113 F.3d 629 (6th Cir. 1997) (no coverage for losses resulting from third-party claims under financial institution bond). *See generally* Mark E. Wilson, *The Boundaries of "Loss" Under Fidelity and Financial Institution Bonds: Toward a Coherent Theory of Set-Off and Allocation of Losses and Recoveries* (unpublished paper submitted at the National Bond Claims Association annual meeting in Pinehurst, N.C. on Oct. 3, 1996) (on file with author) (analyzing "loss resulting directly from" language of standard policy forms).

⁴⁸ The Code makes this abundantly clear. The comparative negligence provision states in general terms that the "person bearing the loss may recover from the person failing to exercise ordinary care to the extent the failure to exercise care contributed to the loss." R.U.C.C. §§ 3-404(d) & 3-405(b). Official Comment 3 to Section 3-404 describe examples in which either a drawer or a drawee bank would have a cause of action against a depository bank under the comparative negligence provision of subsection (d).

The insured bank also will have available to it a claim for breach of presentment warranty against the depositary bank, for a depositary bank makes certain warranties to the drawee bank relating to signatures and title to an instrument by presenting the instrument for payment to drawee bank.⁴⁹ The depositary bank can defend against a breach-of-warranty claim by raising defenses that the drawee of the item could raise against the drawer.⁵⁰ Thus, even a breach-of-warranty claim raises the specter of a fact-intensive suit surrounding banking industry standards of care and how a loss should be allocated between the drawee bank and the bank's customer.

The result is no different if the insured is a depositary bank. A depositary bank has a claim against other banks and individuals to the extent that those other parties acted negligently and therefore caused some portion of the loss under Sections 3-404, 3-405, and 3-406. Moreover, depositary banks receive transfer warranties from whomever transferred the instrument in the first instance.⁵¹ Those transfer warranties, too, can potentially implicate the comparative negligence provisions of the Code.

Second, when the carrier insures a bank customer under a commercial crime policy and the insured suffers a loss due to check fraud by an employee, the carrier often has a potential claim against a bank under the revised Code. If the employee forged signatures on the front of an instrument or altered an instrument, the carrier will have a potential claim against the drawee bank for paying an instrument that was not properly payable under Section 4-401 of the Code. An instrument is "properly payable" if it is "authorized by the customer and is in accordance with any agreement between the customer and the bank."⁵² Significantly, however, a bank cannot, in a contract with the customer, disclaim its obligation to exercise ordinary care.⁵³ Thus, banking standards of care are incorporated as a matter of law into every contract between the customer and its bank. A salvage action against the drawee bank, therefore, whatever the other terms of the insured's deposit contract may be, includes a claim for negligence under the Code. Moreover, the drawee bank will typically defend such suits by claiming that the check bore an effective signature under Sections 3-404 or 3-406 or that the "repeater" rule of Section 4-406(c) precludes the customer from pursuing the claim. Each such defense raises issues of comparative negligence under the revised Code.

⁴⁹ R.U.C.C. §§ 3-417 & 4-208.

⁵⁰ *Id.* § 3-417(c) (referring to defenses under §§ 3-404, 3-405, 3-406, and 4-406); *id.* § 4-208(c) (same).

⁵¹ R.U.C.C. §§ 3-406 & 4-207.

⁵² *Id.* § 4-401(a).

⁵³ *Id.* § 4-103(a).

Third, an employee's check fraud also frequently involves endorsement issues: the employee causes a check to be issued to a fictitious payee, the employee steals bona fide checks to the employer that come in the mail, etc. Under Section 3-420 of the Code, the depository bank or the drawee bank is liable for conversion of the instrument in certain circumstances.

In general, the original payee or other holder of an instrument (but not the issuer) can assert a claim for conversion against either the drawee of the instrument or the depository bank. An instrument is converted if a bank takes it for collection or payment from one who is not entitled to enforce the instrument or receive payment, such as a person to whom the instrument had never been negotiated.⁵⁴ Negotiation requires an endorsement,⁵⁵ and a forged endorsement is ineffective except as the endorsement of the forger.⁵⁶

If the check falls within the scope of Sections 3-404 or 3-405, however, any person in possession of the instrument can be deemed a holder⁵⁷ (thus giving that person the right to enforce the instrument); and an endorsement even by a forger in the name of the payee will be deemed effective.⁵⁸ Similarly, Section 3-406 can work to preclude a negligent party from asserting that an endorsement was forged.⁵⁹ By virtue of these sections, therefore, any forged endorsement claim that under the old Code would have been for the intentional tort of conversion can be transformed into one for comparative negligence, implicating banking standards of care.⁶⁰

In sum, the many coverage, defense, and salvage implications of negligent banking practices should prompt the carrier to familiarize itself with standards of care for banking operations.

IV. THE "KNOW YOUR CUSTOMER" POLICY AND OTHER STANDARDS OF COMMERCIAL REASONABLENESS

All of the comparative negligence provisions of revised Articles 3 and 4 are couched in terms of "ordinary care."⁶¹ The revised Code defines "ordinary care" as the observance of "reasonable commercial standards prevailing

⁵⁴ *Id.* § 3-420(a). *See also id.* § 3-301 (defining who is a person entitled to enforce an instrument).

⁵⁵ *Id.* § 3-201(b).

⁵⁶ *Id.* § 3-403(a).

⁵⁷ *Id.* § 3-404(b)(1).

⁵⁸ *Id.* § 3-404(b)(2) & 3-405(b).

⁵⁹ *Id.* § 3-406(b).

⁶⁰ It should be noted that, even under the old Code, a bank had an absolute defense to conversion if it could show that it exercised reasonable commercial standards. U.C.C. § 3-419(3). Even so, however, this was an all-or-nothing defense; the bank either bore all of the loss or none of it.

⁶¹ *See* R.U.C.C. §§ 3-404(d), 3-405(b), 3-406(b) & 4-406(e).

in the area in which the person is located, with respect to the business in which the person is engaged.”⁶² In the case of a bank that takes an instrument for processing for collection or payment by automated means, reasonable commercial standards do not require the bank to examine the instrument if the failure to do so does not violate the bank’s prescribed procedures and the bank’s procedures do not vary unreasonably from general banking usage, not disapproved elsewhere in the Code.⁶³ In wire fraud cases, the standard is that of “commercial reasonableness.”⁶⁴ The central question presented by any case under these provisions will be whether the bank met this general standards of care.

A. Check Fraud

Under Section 3-107(a)(7), what are “reasonable commercial standards” prevailing in the area in which the bank is located? The geographic limitation to this definition is doubly good for a bank. First, it automatically puts the bank at an advantage in a suit by a non-bank against the bank, for as a practical matter, the bank can often find a senior or retired employee to serve as an expert witness about the bank’s own procedures and why they conform to banking standards within the geographic area. It often will be difficult for a non-bank party in litigation to come up with an expert witness with comparable experience within the banking industry in this geographic location. This is especially true for banks located in small towns or rural areas.

There are two ways to get around this problem for the non-bank litigant. First, the party can emphasize federal or other legal limitations on a bank’s procedures, thus effectively preventing the bank from claiming that it did not have to follow those procedures for risk that it will alert regulators that it breached some other law. Second, the litigant can seek out one of the few consulting firms that specializes in locating expert witnesses in banking cases. Since the major shake-ups in the thrift and banking industries of the 1980s, many former bank executives have gone into consulting and are available to testify about banking procedures in litigation.

Perhaps the most significant “reasonable commercial standard” that becomes relevant involving employee dishonesty or forgery is the “Know Your Customer” policy. In a nutshell, federally insured banks are strongly encouraged by the Federal Reserve Board to have a “Know Your Customer” policy that sets forth specific procedures that tellers should follow to avoid check fraud losses that otherwise could be caused because the bank trusts a cus-

⁶² *Id.* § 3-103(a)(7).

⁶³ *Id.*

⁶⁴ *Id.* § 4A-202(c).

tomers. Under the Bank Secrecy Act,⁶⁵ the FDIC conducts periodic examinations of federally insured institutions. FDIC examiners use, in these examinations, a form (among many others) specifically tailored to the “Know Your Customer” policy.⁶⁶ This form, entitled “Know Your Customer Policy,” states at the top that “‘Know Your Customer’ policies and procedures are not currently required by regulation, [but] institutions should be strongly encouraged to develop and maintain such policies and procedures.”⁶⁷ The form goes on to inquire, among other things:

- Whether the bank has policies and procedures that “require ‘reasonable efforts’ to be made to ascertain the true identity of individual customers and/or the stated business purpose of each commercial enterprise with whom the bank conducts business”;
- Whether the institution’s “Know Your Customer” policy requires, for opening a personal account, (a) the procurement of proper identification, such as a Driver’s License with photograph or U.S. passport or Alien Registration Card together with a major credit card, (b) consideration of the customer’s residence or place of business, (c) consideration of the source of funds used to open an account, and (d) a cross-check with a service bureau “for undesirable situations involving the customer” such as previous check kiting, non-sufficient funds checks, etc.;
- Whether the institution’s “Know Your Customer” policy includes for the opening of business accounts (a) verification of the legal status of the business, (b) verification of the name of the business with a reporting agency, (c) for foreign business accounts, verification that the business is registered in the country of origin, (d) procurement of financial statements, a description of the customer’s principal line of business, a description of business operations and list of major suppliers and customers;
- Whether the bank has adequate ongoing monitoring systems in place to identify “suspicious” transactions, which the form describes by the following examples: “structuring, concentration accounts, transactions inconsistent with

⁶⁵ 31 U.S.C. §§ 5311 *et seq.* (1996).

⁶⁶ FDIC DOS MANUAL OF EXAMINATION POLICIES 9 (Sept. 1995).

⁶⁷ *Id.*

the nature of a customer's stated business purpose, unusual wire activities"; and

- Whether the institution uses fictitious names for customers on the general ledger or other documents of the bank, and if so, whether the bank maintains files containing the customer's real names and other identifying information coupled with knowledge of these customer's activities.⁶⁸

The Comptroller of the Currency published in 1996 a pamphlet entitled *Check Fraud: A Guide to Avoiding Losses*.⁶⁹ Whether intended or not, by publishing this modest twenty-six page pamphlet, the Comptroller has given litigants a potent weapon in a suit against a bank—claiming that the bank failed to exercise ordinary care.

One of the common check fraud schemes discussed in the pamphlet is "Identity Assumption," which a sound "Know Your Customer" policy would help to prevent. As the pamphlet describes the problem:

Identity assumption in check fraud occurs when criminals learn information about a bank customer, such as name, address, bank account number, account balance, social security number, home and work telephone numbers, or employer, and use the information to misrepresent themselves as the valid bank customer. These schemes may involve changing account information, creating fictitious transactions between unsuspecting parties, or preparing checks drawn on a valid account and that are presented using false identification.

This fraud is made easier when organizations, such as state departments of motor vehicles use social security numbers on identification. In such states, because those numbers are more available, banks must be especially careful.⁷⁰

"To protect against such frauds," the pamphlet continues, banks should do three things.⁷¹ First, banks should "ensure that changes to accounts are secure, by requiring customers to request changes in writing or in some other way that guarantees the identity of the customer." Second, the pamphlet encourages banks to train personnel, "including all tellers," to:

- check identification carefully, "particularly in split/deposit transactions";
- require two forms of identification;

⁶⁸ *Id.*

⁶⁹ CHECK FRAUD, *supra* note 4.

⁷⁰ *Id.* at 7.

⁷¹ *Id.* at 8.

-
- record the identification information on the back of the item presented;
 - inspect checks carefully to ensure that they are not counterfeit.⁷²

Third, banks should limit the size of cash transactions at temporary or remote locations to require large item transactions to occur in a regular bank office.⁷³

Another significant type of fraud listed in the pamphlet is “new account fraud.”⁷⁴ The pamphlet’s examples for this sort of fraud include the opening of a new account by a criminal using false employment information and incorrect addresses and telephone numbers, and a criminal’s opening of a corporate account using a fictitious company name just before depositing a large amount in counterfeit checks into the account.⁷⁵ “To protect against such frauds,” the pamphlet states, banks “should thoroughly investigate information presented by a prospective customer to ensure that it is accurate and valid.”⁷⁶ It suggests that banks may accomplish this purpose by:

- Calling the new customer at work or at home;
- Sending thank you notes to new customers, in envelopes marked to request return of improperly addressed items and promising payment and then watching for return;
- Contacting banks listed on the application for information on the customer’s prior banking history;
- Visually inspecting the business;
- Obtaining a federal tax return or state certificate of incorporation for new corporate accounts to ensure that businesses are legitimate;
- Considering whether the business is consistent with the account activity;
- Asking for a copy of a utility bill sent to the customer’s address.⁷⁷

Other typical types of losses discussed in the pamphlet include altered check schemes, counterfeit check schemes, closed account fraud, fraud by bank insiders, telemarketing fraud, and check fraud by gangs.⁷⁸

The pamphlet devotes a section to preventative measures that a bank can take to avoid losses. It emphasizes “[s]trong organizational controls,” including monitoring, classifying, and analyzing losses to identify trends; reporting

⁷² *Id.*

⁷³ *Id.*

⁷⁴ *Id.* at 10.

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ *Id.* at 10-11.

⁷⁸ *Id.* at 4-14.

the findings of monitoring activities to the audit, risk-management, and security divisions in senior management; ensuring communication among departments about check fraud; assessing operating procedures regularly and implementing changes; and targeting check fraud awareness training to specific check fraud schemes.⁷⁹ Separate, specific internal controls are suggested to prevent check fraud by bank insiders.⁸⁰

Education and training of tellers, managers, and operations personnel are also discussed, as well as specific guidelines for cashing checks, opening accounts, positive pay systems, reverse positive pay systems, fingerprinting non-customers, cooperation between check manufacturers and banks, and security features for checks such as watermarks and high-resolution micro-printing.⁸¹ The devil is the details in banking, and any of these details may come back to haunt the bank that elected not to follow one of these various suggested avenues to prevent check fraud.

The Comptroller's website⁸² expands on the suggested "Know Your Customer" policy for banks. It reports that "[f]irm Know Your Customer policies are a bank's most effective weapon against being used unwittingly to launder money."⁸³ The website states that:

Generally, a bank should never establish a relationship with a customer until it knows the customer's true identity. If a potential customer is unwilling to provide the necessary information, the relationship should be reconsidered. If the bank customer has established a customer relationship, it should be alert for any unusual business transactions.⁸⁴

One cannot overemphasize the importance of government publications of this nature in a suit challenging a bank's claim that it exercised ordinary care. The "new account fraud" described in the Comptroller's pamphlet is undoubtedly familiar to all experienced fidelity claim managers. If a commercial crime policy insured's employee steals a blank check of the employer, forges his supervisor's signature on the check, makes the check payable to a fictitious entity, and opens an account at a bank in the name of that entity, the signature is effective under Section 3-404(b), thus precluding the insured (or the carrier in a salvage effort) to assert that the insured's bank breached the

⁷⁹ *Id.* at 15.

⁸⁰ *Id.*

⁸¹ *Id.* at 15-25.

⁸² *Establish an Effective Know Your Customer Policy* (visited Aug. 23, 1999) <<http://www.occ.treas.gov/laundry/eaek.htm>>.

⁸³ *Id.*

⁸⁴ *Id.*

deposit agreement with the insured by paying the check. Nonetheless, under Section 3-404(d), to the extent that the depository bank failed to exercise ordinary care, it must bear the loss. The pamphlet provides a checklist of things the bank should have done to protect against the fraud, according to the Comptroller, all of which are therefore fair game in discovery and at trial.

Perhaps the most useful information to the carrier in litigation involving banking standards will be the teller training manual. The Comptroller, not surprisingly, emphasizes teller education and training to prevent check fraud losses. “Alert and well-trained front line personnel, managers and operations personnel are essential to check fraud prevention programs.”⁸⁵ Before beginning their positions, new employees should be specifically trained concerning (a) what is acceptable identification, (b) opening new accounts, (c) cashing checks and accepting deposits, (d) detecting counterfeit checks, (e) cash-back transactions and (f) back room operations.⁸⁶

The Comptroller also encourages a separate section of a teller manual regarding check fraud.⁸⁷ The section should emphasize “typical check fraud schemes and warning signs,” which the pamphlet describes in some detail.⁸⁸ The non-banker may be surprised at the level of detail the Comptroller suggests for tellers when examining checks. For example, to avoid losses involving counterfeit checks, there are warnings about the magnetic ink character recognition (MICR) line at the bottom of the check. Tellers should watch for the absence of a MICR line, a routing code within the MICR line that does not match the address of the drawee bank, and MICR ink that looks shiny or that feels raised.⁸⁹ The teller manual should also direct tellers to watch for simple irregularities on checks, such as spelling errors, typed rather than printed names on the check form, a personal check with no perforated edge, “a signature that is irregular-looking or shaky, or shows gaps in odd spots,” etc.⁹⁰ The pamphlet even warns against taking checks presented “at busy times by belligerent or distracting, fast-talking customers who try to bypass procedures.”⁹¹

Given the emphases placed on “Know Your Customer” policies by the Comptroller, banks will almost always include such policies and procedures

⁸⁵ CHECK FRAUD, *supra* note 4, at 16.

⁸⁶ *Id.*

⁸⁷ *Id.* at 16-17.

⁸⁸ *Id.* at 17.

⁸⁹ *Id.*

⁹⁰ *Id.*

⁹¹ *Id.* at 18.

in their manuals and teller training materials. Thus, one large publisher's teller's handbook directs tellers to assure that they know the customer but also to check the endorsement on an item carefully:

You should always know your *endorser* when you cash a check, but you should know your *endorsements* whether you cash a check or accept it for deposit. It takes only a second to glance at the back of each check and to be sure it is endorsed properly. If it simply lacks endorsement, ask the customer to sign it. If it is irregularly endorsed, politely refer the matter to your supervisor in order to protect your customers and your institution.⁹²

A manual relating to the design of an adequate "Know Your Customer" policy suggests that "Know Your Customer" procedures should "allow for the collection of sufficient information to develop a transaction profile of each customer."⁹³ This will enable the financial institution "to predict with relative certainty the type of transactions in which a customer is likely to be engaged."⁹⁴ The bank should then establish internal systems for monitoring transactions "to determine if transactions occur that are inconsistent with the customer's transaction profile."⁹⁵

The bonding company should also be aware that supervisors are subject to a full panoply of procedures to avoid check fraud no less than the tellers. The BANK SECURITY DESK REFERENCE lists the following red flags suggesting possible check fraud for both tellers and platform personnel:

- Customer is reluctant to provide any information for proper identification;
- Customer opens several accounts under one or more names and subsequently makes deposits of less than \$10,000 in cash in each of the accounts;
- Customer is reluctant to proceed with the transaction after being informed that a Currency Transaction Report will be filed, or withholds information necessary to complete the form;
- Customer makes frequent deposits or withdrawals of large amounts of currency for no apparent business reason, or for a business that generally does not involve large amounts of cash;
- Customer exchanges large amounts of currency from small to large denomination bills;
- Customer makes frequent purchases of monetary instruments for cash in amounts less than \$10,000 with different tellers;

⁹² JOAN GERMAN-GRAPES, THE TELLER'S HANDBOOK: EVERYTHING A TELLER NEEDS TO KNOW TO SUCCEED 159 (6th ed. 1997).

⁹³ BANK SECURITY DESK REFERENCE, ¶ 8.09[2], at 8-39 (Aug. 1995).

⁹⁴ *Id.*

⁹⁵ *Id.*

•Customer makes constant deposits of funds and almost immediately requests wire transfers to another city or country, and that activity is inconsistent with the customer's stated business.⁹⁶

Bank policy and procedure manuals, as well as teller training manuals, will typically require operational procedures to conform to these guidelines set forth by the Comptroller. Whether the tellers complied with the procedures in any given instance, of course, is a different question. Sometimes tellers are simply inadequately trained or incompetent and, therefore, will not comply with the procedures. The non-bank litigant obviously can use such facts to its benefit in litigation.

Ironically, however, it frequently can be *more* harmful to the bank if the tellers were well-trained or highly competent. In this latter circumstance, the loss typically results from a well-trained or competent teller's decision to bend the rules slightly for a particular reason, such as familiarity with the bank customer (who turns out to be a crook) or a perceived need by the teller to please the individual's employer, who may be a big customer of the bank. If a well-trained or competent teller consciously elects not to comply with bank procedures, the bank's opponent in litigation can usually present an argument that the bank acted in bad faith and is therefore subject to consequential and even potentially punitive damages.⁹⁷

B. Wire Fraud

With regard to wire fraud, banks are typically careful to take advantage of the safe-harbor provisions of Article 4A as well by having standard wire transfer agreements that their customers must sign before conducting wire transfers. Typical agreements will provide that the customer agrees to comply with all security procedures set forth in the agreement, that the customer will be bound by any funds transfer payment order whether or not the order is authorized, and that the security procedure is commercially reasonable. Agreements will often include as well a provision analogous to Section 4-406, *viz.*, that the customer must report any unauthorized transfer to the bank within a specified period of time, such as fourteen days after receipt of confirmation of transfer.

⁹⁶ *Id.* 8.09[4][a].

⁹⁷ R.U.C.C. § 4-103(e) ("If there is also bad faith [the measure of damages] also includes any other damages the party suffered as a proximate consequence"). *See also* *McAdam v. Dean Witter Reynolds, Inc.*, 896 F.2d 750, 771 (3d Cir. 1990) (claim for conversion under U.C.C. § 3-419 can support a claim for punitive damages if the bank's conduct is sufficiently egregious under general state law regarding punitive damages); *D & G Equip. Co. v. First Nat'l Bank*, 764 F.2d 950, 957 n.6 (3d Cir. 1985) (same); *Sherrill White Constr., Inc. v. South Carolina Nat'l Bank*, 713 F.2d 1047, 1051-52 (4th Cir. 1983) (same).

The Code expressly provides that a procedure simply by which the bank compares the signature on the payment order to an authorized signature on file "is not by itself a security procedure" within the meaning of the Code.⁹⁸ Banks, therefore, typically provide other procedures, including optional callbacks to the customer upon receipt of a payment order. Thus, for example, one major international bank with which the writer is familiar gives its customers the option, in every wire transfer agreement, to require a call from the bank to the customer to verify a payment order before processing it. Such calls will typically be recorded. Another option is to require call-backs if the payment order is over a specified dollar amount, such as \$300,000. Provided that the bank gives its customer various options from which to select beyond a mere comparison of specimen signatures, the bank may have an argument under Section 4A-202(c) that the security procedure is commercially reasonable as a matter of law.

As the Code expressly states, and as the official comments made clear, whether these types of procedures are commercially reasonable in any given circumstance depends on the particular facts of the case.⁹⁹ The size, type, and frequency of payment orders common to the customer are all relevant to commercial reasonableness. For instance, individual payment orders are typically issued separately, so any given security procedure would be applied individually to each such payment order. Automated clearing house (ACH) payments, by contrast, are frequently issued in batches by delivery of ACH payment instructions on magnetic tape. These tapes are often accompanied by some transmittal form containing an item count and a dollar total. In this circumstance, the receiving bank can examine the signatures on the form and compare the item count and dollar total to the instructions on the tape, but the testing of individual payment orders contained on the tape may not be at all feasible for a reasonable cost. These factors will all come into play in determining the commercial reasonableness of the chosen procedure.¹⁰⁰

V. CONCLUSION

Bank fraud is an intractable social problem in the United States today, imposing significant social and economic costs. Fidelity insurance provides a valuable service in spreading the risk of losses for such crimes. The law governing those losses thus affects the fidelity carrier, as well as its insureds,

⁹⁸ U.C.C. § 4A-201.

⁹⁹ *Id.* § 4A-202(c) & *id.* Official Comment 4.

¹⁰⁰ J. Kevin French, *Unauthorized and Erroneous Payment Orders*, 45 BUS. LAW. 1425, 1432 (1990).

in a very real and profound way. Because Articles 3, 4, and 4A of the Uniform Commercial Code elevate standards of commercial reasonableness to determinative factors of loss allocation, those standards themselves also affect the bonding industry in a profound way. It is only prudent, therefore, for fidelity carriers to familiarize themselves with the details of commercial banking standards to allow them to make enlightened decisions regarding coverage, defense, and salvage.