THE
AMERICAN LAW REGISTER

FOUNDED 1852.

UNIVERSITY OF PENNSYLVANIA

DEPARTMENT OF LAW.

SUBSCRIPTION PRICE, $3.00 PER ANNUM, SINGLE COPIES, 35 CENTS.

Edited by members of the Department of Law of the University of Pennsylvania under the supervision of the Faculty, and published monthly for the Department by J. AUBREY ANDERSON, Business Manager, at S. W. Cor. Thirty-fourth and Chestnut Streets, Philadelphia, Pa. Address all literary communications to the EDITOR-IN-CHIEF; all business communications to the BUSINESS MANAGER.

BANKS—LIABILITY OF SUBAGENT—COLLECTION—EFFECT OF UNLIMITED INDORSEMENT.—*Continental National Bank* v. *First National Bank of West Point*, 36 S. (Miss.) 189 (1904).—This case, which embodies the latest expression of the law on this subject, makes no attempt to reconcile the "hopeless conflict" found in the decisions of courts of various states. The first bank sought to recover for checks forwarded under a general indorsement to a second bank—by which the checks were forwarded under a similar indorsement to the third bank, which made the collection and credited the second bank therewith on the general account before learning of the insolvency of the latter—by suit against the subagent bank on the ground that, as the subagent bank was, at the date of the receipt of the checks, utterly insolvent, it therefore had no right to receive such checks for deposit, and such action was fraudulent and revoked its employment by the first bank. But the court held that as the checks were received under a general indorsement, the third bank

was entitled to consider them as the property of the second bank and to dispose of the proceeds in accordance with the course of business dealings existing between said banks, and that this right was not affected by the fact that the second bank had been for a long period insolvent, the collection having been fully completed and the money actually received by the third bank and its right thereby established and fixed before such insolvency was disclosed.

Similar to the principal case is *American Exchange National Bank of Chicago* v. *Theummler*, 195 Ill. 90 (1902), in which the court said that possession of the draft by the agent bank indorsed in blank was *prima facie* evidence of ownership, and therefore its correspondent had the right to so treat it and to apply the proceeds to the reduction of an overdraft of said bank, provided such application is made before notice of the capacity in which the forwarding bank held the draft, and the correspondent was under no obligation to inquire whether it was held as agent or owner. However, there is this difference to be noted between the two decisions: in the former the court considered that the controlling legal principle is not different because no advances were made by the subagent on that particular collection; but the Illinois court said that even if the second bank have no notice of the title of the real owner, it is not entitled to retain against the real owners unless credit was given the other bank, or balances suffered to remain in its hands to be met by the negotiable paper transmitted, or expected to be transmitted, in the usual course of the dealings between the two banks. See *Bank of the Metropolis* v. *New England Bank*, 1 How. 234 (1843); *Wilson & Co.* v. *Smith*, 3 How. 763 (1854); 2 Morse, "Banks and Banking," §591-2; *Hackett* v. *Reynolds, Lamberton & Co.*, 114 Pa. 328 (1886). It would seem, as pointed out in the last case, that, not having shown that they had incurred any liability or done anything which made their position worse than it would have been if they had not received the note for collection and credit, the subagent bank would "have no equity which entitles them to withhold the proceeds from the owners of the note."

On the other hand, where the owner of a draft sent it to a bank indorsed "for collection," by which the draft was sent to its correspondent to collect, it was held that the latter received the draft for collection and for no other purpose, and the restrictive character of the indorsement informed the latter that title remained in the initial bank, and that it would own the proceeds when collected, and that the legal force of such indorsement "cannot be defeated by resort to usage or custom, or by any method of bookkeeping." *Commonwealth National Bank of Cincinnati* v. *Hamilton National Bank of Fort Wayne*, 42 Fed. 880 (1890). See *First National Bank of Crown Point* v. *First National Bank of Richmond*, 76 Ind. 561 (1881); *National Butchers' and Drovers' Bank* v. *Hubbell*, 117 N. Y. 384 (1889). In *National Exchange Bank of Dallas* v. *Beal*, 50 Fed. 355

(1892), in discussing the owner's right to the proceeds of the collection, the court said he was affected only by the state of accounts between him and his immediate correspondent, and his title to the paper or its proceeds is not prejudiced by the fact that some other bank holds as the immediate agent of his correspondent until the latter has by suitable entries on its books completed and recognized the relationship of creditor and debtor. This is a distinct modification of the rule above. Therefore where a subagent bank received several items for collection and credit under restrictive indorsements, and part only of the items had been collected and credited to the agent bank when the latter became insolvent, as to such items the relation of debtor and creditor had been established between the agent and the subagent banks, but as to the remaining items the subagent became the direct agent of the principal for their collection, or if they be credited to the receiver for the agent bank, they must be regarded as trust funds in his hands. *Commercial Bank of Pa.* v. *Armstrong*, 148 U. S. 50 (1892).

In the principal case it is stated that "where a bank collects checks received under a general indorsement, and remits the proceeds to the bank from which the items were received, it has discharged its whole duty in the premises, and the initial bank must look to its correspondent for payment; and when by the course of dealing or understanding the bank making the collection has a right to apply the proceeds of such collection to the credit of the bank from which the items were received, and upon making the collection, this is likewise a full discharge of its duty, and the initial bank has no right to hold the collecting bank for the proceeds of the collection." But if the subagent receive notice of the title of the agent bank, it is then liable to the real owner upon the insolvency of the agent bank. *Bank of Chicago* v. *Thcummler*, *supra*; though knowledge of such insolvency be obtained through a newspaper, it is sufficient to charge him with notice thereof. *Bank of Crown Point* v. *Bank of Richmond*, *supra*.

The courts are divided on the question whether the agent or the subagent bank is responsible to the owner of negotiable paper for negligence in its collection. One rule is that by the "receipt of negotiable paper for collection the bank or banker receiving it undertakes that the necessary means shall be taken to charge the drawer, indorser, and other parties upon default or refusal to pay or accept. Whether the bill or note be payable at its counter or elsewhere, the bank is liable for any neglect of duty occurring in its collection, by which any of the parties are discharged, whether of the officers and immediate servants, or other agents of the bank, or its correspondents, or agents employed by such correspondents." *Ayrault* v. *Pacific Bank*, 47 N. Y. 570 (1892); *Mackersay* v. *Ramsays*, 9 Clark and Fin. 818 (1843); *Van Wart* v. *Woolcy et al.*, 3 B. and C. 439 (1824); *Titus & Scudder* v. *Mechanics' National Bank*, 35 N. J. L. 588 (1871);

Hoover v. *Wise et al.*, 91 U. S. 308 (1876); *Bradstreet* v. *Everson*, 72 Pa. 124; *Exchange National Bank* v. *N. Y. Third National Bank*, 112 U. S. 281; *Hyde* v. *First National Bank*, 7 Biss. 156 (1876); *Naser* v. *First National Bank of New York*, 116 N. Y. 492 (1889); Bolles, "Banks and Banking," 472. This general liability may be varied by express contract or by implication arising from general usage. *Ayrault* v. *Pacific Bank, supra.*

On the other hand, there are those cases which hold that on the insolvency of the agent, and before payment by the subagent, and, of course, before any undistinguishable commingling of assets occurs, the principal may, by notice, make the subagent his own; and thus, except as to the right of the subagent to retain for a general balance in his favor against the agent, to render the receipt of the proceeds of the bills or notes by the subagent, in any other capacity than that of immediate agent for the principal, wrongful as against the principal, and so entitle him to recover. Wherever, by express agreement between the parties, a subagent is to be employed by the agent to receive money for the principal, or where an authority to do so may fairly be implied from the usual course of trade or the nature of the transaction, the principal may treat the subagent as his agent, and when he has received the money, may recover it from him. *Lawrence* v. *Stonington Bank*, 6 Conn. 521 (1827); *Bank of the Metropolis* v. *New England Bank*, 1 How. 234 (1843); *Wilson & Co.* v. *Smith*, 3 How. 763 (1845); *Guelick* v. *National Bank of Burlington*, 56 Iowa 434 (1881); *Bank of Lindsborg* v. *Ober*, 3 Pac. (Kan.) 324 (1884); *Milling Co.* v. *Kuenster & Co.*, 158 Ill. 259 (1895); *Anderson* v. *Alton National Bank*, 59 Ill. App. 587 (1895); *Kavanaugh* v. *Farmers' Bank*, 59 Mo. App. 540 (1894); *Dun* v. *City National Bank of Birmingham*, 58 Fed. 174 (1893); 2 Morse, "Banks and Banking," § 591; Storey on Agency, 260.

The case of *Bank of Orleans* v. *Smith*, 3 Hill (N. Y.) 563, decided that the owner "has an election as to the remedy and may resort to either party—the first bank employed to collect the paper, or the one to which it is transmitted and which actually does the default complained of." But it was decided in the later case of *Naser* v. *First National Bank of New York*, 116 N. Y. 492 (1889), that there is no privity between subagent and principal, but the agent "assumes the responsibility and is *alone* chargeable to his principal."

The Missouri Court of Appeals makes an exception to the rule in that state in case the drawer of the check resides at the same place with the bank. In that case the agent is liable for the negligence of the subagent to whom it chooses to confide the duty of making demand upon the drawee. *Kavanaugh* v. *Farmers' Bank, supra.* This is the only rule consistent with the doctrine holding subagents answerable to the principal, in view of the reason upon which it is based.

The first of these conflicting rules rests upon the proposition that from the very nature of the transaction, viewed in its essence, the agent bank is merely the instrument of transmission, and the paper is virtually delivered to the subagent bank by the owner. The other rule is based upon the nature of the contract, which is to perform certain duties necessary for the collection of the paper and the protection of the holder. After reviewing the lines of conflicting decisions in *Exchange National Bank* v. *Third National Bank, supra,* the court says, "The distinction between the liability of one who contracts to do a thing and one who merely receives a delegation of authority to act for another is a fundamental one."

If the banks have mutual and extensive dealings on a running account, each has a lien on paper sent by the other for collection: but in the absence of "mutual arrangement or previous course of dealing between the parties, whereby it is expressly or impliedly understood that such remittances of paper are to go to the credit of the previous account when received and no advance is made nor any credit given on the basis of the particular bill, and one bank merely passes the proceeds of the paper transmitted for collection to the credit of the other on the subsisting indebtedness which it happens to have at the time" against the other, "there is no lien, and no right to apply the money collected in that manner, but the real owner may maintain an action to recover the amount." 2 Morse, "Banks and Banking," § 592; *Wood* v. *Boylston National Bank,* 129 Mass. 358 (1880).

The rule adopted in the principal case, that the subagent bank should not be required to make any inquiry to ascertain who, in point of fact, is the real owner of the proceeds of the collection, where the items for collection are received under a general indorsement, seems to be the better one. The subagent has the right to assume that the ownership is in the bank forwarding the item to it. As the court there points out, "any other rule would render it impossible for the bank making a collection to protect itself unless the remittance was in all cases made to the payee named in the check, and this would often be not in accordance with the real rights of the parties in interest." *W. C. M.*