Chicago-Kent Law Review

Volume 36 | Issue 1 Article 3

April 1959

Banks and Banking - Functions and Dealings - Whether Bank's Liability for Paying a Forged Check is Absolutely Limited by Statutory Duty of Depositor to Notify Bank of Forgery within One Year after Return of Voucher

H. Q. Rohde

CHICAGO-KENT LAW REVIEW

PUBLISHED APRIL AND OCTOBER BY THE STUDENTS OF
CHICAGO-KENT COLLEGE OF LAW, 10 N. FRANKLIN ST., CHICAGO, ILLINOIS

Subscription price, $3.00 per year Single copies, $2.00 Foreign subscription, $3.50

VOLUME 36 APRIL, 1959 NUMBER 1

DISCUSSION OF RECENT DECISIONS

BANKS AND BANKING—FUNCTIONS AND DEALINGS—WHETHER BANK'S LIABILITY FOR PAYING A FORGED CHECK IS ABSOLUTELY LIMITED BY STATUTORY DUTY OF DEPOSITOR TO NOTIFY BANK OF FORGERY WITHIN ONE YEAR AFTER RETURN OF VOUCHER—Banks paying out under forged checks have been offered greater protection as a result of the decision in *Gerber* v. *Continental Illinois National Bank & Trust Company of Chicago.*[1] Therein, the defendant bank paid a check signed by unauthorized persons in con-

[1] 16 Ill. App. (2d) 379, 148 N. E. (2d) 597 (1958).

travention of signature cards in its files and then returned the voucher to those same persons who had, in the interim, become officers of the plaintiff depositor. The plaintiff sued to recover the amount of the forged check[2] which had been charged to its account. The defense was that the plaintiff had failed to notify the defendant of the forgery within one year after the return of the voucher as required by the so-called Liability for Forged and Raised Checks Act.[3] On appeal, the Appellate Court for the First District of Illinois affirmed the judgment for defendant. In so doing it held that receipt of the voucher by an officer of the plaintiff was sufficient to impose an absolute duty to notify the defendant of the forgery within one year so that it could proceed to enforce restitution from the forger.

The plaintiff's action was predicated on its contract of deposit with the defendant, which permitted the defendant to charge the plaintiff's account only on its authentic order. According to the terms of the contract, the bank was absolutely liable if it charged a forged check to the depositor's account.[4] The common law, however, attached a duty upon the depositor to use reasonable care in detecting any mistake made by the bank.[5] And, if the depositor failed to perform that duty, the common law absolved the bank from liability.[6] But an exception to this rule of the common law was that the bank would retain its liability if it had been negligent in charging the forged check to the depositor's account.[7] In this case, the defendant was negligent in charging the forged check to the plaintiff's account because it had prior constructive notice of the forgery through the resolutions and signature cards on file with it. Therefore, at common law, the exception would have applied and the defendant

[2] In an earlier appeal, the Appellate Court for the First District of Illinois held that signing a check without authority amounted to forgery, but reversed the decision of the trial court for the defendant and remanded the case to enable the plaintiff to file a reply to the defendant's answer and special defenses. Barrett v. Continental Illinois National Bank and Trust Company of Chicago, 2 Ill. App. (2d) 70, 118 N. E. (2d) 631 (1954). In both appeals, the plaintiff was the Director of Insurance of the State of Illinois, acting in his capacity as liquidator of the United States Mutual Insurance Company. The change in personnel in the office of Director of Insurance explains the change in the name of the plaintiff in the second appeal.

[3] Ill. Rev. Stat. 1957, Vol. 1, Ch. 16½, § 24, provides that a depositor can hold its bank liable for paying a forged check only if it notifies the bank that the check so paid is forged within one year after the return of the voucher.

[4] People v. Dunham, 344 Ill. 268, 176 N. E. 325 (1931); Dalmatinsko, etc. v. First Union T. & S. Bank, 268 Ill. App. 314 (1932); Chicago Savings Bank v. Block, 126 Ill. App. 128 (1906).

[5] Cosmopolitan Bank v. Lake Shore Bank, 343 Ill. 347, 175 N. E. 583 (1931); Moore & Co. v. Champaign Nat. Bank, 13 Ill. App. (2d) 97 (1957); Phillip v. First Nat. Bank, 297 Ill. App. 498, 18 N. E. (2d) 57 (1939).

[6] Folsom v. Northern Trust Co., 237 Ill. App. 419 (1925); Osborn v. Corn Exchange Nat. Bank of Chicago, 218 Ill. App. 28 (1920); Findlay v. Corn Ex. Nat'l. B'k., 166 Ill. App. 57 (1911).

[7] Illinois Tuberculosis Ass'n. v. Springfield Marine Bank, 282 Ill. App. 14 (1935).

would have been liable even though the plaintiff failed to use reasonable care.

However, the problem is further complicated by the statutory provision which imposes a duty on the depositor to give notice to the bank within one year after the return of the voucher as a condition subsequent to holding the bank liable. The notice requirement may be regarded as a condition subsequent because its effect is to adjust the common law liability by discharging the bank upon the depositor's failure to give notice. It cannot be viewed as a condition precedent because the cause of action existed at common law and was not created by the statute. Nor can it be treated as a statute of limitation because the action can be brought after one year if notice is given. Although the precise point has not been previously decided, the condition imposed would seem to require actual notice. The legislature appears to have expressed this intent by placing a duty on the depositor to take positive action by requiring him to give notice within one year *after* the return of the voucher. The provision requiring notice after the return of the voucher seems consistent with the purposes of the statute except insofar as it does not provide for the situation where actual notice was given after the check was paid but prior to the return of the voucher. In that situation, the bank would get even greater protection because it would be able to proceed against the forger more quickly. But it would seem that the requirement of the provision under discussion is not fulfilled by prior constructive notice because such notice could not result in the bank's discovering its mistake and it could not proceed against the forger until it discovered its mistake.[8]

The plaintiff contended that the statute was not applicable where it had given all the notice it could be reasonably expected to give under the circumstances. The plaintiff's position rests upon the general principle of agency law that where the agent's interest is adverse to that of the principal, notice to the agent will not be imputed to the principal.[9] And, in the present case, it appears that the agents' interests were opposed to the interests of the plaintiff. The Illinois Supreme Court gave effect to the principle here involved in the case of *The Merchants' National Bank*

[8] The courts of other states, construing similar statutes, have confirmed this conclusion. The Supreme Court of Kansas decided that the bank is not liable under any circumstances unless it is notified within the statutory period by the depositor: Herbel v. Peoples State Bank of Ellinwood, 170 Kan. 620, 228 P. (2d) 929 (1951). Also, the Supreme Court of South Dakota found that, irrespective of its knowledge of facts or of its negligence, the bank is not liable when the depositor fails to give notice within the statutory period: Flaherty Bros. v. The Bank of Kimball, 75 S. D. 468, 68 N. W. (2d) 105 (1955).

[9] Neagle v. McMullen, 334 Ill. 168, 165 N. E. 605 (1929); Seaverns v. Presbyterian Hospital, 173 Ill. 414, 50 N. E. 1079 (1898); In re Estate of Wedelius, 266 Ill. App. 69 (1932).

of Peoria v. *The Nichols & Shepard Company.*[10] However, in that case, the agent was a mere sales representative whereas, in the principal case, the agents were the officers of the plaintiff. The cases are distinguishable because officers are charged with the management of a corporation's daily affairs and are vested with more discretion than a mere sales representative. The analogy is further weakened because the forgers had since become authorized signers, although that information had not yet been communicated to the bank. It would appear that the defendant was correct in returning the voucher to the officers because the only other apparent alternative was to return it to the board of directors which met only intermittently and which was effectively incapable of receiving it.[11]

The statute, by imposing an absolute duty, placed an extreme limit upon the period during which the depositor could perfect its cause of action and thus offered the bank an opportunity to seek restitution seasonably. It, in effect, provided that the account between the depositor and the bank became an account stated no later than one year after the return of the voucher unless the depositor gave notice within that period. The statute enhances the equities between the parties because its effect was to give the bank a definite advantage which it did not previously possess. On the other hand, it works no particular hardship on the depositor by imposing the duty of giving notice within one year. While this requirement is inconsistent with the common law of Illinois, the only real obstacle to its easy fulfillment is the carelessness of the depositor in managing its own affairs.

H. Q. ROHDE

CONSTITUTIONAL LAW—DUE PROCESS—WHETHER THE DENIAL OF LOYALTY CLEARANCES MAY BE BASED ON FACELESS INFORMER EVIDENCE—Much recent controversy has centered on the problem of whether or not a person working with classified government material can be denied a loyalty clearance through an administrative proceeding in which he is not allowed to confront and cross-examine adverse witnesses. The "cold war" has tended to accentuate the issues presented, so that both sides of the controversy have now been fully represented by vigorous exponents. Typically this problem has embraced two classes of individuals who have been denied loyalty clearances; those engaged in governmental projects who are privately employed by firms working on government contracts, and those employed directly by the government.

10 223 Ill. 41, 79 N. E. 38 (1906).

11 A case from another jurisdiction supports this conclusion. The Court of Appeals of New York held that when vouchers are returned to the president of the depositor, they have been returned to the depositor within the meaning of the New York statute: Shattuck v. Guardian Trust Co. of New York, 204 N. Y. 200, 97 N. E. 517 (1912).